

CAPITAL CITY BANK GROUP INC  
Form 10-K  
March 06, 2015

**UNITED STATES**

**SECURITIES AND EXCHANGE COMMISSION**

**WASHINGTON, DC 20549**

FORM 10-K

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

**For the fiscal year ended December 31, 2014**

**OR**

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

**For the transition period from \_\_\_\_\_ to \_\_\_\_\_**

(Exact name of Registrant as specified in its charter)

**Florida**                      **0-13358**                      **59-2273542**  
(State of Incorporation) (Commission File Number) (IRS Employer Identification No.)

**217 North Monroe Street, Tallahassee, Florida**      **32301**  
(Address of principal executive offices)                      (Zip Code)

**(850) 671-0300**

(Registrant's telephone number, including area code)

**Securities registered pursuant to Section 12(b) of the Act:**

<u>Title of Each Class</u>	<u>Name of Each Exchange on Which Registered</u>
Common Stock, \$0.01 par value	The Nasdaq Stock Market LLC

**Securities registered pursuant to Section 12(g) of the Act: None**

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.  
Yes  No

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Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act. Yes  No

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 (§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  No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company

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

The aggregate market value of the registrant's common stock, \$0.01 par value per share, held by non-affiliates of the registrant on June 30, 2014, the last business day of the registrant's most recently completed second fiscal quarter, was approximately \$155,431,117 (based on the closing sales price of the registrant's common stock on that date). Shares of the registrant's common stock held by each officer and director and each person known to the registrant to own 10% or more of the outstanding voting power of the registrant have been excluded in that such persons may be deemed to be affiliates. This determination of affiliate status is not a determination for other purposes.

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

Class	Outstanding at February 27, 2015
Common Stock, \$0.01 par value per share	17,520,576

## **DOCUMENTS INCORPORATED BY REFERENCE**

Portions of our Proxy Statement for the Annual Meeting of Shareowners to be held on April 28, 2015, are incorporated by reference in Part III.

**CAPITAL CITY BANK GROUP, INC.**

**ANNUAL REPORT FOR 2014 ON FORM 10-K**

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## INTRODUCTORY NOTE

This Annual Report on Form 10-K contains “forward-looking statements” within the meaning of the Private Securities Litigation Reform Act of 1995. These forward-looking statements include, among others, statements about our beliefs, plans, objectives, goals, expectations, estimates and intentions that are subject to significant risks and uncertainties and are subject to change based on various factors, many of which are beyond our control. The words “may,” “could,” “should,” “would,” “believe,” “anticipate,” “estimate,” “expect,” “intend,” “plan,” “target,” “goal,” and similar expressions are used to identify forward-looking statements.

All forward-looking statements, by their nature, are subject to risks and uncertainties. Our actual future results may differ materially from those set forth in our forward-looking statements.

In addition to those risks discussed in this Annual Report under Item 1A Risk Factors, factors that could cause our actual results to differ materially from those in the forward-looking statements, include, without limitation:

- legislative or regulatory changes, including the Dodd-Frank Act, Basel III, and the ability to repay and qualified mortgage standards;
- our ability to successfully manage interest rate risk, liquidity risk, and other risks inherent to our industry;
- the effects of security breaches and computer viruses that may affect our computer systems or fraud related to credit or debit card products;
- the accuracy of our financial statement estimates and assumptions, including the estimates used for our loan loss provision and deferred tax asset valuation allowance;
- the frequency and magnitude of foreclosure of our loans;
- the effects of our lack of a diversified loan portfolio, including the risks of geographic and industry concentrations;
- the strength of the United States economy in general and the strength of the local economies in which we conduct operations;
- our need and our ability to incur additional debt or equity financing;
- our ability to declare and pay dividends;
- changes in the securities and real estate markets;
- changes in monetary and fiscal policies of the U.S. Government;
- inflation, interest rate, market and monetary fluctuations;
- the effects of harsh weather conditions, including hurricanes, and man-made disasters;
- our ability to comply with the extensive laws and regulations to which we are subject;
- our ability to comply with the laws for each jurisdiction where we operate;
- the willingness of clients to accept third-party products and services rather than our products and services and vice versa;
- increased competition and its effect on pricing;
- technological changes;
- negative publicity and the impact on our reputation;
- changes in consumer spending and saving habits;
- growth and profitability of our noninterest income;
- changes in accounting principles, policies, practices or guidelines;

- the limited trading activity of our common stock;
- the concentration of ownership of our common stock;
- anti-takeover provisions under federal and state law as well as our Articles of Incorporation and our Bylaws;
- other risks described from time to time in our filings with the Securities and Exchange Commission; and
- our ability to manage the risks involved in the foregoing.

However, other factors besides those listed in *Item 1A Risk Factors* or discussed in this Annual Report also could adversely affect our results, and you should not consider any such list of factors to be a complete set of all potential risks or uncertainties. Any forward-looking statements made by us or on our behalf speak only as of the date they are made. We do not undertake to update any forward-looking statement, except as required by applicable law.

## PART I

## Item 1. Business

About Us

## General

Capital City Bank Group, Inc. (“CCBG”) is a financial holding company headquartered in Tallahassee, Florida. CCBG was incorporated under Florida law on December 13, 1982, to acquire five national banks and one state bank that all subsequently became part of CCBG’s bank subsidiary, Capital City Bank (“CCB” or the “Bank”). In this report, the terms “Company,” “we,” “us,” or “our” mean CCBG and all subsidiaries included in our consolidated financial statements.

We provide traditional deposit and credit services, asset management, trust, mortgage banking, merchant services, bank cards, data processing, and securities brokerage services through 63 full-service banking locations in Florida, Georgia, and Alabama operated by CCB. The majority of our revenue, approximately 82%, is derived from our Florida market areas while approximately 17% and 1% of our revenue is derived from our Georgia and Alabama market areas, respectively.

Below is a summary of our financial condition and results of operations for the past three years. Our financial condition and results of operations are more fully discussed in our management discussion and analysis on page 29 and our consolidated financial statements on page 59.

Dollars in millions

Year Ended December 31,	Assets	Deposits	Shareowners’ Equity	Revenue <sup>(1)</sup>	Net Income
2014	\$2,627.2	\$2,146.8	\$ 272.5	\$ 130.8	\$ 9.3
2013	2,611.9	2,136.2	276.4	137.3	6.0
2012	2,634.0	2,145.0	246.9	144.2	0.1

<sup>(1)</sup> Revenue represents interest income plus noninterest income.

Dividends and management fees received from the Bank are CCBG’s primary source of income. Dividend payments by the Bank to CCBG depend on the capitalization, earnings and projected growth of the Bank, and are limited by various regulatory restrictions. See the section entitled “Regulatory Matters” in this *Item 1* and Note 14 in the Notes to Consolidated Financial Statements for a discussion of the restrictions.

We had a total of 937 associates at March 1, 2015. Item 6 contains other financial and statistical information about us.

**Subsidiaries of CCBG**

CCBG's principal asset is the capital stock of the CCB, our wholly owned banking subsidiary, which accounted for approximately 100% of consolidated assets at December 31, 2014, and approximately 100% of consolidated net income for the year ended December 31, 2014. In addition to our banking subsidiary, CCB has three primary wholly owned subsidiaries, Capital City Trust Company, Capital City Banc Investments, Inc., and Capital City Services Company. The nature of these subsidiaries is provided below.

### **Operating Segment**

We have one reportable segment with four principal services: Banking Services (CCB), Data Processing Services (Capital City Services Company), Trust and Asset Management Services (Capital City Trust Company), and Brokerage Services (Capital City Banc Investments, Inc.). Revenues from each of these principal services for the year ended 2014 totaled approximately 92.8%, 1.2%, 3.1%, and 2.9% of our total revenue, respectively. In 2013 and 2012, Banking Services (CCB) revenue was approximately 91.9% and 93.1% of our total revenue for each respective year.

### ***Capital City Bank***

CCB is a Florida-chartered full-service bank engaged in the commercial and retail banking business. Significant services offered by the Bank include:

*Business Banking* – The Bank provides banking services to corporations and other business clients. Credit products are available for a wide variety of general business purposes, including financing for commercial business properties, equipment, inventories and accounts receivable, as well as commercial leasing and letters of credit. We also provide treasury management services, and, through a marketing alliance with Elavon, Inc., merchant credit card transaction processing services.

*Commercial Real Estate Lending* – The Bank provides a wide range of products to meet the financing needs of commercial developers and investors, residential builders and developers, and community development. Credit products are available to purchase land and/or build structures for business use and for investors who are developing residential or commercial property.

*Residential Real Estate Lending* – The Bank provides products to help meet the home financing needs of consumers, including conventional permanent and construction/ permanent (fixed, adjustable, or variable rate) financing arrangements, and FHA/VA loan products. The Bank offers both fixed-rate and adjustable rate residential mortgage (ARM) loans. A portion of our loans originated are sold into the secondary market. The Bank offers these products through its existing network of banking offices. We do not originate subprime residential real estate loans.

*Retail Credit* – The Bank provides a full-range of loan products to meet the needs of consumers, including personal loans, automobile loans, boat/RV loans, home equity loans, and through a marketing alliance with ELAN, we offer credit card programs.

*Institutional Banking* – The Bank provides banking services to meet the needs of state and local governments, public schools and colleges, charities, membership and not-for-profit associations including customized checking and savings accounts, cash management systems, tax-exempt loans, lines of credit, and term loans.

*Retail Banking* – The Bank provides a full-range of consumer banking services, including checking accounts, savings programs, automated teller machines (ATMs), debit/credit cards, night deposit services, safe deposit facilities, online banking, and mobile banking. Clients can use Capital City Bank Direct which offers a “live” call center between the hours of 8 a.m. to 6 p.m. Monday through Friday and from 9 a.m. to 12 noon on Saturday. The call center can also be accessed via live chat through the internet. Bank Direct also offers an automated phone system offering 24-hour access to client deposit and loan account information and transfer of funds between linked accounts. The Bank is a member of the “Star” ATM Network that permits banking clients to access cash at ATMs or “point-of-sale” merchants.

### ***Capital City Trust Company***

Capital City Trust Company (the “Trust Company”) is the investment management arm of CCB. The Trust Company provides asset management for individuals through agency, personal trust, IRA, and personal investment management accounts. The Trust Company also provides services for the administration of pension, profit sharing, and 401(k) plans. Associations, endowments, and other nonprofit entities hire the Trust Company to manage their investment portfolios. Additionally, a staff of well-trained professionals serves individuals requiring the services of a trustee, personal representative, or a guardian. The market value of trust assets under discretionary management exceeded \$726.2 million as of December 31, 2014, with total assets under administration exceeding \$851.8 million.

### ***Capital City Banc Investments, Inc.***

Capital City Banc Investments, Inc. offers access to retail investment products through INVEST Financial Corporation, a member of FINRA and SIPC. Non-deposit investment and insurance products are: (i) not FDIC insured; (ii) not deposits, obligations, or guarantees by any bank; and (iii) subject to investment risk, including the



possible loss of principal amount invested. Capital City Banc Investments, Inc. offers a full line of retail securities products, including U.S. Government bonds, tax-free municipal bonds, stocks, mutual funds, unit investment trusts, annuities, life insurance and long-term health care. We are not an affiliate of INVEST Financial Corporation.

*Capital City Services Company*

Capital City Services Company (the “Services Company”) provides data processing services to financial institutions (including CCB), government agencies, and commercial clients located in North Florida and South Georgia. As of March 1, 2015, the Services Company is providing data processing services to four correspondent banks which have relationships with CCB.

## **Underwriting Standards**

A core goal of CCB is to support the communities in which it operates. The Bank seeks loans from within its primary market area, which is defined as the counties in which the Bank's offices are located. The Bank will originate loans within its secondary market area, defined as adjacent counties to those in which the Bank has offices. There may also be occasions when the Bank will have opportunities to make loans that are out of both the primary and secondary market areas. These loans will only be approved if the applicant is known to the Bank and applicant's primary business is within our primary or secondary market area. Approval of all loans is subject to the Bank's policies and standards described in more detail below.

The Bank has adopted comprehensive lending policies, underwriting standards and loan review procedures. Management and the Bank's Board of Directors reviews and approves these policies and procedures on a regular basis (at least annually).

Management has also implemented reporting systems to monitor loan originations, loan quality, concentrations of credit, loan delinquencies and nonperforming loans and potential problem loans. Bank management and the Credit Risk Oversight Committee periodically review our lines of business to monitor asset quality trends and the appropriateness of credit policies. In addition, total borrower exposure limits are established and concentration risk is monitored. As part of this process, the overall composition of the portfolio is reviewed to gauge diversification of risk, client concentrations, industry group, loan type, geographic area, or other relevant classifications of loans. Specific segments of the portfolio are monitored and reported to the Bank's Board on a quarterly basis (i.e., commercial real estate) and the Bank has strategic plans in place to supplement Board approved credit policies governing exposure limits and underwriting standards. The Bank recognizes that exceptions to the below-listed policy guidelines may occasionally occur and has established procedures for approving exceptions to these policy guidelines.

### ***Residential Real Estate Loans***

The Bank originates 1-4 family, owner-occupied residential real estate loans in its Residential Real Estate line of business. The Bank's policy is to underwrite these loans in accordance with secondary market guidelines in effect at the time of origination, including loan-to-value ("LTV") and documentation requirements. The Bank originates fixed-rate, adjustable-rate and variable-rate residential real estate loans. Over the past five years, the vast majority of residential loan originations have been fixed-rate loans which are sold in the secondary market on a non-recourse basis with related servicing rights (i.e., the Bank does not service sold loans). These loans require private mortgage insurance ("PMI") if the LTV exceeds 80%. Some of the adjustable-rate residential real estate product is retained in the Bank's loan portfolio and loans with LTVs in excess of 85% require PMI. Adjustable rate mortgage ("ARM") loans with an initial fixed interest rate period greater than three years are sold in the secondary market on a non-recourse basis.

The Bank also originates 1-4 family, owner-occupied residential real estate loans throughout its banking office network. These loans are generally not eligible for sale into the secondary market due to not meeting a specific secondary market underwriting requirement. The product offering is a variable rate 3/1 ARM with a maximum term of 30 years and maximum LTV of 80%. The Bank verifies applicants' income, obtains credit reports and independent real estate appraisals in the underwriting process to ensure adequate collateral coverage and that loans are extended to individuals with good credit and income sufficient to repay the loan.

Residential real estate loans also include home equity lines of credit and home equity loans ("HELOCs"). The Bank's home equity portfolio includes revolving open-ended equity loans with interest-only or minimal monthly principal payments and closed-end amortizing loans. Open-ended equity loans typically have an interest only ten year draw period followed by a five year repayment period of 0.75% of principal balance monthly and balloon payment at maturity. As of December 31, 2014, approximately 60% of the Bank's residential home equity loan portfolio consisted of first mortgages. Interest rates may be fixed or adjustable. Adjustable-rate loans are tied to the Prime Rate with a

typical margin of 1.0% or more. Appraisals are normally required for all residential real estate loans, both those sold to the secondary market and those maintained in the Bank's loan portfolio.

The Consumer Financial Protection Bureau finalized its ability to repay ("ATR") rule as well as its qualified mortgage rule in January 2013 (with clarifications adopted in July 2013). The ATR rule applies to residential mortgage loan applications received after January 14, 2014. The scope of the rule specifically applies to loans securing 1-4 unit dwellings and includes purchases, refinances and home equity loans for principal or second homes. Under the ATR rules, a lender may not make a residential mortgage loan unless the lender makes a reasonable and good faith determination that is based on verified, documented information at or before consummation that the borrower has a reasonable ability to repay. The eight underwriting factors that must be considered and verified include the following: (1) income and assets; (2) employment status; (3) monthly payment of loan; (4) monthly payment of any simultaneous loan secured by the same property; (5) monthly payment for other mortgage-related obligations like property taxes and insurance; (6) current debt obligations; (7) monthly debt to income ratio; and (8) credit history (although eight factors are delineated, the ATR rule does not dictate that a lender follow a particular underwriting model). Liability for violations of the ATR rule include actual damages, statutory damages and court costs and attorneys' fees.

Additionally, the Consumer Financial Protection Bureau published regulations required by the Wall Street Reform and Consumer Protection Act of 2010 (“Dodd-Frank”) related to “qualified mortgages,” which are mortgages for which there is a presumption that the lender has satisfied the ATR rules. Pursuant to Dodd-Frank, qualified mortgages (“QMs”) must have certain product-feature prerequisites and affordability underwriting requirements. Generally, to meet the QM test, the lender must calculate the monthly payments based on the highest payment that will apply in the first five years and the consumer must have a total debt-to-income ratio that is less than or equal to 43%. The QM rule provides a safe harbor to the ATR rules for lenders that make loans that satisfy the definition of a QM and are not higher priced. From time to time, the Bank originates non-qualified mortgages under certain predefined internal and investor underwriting parameters to be sold to either secondary market investors or held in the Bank’s loan portfolio.

### ***Commercial Loans***

The Bank’s policy sets forth guidelines for debt service coverage ratios, LTV ratios and documentation standards. Commercial loans are primarily made based on identified cash flows of the borrower with consideration given to underlying collateral and personal or other guarantees. The Bank’s policy establishes debt service coverage ratio limits that require a borrower’s cash flow to be sufficient to cover principal and interest payments on all new and existing debt. The majority of the Bank’s commercial loans are secured by the assets being financed or other business assets such as accounts receivable or inventory. Many of the loans in the commercial portfolio have variable interest rates tied to the Prime Rate or U.S. Treasury indices.

### ***Commercial Real Estate Loans***

The Bank’s policy sets forth guidelines for debt service coverage ratios, LTV ratios and documentation standards. Commercial real estate loans are primarily made based on identified cash flows of the borrower with consideration given to underlying real estate collateral and personal guarantees. The Bank’s policy establishes a maximum LTV specific to property type and minimum debt service coverage ratio limits that require a borrower’s cash flow to be sufficient to cover principal and interest payments on all new and existing debt. Commercial real estate loans may be fixed or variable-rate loans with interest rates tied to the Prime Rate or U.S. Treasury indices. Bank policy requires appraisals for loans in excess of \$250,000 that are secured by real property.

### ***Consumer Loans***

The Bank’s consumer loan portfolio includes personal installment loans, direct and indirect automobile financing, and overdraft lines of credit. The majority of the consumer loan portfolio consists of indirect and direct automobile loans. The majority of the Bank’s consumer loans are short-term and have fixed rates of interest that are set giving consideration to current market interest rates and the financial strength of the borrower. The Bank’s policy establishes maximum debt-to-income ratios, minimum credit scores, and includes guidelines for verification of applicants’ income and receipt of credit reports.

### **Lending Limits and Extensions of Additional Credit**

The Bank has established an internal lending limit of \$10.0 million for the total aggregate amount of credit that will be extended to a client and any related entities within its Board approved policies. This compares to our legal lending limit of approximately \$76 million. In practice, the Bank seeks to maintain an internal lending limit of \$7.5 million in order to maintain a well-diversified loan portfolio.

### **Loan Modification and Restructuring**

In the normal course of business, CCB receives requests from its clients to renew, extend, refinance, or otherwise modify their current loan obligations. In most cases, this may be the result of a balloon maturity that is typical in most commercial loan agreements, a request to refinance to obtain current market rates of interest, competitive reasons, or the conversion of a construction loan to a permanent financing structure at the completion or stabilization of the property. In these cases, the request is held to the normal underwriting standards and pricing strategies as any other loan request, whether new or renewal.

In other cases, we may modify a loan because of a reduction in debt service capacity experienced by the client (i.e., potentially troubled loan whereby the client may be experiencing financial difficulties). To maximize the collection of loan balances, we evaluate troubled loans on a case-by-case basis to determine if a loan modification would be appropriate. We pursue loan modifications when there is a reasonable chance that an appropriate modification would allow our client to continue servicing the debt.

## Expansion of Business

Our philosophy is to build long-term client relationships based on quality service, high ethical standards, and safe and sound banking practices. We maintain a locally oriented, community-based focus, which is augmented by experienced, centralized support in select specialized areas. Our local market orientation is reflected in our network of banking office locations, experienced community executives with a dedicated President for each market, and community boards which support our focus on responding to local banking needs. We strive to offer a broad array of sophisticated products and to provide quality service by empowering associates to make decisions in their local markets.

We have sought to build a franchise in small- to medium-sized markets, located on the outskirts of the larger metropolitan markets where we are positioned as a market leader. Many of our markets are on the outskirts of these larger markets in close proximity to major interstate thoroughfares such as Interstates I-10 and I-75. Our three largest markets are Tallahassee (Leon, Florida), Gainesville (Alachua, Florida), and Macon (Bibb, Georgia). In 13 of 20 markets in Florida and three of five markets in Georgia, we rank within the top 4 banks in terms of market share. Furthermore, in the counties in which we operate, we maintain an average 9.10% market share in the Florida counties and 5.82% in the Georgia counties, suggesting that there is significant opportunity to grow market share within these geographic areas. The larger employers in many of our markets are state and local governments, healthcare providers, educational institutions, and small businesses. While we realize that the markets in our footprint do not provide for a level of potential growth that the larger metropolitan markets may provide, our markets do provide good growth dynamics and have historically grown in excess of the national average. We strive to provide value added services to our clients by being their banker, not just a bank. This element of our strategy distinguishes Capital City Bank from our competitors.

As a result of the contracted credit cycle over the last several years and the overall regulatory environment, we have not pursued additional acquisitions; however, our long-term vision remains to profitably expand our franchise through a combination of organic growth in existing markets and through acquisitions. We have long understood that our core deposit funding base is the predominant driver of our profitability and overall franchise value, and have focused extensively on this component of our organic growth efforts in recent years.

Potential acquisition growth will continue to be focused on Florida, Georgia, and Alabama with a particular focus on financial institutions located on the outskirts of larger, metropolitan areas. Five markets have been identified, four in Florida and one in Georgia, in which management intends to proactively pursue expansion opportunities. These markets include Alachua, Marion, Hernando/Pasco counties in Florida, the western panhandle of Florida, and Bibb and surrounding counties in central Georgia. Our focus on some of these markets may change as we continue to evaluate our strategy and the impact the current economic cycle is having on any individual market. We will also continue to evaluate de novo expansion opportunities in attractive new markets in the event that acquisition opportunities in those markets are not feasible. Other expansion opportunities that will be evaluated include asset management, mortgage banking, and insurance. Embedded in our acquisition strategy is our desire to partner with institutions that are culturally similar, have experienced management and possess either established market presence or have potential for improved profitability through growth, economies of scale, or expanded services. Generally, these target institutions would range in asset size from \$100 million to \$400 million.

## Competition

We operate in a highly competitive environment, especially with respect to services and pricing. In addition, the banking business is experiencing enormous changes. Since 2009, nearly 500 financial institutions have failed in the U.S., including 83 in Georgia and 70 in Florida. Nearly all of the failed banks were community banks. The assets and deposits of many of these failed community banks were acquired mostly by larger financial institutions. We expect consolidation to continue during 2015, but primarily through traditional merger and acquisition activity. We believe that the larger financial institutions acquiring banks in our market areas are less familiar with the markets in which we operate and typically target a different client base. We believe clients who bank at community banks tend to prefer the relationship style service of community banks compared to larger banks. As a result, we believe the reduction of the number of community banks could further enhance our competitive position and opportunities in many of our markets. Larger financial institutions, however, can benefit from economies of scale. Therefore, these larger institutions may be able to offer banking products and services at more competitive prices than us. Additionally, these larger financial institutions may offer financial products that we do not offer.

Our primary market area consists of 20 counties in Florida, five counties in Georgia, and one county in Alabama. In these markets, the Bank competes against a wide range of banking and nonbanking institutions including savings and loan associations, credit unions, money market funds, mutual fund advisory companies, mortgage banking companies, investment banking companies, finance companies and other types of financial institutions. Most of Florida's major banking concerns have a presence in Leon County. CCB's Leon County deposits totaled \$782.2 million, or 36.4% of our consolidated deposits at December 31, 2014.

The table below depicts our market share percentage within each county, based on commercial bank deposits within the county.

County	Market Share as of June 30, <sup>(1)</sup>		
	2014	2013	2012
Florida			
Alachua	4.8 %	4.5 %	4.5 %
Bradford	51.5%	51.8%	52.3%
Citrus	3.6 %	3.6 %	3.3 %
Clay	2.0 %	1.8 %	1.8 %
Dixie	9.9 %	15.1%	18.5%
Gadsden	77.4%	70.2%	62.1%
Gilchrist	42.2%	40.8%	42.1%
Gulf	14.0%	14.0%	13.7%
Hernando	1.8 %	1.9 %	1.9 %
Jefferson	22.1%	19.8%	21.4%
Leon	15.3%	15.3%	16.5%
Levy	28.0%	27.8%	28.7%
Madison	10.3%	9.0 %	9.7 %
Pasco	0.1 %	0.1 %	0.2 %
Putnam	19.5%	18.9%	18.0%
St. Johns	0.9 %	0.9 %	1.1 %
Suwannee	6.8 %	6.8 %	6.9 %
Taylor	22.0%	21.8%	30.8%
Wakulla	13.6%	13.6%	11.7%
Washington	13.6%	13.8%	12.3%
Georgia			
Bibb	3.6 %	3.8 %	3.5 %
Burke	6.8 %	12.7%	8.4 %
Grady	14.3%	14.6%	17.4%
Laurens	9.1 %	9.0 %	10.4%
Troup	5.3 %	5.1 %	7.2 %
Alabama			
Chambers	7.6 %	8.1 %	7.7 %

<sup>(1)</sup> Obtained from the FDIC Summary of Deposits Report for the year indicated.



The following table sets forth the number of commercial banks and offices, including our offices and our competitors' offices, within each of the respective counties.

County	Number of Commercial Banks	Number of Commercial Bank Offices
Florida		
Alachua	17	64
Bradford	3	3
Citrus	12	43
Clay	13	30
Dixie	4	5
Gadsden	2	3
Gilchrist	4	6
Gulf	3	5
Hernando	14	40
Jefferson	2	2
Leon	17	79
Levy	2	11
Madison	5	5
Pasco	21	105
Putnam	6	13
St. Johns	23	64
Suwannee	5	8
Taylor	3	4
Wakulla	3	4
Washington	6	6
Georgia		
Bibb	10	50
Burke	5	10
Grady	5	8
Laurens	10	20
Troup	10	23
Alabama		
Chambers	6	9

*Data obtained from the June 30, 2014 FDIC Summary of Deposits Report.*

### **Seasonality**

We believe our commercial banking operations are not generally seasonal in nature; however, public deposits tend to increase with tax collections in the fourth and first quarters of each year and decline with spending thereafter.

## **Regulatory Considerations**

*We must comply with state and federal banking laws and regulations that control virtually all aspects of our operations. These laws and regulations generally aim to protect our depositors, not necessarily our shareowners or our creditors. Any changes in applicable laws or regulations may materially affect our business and prospects. Proposed legislative or regulatory changes may also affect our operations. The following description summarizes some of the laws and regulations to which we are subject. References to applicable statutes and regulations are brief summaries, do not purport to be complete, and are qualified in their entirety by reference to such statutes and regulations.*

### **The Company**

We are registered with the Board of Governors of the Federal Reserve as a financial holding company under the Bank Holding Company Act of 1956. As a result, we are subject to supervisory regulation and examination by the Federal Reserve. The Gramm-Leach-Bliley Act, the Bank Holding Company Act, and other federal laws subject financial holding companies to particular restrictions on the types of activities in which they may engage, and to a range of supervisory requirements and activities, including regulatory enforcement actions for violations of laws and regulations.

### ***Permitted Activities***

The Gramm-Leach-Bliley Act modernized the U.S. banking system by: (i) allowing bank holding companies that qualify as “financial holding companies” such as CCBG to engage in a broad range of financial and related activities; (ii) allowing insurers and other financial service companies to acquire banks; (iii) removing restrictions that applied to bank holding company ownership of securities firms and mutual fund advisory companies; and (iv) establishing the overall regulatory scheme applicable to bank holding companies that also engage in insurance and securities operations. The general effect of the law was to establish a comprehensive framework to permit affiliations among commercial banks, insurance companies, securities firms, and other financial service providers. Activities that are financial in nature are broadly defined to include not only banking, insurance, and securities activities, but also merchant banking and additional activities that the Federal Reserve, in consultation with the Secretary of the Treasury, determines to be financial in nature, incidental to such financial activities, or complementary activities that do not pose a substantial risk to the safety and soundness of depository institutions or the financial system generally.

In contrast to financial holding companies, bank holding companies are limited to managing or controlling banks, furnishing services to or performing services for its subsidiaries, and engaging in other activities that the Federal Reserve determines by regulation or order to be so closely related to banking or managing or controlling banks as to be a proper incident thereto. In determining whether a particular activity is permissible, the Federal Reserve must consider whether the performance of such an activity reasonably can be expected to produce benefits to the public that outweigh possible adverse effects. Possible benefits include greater convenience, increased competition, and gains in efficiency. Possible adverse effects include undue concentration of resources, decreased or unfair competition, conflicts of interest, and unsound banking practices. Despite prior approval, the Federal Reserve may order a bank holding company or its subsidiaries to terminate any activity or to terminate ownership or control of any subsidiary when the Federal Reserve has reasonable cause to believe that a serious risk to the financial safety, soundness or stability of any bank subsidiary of that bank holding company may result from such an activity.

### ***Changes in Control***

Subject to certain exceptions, the Bank Holding Company Act and the Change in Bank Control Act, together with the applicable regulations, require Federal Reserve approval (or, depending on the circumstances, no notice of disapproval) prior to any person or company acquiring “control” of a bank or bank holding company. A conclusive presumption of control exists if an individual or company acquires the power, directly or indirectly, to direct the management or policies of an insured depository institution or to vote 25% or more of any class of voting securities of any insured depository institution. A rebuttable presumption of control exists if a person or company acquires 10% or more but less than 25% of any class of voting securities of an insured depository institution and either the institution has registered securities under Section 12 of the Securities Exchange Act of 1934, which we will refer to as the Exchange Act, or no other person will own a greater percentage of that class of voting securities immediately after the acquisition. Our common stock is registered under Section 12 of the Exchange Act.

The Federal Reserve Board maintains a policy statement on minority equity investments in banks and bank holding companies, that generally permits investors to (i) acquire up to 33% of the total equity of a target bank or bank holding company, subject to certain conditions, including (but not limited to) that the investing firm does not acquire 15% or more of any class of voting securities, and (ii) designate at least one director, without triggering the various regulatory requirements associated with control.

As a financial holding company, we are required to obtain prior approval from the Federal Reserve before (i) acquiring all or substantially all of the assets of a bank or bank holding company, (ii) acquiring direct or indirect ownership or control of more than 5% of the outstanding voting stock of any bank or bank holding company (unless we own a majority of such bank’s voting shares), or (iii) merging or consolidating with any other bank or bank holding company. In determining whether to approve a proposed bank acquisition, federal bank regulators will consider, among other factors, the effect of the acquisition on competition, the public benefits expected to be received from the acquisition, the projected capital ratios and levels on a post-acquisition basis, and the acquiring institution’s record of addressing the credit needs of the communities it serves, including the needs of low and moderate income neighborhoods, consistent with the safe and sound operation of the bank, under the Community Reinvestment Act of 1977.

Under Florida law, a person or entity proposing to directly or indirectly acquire control of a Florida bank must also obtain permission from the Florida Office of Financial Regulation. Florida statutes define “control” as either (i) indirectly or directly owning, controlling or having power to vote 25% or more of the voting securities of a bank; (ii) controlling the election of a majority of directors of a bank; (iii) owning, controlling, or having power to vote 10% or more of the voting securities as well as directly or indirectly exercising a controlling influence over management or policies of a bank; or (iv) as determined by the Florida Office of Financial Regulation. These requirements will affect us because CCB is chartered under Florida law and changes in control of CCBG are indirect changes in control of CCB.

### ***Tying***

Financial holding companies and their affiliates are prohibited from tying the provision of certain services, such as extending credit, to other services or products offered by the holding company or its affiliates, such as deposit products.

### ***Capital; Dividends; Source of Strength***

The Federal Reserve imposes certain capital requirements on financial holding companies under the Bank Holding Company Act, including a minimum leverage ratio and a minimum ratio of “qualifying” capital to risk-weighted assets. These requirements are described below under “Capital Regulations.” Subject to its capital requirements and certain other restrictions, we are generally able to borrow money to make a capital contribution to CCB, and such loans may be repaid from dividends paid from CCB to us. We are also able to raise capital for contributions to CCB by issuing securities without having to receive regulatory approval, subject to compliance with federal and state securities laws.

In accordance with Federal Reserve policy, which has been codified by the Dodd-Frank Act, we are expected to act as a source of financial strength to CCB and to commit resources to support CCB in circumstances in which we might not otherwise do so. In furtherance of this policy, the Federal Reserve may require a financial holding company to terminate any activity or relinquish control of a nonbank subsidiary (other than a nonbank subsidiary of a bank) upon the Federal Reserve’s determination that such activity or control constitutes a serious risk to the financial soundness or stability of any subsidiary depository institution of the financial holding company. Further, federal bank regulatory authorities have additional discretion to require a financial holding company to divest itself of any bank or nonbank subsidiary if the agency determines that divestiture may aid the depository institution’s financial condition.

### **Capital City Bank**

CCB is a banking institution that is chartered by and headquartered in the State of Florida, and it is subject to supervision and regulation by the Florida Office of Financial Regulation. The Florida Office of Financial Regulation supervises and regulates all areas of CCB’s operations including, without limitation, the making of loans, the issuance of securities, the conduct of CCB’s corporate affairs, the satisfaction of capital adequacy requirements, the payment of dividends, and the establishment or closing of banking centers. CCB is also a member bank of the Federal Reserve System, which makes CCB’s operations subject to broad federal regulation and oversight by the Federal Reserve. In addition, CCB’s deposit accounts are insured by the FDIC to the maximum extent permitted by law, and the FDIC has certain enforcement powers over CCB.

As a state-chartered banking institution in the State of Florida, CCB is empowered by statute, subject to the limitations contained in those statutes, to take and pay interest on, savings and time deposits, to accept demand deposits, to make loans on residential and other real estate, to make consumer and commercial loans, to invest, with certain limitations, in equity securities and in debt obligations of banks and corporations and to provide various other banking services for

the benefit of CCB's clients. Various consumer laws and regulations also affect the operations of CCB, including state usury laws, laws relating to fiduciaries, consumer credit and equal credit opportunity laws, and fair credit reporting. In addition, the Federal Deposit Insurance Corporation Improvement Act of 1991 ("FDICIA") prohibits insured state chartered institutions from conducting activities as principal that are not permitted for national banks. A bank, however, may engage in an otherwise prohibited activity if it meets its minimum capital requirements and the FDIC determines that the activity does not present a significant risk to the Deposit Insurance Fund.

***Reserves***

The Federal Reserve requires all depository institutions to maintain reserves against some transaction accounts (primarily NOW and Super NOW checking accounts). The balances maintained to meet the reserve requirements imposed by the Federal Reserve may be used to satisfy liquidity requirements. An institution may borrow from the Federal Reserve Bank "discount window" as a secondary source of funds, provided that the institution meets the Federal Reserve Bank's credit standards.

### ***Dividends***

CCB is subject to legal limitations on the frequency and amount of dividends that can be paid to us. The Federal Reserve may restrict the ability of CCB to pay dividends if such payments would constitute an unsafe or unsound banking practice.

In addition, Florida law and Federal regulation also places restrictions on the declaration of dividends from state chartered banks to their holding companies. Pursuant to the Florida Financial Institutions Code, the board of directors of state-chartered banks, after charging off bad debts, depreciation and other worthless assets, if any, and making provisions for reasonably anticipated future losses on loans and other assets, may quarterly, semi-annually or annually declare a dividend of up to the aggregate net profits of that period combined with the bank's retained net profits for the preceding two years and, with the approval of the Florida Office of Financial Regulation and Federal Reserve, declare a dividend from retained net profits which accrued prior to the preceding two years. Before declaring such dividends, 20% of the net profits for the preceding period as is covered by the dividend must be transferred to the surplus fund of the bank until this fund becomes equal to the amount of the bank's common stock then issued and outstanding. A state-chartered bank may not declare any dividend if (i) its net income (loss) from the current year combined with the retained net income (loss) for the preceding two years aggregates a loss or (ii) the payment of such dividend would cause the capital account of the bank to fall below the minimum amount required by law, regulation, order or any written agreement with the Florida Office of Financial Regulation or a federal regulatory agency.

### ***Insurance of Accounts and Other Assessments***

CCB pays its deposit insurance assessments to the Deposit Insurance Fund, which is determined through a risk-based assessment system. Our deposit accounts are currently insured by the Deposit Insurance Fund generally up to a maximum of \$250,000 per separately insured depositor.

Under the current assessment system, the FDIC assigns an institution to one of four categories designed to measure risk, with the first category having two sub-categories based on the institution's most recent supervisory and capital evaluations. Total base assessment rates currently range from 0.025% of deposits for an institution in the highest sub-category of the highest category to 0.45% of deposits for an institution in the lowest category.

In addition, all FDIC insured institutions are required to pay assessments to the FDIC at an annual rate of approximately six tenths of a basis point of insured deposits to fund interest payments on bonds issued by the Financing Corporation, an agency of the federal government established to recapitalize the predecessor to the Savings Association Insurance Fund. These assessments will continue until the Financing Corporation bonds mature in 2017 through 2019.

Under the Federal Deposit Insurance Act, or FDIA, the FDIC may terminate deposit insurance upon a finding that the institution has engaged in unsafe and unsound practices, is in an unsafe or unsound condition to continue operations, or has violated any applicable law, regulation, rule, order or condition imposed by the FDIC.

### ***Transactions With Affiliates***

Pursuant to Sections 23A and 23B of the Federal Reserve Act and Regulation W, the authority of CCB to engage in transactions with related parties or "affiliates" or to make loans to insiders is limited. Loan transactions with an "affiliate" generally must be collateralized and certain transactions between CCB and its "affiliates", including the sale of assets, the payment of money or the provision of services, must be on terms and conditions that are substantially the same, or at least as favorable to CCB, as those prevailing for comparable nonaffiliated transactions. In addition, CCB generally

may not purchase securities issued or underwritten by affiliates.

Loans to executive officers, directors or to any person who directly or indirectly, or acting through or in concert with one or more persons, owns, controls or has the power to vote more than 10% of any class of voting securities of a bank, which we refer to as “10% Shareowners”, or to any political or campaign committee the funds or services of which will benefit those executive officers, directors, or 10% Shareowners or which is controlled by those executive officers, directors or 10% Shareowners, are subject to Sections 22(g) and 22(h) of the Federal Reserve Act and their corresponding regulations (Regulation O) and Section 13(k) of the Exchange Act relating to the prohibition on personal loans to executives (which exempts financial institutions in compliance with the insider lending restrictions of Section 22(h) of the Federal Reserve Act). Among other things, these loans must be made on terms substantially the same as those prevailing on transactions made to unaffiliated individuals and certain extensions of credit to those persons must first be approved in advance by a disinterested majority of the entire board of directors. Section 22(h) of the Federal Reserve Act prohibits loans to any of those individuals where the aggregate amount exceeds an amount equal to 15% of an institution’s unimpaired capital and surplus plus an additional 10% of unimpaired capital and surplus in the case of loans that are fully secured by readily marketable collateral, or when the aggregate amount on all of the extensions of credit outstanding to all of these persons would exceed CCB’s unimpaired capital and unimpaired surplus. Section 22(g) identifies limited circumstances in which CCB is permitted to extend credit to executive officers.

### ***Community Reinvestment Act***

The Community Reinvestment Act and its corresponding regulations are intended to encourage banks to help meet the credit needs of their service area, including low and moderate income neighborhoods, consistent with the safe and sound operations of the banks. These regulations provide for regulatory assessment of a bank's record in meeting the credit needs of its service area. Federal banking agencies are required to make public a rating of a bank's performance under the Community Reinvestment Act. The Federal Reserve considers a bank's Community Reinvestment Act rating when the bank submits an application to establish bank branches, merge, or acquire the assets and assume the liabilities of another bank. In the case of a financial holding company, the Community Reinvestment Act performance record of all banks involved in the merger or acquisition are reviewed in connection with the filing of an application to acquire ownership or control of shares or assets of a bank or to merge with any other bank or financial holding company. An unsatisfactory record can substantially delay or block the transaction. CCB received a satisfactory rating on its most recent Community Reinvestment Act assessment.

### ***Capital Regulations***

The federal banking regulators have adopted risk-based, capital adequacy guidelines for financial holding companies and their subsidiary state-chartered banks. The risk-based capital guidelines are designed to make regulatory capital requirements more sensitive to differences in risk profiles among banks and financial holding companies, to account for off-balance sheet exposure, to minimize disincentives for holding liquid assets and to achieve greater consistency in evaluating the capital adequacy of major banks throughout the world. Under these guidelines, assets and off-balance sheet items are assigned to broad risk categories each with designated weights. The resulting capital ratios represent capital as a percentage of total risk-weighted assets and off-balance sheet items.

The federal banking regulators adopted risk-based capital adequacy guidelines for U.S. banks. As described above, the federal banking regulators have adopted final rules that became effective January 1, 2015 for community banks. These final rules represent major changes to the current general risk-based capital rule, and are designed to substantially conform to the Basel III international standards. The risk-based capital guidelines are designed to make regulatory capital requirements more sensitive to differences in risk profiles among banks and bank holding companies, to account for off-balance sheet exposure, to minimize disincentives for holding liquid assets, and to achieve greater consistency in evaluating the capital adequacy of major banks throughout the world. Under these guidelines, assets and off-balance sheet items are assigned to broad risk categories each with designated weights. The resulting capital ratios represent capital as a percentage of total risk-weighted assets and off-balance sheet items.

Under the final rule, minimum requirements increased for both the quality and quantity of capital held by banking organizations. In this respect, the final rule implements strict eligibility criteria for regulatory capital instruments and improves the methodology for calculating risk-weighted assets to enhance risk sensitivity. Consistent with the international Basel framework, the rule includes a new minimum ratio of Common Equity Tier I Capital to Risk-Weighted Assets of 4.5% and a Common Equity Tier I Capital conservation buffer of 2.5% of risk-weighted assets. The conservation buffer will be phased in beginning on January 1, 2016 through 2019. The rule also, among other things, raises the minimum ratio of Tier I Capital to Risk-Weighted Assets from 4% to 6% and includes a minimum leverage ratio of 4% for all banking organizations.

In computing total risk-weighted assets, bank and bank holding company assets are given risk-weights of 0%, 20%, 50% and 100%. In addition, certain off-balance sheet items are given similar credit conversion factors to convert them to asset equivalent amounts to which an appropriate risk-weight will apply. Most loans will be assigned to the 100% risk category, except for performing first mortgage loans fully secured by 1- to 4-family and certain multi-family residential property, which carry a 50% risk rating. Most investment securities (including, primarily, general



obligation claims on states or other political subdivisions of the United States) will be assigned to the 20% category, except for municipal or state revenue bonds, which have a 50% risk-weight, and direct obligations of the U.S. Treasury or obligations backed by the full faith and credit of the U.S. Government, which have a 0% risk-weight. In covering off-balance sheet items, direct credit substitutes, including general guarantees and standby letters of credit backing financial obligations, are given a 100% conversion factor. Transaction-related contingencies such as bid bonds, standby letters of credit backing nonfinancial obligations, and undrawn commitments (including commercial credit lines with an initial maturity of more than one year) have a 50% conversion factor. Short-term commercial letters of credit are converted at 20% and certain short-term unconditionally cancelable commitments have a 0% factor.

The new capital regulations may also impact the treatment of accumulated comprehensive income (“AOCI”) for regulatory capital purposes. Under the new rules, AOCI would generally flow through to regulatory capital, however, community banks and their holding companies may make a one-time irrevocable opt-out election to continue to treat ACOI the same as under the old regulations for regulatory capital purposes. This election must be made on the first call report or bank holding company annual report (on form FR Y-9C) filed after January 1, 2015. Additionally, the new rules also permit community banks with less than \$15 billion in total assets to continue to count certain non-qualifying capital instruments issued prior to May 19, 2010, including trust preferred securities and cumulative perpetual preferred stock, as Tier I capital (subject to a limit of 25% of Tier I capital). However, non-qualifying capital instruments issued on or after May 19, 2010 will not qualify for Tier I capital treatment.

Federal law and regulations establish a capital-based regulatory scheme designed to promote early intervention for troubled banks and require the FDIC to choose the least expensive resolution of bank failures. The capital-based regulatory framework contains five categories of compliance with regulatory capital requirements, including “well capitalized,” “adequately capitalized,” “undercapitalized,” “significantly undercapitalized,” and “critically undercapitalized.” To qualify as a “well-capitalized” institution under the new rules in effect as of January 1, 2015, a bank must have a leverage ratio of not less than 5%, a Tier I Common Equity ratio of not less than 6.5%, a Tier I Capital ratio of not less than 8%, and a total risk-based capital ratio of not less than 10%, and the bank must not be under any order or directive from the appropriate regulatory agency to meet and maintain a specific capital level. To qualify as a “well-capitalized” institution under the rules in effect prior to January 1, 2015, a bank must have had a leverage ratio of not less than 5%, a Tier I Capital ratio of not less than 6%, and a total risk-based capital ratio of not less than 10%, and the bank must not have been under any order or directive from the appropriate regulatory agency that required the bank to meet and maintain a specific capital level.

Under the regulations, the applicable agency can treat an institution as if it were in the next lower category if the agency determines (after notice and an opportunity for hearing) that the institution is in an unsafe or unsound condition or is engaging in an unsafe or unsound practice. The degree of regulatory scrutiny of a financial institution will increase, and the permissible activities of the institution will decrease, as it moves downward through the capital categories. Institutions that fall into one of the three undercapitalized categories may be required to (i) submit a capital restoration plan; (ii) raise additional capital; (iii) restrict their growth, deposit interest rates, and other activities; (iv) improve their management; (v) eliminate management fees; or (vi) divest themselves of all or a part of their operations. It should be noted that the minimum ratios referred to above are merely guidelines and the bank regulators possess the discretionary authority to require higher capital ratios.

As of December 31, 2014, we exceeded the requirements contained in the applicable regulations, policies and directives pertaining to capital adequacy to be classified as “well capitalized” under both the prior capital adequacy rules and those now in effect for community banks as of January 1, 2015, and are unaware of any material violation or alleged violation of these regulations, policies or directives (see table below). Rapid growth, poor loan portfolio performance, or poor earnings performance, or a combination of these factors, could change our capital position in a relatively short period of time, making additional capital infusions necessary.

	Actual		Required For Capital Adequacy Purposes <sup>(1)</sup>		To Be Well-Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
(Dollars in thousands)						
As of December 31, 2014:						
Tier I Capital:						
CCBG	\$269,503	16.67 %	\$64,656	4.00 %	*	*
CCB	261,655	16.24 %	64,458	4.00 %	96,687	6.00 %
Total Capital:						
CCBG	287,042	17.76 %	129,313	8.00 %	*	*
CCB	279,194	17.33 %	128,916	8.00 %	161,145	10.00 %
Tier I Leverage:						
CCBG	269,503	10.99 %	98,090	4.00 %	*	*
CCB	261,655	10.70 %	97,834	4.00 %	122,293	5.00 %

<sup>(1)</sup> Based on the capital adequacy guidelines in effect prior to January 1, 2015.

***Prompt Corrective Action***

Immediately upon becoming undercapitalized, a depository institution becomes subject to the provisions of Section 38 of the Federal Deposit Insurance Act, which: (i) restrict payment of capital distributions and management fees; (ii) require that the appropriate federal banking agency monitor the condition of the institution and its efforts to restore its capital; (iii) require submission of a capital restoration plan; (iv) restrict the growth of the institution's assets; and (v) require prior approval of certain expansion proposals. The appropriate federal banking agency for an undercapitalized institution also may take any number of discretionary supervisory actions if the agency determines that any of these actions is necessary to resolve the problems of the institution at the least possible long-term cost to the deposit insurance fund, subject in certain cases to specified procedures. These discretionary supervisory actions include: (i) requiring the institution to raise additional capital; (ii) restricting transactions with affiliates; (iii) requiring divestiture of the institution or the sale of the institution to a willing purchaser; and (iv) any other supervisory action that the agency deems appropriate. These and additional mandatory and permissive supervisory actions may be taken with respect to significantly undercapitalized and critically undercapitalized institutions.

### ***Interstate Banking and Branching***

The Bank Holding Company Act, amended by the Interstate Banking Act, provides that adequately capitalized and managed financial and bank holding companies are permitted to acquire banks in any state.

State laws prohibiting interstate banking or discriminating against out-of-state banks are preempted. States are not permitted to enact laws opting out of this provision; however, states are allowed to adopt a minimum age restriction requiring that target banks located within the state be in existence for a period of time, up to a maximum of five years, before a bank may be subject to the Interstate Banking Act. Also, the Dodd-Frank Act, added deposit caps which prohibit acquisitions that result in the acquiring company controlling 30% or more of the deposits of insured banks and thrift institutions held in the state in which the target maintains a branch or 10% or more of the deposits nationwide. States have the authority to waive the 30% deposit cap. State-level deposit caps are not preempted as long as they do not discriminate against out-of-state companies, and the federal deposit caps apply only to initial entry acquisitions.

Under the Dodd-Frank Act, national banks and state banks are able to establish branches in any state if that state would permit the establishment of the branch by a state bank chartered in that state. Florida law permits a state bank to establish a branch of the bank anywhere in Florida. Accordingly, under the Dodd-Frank Act, a bank with its headquarters outside the State of Florida may establish branches anywhere within Florida.

### ***Anti-money Laundering***

The Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001 (“USA PATRIOT Act”), provides the federal government with additional powers to address terrorist threats through enhanced domestic security measures, expanded surveillance powers, increased information sharing and broadened anti-money laundering requirements. By way of amendments to the Bank Secrecy Act (“BSA”), the USA PATRIOT Act puts in place measures intended to encourage information sharing among bank regulatory and law enforcement agencies. In addition, certain provisions of the USA PATRIOT Act impose affirmative obligations on a broad range of financial institutions.

Among other requirements, the USA PATRIOT Act and the related Federal Reserve regulations require banks to establish anti-money laundering programs that include, at a minimum:

- internal policies, procedures and controls designed to implement and maintain the savings association’s compliance with all of the requirements of the USA PATRIOT Act, the BSA and related laws and regulations;
- systems and procedures for monitoring and reporting of suspicious transactions and activities;
- a designated compliance officer;
- employee training;
- an independent audit function to test the anti-money laundering program;
- procedures to verify the identity of each clients upon the opening of accounts; and
- heightened due diligence policies, procedures and controls applicable to certain foreign accounts and relationships.

Additionally, the USA PATRIOT Act requires each financial institution to develop a customer identification program (“CIP”) as part of our anti-money laundering program. The key components of the CIP are identification, verification, government list comparison, notice and record retention. The purpose of the CIP is to enable the financial institution to determine the true identity and anticipated account activity of each customer. To make this determination, among other things, the financial institution must collect certain information from customers at the time they enter into the customer relationship with the financial institution. This information must be verified within a reasonable time through documentary and non-documentary methods. Furthermore, all customers must be screened against any

CIP-related government lists of known or suspected terrorists. We and our affiliates have adopted policies, procedures and controls designed to comply with the BSA and the USA PATRIOT Act.

***Regulatory Enforcement Authority***

Federal and state banking laws grant substantial enforcement powers to federal and state banking regulators. This enforcement authority includes, among other things, the ability to assess civil money penalties, to issue cease and desist or removal orders and to initiate injunctive actions against banking organizations and institution-affiliated parties. In general, these enforcement actions may be initiated for violations of laws and regulations and unsafe or unsound practices. Other actions or inactions may provide the basis for enforcement action, including misleading or untimely reports filed with regulatory authorities.

### ***Federal Home Loan Bank System***

CCB is a member of the Federal Home Loan Bank (“FHLB”) of Atlanta, which is one of 12 regional Federal Home Loan Banks. Each FHLB serves as a reserve or central bank for its members within its assigned region. It is funded primarily from funds deposited by member institutions and proceeds from the sale of consolidated obligations of the FHLB system. It makes loans to members (i.e. advances) in accordance with policies and procedures established by the board of trustees of the FHLB.

As a member of the FHLB of Atlanta, CCB is required to own capital stock in the FHLB in an amount at least equal to 0.09% (or 9 basis points), which is subject to annual adjustments, of the CCB’s total assets at the end of each calendar year (with a dollar cap of \$15 million), plus 4.5% of its outstanding advances (borrowings) from the FHLB of Atlanta under the activity-based stock ownership requirement. As of December 31, 2014, CCB was in compliance with this requirement.

### ***Privacy***

Under the Gramm-Leach-Bliley Act, federal banking regulators adopted rules limiting the ability of banks and other financial institutions to disclose nonpublic information about consumers to nonaffiliated third parties. The rules require disclosure of privacy policies to consumers and, in some circumstances, allow consumers to prevent disclosure of certain personal information to nonaffiliated third parties.

### ***Overdraft Fee Regulation***

The Electronic Fund Transfer Act prohibits financial institutions from charging consumers fees for paying overdrafts on automated teller machines (“ATM”) and one-time debit card transactions, unless a consumer consents, or opts in, to the overdraft service for those type of transactions. If a consumer does not opt in, any ATM transaction or debit that overdraws the consumer’s account will be denied. Overdrafts on the payment of checks and regular electronic bill payments are not covered by this rule. Before opting in, the consumer must be provided a notice that explains the financial institution’s overdraft services, including the fees associated with the service, and the consumer’s choices. Financial institutions must provide consumers who do not opt in with the same account terms, conditions and features (including pricing) that they provide to consumers who do opt in.

### ***Consumer Laws and Regulations***

CCB is also subject to other federal and state consumer laws and regulations that are designed to protect consumers in transactions with banks. While the list set forth below is not exhaustive, these laws and regulations include the Truth in Lending Act, the Truth in Savings Act, the Electronic Funds Transfer Act, the Expedited Funds Availability Act, the Check Clearing for the 21st Century Act, the Fair Credit Reporting Act, the Equal Credit Opportunity Act, the Fair Housing Act, the Home Mortgage Disclosure Act, the Fair and Accurate Credit Transactions Act, the Mortgage Disclosure Improvement Act, and the Real Estate Settlement Procedures Act, among others. These laws and regulations mandate certain disclosure requirements and regulate the manner in which financial institutions must deal with customers when taking deposits or making loans to such customers. CCB must comply with the applicable provisions of these consumer protection laws and regulations as part of its ongoing customer relations.

### ***The Volcker Rule***

Section 619 of the Dodd-Frank Act, commonly known as the Volcker Rule, prohibits us from owning, sponsoring, or having certain relationships with any hedge funds or private equity funds, subject to certain exemptions. The Volcker Rule directed the federal banking, securities and commodities and futures regulatory agencies to undertake a coordinated rulemaking effort to create rules implementing the Volcker Rule. The final interagency rules

implementing the Volcker Rule, which were issued in December 2013 and became effective on April 1, 2014, afford financial institutions a two-year conformance period during which they can wind-down, sell, or otherwise conform their respective activities, investments and relationships to the requirements of the Volcker Rule and its implementing regulations. We do not believe that the Volcker Rule or the final interagency rules implementing the Volcker Rule will have a material impact on our investment activities since we do not engage in transactions covered by the regulation.

### **Future Legislative Developments**

Various legislative acts are from time to time introduced in Congress and the Florida legislature. This legislation may change banking statutes and the environment in which our banking subsidiary and we operate in substantial and unpredictable ways. We cannot determine the ultimate effect that potential legislation, if enacted, or implementing regulations with respect thereto, would have upon our financial condition or results of operations or that of our banking subsidiary.

### **Effect of Governmental Monetary Policies**

The commercial banking business in which CCB engages is affected not only by general economic conditions, but also by the monetary policies of the Federal Reserve. Changes in the discount rate on member bank borrowing, availability of borrowing at the “discount window,” open market operations, the imposition of changes in reserve requirements against member banks’ deposits and assets of foreign banking centers and the imposition of and changes in reserve requirements against certain borrowings by banks and their affiliates are some of the instruments of monetary policy available to the Federal Reserve. These monetary policies are used in varying combinations to influence overall growth and distributions of bank loans, investments and deposits, and this use may affect interest rates charged on loans or paid on deposits. The monetary policies of the Federal Reserve have had a significant effect on the operating results of commercial banks and are expected to continue to do so in the future. The monetary policies of the Federal Reserve are influenced by various factors, including inflation, unemployment, and short-term and long-term changes in the international trade balance and in the fiscal policies of the U.S. Government. Future monetary policies and the effect of such policies on the future business and earnings of CCB cannot be predicted.

### **Income Taxes**

We are subject to income taxes at the federal level and subject to state taxation based on the laws of each state in which we operate. We file a consolidated federal tax return with a fiscal year ending on December 31.

### **Website Access to Company’s Reports**

Our Internet website is [www.ccbg.com](http://www.ccbg.com). Our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, including any amendments to those reports filed or furnished pursuant to section 13(a) or 15(d), and reports filed pursuant to Section 16, 13(d), and 13(g) of the Exchange Act are available free of charge through our website as soon as reasonably practicable after they are electronically filed with, or furnished to, the Securities and Exchange Commission. The information on our website is not incorporated by reference into this report.



## ***Item 1A. Risk Factors***

*An investment in our common stock contains a high degree of risk. You should consider carefully the following risk factors before deciding whether to invest in our common stock. Our business, including our operating results and financial condition, could be harmed by any of these risks. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially and adversely affect our business. The trading price of our common stock could decline due to any of these risks, and you may lose all or part of your investment. In assessing these risks, you should also refer to the other information contained in our filings with the SEC, including our financial statements and related notes.*

### **Risks Related to Our Business**

#### **We may incur losses if we are unable to successfully manage interest rate risk.**

Our profitability depends to a large extent on Capital City Bank's net interest income, which is the difference between income on interest-earning assets, such as loans and investment securities, and expense on interest-bearing liabilities such as deposits and borrowings. We are unable to predict changes in market interest rates, which are affected by many factors beyond our control, including inflation, recession, unemployment, federal funds target rate, money supply, domestic and international events and changes in the United States and other financial markets. Our net interest income may be reduced if: (i) more interest-earning assets than interest-bearing liabilities reprice or mature during a time when interest rates are declining or (ii) more interest-bearing liabilities than interest-earning assets reprice or mature during a time when interest rates are rising.

Changes in the difference between short- and long-term interest rates may also harm our business. For example, short-term deposits may be used to fund longer-term loans. When differences between short-term and long-term interest rates shrink or disappear, as is likely to continue in the current zero-interest-rate-policy environment, the spread between rates paid on deposits and received on loans could narrow significantly, decreasing our net interest income.

If market interest rates rise rapidly, interest rate adjustment caps may limit increases in the interest rates on adjustable rate loans, thereby reducing our net interest income.

#### **Our loan portfolio includes loans with a higher risk of loss which could lead to higher loan losses and nonperforming assets.**

We originate commercial real estate loans, commercial loans, construction loans, vacant land loans, consumer loans, and residential mortgage loans primarily within our market area. Commercial real estate, commercial, construction, vacant land, and consumer loans may expose a lender to greater credit risk than traditional fixed rate fully amortizing loans secured by single-family residential real estate because the collateral securing these loans may not be sold as easily as single-family residential real estate. In addition, these loan types tend to involve larger loan balances to a single borrower or groups of related borrowers and are more susceptible to a risk of loss during a downturn in the business cycle. These loans also have historically had greater credit risk than other loans for the following reasons:

**Commercial Real Estate Loans.** Repayment is dependent on income being generated in amounts sufficient to cover operating expenses and debt service. These loans also involve greater risk because they are generally not fully amortizing over the loan period, but rather have a balloon payment due at maturity. A borrower's ability to make a balloon payment typically will depend on the borrower's ability to either refinance the loan or timely sell the underlying property. As of December 31, 2014, commercial mortgage loans comprised approximately 35.4% of our total loan portfolio.

**Commercial Loans.** Repayment is generally dependent upon the successful operation of the borrower's business. In addition, the collateral securing the loans may depreciate over time, be difficult to appraise, be illiquid, or fluctuate in value based on the success of the business. As of December 31, 2014, commercial loans comprised approximately 9.5% of our total loan portfolio.

**Construction Loans.** The risk of loss is largely dependent on our initial estimate of whether the property's value at completion equals or exceeds the cost of property construction and the availability of take-out financing. During the construction phase, a number of factors can result in delays or cost overruns. If our estimate is inaccurate or if actual construction costs exceed estimates, the value of the property securing our loan may be insufficient to ensure full repayment when completed through a permanent loan, sale of the property, or by seizure of collateral. As of December 31, 2014, construction loans comprised approximately 3.0% of our total loan portfolio.

**Vacant Land Loans.** Because vacant or unimproved land is generally held by the borrower for investment purposes or future use, payments on loans secured by vacant or unimproved land will typically rank lower in priority to the borrower than a loan the borrower may have on their primary residence or business. These loans are susceptible to adverse conditions in the real estate market and local economy. As of December 31, 2014, vacant land loans comprised approximately 4.6% of our total loan portfolio.

**HELOCS.** Our open-ended home equity loans have an interest-only draw period followed by a five year repayment period of 0.75% of the principal balance monthly and a balloon payment at maturity. Upon the commencement of the repayment period, the monthly payment can increase significantly, thus, there is a heightened risk that the borrower will be unable to pay the increased payment. Further, these loans also involve greater risk because they are generally not fully amortizing over the loan period, but rather have a balloon payment due at maturity. A borrower's ability to make a balloon payment may depend on the borrower's ability to either refinance the loan or timely sell the underlying property. As of December 31, 2014, HELOCs comprised approximately 15.9% of our total loan portfolio.

**Consumer Loans.** Consumer loans (such as personal lines of credit) are collateralized, if at all, with assets that may not provide an adequate source of payment of the loan due to depreciation, damage, or loss. As of December 31, 2014, consumer loans comprised approximately 15.1% of our total loan portfolio.

The increased risks associated with these types of loans result in a correspondingly higher probability of default on such loans (as compared to fixed rated fully amortizing single-family real estate loans). Loan defaults would likely increase our loan losses and nonperforming assets and could adversely affect our allowance for loan losses.

**We process, maintain, and transmit confidential client information through our information technology systems, such as our online banking service. Cybersecurity issues, such as security breaches and computer viruses, affecting our information technology systems or fraud related to our credit or debit card products could disrupt our business, result in the unintended disclosure or misuse of confidential or proprietary information, damage our reputation, increase our costs, and cause losses.**

We collect and store sensitive data, including our proprietary business information and that of our clients, and personally identifiable information of our clients and employees, in our information technology systems. We also provide our clients the ability to bank online. The secure processing, maintenance, and transmission of this information is critical to our operations. Our network, or those of our clients, could be vulnerable to unauthorized access, computer viruses, phishing schemes and other security problems. Financial institutions and companies engaged in data processing have increasingly reported breaches in the security of their websites or other systems, some of which have involved sophisticated and targeted attacks intended to obtain unauthorized access to confidential information, destroy data, disrupt or degrade service, sabotage systems or cause other damage.

We may be required to spend significant capital and other resources to protect against the threat of security breaches and computer viruses, or to alleviate problems caused by security breaches or viruses. Security breaches and viruses could expose us to claims, litigation and other possible liabilities. Any inability to prevent security breaches or computer viruses could also cause existing clients to lose confidence in our systems and could adversely affect our reputation and our ability to generate deposits.

Additionally, fraud losses related to credit and debit cards have risen in recent years due in large part to growing and evolving schemes to illegally use cards or steal consumer credit card information despite risk management practices employed by the credit and debit card industry. Many issuers of debit and credit cards have suffered significant losses in recent years due to the theft of cardholder data that has been illegally exploited for personal gain.

The potential for credit and debit card fraud against us or our clients and our third party service providers is a serious issue. Credit card fraud is pervasive and the risks of cybercrime are complex and continue to evolve. In view of the recent high-profile retail data breaches involving client personal and financial information, the potential impact on us and any exposure to consumer losses and the cost of technology investments to improve security could cause losses to us or our clients, damage to our brand, and an increase in our costs.

**An inadequate allowance for loan losses would reduce our earnings.**

We are exposed to the risk that our clients will be unable to repay their loans according to their terms and that any collateral securing the payment of their loans will not be sufficient to assure full repayment. This could result in credit losses that are inherent in the lending business. We evaluate the collectability of our loan portfolio and provide an allowance for loan losses that we believe is adequate based upon such factors as:

- the risk characteristics of various classifications of loans;
- previous loan loss experience;
- specific loans that have loss potential;
- delinquency trends;
- estimated fair market value of the collateral;
- current economic conditions; and
- geographic and industry loan concentrations.

As of December 31, 2014, the Bank's allowance for loan losses was \$17.5 million, which represented approximately 1.22% of its total amount of loans. The Bank had \$16.8 million in nonaccruing loans as of December 31, 2014. The allowance is based on management's reasonable estimate and may not prove sufficient to cover future loan losses. Although management uses the best information available to make determinations with respect to the allowance for loan losses, future adjustments may be necessary if economic conditions differ substantially from the assumptions used or adverse developments arise with respect to the Bank's nonperforming or performing loans. In addition, regulatory agencies, as an integral part of their examination process, periodically review the estimated losses on loans. Such agencies may require us to recognize additional losses based on their judgments about information available to them at the time of their examination. Accordingly, the allowance for loan losses may not be adequate to cover loan losses or significant increases to the allowance may be required in the future if economic conditions should worsen. Material additions to the Bank's allowance for loan losses would adversely impact our net income and capital in future periods, while having the effect of overstating our current period earnings.

**Since we engage in lending secured by real estate and may be forced to foreclose on the collateral property and own the underlying real estate, we may be subject to the increased costs associated with the ownership of real property, which could result in reduced net income.**

Since we originate loans secured by real estate, we may have to foreclose on the collateral property to protect our investment and may thereafter own and operate such property, in which case we are exposed to the risks inherent in the ownership of real estate.

The amount that we, as a mortgagee, may realize after a default is dependent upon factors outside of our control, including, but not limited to:

- general or local economic conditions;
- environmental cleanup liability;
- neighborhood values;
- interest rates;
- real estate tax rates;
- operating expenses of the mortgaged properties;
- supply of and demand for rental units or properties;
- ability to obtain and maintain adequate occupancy of the properties;
- zoning laws;
- governmental rules, regulations and fiscal policies; and
- acts of God.

Certain expenditures associated with the ownership of real estate, principally real estate taxes and maintenance costs, may adversely affect the income from the real estate. Therefore, the cost of operating real property may exceed the rental income earned from such property, and we may have to advance funds in order to protect our investment or we may be required to dispose of the real property at a loss.

**Liquidity risk could impair our ability to fund operations and jeopardize our financial condition.**

Liquidity is essential to our business. An inability to raise funds through deposits, borrowings, and other sources, could have a substantial negative effect on our liquidity. Our access to funding sources in amounts adequate to finance our activities on terms that are acceptable to us could be impaired by factors that affect us specifically or the financial services industry or economy in general. Factors that could negatively impact our access to liquidity sources include a decrease in the level of our business activity as a result of a downturn in the markets in which our loans are concentrated, adverse regulatory action against us, or our inability to attract and retain deposits. Our ability to borrow could be impaired by factors that are not specific to us, such a disruption in the financial markets or negative views and expectations about the prospects for the financial services industry.

**Our future success is dependent on our ability to compete effectively in the highly competitive banking industry.**

We face vigorous competition from other banks and other financial institutions, including savings and loan associations, savings banks, finance companies and credit unions for deposits, loans and other financial services in our market area. A number of these banks and other financial institutions are significantly larger than we are and have substantially greater access to capital and other resources, as well as larger lending limits and branch systems, and offer a wider array of banking services. To a limited extent, we also compete with other providers of financial services, such as money market mutual funds, brokerage firms, consumer finance companies, insurance companies and governmental organizations which may offer more favorable financing than we can. Many of our non-bank competitors are not subject to the same extensive regulations that govern our activities. As a result, these non-bank competitors have advantages over us in providing certain services. This competition may reduce or limit our margins

and our market share and may adversely affect our results of operations and financial condition.

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### **Risks Related to Regulation and Legislation**

**We are subject to extensive regulation, including an unprecedented increase in new regulation, which could restrict our activities and impose financial requirements or limitations on the conduct of our business.**

Both CCBG and the Bank are subject to extensive regulation, supervision and examination by our regulators, including the Florida Office of Financial Regulation, the Federal Reserve, and the FDIC. Our compliance with these industry regulations is costly and restricts certain of our activities, including payment of dividends, mergers and acquisitions, investments, loans and interest rates charged, interest rates paid on deposits, access to capital and brokered deposits and locations of banking offices. If we are unable to meet these regulatory requirements, our financial condition, liquidity and results of operations would be materially and adversely affected.

We are experiencing an unprecedented increase in regulations and supervision. Significant new legislation and regulations affecting the financial services industry have been adopted or proposed in recent years, such as the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, or the Dodd-Frank Act, into law. Congress and our regulators continue to develop, propose and adopt rules and propose new regulatory initiatives, so the cumulative effect of all of the new legislation and regulations on our business and operations remains uncertain.

We must also meet regulatory capital requirements imposed by our regulators. An inability to meet these capital requirements would result in numerous mandatory supervisory actions and additional regulatory restrictions, and could have a negative impact on our financial condition, liquidity and results of operations.

In addition to the regulations of the Florida Office of Financial Regulation, the Federal Reserve, and the FDIC, as a member of the Federal Home Loan Bank, the Bank must also comply with applicable regulations of the Federal Housing Finance Agency and the Federal Home Loan Bank.

The Bank's activities are also regulated under consumer protection laws applicable to our lending, deposit and other activities. Many of these regulations are intended primarily for the protection of our depositors and the Deposit Insurance Fund and not for the benefit of our shareowners. Our failure to comply with these laws and regulations, even if the failure follows good faith effort or reflects a difference in interpretation, could subject us to restrictions on our business activities, fines and other penalties, any of which could adversely affect our results of operations, capital base and the price of our securities. Further, any new laws, rules and regulations could make compliance more difficult or expensive or otherwise adversely affect our business and financial condition. Please refer to the Section entitled "Business – Regulatory Considerations" in this Report.

**The new Basel III Capital Standards may have an adverse effect on us.**

In 2013, the Federal Reserve Board released its final rules which implement in the United States the Basel III regulatory capital reforms from the Basel Committee on Banking Supervision and certain changes required by the Dodd-Frank Act. Under the final rule, minimum requirements increased for both the quality and quantity of capital held by banking organizations. Consistent with the international Basel framework, the rule includes a new minimum ratio of Common Equity Tier I Capital to Risk-Weighted Assets of 4.5% and a Common Equity Tier I Capital conservation buffer of 2.5% of risk-weighted assets that apply to all supervised financial institutions. The rule also, among other things, raised the minimum ratio of Tier I Capital to Risk-Weighted Assets from 4% to 6% and included a minimum leverage ratio of 4% for all banking organizations. We became subject to the new rules effective January 1, 2015. The impact of the new capital rules requires us to maintain higher levels of capital, which we expect will lower our return on equity.

**Compliance with the Consumer Financial Protection Bureau's ability-to-repay rule safe-harbor could adversely impact our growth or profitability.**

The Consumer Financial Protection Bureau issued a rule, effective as of January 14, 2014, designed to clarify for lenders how they can avoid monetary damages under the Dodd-Frank Act, which holds lenders accountable for ensuring a borrower's ability to repay a mortgage. Loans that satisfy the "qualified mortgage" safe-harbor will be presumed to have complied with the new ability-to-repay standard. Under the Consumer Financial Protection Bureau's rule, a "qualified mortgage" loan must not contain certain specified features, including but not limited to:

- excessive upfront points and fees (those exceeding 3% of the total loan amount, less "bona fide discount points" for prime loans);
- interest-only payments;
- negative-amortization; and
- terms longer than 30 years.

Also, to qualify as a "qualified mortgage," a borrower's total monthly debt-to-income ratio may not exceed 43%. Lenders must also verify and document the income and financial resources relied upon to qualify the borrower for the loan and underwrite the loan based on a fully amortizing payment schedule and maximum interest rate during the first five years, taking into account all applicable taxes, insurance and assessments. The Consumer Financial Protection Bureau's rule on qualified mortgages could limit our ability or desire to make certain types of loans or loans to certain borrowers, or could make it more expensive and/or time consuming to make these loans, which could adversely impact our growth or profitability.



**The Federal Reserve’s repeal of the prohibition against payment of interest on demand deposits (Regulation Q) may increase competition for such deposits and ultimately increase interest expense.**

A major portion of our net income comes from our interest rate spread, which is the difference between the interest rates we pay on amounts used to fund assets, such as deposits, and the interest rates and fees we receive on our interest-earning assets. Our interest-earning assets include outstanding loans extended to our clients and securities held in our investment portfolio. We fund assets using deposits and other borrowings. Our strategy is to manage the mix of our deposits rather than compete on rate. As a result, approximately 30.7% of our deposits were noninterest-bearing as of December 31, 2014.

In 2011, the Federal Reserve issued final rules to repeal Regulation Q, which had prohibited the payment of interest on demand deposits by institutions that are member banks of the Federal Reserve System. The final rules implement Section 627 of the Dodd-Frank Act, which repealed Section 19(i) of the Federal Reserve Act in its entirety. As a result, banks and thrifts are now permitted to offer interest-bearing demand deposit accounts to commercial clients, which were previously forbidden under Regulation Q. The repeal of Regulation Q may cause increased competition from other financial institutions for these deposits. If we decide to pay interest on demand accounts, we would expect our interest expense to increase. Although Regulation Q has been effective for over three years, the impact may not have been realized yet because of the current zero interest rate policy environment.

**Florida financial institutions, such as the Bank, face a higher risk of noncompliance and enforcement actions with the Bank Secrecy Act and other anti-money laundering statutes and regulations.**

Since September 11, 2001, banking regulators have intensified their focus on anti-money laundering and Bank Secrecy Act compliance requirements, particularly the anti-money laundering provisions of the USA PATRIOT Act. There is also increased scrutiny of compliance with the rules enforced by the Office of Foreign Assets Control (“OFAC”). Since 2004, federal banking regulators and examiners have been extremely aggressive in their supervision and examination of financial institutions located in the State of Florida with respect to the institution’s Bank Secrecy Act/anti-money laundering compliance. Consequently, numerous formal enforcement actions have been instituted against financial institutions.

In order to comply with regulations, guidelines and examination procedures in this area, the Bank has been required to adopt new policies and procedures and to install new systems. If the Bank’s policies, procedures and systems are deemed deficient or the policies, procedures and systems of the financial institutions that it has already acquired or may acquire in the future are deficient, the Bank would be subject to liability, including fines and regulatory actions such as restrictions on its ability to pay dividends and the necessity to obtain regulatory approvals to proceed with certain aspects of its business plan, including its acquisition plans.

**Risks Related to Market Events**

**Our loan portfolio is heavily concentrated in mortgage loans secured by properties in Florida and Georgia which causes our risk of loss to be higher than if we had a more geographically diversified portfolio.**

Our interest-earning assets are heavily concentrated in mortgage loans secured by real estate, particularly real estate located in Florida and Georgia. As of December 31, 2014, approximately 75.4% of our loans had real estate as a primary, secondary, or tertiary component of collateral. The real estate collateral in each case provides an alternate source of repayment in the event of default by the borrower; however, the value of the collateral may decline during the time the credit is extended. If we are required to liquidate the collateral securing a loan during a period of reduced real estate values to satisfy the debt, our earnings and capital could be adversely affected.

Additionally, as of December 31, 2014, substantially all of our loans secured by real estate are secured by commercial and residential properties located in Northern Florida and Middle Georgia. The concentration of our loans in these areas subjects us to risk that a downturn in the economy or recession in these areas, such as the one from which these areas are currently recovering, could result in a decrease in loan originations and increases in delinquencies and foreclosures, which would more greatly affect us than if our lending were more geographically diversified. In addition, since a large portion of our portfolio is secured by properties located in Florida and Georgia, the occurrence of a natural disaster, such as a hurricane, or a man-made disaster could result in a decline in loan originations, a decline in the value or destruction of mortgaged properties and an increase in the risk of delinquencies, foreclosures or loss on loans originated by us. We may suffer further losses due to the decline in the value of the properties underlying our mortgage loans, which would have an adverse impact on our results of operations and financial condition.

**Our concentration in loans secured by real estate may increase our credit losses, which would negatively affect our financial results.**

Due to the lack of diversified industry within the markets served by the Bank and the relatively close proximity of our geographic markets, we have both geographic concentrations as well as concentrations in the types of loans funded. Specifically, due to the nature of our markets, a significant portion of the portfolio has historically been secured with real estate. As of December 31, 2014, approximately 35.4% and 37.1% of our \$1.442 billion loan portfolio was secured by commercial real estate and residential real estate, respectively. As of this same date, approximately 3.0% was secured by property under construction.

In the event we are required to foreclose on a property securing one of our mortgage loans or otherwise pursue our remedies in order to protect our investment, we may be unable to recover funds in an amount equal to our projected return on our investment or in an amount sufficient to prevent a loss to us due to prevailing economic conditions, real estate values and other factors associated with the ownership of real property. As a result, the market value of the real estate or other collateral underlying our loans may not, at any given time, be sufficient to satisfy the outstanding principal amount of the loans, and consequently, we would sustain loan losses.

**The fair value of our investments could decline which would cause a reduction in shareowners' equity.**

A large portion of our investment securities portfolio as of December 31, 2014 has been designated as available-for-sale pursuant to U.S. generally accepted accounting principles relating to accounting for investments. Such principles require that unrealized gains and losses in the estimated value of the available-for-sale portfolio be "marked to market" and reflected as a separate item in shareowners' equity (net of tax) as accumulated other comprehensive income/loss. Shareowners' equity will continue to reflect the unrealized gains and losses (net of tax) of these investments. The fair value of our investment portfolio may decline, causing a corresponding decline in shareowners' equity.

Management believes that several factors will affect the fair values of our investment portfolio. These include, but are not limited to, changes in interest rates or expectations of changes, the degree of volatility in the securities markets, inflation rates or expectations of inflation and the slope of the interest rate yield curve (the yield curve refers to the differences between shorter-term and longer-term interest rates; a positively sloped yield curve means shorter-term rates are lower than longer-term rates). These and other factors may impact specific categories of the portfolio differently, and we cannot predict the effect these factors may have on any specific category.

**Risks Related to an Investment in Our Common Stock**

**We may be unable to pay dividends in the future.**

In 2014, our Board of Directors declared four quarterly cash dividends. These dividends were the first dividends declared since we announced the suspension of our quarterly dividend on our common stock on December 14, 2011. Declarations of any future dividends will be contingent on our ability to earn sufficient profits and to remain adequately capitalized. In addition, due to our contractual obligations with the holders of the trust preferred securities, if we defer the payment of accrued interest owed to the holders of the trust preferred securities, we may not make dividend payments to our shareowners.

Further, under applicable statutes and regulations, the Bank's board of directors, after charging-off bad debts, depreciation and other worthless assets, if any, and making provisions for reasonably anticipated future losses on loans and other assets, may quarterly, semi-annually, or annually declare and pay dividends to CCBG of up to the aggregate net income of that period combined with the Bank's retained net income for the preceding two years and, with the approval of the Florida Office of Financial Regulation and Federal Reserve, declare a dividend from retained

net income which accrued prior to the preceding two years. Additional state laws generally applicable to Florida corporations may also limit our ability to declare and pay dividends. Thus, our ability to fund future dividends may be restricted by state law.

**Limited trading activity for shares of our common stock may contribute to price volatility.**

While our common stock is listed and traded on the Nasdaq Global Select Market, there has been limited trading activity in our common stock. The average daily trading volume of our common stock over the 12-month period ending December 31, 2014 was approximately 26,219 shares. Due to the limited trading activity of our common stock, relatively small trades may have a significant impact on the price of our common stock.

**Securities analysts may not initiate coverage or continue to cover our common stock, and this may have a negative impact on its market price.**

The trading market for our common stock will depend in part on the research and reports that securities analysts publish about us and our business. We do not have any control over securities analysts and they may not initiate coverage or continue to cover our common stock. If securities analysts do not cover our common stock, the lack of research coverage may adversely affect its market price. If we are covered by securities analysts, and our common stock is the subject of an unfavorable report, our stock price would likely decline. If one or more of these analysts ceases to cover our Company or fails to publish regular reports on us, we could lose visibility in the financial markets, which may cause our stock price or trading volume to decline.

**Our directors, executive officers, and principal shareowners, if acting together, have substantial control over all matters requiring shareowner approval, including changes of control. Because Mr. William G. Smith, Jr. is a principal shareowner and our Chairman, President, and Chief Executive Officer and Chairman of the Bank, he has substantial control over all matters on a day to day basis.**

Our directors, executive officers, and principal shareowners beneficially owned approximately 39% of the outstanding shares of our common stock as of December 31, 2014. Our principal shareowners include the Estate of Robert H. Smith, who was the brother of William G. Smith, Jr., our Chairman, President and Chief Executive Officer, which beneficially owns 17.5% of our shares. William G. Smith, Jr. beneficially owns 21.7% of our shares. In addition, 2S Partnership beneficially owns 6.0% of our shares, however, its shares were historically deemed to be beneficially owned by Messrs. Smith and Smith. Together, Mr. Smith and the Estate of Robert H. Smith beneficially own approximately 33% of our shares.

Accordingly, these directors, executive officers, and principal shareowners, if acting together, may be able to influence or control matters requiring approval by our shareowners, including the election of directors and the approval of mergers, acquisitions or other extraordinary transactions. In addition, because William G. Smith, Jr. is the Chairman, President, and Chief Executive Officer of CCBG and Chairman of the Bank, he has substantial control over all matters on a day-to-day basis, including the nomination and election of directors.

These directors, executive officers, and principal shareowners may also have interests that differ from yours and may vote in a way with which you disagree and which may be adverse to your interests. The concentration of ownership may have the effect of delaying, preventing or deterring a change of control of our company, could deprive our shareowners of an opportunity to receive a premium for their common stock as part of a sale of our Company and might ultimately affect the market price of our common stock. You may also have difficulty changing management, the composition of the Board of Directors, or the general direction of our Company.

**Our Articles of Incorporation, Bylaws, and certain laws and regulations may prevent or delay transactions you might favor, including a sale or merger of CCBG.**

CCBG is registered with the Federal Reserve as a financial holding company under the Bank Holding Company Act (“BHCA”). As a result, we are subject to supervisory regulation and examination by the Federal Reserve. The Gramm-Leach-Bliley Act, the BHCA, and other federal laws subject financial holding companies to particular restrictions on the types of activities in which they may engage, and to a range of supervisory requirements and activities, including regulatory enforcement actions for violations of laws and regulations.

Provisions of our Articles of Incorporation, Bylaws, certain laws and regulations and various other factors may make it more difficult and expensive for companies or persons to acquire control of us without the consent of our Board of Directors. It is possible, however, that you would want a takeover attempt to succeed because, for example, a potential buyer could offer a premium over the then prevailing price of our common stock.

For example, our Articles of Incorporation permit our Board of Directors to issue preferred stock without shareowner action. The ability to issue preferred stock could discourage a company from attempting to obtain control of us by means of a tender offer, merger, proxy contest or otherwise. Additionally, our Articles of Incorporation and Bylaws divide our Board of Directors into three classes, as nearly equal in size as possible, with staggered three-year terms. One class is elected each year. The classification of our Board of Directors could make it more difficult for a company to acquire control of us. We are also subject to certain provisions of the Florida Business Corporation Act and our Articles of Incorporation that relate to business combinations with interested shareowners. Other provisions in our Articles of Incorporation or Bylaws that may discourage takeover attempts or make them more difficult include:

- Supermajority voting requirements to remove a director from office;

- Provisions regarding the timing and content of shareowner proposals and nominations; Supermajority voting requirements to amend Articles of Incorporation unless approval is received by a majority of “disinterested directors”;
- Absence of cumulative voting; and
- Inability for shareowners to take action by written consent.

**Shares of our common stock are not an insured deposit and may lose value.**

The shares of our common stock are not a bank deposit and will not be insured or guaranteed by the FDIC or any other government agency. Your investment will be subject to investment risk, and you must be capable of affording the loss of your entire investment.

***Item 1B. Unresolved Staff Comments***

None.

***Item 2. Properties***

We are headquartered in Tallahassee, Florida. Our executive office is in the Capital City Bank building located on the corner of Tennessee and Monroe Streets in downtown Tallahassee. The building is owned by the Bank, but is located on land leased under a long-term agreement.

As of February 27, 2015, the Bank had 63 full-service banking locations. Of the 63 locations, the Bank leases the land, buildings, or both at seven locations and owns the land and buildings at the remaining 56.

***Item 3. Legal Proceedings***

We are party to lawsuits and claims arising out of the normal course of business. In management's opinion, there are no known pending claims or litigation, the outcome of which would, individually or in the aggregate, have a material effect on our consolidated results of operations, financial position, or cash flows.

***Item 4. Mine Safety Disclosure.***

Not applicable.

**PART II**

***Item 5. Market for the Registrant's Common Equity, Related Shareowner Matters, and Issuer Purchases of Equity Securities***

*Common Stock Market Prices and Dividends*

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Our common stock trades on the Nasdaq Global Select Market under the symbol “CCBG.” We had a total of 1,589 shareowners of record as of February 27, 2015.

The following table presents the range of high and low closing sales prices reported on the Nasdaq Global Select Market and cash dividends declared for each quarter during the past two years.

	<b>2014</b>				<b>2013</b>			
	Fourth	Third	Second	First	Fourth	Third	Second	First
	Quarter	Quarter	Quarter	Quarter	Quarter	Quarter	Quarter	Quarter
Common stock price:								
High	\$16.00	\$14.98	\$14.71	\$14.59	\$12.69	\$13.08	\$12.64	\$12.54
Low	13.00	13.26	12.60	11.56	11.33	11.06	10.12	10.95
Close	15.54	13.54	14.53	13.28	11.77	11.78	11.53	12.35
Cash dividends per share	0.03	0.02	0.02	0.02	0.00	0.00	0.00	0.00

Florida law and Federal regulations impose restrictions on our ability to pay dividends and limitations on the amount of dividends that the Bank can pay annually to us. See Item 1. “Capital; Dividends; Sources of Strength” and “Dividends” in the Business section on page 12 and 13 and the section entitled “Liquidity and Capital Resources – Dividends” -- in Management’s Discussion and Analysis of Financial Condition and Operating Results on page 54 and Note 14 in the Notes to Consolidated Financial Statements.



*Performance Graph*

This performance graph compares the cumulative total shareholder return on our common stock with the cumulative total shareholder return of the Nasdaq Composite Index and the SNL Financial LC \$1B-\$5B Bank Index for the past five years. The graph assumes that \$100 was invested on December 31, 2009 in our common stock and each of the above indices, and that all dividends were reinvested. The shareholder return shown below represents past performance and should not be considered indicative of future performance.

<i>Index</i>	<i>Period Ending</i>					
	<b>12/31/09</b>	<b>12/31/10</b>	<b>12/31/11</b>	<b>12/31/12</b>	<b>12/31/13</b>	<b>12/31/14</b>
Capital City Bank Group, Inc.	\$100.00	\$94.53	\$73.64	\$87.67	\$90.76	\$120.59
Nasdaq Composite	100.00	118.15	117.22	138.02	193.47	222.16
SNL \$1B-\$5B Bank Index	100.00	113.35	103.38	127.47	185.36	193.81

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**Item 6. Selected Financial Data**

(Dollars in Thousands, Except Per Share Data)	2014	2013	2012	2011	2010
Interest Income	\$78,221	\$82,152	\$89,680	\$99,459	\$110,495
Net Interest Income	74,641	77,736	84,312	91,922	97,533
Provision for Loan Losses	1,905	3,472	16,166	18,996	23,824
Noninterest Income	52,536	55,111	54,569	57,244	55,870
Noninterest Expense	114,358	121,405	123,943	124,643	132,961
Net Income (Loss)	9,260	6,045	108	4,897	(413)
Per Common Share:					
Basic Net Income (Loss)	\$0.53	\$0.35	\$0.01	\$0.29	\$(0.02)
Diluted Net Income (Loss)	0.53	0.35	0.01	0.29	(0.02)
Cash Dividends Declared	0.09	—	—	0.30	0.49
Diluted Book Value	15.53	15.85	14.31	14.68	15.15
Performance Ratios:					
Return on Average Assets	0.36	% 0.24	% 0.00	% 0.19	% (0.02)
Return on Average Equity	3.27	2.40	0.04	1.86	(0.16)
Net Interest Margin (FTE)	3.36	3.54	3.81	4.18	4.32
Noninterest Income as % of Operating Revenues	41.30	41.48	39.29	38.38	36.42
Efficiency Ratio	89.68	91.09	88.72	83.24	85.95
Asset Quality:					
Allowance for Loan Losses	\$17,539	\$23,095	\$29,167	\$31,035	\$35,436
Allowance for Loan Losses to Loans	1.22	% 1.65	% 1.93	% 1.91	% 2.01
Nonperforming Assets	52,449	85,035	117,648	137,623	123,637
Nonperforming Assets to Assets	2.00	3.26	4.47	5.21	4.72
Nonperforming Assets to Loans + OREO	3.55	5.87	7.47	8.14	6.81
Allowance to Nonperforming Loans	104.60	62.48	45.42	41.37	53.94
Net Charge-Offs to Average Loans	0.53	0.66	1.16	1.39	1.77
Capital Ratios:					
Tier I Capital	16.67	% 16.56	% 14.35	% 13.96	% 13.24
Total Capital	17.76	17.94	15.72	15.32	14.59
Tangible Capital	7.38	7.58	6.35	6.51	6.82
Leverage	10.99	10.46	9.90	10.26	10.10
Equity to Assets	10.37	10.58	9.37	9.54	9.88
Dividend Pay-Out	16.98	NM	NM	103.45	NM
Averages for the Year:					
Loans, Net of Unearned Income	\$1,414,000	\$1,450,806	\$1,556,565	\$1,686,995	\$1,829,193
Earning Assets	2,237,623	2,213,686	2,229,621	2,221,317	2,294,282
Total Assets	2,564,176	2,568,662	2,590,173	2,583,197	2,644,731
Deposits	2,093,477	2,070,073	2,105,672	2,081,583	2,192,323
Shareowners' Equity	283,079	251,427	252,960	263,048	264,679

## Year-End Balances:

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Loans, Net of Unearned Income	\$1,442,062	\$1,399,669	\$1,521,302	\$1,628,683	\$1,758,671
Earning Assets	2,276,781	2,274,019	2,261,781	2,266,193	2,269,185
Total Assets	2,627,169	2,611,903	2,633,984	2,641,312	2,622,053
Deposits	2,146,794	2,136,248	2,144,996	2,172,519	2,103,976
Shareowners' Equity	272,540	276,400	246,889	251,942	259,019
Other Data:					
Basic Average Shares Outstanding	17,424,788	17,324,759	17,204,559	17,139,558	17,075,867
Diluted Average Shares Outstanding	17,488,020	17,399,355	17,219,765	17,140,390	17,076,724
Shareowners of Record <sup>(1)</sup>	1,589	1,651	1,691	1,701	1,768
Banking Locations <sup>(1)</sup>	63	63	66	70	70
Full-Time Equivalent Associates <sup>(1)</sup>	895	891	913	959	975

*(1)As of record date. The record date is on or about March 1<sup>st</sup> of the following year.*

*NM – Not Meaningful*

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## ***Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations***

Management's discussion and analysis ("MD&A") provides supplemental information, which sets forth the major factors that have affected our financial condition and results of operations and should be read in conjunction with the Consolidated Financial Statements and related notes included in the Annual Report on Form 10-K. The MD&A is divided into subsections entitled "Business Overview," "Executive Overview," "Results of Operations," "Financial Condition," "Liquidity and Capital Resources," "Off-Balance Sheet Arrangements," "Fourth Quarter, 2014 Financial Results," and "Accounting Policies." The following information should provide a better understanding of the major factors and trends that affect our earnings performance and financial condition, and how our performance during 2014 compares with prior years. Throughout this section, Capital City Bank Group, Inc., and its subsidiaries, collectively, are referred to as "CCBG," "Company," "we," "us," or "our."

### **CAUTION CONCERNING FORWARD-LOOKING STATEMENTS**

This Annual Report on Form 10-K, including this MD&A section, contains "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. These forward-looking statements include, among others, statements about our beliefs, plans, objectives, goals, expectations, estimates and intentions that are subject to significant risks and uncertainties and are subject to change based on various factors, many of which are beyond our control. The words "may," "could," "should," "would," "believe," "anticipate," "estimate," "expect," "intend," "plan," "target," similar expressions are intended to identify forward-looking statements.

All forward-looking statements, by their nature, are subject to risks and uncertainties. Our actual future results may differ materially from those set forth in our forward-looking statements. Please see the Introductory Note and *Item 1A Risk Factors* of this Annual Report for a discussion of factors that could cause our actual results to differ materially from those in the forward-looking statements.

However, other factors besides those listed in *Item 1A Risk Factors* or discussed in this Annual Report also could adversely affect our results, and you should not consider any such list of factors to be a complete set of all potential risks or uncertainties. Any forward-looking statements made by us or on our behalf speak only as of the date they are made. We do not undertake to update any forward-looking statement, except as required by applicable law.

### **BUSINESS OVERVIEW**

#### **Our Business**

We are a financial holding company headquartered in Tallahassee, Florida, and we are the parent of our wholly owned subsidiary, Capital City Bank (the “Bank” or “CCB”). The Bank offers a broad array of products and services through a total of 63 full-service offices located in Florida, Georgia, and Alabama. The Bank offers commercial and retail banking services, as well as trust and asset management, retail securities brokerage and data processing services. Please see the section captioned “About Us” beginning on page 4 for more detailed information about our business.

Our profitability, like most financial institutions, is dependent to a large extent upon net interest income, which is the difference between the interest and fees received on interest earning assets, such as loans and securities, and the interest paid on interest-bearing liabilities, principally deposits and borrowings. Results of operations are also affected by the provision for loan losses, operating expenses such as salaries and employee benefits, occupancy and other operating expenses including income taxes, and noninterest income such as deposit fees, wealth management fees, mortgage banking fees, bank card fees, and data processing fees.

### **Strategic Review**

Our philosophy is to build long-term client relationships based on quality service, high ethical standards, and safe and sound banking practices. We maintain a locally oriented, community-based focus, which is augmented by experienced, centralized support in select specialized areas. Our local market orientation is reflected in our network of banking office locations, experienced community executives with a dedicated President for each market, and community boards which support our focus on responding to local banking needs. We strive to offer a broad array of sophisticated products and to provide quality service by empowering associates to make decisions in their local markets.

We have sought to build a franchise in small-to medium-sized, less competitive markets, located on the outskirts of the larger metropolitan markets where we are positioned as a market leader. Many of our markets are on the outskirts of these larger markets in close proximity to major interstate thoroughfares such as Interstates I-10 and I-75. Our three largest markets are Tallahassee (Leon-Florida), Gainesville (Alachua-Florida), and Macon (Bibb-Georgia). In 13 of 20 markets in Florida and three of five markets in Georgia, we rank within the top four banks in terms of market share. Furthermore, in the counties in which we operate, we maintain an average 9.10% market share in the Florida counties and 5.82% in the Georgia counties, suggesting that there is significant opportunity to grow market share within these geographic areas. The larger employers in many of our markets are state and local governments, healthcare providers, educational institutions, and small businesses. While we realize that the markets in our footprint do not provide for a level of potential growth that the larger metropolitan markets may provide, our markets do provide good growth dynamics and have historically grown in excess of the national average. The value of these markets stems from the fact they are less competitive, secondary markets. We strive to provide value added services to our clients by being not just their bank, but their banker. This element of our strategy distinguishes Capital City Bank from our competitors.

Our long-term vision remains to profitably expand our franchise through a combination of organic growth in existing markets and acquisitions. We have long understood that our core deposit funding base is a predominant driver of our profitability and overall franchise value, and have focused extensively on this component of our organic growth efforts in recent years. While we have not been an active acquirer of banks since 2005, this component of our strategy is still in place.

Potential acquisition growth will continue to be focused on Florida, Georgia, and Alabama with a particular focus on financial institutions located on the outskirts of larger, metropolitan areas. Five markets have been identified, four in Florida and one in Georgia, in which management intends to proactively pursue expansion opportunities. These markets include Alachua, Marion, Hernando/Pasco counties in Florida, the western panhandle of Florida, and Bibb and surrounding counties in central Georgia. Our focus on some of these markets may change as we continue to evaluate our strategy and the economic conditions and demographics of any individual market. We will also continue to evaluate de novo expansion opportunities in attractive new markets in the event that acquisition opportunities are not feasible. Other expansion opportunities that will be evaluated include asset management, mortgage banking, and insurance. Embedded in our acquisition strategy is our desire to partner with institutions that are culturally similar, have experienced management and possess either established market presence or have potential for improved profitability through growth, economies of scale, or expanded services. Generally, these target institutions will range in asset size from \$100 million to \$400 million.

## EXECUTIVE OVERVIEW

Our 2014 performance reflects meaningful progress made across all aspects of our business. We reported net income of \$9.3 million, or \$0.53 per diluted share, compared to \$6.0 million, or \$0.35 per diluted share in 2013. The growth in net income reflects lower noninterest expense of \$7.0 million, a lower loan loss provision of \$1.6 million, and lower income taxes of \$0.4 million, partially offset by lower net interest income of \$3.1 million and noninterest income of \$2.6 million.

Below are summary highlights that impacted our performance for the year:

- Margin expansion driven by four consecutive quarters of loan growth and increased deployment of liquidity into the investment portfolio.
- Loan balances grew at an annual rate of 3% reflective of improved loan demand and calling efforts.
- 38% reduction in nonperforming assets -- improvement in credit quality favorably impacted credit costs.
- Core operating costs (excluding OREO) declined 5% year over year.

Efforts to improve our earning asset mix stabilized our net interest margin in 2014. Sequential loan growth for each quarter during 2014 and the deployment of more liquidity into our investment portfolio drove growth in net interest income for the last three quarters of the year. The development of new consumer and business loan programs drove a majority of the growth, but increased production and a slow-down in pay-downs/pay-offs in our real estate portfolios

also contributed. The extended low interest rate environment and increased competition for loans continues to pressure asset yields, but we have not changed our risk profile by extending asset durations for yield which positions us better to respond to changing market conditions. Over time, this strategy has produced consistent outcomes and a net interest margin that exceeds our peer median.

We continue to maintain several sources of noninterest income which diversifies our operating revenue. Changing client behavior and regulatory changes have slowed growth in our deposit and bank card fee revenues over the past three years, but growth in other lines of business have helped mitigate the impact. The development of strategic initiatives aimed at segmenting our client base and target marketing to more fully realize the fee income opportunities inherent in our strong core deposit base franchise are ongoing.

Core operating costs (excluding OREO) declined noticeably in 2014 driven by lower pension expense. Reduction in ancillary costs related to the prolonged credit cycle are also being removed from our cost structure and contributed to the decline in 2014. We continue to evaluate strategies aimed at optimizing our delivery systems to improve our operating efficiency.

Our credit quality metrics continued to improve in 2014 reflective of further reduction in the level of our nonperforming assets driven by strong OREO sales and a significant reduction in the level of problem loan inflows. As a result, our loan loss provision has stabilized and OREO costs continue to decline. We continue to believe our disciplined approach to capturing the maximum value possible when disposing of our problem assets has proven to be in the best long-term interest of our shareowners and 2014 further validated that approach.

We realized good progress in 2014 and re-evaluated many aspects of our business in response to a changing industry. We enter 2015 with a great deal of momentum as we focus on strategies aimed at driving loan growth and optimizing our delivery systems to return us to our historical levels of efficiency.

Key components of our 2014 financial performance are summarized below:

## Results of Operations

For 2014, taxable equivalent net interest income decreased \$3.2 million, or 4.1%, to \$75.1 million driven by a decline in loan income attributable to lower average portfolio balances and unfavorable asset repricing, which was partially offset by a reduction in interest expense. Our net interest margin of 3.36% in 2014 was 18 basis points lower than the 3.54% recorded in 2013. In 2014, compared to 2013, the yield on interest earning assets declined 22 basis points and was partially offset by a decline in the cost of funds of four basis points.

Total credit costs (loan loss provision plus other real estate owned (“OREO”) expenses) were \$8.7 million in 2014 compared to \$11.7 million for 2013. Favorable problem loan migration, lower loan losses, and improved credit metrics resulted in a \$1.6 million decrease in our loan loss provision to \$1.9 million for the year. Continued progress in disposing of OREO properties and firming of property values favorably impacted our level of OREO costs which declined by \$1.4 million to \$6.8 million for the year.

For 2014, noninterest income totaled \$52.5 million, a \$2.6 million, or 4.7%, decrease from 2013 primarily reflective of lower deposit fees of \$0.9 million, data processing fees of \$1.1 million, wealth management fees of \$0.4 million and mortgage banking fees of \$0.5 million.

For 2014, noninterest expense totaled \$114.4 million, a \$7.0 million, or 5.8%, decrease primarily attributable to lower compensation expense of \$3.9 million, OREO expense of \$1.4 million, and other expense (excluding OREO expenses) of \$2.2 million.

## Financial Condition

Average assets totaled approximately \$2.564 billion for 2014, consistent with 2013. Average earning assets were approximately \$2.238 billion, representing an increase of \$23.9 million, or 1.1%, over 2013. Year-over-year, average short-term investments decreased \$52.8 million, while investment securities increased \$113.5 million and average gross loans declined by \$36.8 million. We continue to maintain a strong liquidity position as evidenced by average funds sold of approximately \$369.9 million for the year and were able to shift some overnight funds balances into the investment portfolio during the year to improve our mix.

Average gross loans totaled \$1.414 billion, a \$36.8 million, or 2.5%, decrease from 2013. We experienced runoff in all loan types except commercial loans and indirect auto loans, which grew year-over-year. New loan production increased in 2014 and the levels of payoffs and pay downs declined resulting in average loan growth for the last three quarters of the year.



Average total deposits for 2014 were \$2.093 billion, a decrease of \$23.4 million, or 1.1%, over 2013. Increases in average noninterest bearing deposits and savings accounts were partially offset by declines in the remaining product types.

At year-end 2014, our nonperforming assets totaled \$52.4 million, a decrease of \$32.6 million from year-end 2013. Nonaccrual loans totaled \$16.8 million at year-end 2014, a decrease of \$20.2 million from year-end 2013, reflective of loan resolutions which outpaced gross additions. Nonaccrual loan additions slowed again for the third consecutive year, by \$21.6 million, or 49%. The balance of OREO totaled \$35.7 million at year-end 2014, a decrease of \$12.4 million from year-end 2013. We continued to experience progress during 2014 in our efforts to dispose of OREO selling properties totaling \$23.8 million compared to \$25.9 million in 2013. Nonperforming assets represented 2.00% of total assets at December 31, 2014 compared to 3.26% at December 31, 2013.

Our allowance for loan losses at year-end 2014 was \$17.5 million (1.22% of loans) and provided coverage of 105% of nonperforming loans compared to \$23.1 million (1.65% of loans) and 62% of nonperforming loans at year-end 2013. Net charge-offs for 2014 totaled \$7.5 million, or 0.53% of average loans compared to \$9.5 million, or 0.66% in 2013, reflective of lower residential and construction loan charge-offs.

Shareowners' equity decreased by \$3.9 million from \$276.4 million at December 31, 2013 to \$272.5 million at December 31, 2014, attributable to an unfavorable adjustment to pension related OCI reflecting an increase in our pension liabilities driven by a lower discount rate and a change in the mortality tables. We continue to maintain a strong capital base as evidenced by a risk-based capital ratio of 17.76% and a tangible common equity ratio of 7.38% at year-end 2014 compared to 17.94% and 7.58%, respectively, at year-end 2013.

**RESULTS OF OPERATIONS**

For 2014, we realized net income of \$9.3 million, or \$0.53 per diluted share compared to \$6.0 million, or \$0.35 per diluted share, in 2013, and \$0.1 million, or \$0.01 per diluted share in 2012.

The increase in earnings for 2014 was attributable to lower noninterest expense of \$7.0 million, a lower loan loss provision of \$1.6 million, and lower income taxes of \$0.4 million, partially offset by lower net interest income of \$3.1 million and noninterest income of \$2.6 million.

The increase in earnings for 2013 as compared to 2012 reflects a lower loan loss provision of \$12.7 million, higher noninterest income of \$0.5 million, and lower noninterest expense of \$2.5 million, partially offset by a reduction in net interest income of \$6.6 million and higher income taxes of \$3.2 million.

A condensed earnings summary for the last three years is presented in Table 1 below:

**Table 1****CONDENSED SUMMARY OF EARNINGS**

(Dollars in Thousands, Except Per Share Data)	2014	2013	2012
Interest Income	\$78,221	\$82,152	\$89,680
Taxable Equivalent Adjustments	494	583	616
Total Interest Income (FTE)	78,715	82,735	90,296
Interest Expense	3,580	4,416	5,368
Net Interest Income (FTE)	75,135	78,319	84,928
Provision for Loan Losses	1,905	3,472	16,166
Taxable Equivalent Adjustments	494	583	616
Net Interest Income After Provision for Loan Losses	72,736	74,264	68,146
Noninterest Income	52,536	55,111	54,569
Noninterest Expense	114,358	121,405	123,943
Income (Loss) Before Income Taxes	10,914	7,970	(1,228 )
Income Tax Expense (Benefit)	1,654	1,925	(1,336 )
Net Income	\$9,260	\$6,045	\$108
Basic Net Income Per Share	\$0.53	\$0.35	\$0.01
Diluted Net Income Per Share	\$0.53	\$0.35	\$0.01

**Net Interest Income**

Net interest income represents our single largest source of earnings and is equal to interest income and fees generated by earning assets, less interest expense paid on interest bearing liabilities. We provide an analysis of our net interest income, including average yields and rates in Tables 2 and 3 below. We provide this information on a “taxable equivalent” basis to reflect the tax-exempt status of income earned on certain loans and investments, the majority of which are state and local government debt obligations.

In 2014, our taxable equivalent net interest income decreased \$3.2 million, or 4.1%. This follows a decrease of \$6.6 million, or 7.8%, in 2013, and a decrease of \$7.9 million, or 8.5%, in 2012. The decrease in our taxable equivalent net interest income in these years was primarily driven by declines in loan income attributable to lower average portfolio balances and unfavorable asset repricing, which was partially offset by reductions in interest expense. The lower interest expense is primarily attributable to declines in certificates of deposit balances and reflects favorable repricing in all interest-bearing deposit categories.

For 2014, taxable equivalent interest income declined \$4.0 million, or 4.9%, from 2013 and \$7.6 million, or 8.4% in 2013 from 2012. The decrease for all periods is specifically attributable to both the shift in earning asset mix and lower yields. The reduction in average loans has resulted in the higher yielding interest earning assets being replaced with lower yielding federal funds or investment securities. Lower yields on new loan and investment production and loan portfolio repricing continue to adversely affect net interest income.

These factors produced a 22 basis point decline in the yield on interest earning assets, which decreased from 3.74% in 2013 to 3.52% for 2014. This compares to a 31 basis point decline in 2013 over 2012.

Interest expense decreased \$836,000, or 18.9%, from 2013, and \$952,000, or 17.7%, in 2013 over 2012. The lower cost of funds when compared to both periods was a result of both certificates of deposit repricing to lower rates, and rate reductions on several deposit products. The rate reductions on deposits reflect our response to a historically low interest rate environment and desire to continue our focus on core banking relationships. The average rate paid on interest-bearing liabilities decreased five basis points from 2013, and declined five basis points in 2013 from 2012, reflecting the factors mentioned above.

Our interest rate spread (defined as the taxable equivalent yield on average earning assets less the average rate paid on interest bearing liabilities) decreased 17 basis points in 2014 compared to 2013 and declined 26 basis points in 2013 compared to 2012. The decrease in both years was primarily attributable to the adverse impact of lower rates and a change in the mix of interest earning assets, which more than offset the repricing of our deposit base.

Our net interest margin (defined as taxable equivalent interest income less interest expense divided by average earning assets) of 3.36% in 2014 was 18 basis points lower than the 3.54% recorded in 2013 and was 27 basis points lower in 2013 than the 3.81% reported in 2012. In 2014, compared to 2013, the yield on earning assets declined 22 basis points and was partially offset by a decline in the cost of funds of four basis points. The earning asset yield decline of 31 basis points in 2013 over 2012 was partially offset by a reduction in the cost of funds by four basis points.

The net interest margin for the fourth quarter of 2014 was 3.43%, a decline of two basis points from the fourth quarter of 2013. The decrease in the margin from the comparable prior year period was attributable to unfavorable asset repricing, partially offset by a lower average cost of funds. Growth in our investment portfolio has partially helped mitigate this decline.

Although down year-over-year, net interest income increased for the third straight quarter and was slightly higher than the fourth quarter of 2013. Historically low interest rates and increased competition for loans continue to put pressure on loan yields, partially offsetting the favorable impact attributable to growth in the loan and investment portfolios.

Our current strategy, which is consistent with our historical strategy, is to not accept greater interest rate risk by reaching further out the curve for yield, particularly given the fact that short term rates are at historical lows. We continue to maintain short duration portfolios on both sides of the balance sheet and believe we are well positioned to respond to changing market conditions. Over time, this strategy has produced fairly consistent outcomes and a net interest margin that is significantly above peer comparisons.

**Table 2****AVERAGE BALANCES AND INTEREST RATES**

(Taxable Equivalent Basis - Dollars in Thousands)	2014		2013		2012		
	Average Balance	Interest	Average Rate	Average Balance	Interest	Average Rate	
<b>ASSETS</b>							
Loans, Net of Unearned Income <sup>(1)(2)</sup>	\$1,414,000	\$73,637	5.21%	\$1,450,806	\$78,484	5.41%	\$1,556,5
Taxable Investment Securities	362,393	3,423	0.91	232,173	2,344	0.94	223,42
Tax-Exempt Investment Securities <sup>(2)</sup>	91,324	722	0.79	108,042	830	0.76	65,560
Funds Sold	369,906	933	0.25	422,665	1,077	0.25	384,06
Total Earning Assets	2,237,623	78,715	3.52%	2,213,686	82,735	3.74%	2,229,6
Cash & Due From Banks	45,367			49,978			48,924
Allowance for Loan Losses	(21,234 )			(28,167 )			(30,95)
Other Assets	302,420			333,165			342,58
<b>TOTAL ASSETS</b>	<b>\$2,564,176</b>			<b>\$2,568,662</b>			<b>\$ 2,590,1</b>
<b>LIABILITIES</b>							
NOW Accounts	\$715,846	\$318	0.04%	\$719,493	\$482	0.07%	\$ 771,61
Money Market Accounts	273,092	190	0.07	284,245	211	0.07	280,16
Savings Accounts	227,215	112	0.05	203,864	101	0.05	175,71
Other Time Deposits	206,136	479	0.23	231,354	637	0.28	267,26
Total Interest Bearing Deposits	1,422,289	1,099	0.08%	1,438,956	1,431	0.10%	1,494,7
Short-Term Borrowings	44,403	78	0.18	53,922	235	0.44	52,178
Subordinated Notes Payable	62,887	1,328	2.08	62,887	1,420	2.23	62,887
Other Long-Term Borrowings	33,727	1,075	3.19	41,077	1,330	3.24	41,513
Total Interest Bearing Liabilities	1,563,306	3,580	0.23%	1,596,842	4,416	0.28%	1,651,3
Noninterest Bearing Deposits	671,188			631,117			610,91
Other Liabilities	46,603			89,276			74,963
<b>TOTAL LIABILITIES</b>	<b>2,281,097</b>			<b>2,317,235</b>			<b>2,337,2</b>
<b>SHAREOWNERS' EQUITY</b>							
<b>TOTAL SHAREOWNERS' EQUITY</b>	<b>283,079</b>			<b>251,427</b>			<b>252,96</b>
<b>TOTAL LIABILITIES &amp; EQUITY</b>	<b>\$2,564,176</b>			<b>\$2,568,662</b>			<b>\$ 2,590,1</b>
Interest Rate Spread			3.29%			3.46%	
Net Interest Income		\$75,135			\$78,319		
Net Interest Margin <sup>(3)</sup>			3.36%			3.54%	

<sup>(1)</sup> Average balances include nonaccrual loans. Interest income includes loan fees of \$1.6 million for 2014, 2013, and 2012.

<sup>(2)</sup> Interest income includes the effects of taxable equivalent adjustments using a 35% tax rate.

<sup>(3)</sup> Taxable equivalent net interest income divided by average earning assets.

**Table 3****RATE/VOLUME ANALYSIS<sup>(1)</sup>**

(Taxable Equivalent Basis - Dollars in Thousands)	2014 vs. 2013			2013 vs. 2012		
	Increase (Decrease) Due to			Increase (Decrease) Due to		
	Total	Volume	Rate	Total	Volume	Rate
<b>Earnings Assets:</b>						
Loans, Net of Unearned Interest <sup>(2)</sup>	\$(4,847)	\$(1,991)	\$(2,856)	\$(7,296)	\$(5,828)	\$(1,468)
<b>Investment Securities:</b>						
Taxable	1,079	1,315	(236 )	(568 )	114	(682 )
Tax-Exempt <sup>(2)</sup>	(108 )	(128 )	20	172	519	(347 )
Funds Sold	(144 )	(134 )	(10 )	131	95	36
Total	(4,020)	(938 )	(3,082)	(7,561)	(5,100)	(2,461)
<b>Interest Bearing Liabilities:</b>						
NOW Accounts	(164 )	(2 )	(162 )	(152 )	(34 )	(118 )
Money Market Accounts	(21 )	(8 )	(13 )	(44 )	4	(48 )
Savings Accounts	11	12	(1 )	14	14	—
Time Deposits	(158 )	(69 )	(89 )	(495 )	(152 )	(343 )
Short-Term Borrowings	(157 )	(41 )	(116 )	39	7	32
Subordinated Notes Payable	(92 )	—	(92 )	(57 )	—	(57 )
Other Long-Term Borrowings	(255 )	(238 )	(17 )	(257 )	(13 )	(244 )
Total	(836 )	(346 )	(490 )	(952 )	(174 )	(778 )
Changes in Net Interest Income	\$(3,184)	\$(592 )	\$(2,592)	\$(6,609)	\$(4,926)	\$(1,683)

*This table shows the change in taxable equivalent net interest income for comparative periods based on either changes in average volume or changes in average rates for interest earning assets and interest-bearing liabilities.*

<sup>(1)</sup> *Changes which are not solely due to volume changes or solely due to rate changes have been attributed to rate changes.*

<sup>(2)</sup> *Interest income includes the effects of taxable equivalent adjustments using a 35% tax rate to adjust interest on tax-exempt loans and securities to a taxable equivalent basis.*

## Provision for Loan Losses

The provision for loan losses was \$1.9 million in 2014 compared to \$3.5 million in 2013 and \$16.2 million in 2012. The decline in the provision for all periods reflects favorable problem loan migration, lower loan losses, and overall improvement in key credit metrics. We discuss these trends in further detail below under Risk Element Assets and Allowance for Loan Losses.

## Noninterest Income

Noninterest income totaled \$52.5 million in 2014, \$55.1 million in 2013, and \$54.6 million in 2012. For 2014, the \$2.6 million, or 4.7%, decrease from 2013 reflects lower deposit fees of \$0.9 million, data processing fees of \$1.1 million, wealth management fees of \$0.4 million and mortgage banking fees of \$0.5 million, partially offset by higher bank card fees of \$0.1 million and other income of \$0.2 million. Lower overdraft fees drove the reduction in deposit fees. The loss of a large government processing contract drove the decline in data processing fees. Wealth management declined due to a lower level of client trading activity as well as strong new retail investment product sales in 2013. Lower refinancing activity drove the reduction in mortgage banking fees.

For 2013, the \$0.5 million, or 1.0%, increase over 2012 was attributable to higher wealth management fees of \$1.0 million partially offset by lower deposit fees of \$0.5 million. The increase in wealth management fees was attributable to higher trading activity by our clients, new account growth, as well as strong new retail investment product sales. Lower overdraft fees partially offset by higher business account analysis fees drove the decline in deposit fees.

Noninterest income as a percent of total operating revenues (net interest income plus noninterest income) was 41.30% in 2014, 42.48% in 2013, and 39.29% in 2012.

The table below reflects the major components of noninterest income.

(Dollars in Thousands)	2014	2013	2012
Deposit Fees	\$24,320	\$25,254	\$25,792
Bank Card Fees	10,892	10,786	10,783
Wealth Management Fees	7,808	8,179	7,181
Securities Transactions	1	3	—
Mortgage Banking Fees	3,082	3,534	3,600
Data Processing Fees	1,543	2,674	2,713
Other	4,890	4,681	4,500
Total Noninterest Income	\$52,536	\$55,111	\$54,569

Various significant components of noninterest income are discussed in more detail below.

*Deposit Fees.* For 2014, deposit service charge fees totaled \$24.3 million compared to \$25.3 million in 2013 and \$25.8 million in 2012. The \$0.9 million, or 3.7%, decrease in 2014 compared to 2013 was due to a lower level of overdraft fees generally reflective of improved financial management by our clients. The \$0.5 million, or 2.1%, decrease in 2013 compared to 2012 was driven by a lower level of overdraft fees, partially offset by higher business account analysis fees.

*Bank Card Fees.* Bank card fees totaled \$10.9 million in 2014 compared to \$10.8 million in 2013 and \$10.8 million in 2012. The slight increase in 2014 compared to 2013 reflects higher card spend by our clients. Bank card fees were essentially flat in 2013 compared to 2012 due to a reduction in the interchange rate for PIN based transactions.

*Wealth Management Fees.* Wealth management fees including both trust fees (i.e., managed accounts, trusts/estates, and retirement plans) and retail brokerage fees (i.e., investment and insurance products) totaled \$7.8 million in 2014 compared to \$8.2 million in 2013 and \$7.2 million in 2012. The \$0.4 million, or 4.5%, decrease in 2014 compared to 2013 was attributable to lower fees from our retail brokerage business generally reflective of lower client trading activity as well as strong new retail investment product sales in 2013. The \$1.0 million, or 13.9%, increase in 2013 compared to 2012 reflects a \$1.2 million increase in retail brokerage fees partially offset by a \$0.1 million decrease in trust fees. The growth in retail brokerage fees was driven by higher trading activity by our clients and new account growth. The slight decline in trust fees reflects a decline in trust assets under management primarily attributable to account distributions. At December 31, 2014, total assets under management were approximately \$1.278 billion compared to \$1.259 billion at December 31, 2013 and \$1.124 billion at December 31, 2012.

*Mortgage Banking Fees.* Mortgage banking fees totaled \$3.1 million in 2014 compared to \$3.5 million in 2013 and \$3.6 million in 2012. The \$0.5 million, or 12.8%, decrease in 2014 compared to 2013 was due to a lower level of refinancing activity, partially offset by higher home purchase financing and a higher margin realized for sold loans. The \$0.1 million, or 1.8%, decrease in 2013 compared to 2012 was also driven by a slowdown in refinance activity, but was substantially offset by a higher margin realized for sold loans. Refinancing activity represented 14% of our loan production in 2014 compared to 32% and 39% for 2013 and 2012, respectively. Market conditions, housing activity, the level of interest rates and the percent of our fixed-rate production have significant impacts on our mortgage banking fees.



*Data Processing Fees.* For 2014, data processing fees totaled \$1.5 million compared to \$2.7 million for both 2013 and 2012. The decrease in 2014 compared to 2013 was attributable to the loss of a large government processing contract that began migrating to another processor in mid-2013, completing the transition in mid-2014. We currently maintain processing arrangements with four banks and two government agencies.

*Other.* Other noninterest income totaled \$4.9 million in 2014 compared to \$4.7 million in 2013 and \$4.5 million in 2012. The increase in 2014 compared to 2013 reflects higher bank owned life insurance income and working capital financing fees. The increase in 2013 compared to 2012 was due to higher bonus income received from our debit card processor reflecting renegotiation of our processing agreement.

### **Noninterest Expense**

Noninterest expense totaled \$114.4 million in 2014 compared to \$121.4 million in 2013 and \$123.9 million in 2012. For 2014, the \$7.0 million, or 5.8%, decrease was attributable to lower compensation expense of \$3.9 million, OREO expense of \$1.4 million, and other expense (excluding OREO expenses) of \$2.2 million, partially offset by higher occupancy expense of \$0.5 million. The reduction in compensation expense was primarily due to a decrease in pension plan expense partially offset by higher incentive expense for both cash and stock plans. Lower property carrying costs as well as a reduction in property valuation adjustments were the primary reasons for the reduction in OREO expense. The reduction in other expense was primarily attributable to lower FDIC insurance fees reflective of a favorable premium adjustment and reductions in both legal and professional fees. The increase in occupancy expense was due to higher maintenance contract costs reflective of security and technology upgrades and to a lesser extent higher building maintenance costs attributable to non-recurring expenditures.

For 2013, the \$2.5 million, or 2.0%, decrease was attributable to lower occupancy expense of \$0.7 million, OREO expense of \$2.6 million, and other expense (excluding OREO expenses) of \$1.1 million, partially offset by higher compensation of \$1.9 million. The reduction in OREO expense was due to lower carrying costs and valuation adjustments reflecting improving property values in our markets. Declines were realized in most of the occupancy expense categories and were generally driven by stronger cost controls and other cost reduction initiatives. Lower legal fees, professional fees, and miscellaneous expense contributed to the reduction in other expense. The increase in compensation expense was attributable to an increase in associate benefit expense of \$2.2 million, reflective of higher pension plan expense of \$1.0 million and stock compensation expense of \$0.9 million, partially offset by a \$0.3 million reduction in salary expense.

Our operating efficiency ratio (expressed as noninterest expense as a percent of taxable equivalent net interest income plus noninterest income) was 89.68%, 91.09% and 88.72% in 2014, 2013 and 2012, respectively. A reduction in net interest income as well as elevated expenses for OREO expense, FDIC insurance fees, and pension costs was the primary reasons for the elevated efficiency ratio for all periods.

Expense management is an important part of our culture and strategic focus and we will continue to review and evaluate opportunities to optimize our operations, reduce operating costs and manage our discretionary expenses.

The table below reflects the major components of noninterest expense.

(Dollars in Thousands)	2014	2013	2012
Salaries	\$48,896	\$48,584	\$48,925
Associate Benefits	13,319	17,543	15,317
Total Compensation	62,215	66,127	64,242
Premises	9,126	8,863	9,152
Equipment	8,692	8,468	8,903
Total Occupancy	17,818	17,331	18,055
Legal Fees	3,187	3,663	4,303
Professional Fees	3,732	4,304	4,882
Processing Services	6,062	5,396	3,967
Advertising	1,461	1,719	1,815
Travel and Entertainment	900	870	839
Printing and Supplies	865	994	1,154
Telephone	1,903	1,891	1,896
Postage	1,147	1,309	1,595
Insurance – Other	2,934	4,144	4,104
Intangible Amortization	32	210	431
Other Real Estate	6,811	8,234	10,812
Miscellaneous	5,291	5,213	5,848
Total Other Expense	34,325	37,947	41,646
Total Noninterest Expense	\$114,358	\$121,405	\$123,943

Various significant components of noninterest expense are discussed in more detail below.

*Compensation.* Compensation expense totaled \$62.2 million in 2014, \$66.1 million in 2013, and \$64.2 million in 2012. For 2014, the \$3.9 million, or 5.9%, decrease from 2013 was attributable to lower associate benefit expense of \$4.2 million partially offset by higher salary expense of \$0.3 million. The decrease in associate benefit expense reflects lower pension plan expense of \$5.0 million partially offset by higher stock compensation expense of \$0.5 million and associate insurance expense of \$0.3 million. The lower level of pension plan expense was attributable to the utilization of a higher discount rate (attributable to higher long-term rates at the end of 2013) for determining pension plan liabilities. Pension plan expense is determined by an external actuarial valuation based on assumptions that are evaluated annually, taking into consideration both current market conditions and anticipated long-term market conditions. A discussion of the sensitivity to these assumptions is detailed in the Critical Accounting Policy section of this report. Improved company performance drove the increase in stock compensation expense and rising health care costs contributed to the increase in associate insurance expense. The increase in salary expense was attributable to higher expense for our cash incentive plans reflective of improved individual and company performance. Lower associate salary expense reflective of reduced headcount partially offset the increase in cash incentives.

For 2013, the \$1.9 million, or 2.9%, increase was due to higher associate benefit expense of \$2.2 million partially offset by lower salary expense of \$0.3 million. The increase in associate benefit expense reflects higher expense for our pension plans of \$1.0 million primarily driven by the lower discount rate used for computing plan cost. Higher stock compensation expense of \$0.9 million also contributed to the increase reflecting an improvement in company performance. The reduction in salary expense was driven by a reduction in base salary expense of \$0.8 million attributable to further reduction in associate headcount that was partially offset by higher cash basis performance pay.

*Occupancy.* Occupancy expense (including premises and equipment) totaled \$17.8 million for 2014, \$17.3 million for 2013, and \$18.1 million for 2012. For 2014, the \$0.5 million, or 2.8%, increase over 2013 reflects higher premises expense of \$0.3 million and equipment expense of \$0.2 million. Higher building maintenance costs partially attributable to non-recurring expenditures drove the increase in premises expense. Higher maintenance contract costs reflective of security and technology upgrades drove the majority of the increase in equipment expense. For 2013, the \$0.7 million, or 4.0%, decline from 2012 was attributable to a reduction in premises expense of \$0.3 million and equipment expense of \$0.4 million. The decrease in premises expense was primarily driven by lower lease and utility expense. During 2012 and 2013, we did not renew leases on two banking offices. An internal energy efficiency program initiated in early 2013 drove the reduction in utility costs. The decrease in equipment expense reflects lower depreciation expense reflecting full depreciation of our item processing system as well as lower expense for maintenance agreements.

*Other.* Other noninterest expense totaled \$34.3 million in 2014, \$37.9 million in 2013, and \$41.6 million in 2012. For 2014, the \$3.6 million, or 9.5%, decrease from 2013 was primarily attributable to lower OREO expense of \$1.4 million, FDIC insurance fees of \$1.2 million, legal fees of \$0.5 million, and professional fees of \$0.6 million. Lower property carrying costs driven by strong property sales during the year as well as a reduction in property valuation adjustments reflective of improving property values were the primary reasons for the reduction in OREO expense. The decrease in FDIC insurance fees was attributable to a favorable premium adjustment due to our improved financial performance. Legal fees declined due to a lower level of legal support needed for problem loan resolutions. Lower audit costs and consulting costs drove the reduction in professional fees.

For 2013, the \$3.7 million, or 8.9%, decrease compared to 2012 reflects lower expense for OREO properties of \$2.6 million, legal fees of \$0.6 million, professional fees of \$0.6 million, postage of \$0.3 million, printing/supplies of \$0.2 million, intangible amortization of \$0.2 million, and miscellaneous expense of \$0.6 million, partially offset by higher processing services of \$1.4 million. OREO expense decreased due to lower property carrying costs and a reduction in net losses from the sale of properties reflecting improving property values in our markets. Lower legal costs to support collection/foreclosure activity and borrower bankruptcy proceedings drove the decline in legal fees. Professional fees decreased due to a reduction in cost for performing our goodwill analysis during the year as well as lower internal audits costs and real estate appraisal costs. The decline in postage costs reflects our initiative to migrate our clients to e-statements. Printing and supplies expense decreased due to stronger cost controls. Full amortization of our remaining core deposit intangible drove the decline in intangible amortization expense. The reduction in miscellaneous expense was attributable to the reclassification of our debit card processing costs to the processing services expense category. Processing services expense increased primarily due to the outsourcing of our item processing system in early 2013 and to a lesser extent the aforementioned reclassification of debit card processing costs.

## **Income Taxes**

For 2014, we realized income tax expense of \$1.7 million (effective tax rate of 15.2%) compared to income tax expense of \$1.9 million (effective tax rate of 24.2%) in 2013 and an income tax benefit of \$1.3 million (effective tax rate of 108.7%) in 2012. The tax provision for 2014 was favorably impacted by a \$2.2 million state tax benefit attributable to an adjustment in our reserve for uncertain tax positions associated with prior year matters. These tax matters have been fully resolved and should not impact our tax provision going forward. The tax provisions for 2013 and 2012 were favorably affected by the resolution of state tax contingencies totaling approximately \$0.8 million and \$0.3, respectively. In 2015, we would expect the effective tax rate to return to a more normalized level of 35% to 36%.

## **FINANCIAL CONDITION**

Average assets totaled approximately \$2.564 billion for the year 2014, consistent with 2013. Average interest earning assets were approximately \$2.238 billion, representing an increase of \$23.9 million, or 1.1%, over 2013. Year-over-year, average short-term investments decreased \$52.8 million, while investment securities increased \$113.5 million. Average gross loans declined \$36.8 million. We discuss these variances in more detail below.

Table 2 provides information on average balances and rates, Table 3 provides an analysis of rate and volume variances and Table 4 highlights the changing mix of our interest earning assets over the last three years.

## **Loans**

In 2014, average loans decreased \$36.8 million, or 2.5%, compared to a decrease of \$105.8 million, or 6.8%, in 2013. Loans as a percent of average earning assets declined to 63.2% in 2014, down from the 2013 and 2012 levels of 65.5% and 69.8%, respectively. Year-over-year average balances in the loan portfolio experienced runoff in all loan types except commercial loans and indirect auto loans, which grew year-over year. Although our core loan portfolio continues to be impacted by normal amortization, levels of payoffs and pay downs declined in 2014 compared to the prior year, and the loan portfolio began experiencing overall growth beginning in the first quarter of 2014.

Without compromising our credit standards or taking on inordinate interest rate risk, we have modified several lending programs in our business (commercial real estate and consumer portfolios) to try to mitigate the significant impact that consumer and business deleveraging is having on our portfolio. These programs, coupled with economic improvements in our anchor markets, have helped to increase overall production. On a year-over-year basis, period-end loans increased \$42.4 million, with the low point of loan balances occurring during the first quarter of 2014. These increases have occurred primarily in the commercial, construction, and indirect auto loan portfolios.

We originate mortgage loans secured by 1-4 family residential properties through our Residential Real Estate line of business, a majority of which are fixed-rate loans that are sold into the secondary market to third party purchasers on a best efforts delivery basis with servicing released. A majority of our adjustable rate loan product is retained in our loan portfolio.

**Table 4****SOURCES OF EARNING ASSET GROWTH**

(Average Balances – Dollars In Thousands)	2013 to 2014 Change	Percentage Total Change	Components of Average Earning Assets						
			2014	2013	2012				
<b>Loans:</b>									
Commercial, Financial, and Agricultural	\$4,174	17.0	%	5.9	%	5.8	%	6.0	%
Real Estate – Construction	(382 )	(2.0	)	1.8		1.9		1.8	
Real Estate – Commercial Mortgage	(64,520 )	(270.0	)	23.1		26.2		27.5	
Real Estate – Residential	(5,961 )	(25.0	)	14.1		14.5		16.3	
Real Estate – Home Equity	(4,512 )	(19.0	)	10.1		10.5		10.8	
Consumer	34,395	145.0		8.2		6.8		7.5	
Total Loans	\$(36,806 )	(154.0	)%	63.2	%	65.7	%	69.9	%
<b>Investment Securities:</b>									
Taxable	\$130,220	544.0	%	16.2	%	10.5	%	10.0	%
Tax-Exempt	(16,718 )	(70.0	)	4.1		4.9		2.9	
Total Securities	113,502	474.0		20.3		15.4		12.9	
Funds Sold	(52,759 )	(220.0	)	16.5		18.9		17.2	
Total Earning Assets	\$23,937	100.0	%	100.0%		100.0%		100.0%	

Our average loan-to-deposit ratio decreased to 67.5% in 2014 from 70.1% in 2013. The lower loan-to-deposit ratio reflects both the decline in average loan balances, and growth in average deposits.

The composition of our loan portfolio at December 31<sup>st</sup> for each of the past five years is shown in Table 5. Table 6 arrays our total loan portfolio as of December 31, 2014, based upon maturities. As a percent of the total portfolio, loans with fixed interest rates represent 32.2% as of December 31, 2014, unchanged from December 31, 2013.

**Table 5****LOANS BY CATEGORY**

(Dollars in Thousands)	2014	2013	2012	2011	2010
Commercial, Financial and Agricultural	\$136,925	\$126,607	\$139,850	\$130,879	\$157,394
Real Estate – Construction <sup>f)</sup>	43,472	36,187	43,740	26,367	43,239
Real Estate – Commercial Mortgage	510,120	533,871	613,625	639,140	671,702
Real Estate – Residential <sup>f)</sup>	304,781	315,582	329,947	399,371	430,541
Real Estate – Home Equity	229,572	227,922	236,263	244,263	251,565

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Consumer	217,192	159,500	157,877	188,663	204,230
Total Loans, Net of Unearned Income	\$1,442,062	\$1,399,669	\$1,521,302	\$1,628,683	\$1,758,671

*(1) Includes loans held for sale.*

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**Table 6****LOAN MATURITIES**

(Dollars in Thousands)	Maturity Periods			Total
	One Year or Less	Over One Through Five Years	Over Five Years	
Commercial, Financial and Agricultural	\$56,288	\$61,770	\$18,867	\$136,925
Real Estate – Construction	38,289	2,542	2,641	43,472
Real Estate – Commercial Mortgage	59,368	100,663	350,089	510,120
Real Estate – Residential	29,753	42,290	232,738	304,781
Real Estate – Home Equity	593	46,855	182,124	229,572
Consumer <sup>(1)</sup>	13,822	193,695	9,675	217,192
<b>Total</b>	<b>\$198,113</b>	<b>\$447,815</b>	<b>\$796,134</b>	<b>\$1,442,062</b>
Loans with Fixed Rates	\$82,374	\$322,696	\$59,800	\$464,870
Loans with Floating or Adjustable Rates	115,739	125,119	736,334	977,192
<b>Total</b>	<b>\$198,113</b>	<b>\$447,815</b>	<b>\$796,134</b>	<b>\$1,442,062</b>

*(1) Demand loans and overdrafts are reported in the category of one year or less.*

**Risk Element Assets**

Risk element assets consist of nonaccrual loans, OREO, TDRs, past due loans, potential problem loans, and loan concentrations. Table 7 depicts certain categories of our risk element assets as of December 31<sup>st</sup> for each of the last five years. Activity within our nonperforming asset portfolio is provided below in Table 8.

Nonperforming assets (nonaccrual loans and OREO) totaled \$52.4 million at year-end 2014 compared to \$85.0 million at year-end 2013. Nonaccrual loans totaled \$16.8 million at year-end 2014, a decrease of \$20.2 million from year-end 2013, reflective of loan resolutions (charge-offs, transfer of loans to OREO, and payments) and loans restored to an accrual status, which outpaced gross additions. Gross additions declined by \$22 million and \$17 million in 2014 and 2013, respectively. The balance of OREO totaled \$35.7 million at year-end 2014, a decrease of \$12.4 million from year-end 2013. We continued to experience progress during 2014 in our efforts to dispose of OREO selling properties totaling \$23.8 million compared to \$25.9 million in 2013. Nonperforming assets represented 2.00% of total assets at December 31, 2014 compared to 3.26% at December 31, 2013.

We continue to allocate significant resources to reduce our level of nonperforming assets, while mitigating losses and 2014 was another productive year in this respect.

Table 7

**RISK ELEMENT ASSETS**

(Dollars in Thousands)	2014	2013	2012	2011	2010
Nonaccruing Loans:					
Commercial, Financial and Agricultural	\$507	\$188	\$1,069	\$755	\$1,059
Real Estate – Construction	424	426	4,071	334	1,907
Real Estate – Commercial Mortgage	5,806	25,227	41,045	42,820	26,874
Real Estate – Residential	6,737	6,440	13,429	25,671	30,189
Real Estate – Home Equity	2,544	4,084	4,034	4,283	4,803
Consumer	751	599	574	1,160	868
Total Nonperforming Loans (“NPLs” <sup>(1)</sup> )	\$16,769	\$36,964	\$64,222	\$75,023	\$65,700
Other Real Estate Owned	35,680	48,071	53,426	62,600	57,937
Total Nonperforming Assets (“NPAs”)	\$52,449	\$85,035	\$117,648	\$137,623	\$123,637
Past Due Loans 30 – 89 Days	\$6,792	\$7,746	\$9,934	\$19,425	\$24,193
Past Due Loans 90 Days or More (accruing)	—	—	—	224	159
Performing Troubled Debt Restructurings	\$44,409	\$44,764	\$47,474	\$37,675	\$21,649
Nonperforming Loans/Loans	1.16 %	2.64 %	4.22 %	4.61 %	3.74 %
Nonperforming Assets/Total Assets	2.00	3.26	4.47	5.21	4.72
Nonperforming Assets/Loans Plus OREO	3.55	5.87	7.47	8.14	6.81
Allowance/Nonperforming Loans	104.60%	62.48 %	45.42 %	41.37 %	53.94 %

<sup>(1)</sup> Nonaccrual TDRs totaling \$2.2 million and \$11.0 million are included in nonaccrual/NPL totals for December 31, 2014 and December 31, 2013, respectively.

**Table 8****NONPERFORMING ASSET ACTIVITY**

(Dollars in Thousands)	2014	2013
NPA Beginning Balance:	\$85,035	\$117,648
Change in Nonaccrual Loans:		
Beginning Balance	36,964	64,222
Additions	22,466	44,070
Charge-Offs	(8,857 )	(11,523 )
Transferred to OREO	(13,888)	(23,355 )
Paid Off/Payments	(9,639 )	(18,311 )
Restored to Accrual	(10,277)	(18,139 )
Ending Balance	16,769	36,964
Change in OREO:		
Beginning Balance	48,071	53,426
Additions <sup>(1)</sup>	15,271	24,488
Valuation Write-downs	(3,142 )	(3,592 )
Sales	(23,791)	(25,940 )
Other	(729 )	(311 )
Ending Balance	35,680	48,071
NPA Net Change	(32,586)	(32,613 )
NPA Ending Balance	\$52,449	\$85,035

<sup>(1)</sup> *The difference in OREO additions and nonaccrual loans transferred to OREO represents loans migrating to OREO status that were not in a nonaccrual status in a prior period.*

*Nonaccrual Loans.* Nonaccrual loans totaled \$16.8 million at year-end 2014, a decrease of \$20.2 million from year-end 2013. Gross additions to nonaccrual status during 2014 totaled \$22.5 million compared to \$44.1 million in 2013. A majority of the year-over-year decrease in nonaccrual loans was realized in the commercial mortgage loan category.

Generally, loans are placed on nonaccrual status if principal or interest payments become 90 days past due and/or management deems the collectability of the principal and/or interest to be doubtful. Once a loan is placed in nonaccrual status, all previously accrued and uncollected interest is reversed against interest income. Interest income on nonaccrual loans is recognized when the ultimate collectability is no longer considered doubtful. Loans are returned to accrual status when the principal and interest amounts contractually due are brought current or when future payments are reasonably assured. If interest on our loans classified as nonaccrual during 2014 had been recognized on a fully accruing basis, we would have recorded an additional \$1.5 million of interest income for the year ended December 31, 2014.

*Other Real Estate Owned.* OREO represents property acquired as the result of borrower defaults on loans or by receiving a deed in lieu of foreclosure. OREO is recorded at the lower of cost or estimated fair value, less estimated selling costs, at the time of foreclosure. Write-downs occurring at foreclosure are charged against the allowance for loan losses. On an ongoing basis, properties are either revalued internally or by a third party appraiser as required by applicable regulations. Subsequent declines in value are reflected as other noninterest expense. Carrying costs related to maintaining the OREO properties are expensed as incurred and are also reflected as other noninterest expense.

OREO totaled \$35.7 million at December 31, 2014 versus \$48.1 million at December 31, 2013. During 2014, we added properties totaling \$15.3 million and partially or completely liquidated properties totaling \$23.8 million. Revaluation adjustments for other real estate owned properties during 2014 totaled \$3.1 million and were charged to noninterest expense when realized. For 2013, we added properties totaling \$24.5 million and partially or completely liquidated properties totaling \$26.3 million. Revaluation adjustments for other real estate owned properties during 2013 totaled \$3.6 million and were charged to noninterest expense when realized.

The composition of our OREO portfolio as of December 31 is provided in the table below.

(Dollars in Thousands)	2014	2013
Lots/Land	\$19,405	\$29,821
Residential 1-4	4,430	3,964
Commercial Building	10,197	12,702
Other	1,648	1,584
Total OREO	\$35,680	\$48,071

*Troubled Debt Restructurings.* TDRs are loans on which, due to the deterioration in the borrower's financial condition, the original terms have been modified and deemed a concession to the borrower. From time to time we will modify a loan as a workout alternative. Most of these instances involve a principal moratorium, extension of the loan term, or interest rate reduction.

Loans classified as TDRs at year-end 2014 totaled \$46.7 million compared to \$55.8 million at year-end 2013. Accruing TDRs make up approximately \$44.4 million, or 95%, of our TDR portfolio at year-end 2014 of which \$2.1 million was over 30 days past due. The weighted average rate for the loans within the accruing TDR portfolio is 5.2%. During 2014, we modified 28 loan contracts totaling approximately \$4.1 million of which four loan contracts totaling \$0.4 million have defaulted. Our TDR default rate (default balance as a percentage of average TDRs) during 2014 and 2013 was 16% and 10%, respectively.

The composition of our TDR portfolio as of December 31 is provided in the table below.

(Dollars in Thousands)	2014		2013	
	Accruing	Nonaccruing <sup>(1)</sup>	Accruing	Nonaccruing <sup>(1)</sup>
Commercial, Financial and Agricultural	\$838	\$ 266	\$1,511	\$ —
Real Estate – Construction	—	—	156	—
Real Estate – Commercial Mortgage	26,565	—	24,735	10,308
Real Estate – Residential	14,940	1,622	16,441	458
Real Estate – Home Equity	1,856	356	1,576	241
Consumer	211	—	345	—
Total TDRs	\$44,410	\$ 2,244	\$44,764	\$ 11,007

<sup>(1)</sup> *Nonaccruing TDRs are included in nonaccrual/NPL totals and NPA/NPL ratio calculations.*

Activity within our TDR portfolio is provided in the table below.

(Dollars in Thousands)	2014	2013
TDR Beginning Balance:	\$55,770	\$57,353
Additions	4,978	12,742
Charge-Offs	(370 )	(1,018 )
Paid Off/Payments	(5,573 )	(5,724 )
Removal Due to Change in TDR Status	(73 )	(1,632 )
Defaults	(8,078 )	(5,950 )
TDR Ending Balance	\$46,654	\$55,771

*Past Due Loans.* A loan is defined as a past due loan when one full payment is past due or a contractual maturity is over 30 days past due. Past due loans at year-end 2014 totaled \$6.8 million compared to \$7.7 million at year-end 2013.

*Potential Problem Loans.* Potential problem loans are defined as those loans which are now current but where management has doubt as to the borrower's ability to comply with present loan repayment terms. At December 31, 2014, we had \$6.4 million in loans of this type which are not included in either of the nonaccrual, TDR or 90 day past due loan categories compared to \$7.4 million at December 31, 2013. Management monitors these loans closely and reviews their performance on a regular basis.

*Loan Concentrations.* Loan concentrations are considered to exist when there are amounts loaned to multiple borrowers engaged in similar activities which cause them to be similarly impacted by economic or other conditions and such amount exceeds 10% of total loans. Due to the lack of diversified industry within the markets served by the Bank and the relatively close proximity of the markets, we have both geographic concentrations as well as concentrations in the types of loans funded. Specifically, due to the nature of our markets, a significant portion of the loan portfolio has historically been secured with real estate, approximately 75% at year-end 2014 and 79% at year-end 2013. The primary types of real estate collateral are commercial properties and 1-4 family residential properties. At December 31, 2014, commercial real estate and residential real estate mortgage loans (including home equity loans) accounted for 35.4% and 37.1%, respectively, of the total loan portfolio.

The following table summarizes our real estate loan portfolio as segregated by the type of property. Property type concentrations are stated as a percentage of year-end total real estate loans.

	2014		2013		
	Investor Real Estate	Owner Occupied Real Estate	Investor Real Estate	Owner Occupied Real Estate	
Vacant Land, Construction, and Land Development	10.0%	—	10.0%	—	
Improved Property	22.0%	68.0	% 23.2%	66.8	%
Total Real Estate Loans	32.0%	68.0	% 33.2%	66.8	%

A major portion of our real estate loan portfolio is centered in the owner occupied category which carries a lower risk of non-collection than certain segments of the investor category. Approximately 74% of the land/construction category was secured by residential real estate at year-end 2014.

#### Allowance for Loan Losses

Management believes it maintains the allowance for loan losses at a level sufficient to provide for probable credit losses inherent in the loan portfolio as of the balance sheet date. Credit losses arise from the borrowers' inability or unwillingness to repay, and from other risks inherent in the lending process including collateral risk, operations risk, concentration risk, and economic risk. As such, all related risks of lending are considered when assessing the adequacy of the allowance. The allowance for loan losses is established through a provision charged to expense. Loans are charged-off against the allowance when losses are probable and reasonably quantifiable. The allowance for loan losses is based on management's judgment of overall credit quality. This is a significant estimate based on a detailed analysis of the loan portfolio. The balance can and will change based on revisions to our assessment of the loan portfolio's overall credit quality and other risk factors both internal and external to us.

Management evaluates the adequacy of the allowance for loan losses on a quarterly basis. The allowance consists of two components. The first component consists of amounts reserved for impaired loans. A loan is deemed impaired when, based on current information and events, it is probable that the company will not be able to collect all amounts due (principal and interest payments), according to the contractual terms of the loan agreement. Loans are monitored for potential impairment through our ongoing loan review procedures and portfolio analysis. Classified loans and past due loans over a specific dollar amount, and all troubled debt restructurings are individually evaluated for impairment.

The approach for assigning reserves for the impaired loans is determined by the dollar amount of the loan and loan type. Impairment measurement for loans over a specific dollar are assigned on an individual loan basis with the amount reserved dependent on whether repayment of the loan is dependent on the liquidation of collateral or from some other source of repayment. If repayment is dependent on the sale of collateral, the reserve is equivalent to the

recorded investment in the loan less the fair value of the collateral after estimated sales expenses. If repayment is not dependent on the sale of collateral, the reserve is equivalent to the recorded investment in the loan less the estimated cash flows discounted using the loan's effective interest rate. The discounted value of the cash flows is based on the anticipated timing of the receipt of cash payments from the borrower. The reserve allocations for individually measured impaired loans are sensitive to the extent market conditions or the actual timing of cash receipts change. Impairment reserves for smaller-balance loans under a specific dollar amount are assigned on a pooled basis utilizing loss factors for impaired loans of a similar nature.

The second component is a general reserve on all loans other than those identified as impaired. General reserves are assigned to various homogenous loan pools, including commercial, commercial real estate, construction, residential 1-4 family, home equity, and consumer. General reserves are assigned based on historical loan loss ratios determined by loan pool and internal risk rating that are adjusted for various internal and external risk factors unique to each loan pool.

Table 9 analyzes the activity in the allowance over the past five years.

For 2014, our net charge-offs totaled \$7.5 million, or 0.53%, of average loans, compared to \$9.5 million, or 0.66%, for 2013, and \$18.0 million, or 1.16%, for 2012. Lower residential and construction loan charge-offs of \$1.6 million and \$1.1 million, respectively, drove the decrease in net charge-offs in 2014. Reductions in residential and commercial real estate loan charge-offs of \$5.9 million and \$2.4 million, respectively, drove the decline in net charge-offs in 2013. At year-end 2014, the allowance for loan losses of \$17.5 million was 1.22% of outstanding loans (net of overdrafts) and provided coverage of 105% of nonperforming loans compared to 1.65% and 62%, respectively, at year-end 2013, and 1.93% and 45%, respectively, at year-end 2012.

Table 10 provides an allocation of the allowance for loan losses to specific loan types for each of the past five years. The reserve allocations, as calculated using the above methodology, are assigned to specific loan categories corresponding to the type represented within the components discussed.



The reduction in the allowance for loan losses from December 31, 2013 to December 31, 2014 was primarily attributable to a decline in general reserves reflective of slower problem loan migration, lower loan loss experience, as well as continued improvement in credit quality metrics. A decrease in our impaired loan balance and related reserves contributed to a lesser extent and reflects slower inflow and successful resolutions, as well as lower loss content. It is management's opinion that the allowance at December 31, 2014 is adequate to absorb probable losses inherent in the loan portfolio at year-end. The reduction in the allowance for loan losses from December 31, 2012 to December 31, 2013 was primarily attributable to a decline in impaired loan reserves and to a lesser extent lower general reserves. Successful impaired loan resolutions and slower inflow drove the decrease in impaired loan reserves. The reduction in general reserves was primarily attributable to favorable problem loan migration and lower loan loss experience. In 2013, we incorporated subjective factors of estimation risk into each loan category which eliminated the unallocated portion of the allowance.

**Table 9****ANALYSIS OF ALLOWANCE FOR LOAN LOSSES**

(Dollars in Thousands)	2014	2013	2012	2011	2010
Balance at Beginning of Year	\$23,095	\$29,167	\$31,035	\$35,436	\$43,999
Charge-Offs:					
Commercial, Financial and Agricultural	871	748	822	1,843	2,118
Real Estate - Construction	28	1,070	629	114	5,877
Real Estate - Commercial	3,788	3,651	6,031	6,713	8,762
Real Estate - Residential	2,160	3,835	9,719	11,870	12,168
Real Estate - Home Equity	1,379	1,159	2,896	2,727	3,087
Consumer	1,820	1,751	2,125	2,924	3,502
Total Charge-Offs	10,046	12,214	22,222	26,191	35,514
Recoveries:					
Commercial, Financial and Agricultural	214	209	290	387	370
Real Estate - Construction	9	1	43	14	8
Real Estate - Commercial	468	363	682	251	261
Real Estate - Residential	752	838	1,291	478	385
Real Estate - Home Equity	141	294	399	214	555
Consumer	1,001	965	1,483	1,450	1,548
Total Recoveries	2,585	2,670	4,188	2,794	3,127
Net Charge-Offs	7,461	9,544	18,034	23,397	32,387
Provision for Loan Losses	1,905	3,472	16,166	18,996	23,824
Balance at End of Year	\$17,539	\$23,095	\$29,167	\$31,035	\$35,436
Ratio of Net Charge-Offs to Average Loans Outstanding	0.53 %	0.66 %	1.16 %	1.39 %	1.77 %
	1.22 %	1.65 %	1.93 %	1.91 %	2.01 %

Allowance for Loan Losses as a Percent of Loans at End of  
Year

Allowance for Loan Losses as a Multiple of Net  
Charge-Offs  
45

2.35 x 2.42 x 1.62 x 1.33 x 1.09 x

**Table 10****ALLOCATION OF ALLOWANCE FOR LOAN LOSSES**

	2014		2013		2012		2011		2010	
	Allow- ance Amount	Percent of Loans in Each Category To Total Loans	Allow- ance Amount	Percent of Loans in Each Category To Total Loans	Allow- ance Amount	Percent of Loans in Each Category To Total Loans	Allow- ance Amount	Percent of Loans in Each Category To Total Loans	Allow- ance Amount	Percent of Loans in Each Category To Total Loans
(Dollars in Thousands)										
Commercial, Financial and Agricultural Real Estate:	\$784	9.5 %	\$699	9.0 %	\$1,253	9.2 %	\$1,534	8.0 %	\$1,544	8.9 %
Construction	843	3.0	1,580	2.6	2,856	2.9	1,133	1.6	2,060	2.5
Commercial	5,287	35.4	7,710	38.1	11,081	40.3	10,660	39.2	8,645	38.2
Residential	6,520	21.1	9,073	22.6	8,678	21.7	12,518	24.5	17,046	24.5
Home Equity	2,882	15.9	3,051	16.3	2,945	15.5	2,392	15.0	2,522	14.3
Consumer	1,223	15.1	982	11.4	1,327	10.4	1,887	11.7	2,612	11.6
Not Allocated	—	—	—	—	1,027	—	911	—	1,007	—
Total	\$17,539	100.0%	\$23,095	100.0%	\$29,167	100.0%	\$31,035	100.0%	\$35,436	100.0%

**Investment Securities**

In 2014, our average investment portfolio increased \$113.5 million, or 33.4%, from 2013 and increased \$51.2 million, or 17.7%, from 2012 to 2013. As a percentage of average earning assets, the investment portfolio represented 20.3% in 2014, compared to 15.4% in 2013. In both 2013 and 2014, the increase in the average balance of the investment portfolio resulted from strategically growing investment purchases to better deploy our overnight funds and improve the overall composition of our earning assets. In 2015, we will continue to closely monitor liquidity levels and pledging requirements to assess the need to purchase additional investments, as well as look for new investment products that are prudent relative to our risk profile and the Bank's overall investment strategy.

The investment portfolio is a significant component of our operations and, as such, it functions as a key element of liquidity and asset/liability management. Two types of classifications are approved for investment securities which are Available-for-Sale ("AFS") and Held-for-Maturity ("HTM"). In 2013 and 2014, securities were purchased under both the AFS and HTM designations. As of December 31, 2014, \$332.8 million, or 67.1% of the investment portfolio was classified as AFS, with the remaining \$163.4 million classified as HTM.

In 2014, average taxable investments increased \$130.2 million, or 56.1%, while tax-exempt investments decreased \$16.7 million, or 15.5%. Taxable investments increased as part of our overall investment strategy in 2014. Short-term yields improved during the year making these investments more attractive. Average balances of tax-exempt investments decreased as high quality non-taxable securities with attractive spreads were less readily available in 2014. Management will continue to purchase municipal issues as they become available and when it considers the yield to be attractive.

At acquisition, the classification of the security will be determined based on how the purchase will affect the company's asset/liability strategy and future business plans and opportunities. Such decisions will be weighed against multiple factors, including regulatory capital requirements, volatility in earnings or other comprehensive income, and liquidity needs. Securities in the AFS portfolio are recorded at fair value with unrealized gains and losses associated with these securities recorded net of tax, in the accumulated other comprehensive income (loss) component of shareowners' equity. Securities that are HTM will be acquired or owned with the intent of holding them to maturity (final payment date). HTM investments are measured at amortized cost. It is neither management's current intent nor practice to participate in the trading of investment securities for the purpose of recognizing gains and therefore we do not maintain a trading portfolio.

At December 31, 2014, the investment portfolio maintained a net pre-tax unrealized gain of \$0.5 million in the AFS portfolio compared to a net pre-tax unrealized gain of \$0.3 million at December 31, 2013. At December 31, 2014, there were 157 positions (combined AFS and HTM) with unrealized losses totaling \$0.7 million. Of the 157 positions, 84 were Ginnie Mae mortgage-backed securities (GNMA), US Treasuries, or SBA securities, all of which carry the full faith and credit guarantee of the US Government. SBA securities float monthly or quarterly to the prime rate and are uncapped. There were 24 SBA positions and 24 GMNA positions in an unrealized loss position for longer than 12 months, and have unrealized losses of \$231,000 and \$88,000, respectively. There were 64 municipal bonds in an unrealized loss position that were pre-refunded, or rated "AA-" or better. One of these positions was in an unrealized loss position for longer than 12 months, and had an unrealized loss of \$5,000. The remaining nine securities are Federal Farm Credit or Federal Home Loan Bank agency bonds, none of which have been in an unrealized loss position for longer than 12 months. No positions with unrealized losses are considered impaired, and all positions are expected to mature at par or better.

The average maturity of the total portfolio at December 31, 2014 and 2013 was 2.17 and 1.95 years, respectively. Balances in all asset classes increased compared to last year with the exception of GNMA mortgage-backed securities and non-taxable municipal bonds. Purchases of U.S. Treasuries with maturities out to three and one-half years were added in 2014 which extended the average life of the investment portfolio. See Table 12 for a breakdown of maturities by investment type.

The weighted average taxable equivalent yield of the investment portfolio at December 31, 2014 was 1.00% versus 0.94% in 2013. This higher yield was a result of most new purchases being made at higher market rates during 2014. Our bond portfolio contained no investments in obligations, other than U.S. Governments, of any one state, municipality, political subdivision or any other issuer that exceeded 10% of our shareholders' equity at December 31, 2014. New investments continue to be made selectively in short-duration, high quality bonds.

Table 11 and Table 12 present a detailed analysis of our investment securities as to type, maturity and yield at December 31.

**Table 11**

**INVESTMENT SECURITIES BY CATEGORY**

(Dollars in Thousands)	2014		2013		2012	
	Carrying Amount	Percent	Carrying Amount	Percent	Carrying Amount	Percent
Available for Sale						
U.S. Government Treasury	\$186,031	37 %	\$71,833	18 %	\$97,249	33 %
U.S. Government Agency	96,097	19 %	75,146	19 %	51,664	17 %
States and Political Subdivisions	2,287	— %	91,753	23 %	79,879	27 %
Mortgage-Backed Securities	48,388	10 %	2,795	1 %	56,982	19 %

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Equity Securities	8,745	2 %	9,893	2 %	11,211	4 %
Total	341,548	68 %	251,420	63 %	296,985	100 %
Held to Maturity						
U.S. Government Treasury	76,179	15 %	43,533	11 %	—	— %
U.S. Government Agency	19,807	4 %	15,794	4 %	—	— %
States and Political Subdivisions	40,878	8 %	33,216	8 %	—	— %
Mortgage-Backed Securities	26,717	5 %	55,668	14 %	—	— %
Total	163,581	32 %	148,211	37 %	—	— %
Total Investment Securities	\$505,129	100 %	\$399,631	100 %	296,985	100 %

**Table 12****MATURITY DISTRIBUTION OF INVESTMENT SECURITIES**

(Dollars in Thousands)	Within 1 year		1 - 5 years		5 - 10 years		After 10 years		Total	
	Amount	WAY <sup>(3)</sup>	Amount	WAY <sup>(3)</sup>	Amount	WAY <sup>(3)</sup>	Amount	WAY <sup>(3)</sup>	Amount	WAY <sup>(3)</sup>
Available for Sale										
U.S. Government Treasury	\$ 14,222	0.34 %	\$ 171,809	0.92 %	\$—	— %	\$—	— %	\$ 186,031	0.88 %
U.S. Government Agency	11,841	0.45	84,256	0.84	—	—	—	—	96,097	0.79
States and Political Subdivisions	20,620	0.81	27,768	1.06	—	—	—	—	48,388	0.95
Mortgage-Backed Securities <sup>(1)</sup>	136	1.91	2,097	5.08	54	1.54	—	—	2,287	4.81
Other Securities <sup>(2)</sup>	—	—	—	—	—	—	8,745	5.15	8,745	5.15
Total	\$46,819	0.58 %	\$285,930	0.94 %	\$54	1.54 %	\$8,745	5.15 %	\$341,548	1.00 %
Held to Maturity										
U.S. Government Treasury	\$—	— %	\$76,179	0.83 %	\$—	— %	\$—	— %	\$76,179	0.83 %
U.S. Government Agency	—	—	19,807	0.79	—	—	—	—	19,807	0.79
States and Political Subdivisions	17,958	0.60	8,759	0.90	—	—	—	—	26,717	0.70
Mortgage-Backed Securities <sup>(1)</sup>	3,983	1.24	36,895	1.72	—	—	—	—	40,878	1.67
Total	\$21,941	0.72 %	\$141,640	1.06 %	\$—	— %	\$—	— %	\$163,581	1.02 %
Total Investment Securities	\$68,760	0.63 %	\$427,570	0.98 %	\$54	1.54 %	\$8,745	5.15 %	\$505,129	1.01 %

<sup>(1)</sup>Based on weighted-average life.

<sup>(2)</sup>Federal Home Loan Bank Stock and Federal Reserve Bank Stock are included in this category for weighted average yield, but do not have stated maturities.

<sup>(3)</sup>Weighted average yield calculated based on current amortized cost balances – not presented on a tax equivalent basis.

## Deposits and Funds Purchased

Average total deposits for the year were \$2.093 billion; an increase of \$23.4 million, or 1.1%, compared to the same period in 2013 and deposits decreased \$35.6 million, or 1.7%, from 2012 to 2013. Increases in noninterest bearing deposits and savings accounts were partially offset by declines in the remaining product types. The decline occurring from 2012 to 2013 was attributable to decreases in NOW accounts and certificates of deposit, and was partially offset by increases in noninterest bearing deposits, money market accounts, and savings accounts.

As is typical, the seasonal inflow of public funds started in the fourth quarter of 2014 and is expected to continue through the first quarter of 2015. Deposit levels remain strong and our mix of deposits continues to improve slightly as higher cost certificates of deposit are replaced with lower rate non-maturity deposits and noninterest bearing demand accounts. Prudent pricing discipline will continue to be the key to managing our mix of deposits. Our strategy is to manage the mix of our deposits rather than compete on rate, which enables us to maintain an exceptionally low cost of funds – 15 basis points in the fourth quarter and 16 basis points for the year 2014.

Average total deposits were \$2.077 billion for the fourth quarter of 2014, an increase of \$14.5 million, or 0.7%, from the third quarter of 2014. The higher level of deposits when compared to the prior period reflects higher noninterest bearing deposits and NOW accounts (reflecting the inflow of public funds), and savings accounts, partially offset by declines in money markets and certificates of deposit.

Table 2 provides an analysis of our average deposits, by category, and average rates paid thereon for each of the last three years. Table 13 reflects the shift in our deposit mix over the last year and Table 13 provides a maturity distribution of time deposits in denominations of \$100,000 and over at December 31, 2014.

Average short-term borrowings, which include federal funds purchased, securities sold under agreements to repurchase, FHLB advances (maturing in less than one year), and other borrowings, decreased \$9.5 million, or 17.7% in 2014. The lower balance is attributable to decreases in both repurchase agreements and other borrowed funds by \$5.4 million and \$4.1 million, respectively. See Note 7 in the Notes to Consolidated Financial Statements for further information on short-term borrowings.

We continue to focus on the value of our deposit franchise, which produces a strong base of core deposits with minimal reliance on wholesale funding.

### Table 13

## SOURCES OF DEPOSIT GROWTH



(Average Balances - Dollars in Thousands)	2013 to	Percentage	Components of		
	2014	of Total	Total Deposits		
	Change	Change	2014	2013	2012
Noninterest Bearing Deposits	\$40,071	171.2 %	32.1 %	30.5 %	29.0 %
NOW Accounts	(3,647 )	(15.6 )	34.2	34.8	36.6
Money Market Accounts	(11,153)	(47.6 )	13.0	13.7	13.3
Savings	23,351	99.8	10.9	9.8	8.3
Time Deposits	(25,218)	(107.8 )	9.8	11.2	12.8
Total Deposits	\$23,404	100.0 %	100.0%	100.0%	100.0%

**Table 14****MATURITY DISTRIBUTION OF CERTIFICATES OF DEPOSIT \$100,000 OR OVER**

(Dollars in Thousands)	2014	Percent
	Time Certificates of Deposit	
Three months or less	\$ 16,830	32.0 %
Over three through six months	13,031	24.8
Over six through twelve months	16,518	31.4
Over twelve months	6,232	11.8
Total	\$ 52,611	100.0 %

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## Market Risk and Interest Rate Sensitivity

*Overview.* Market risk arises from changes in interest rates, exchange rates, commodity prices, and equity prices. We have risk management policies to monitor and limit exposure to market risk and do not participate in activities that give rise to significant market risk involving exchange rates, commodity prices, or equity prices. In asset and liability management activities, our policies are designed to minimize structural interest rate risk.

*Interest Rate Risk Management.* Our net income is largely dependent on net interest income. Net interest income is susceptible to interest rate risk to the degree that interest-bearing liabilities mature or reprice on a different basis than interest-earning assets. When interest-bearing liabilities mature or reprice more quickly than interest-earning assets in a given period, a significant increase in market rates of interest could adversely affect net interest income. Similarly, when interest-earning assets mature or reprice more quickly than interest-bearing liabilities, falling interest rates could result in a decrease in net interest income. Net interest income is also affected by changes in the portion of interest-earning assets that are funded by interest-bearing liabilities rather than by other sources of funds, such as noninterest-bearing deposits and shareowners' equity.

We have established a comprehensive interest rate risk management policy, which is administered by management's Asset Liability Management Committee ("ALCO"). The policy establishes limits of risk, which are quantitative measures of the percentage change in net interest income (a measure of net interest income at risk) and the fair value of equity capital (a measure of economic value of equity ("EVE") at risk) resulting from a hypothetical change in interest rates for maturities from one day to 30 years. We measure the potential adverse impacts that changing interest rates may have on our short-term earnings, long-term value, and liquidity by employing simulation analysis through the use of computer modeling. The simulation model captures optionality factors such as call features and interest rate caps and floors imbedded in investment and loan portfolio contracts. As with any method of gauging interest rate risk, there are certain shortcomings inherent in the interest rate modeling methodology used by us. When interest rates change, actual movements in different categories of interest-earning assets and interest-bearing liabilities, loan prepayments, and withdrawals of time and other deposits, may deviate significantly from assumptions used in the model. Finally, the methodology does not measure or reflect the impact that higher rates may have on adjustable-rate loan clients' ability to service their debts, or the impact of rate changes on demand for loan and deposit products.

We prepare a current base case and four alternative interest rate simulations (Down 100, Up 100, Up 200 and Up 300) basis points, at least once per quarter, and report the analysis to ALCO, our Market Risk Oversight Committee ("MROC"), our Enterprise Risk Oversight Committee ("EROC") and the Board of Directors. In addition, more frequent forecasts may be produced when interest rates are particularly uncertain or when other business conditions so dictate.

Our interest rate risk management goal is to avoid unacceptable variations in net interest income and capital levels due to fluctuations in market rates. Management attempts to achieve this goal by balancing, within policy limits, the volume of floating-rate liabilities with a similar volume of floating-rate assets, by keeping the average maturity of fixed-rate asset and liability contracts reasonably matched, by managing the mix of our core deposits, and by adjusting our rates to market conditions on a continuing basis.

The balance sheet is subject to testing for interest rate shock possibilities to indicate the inherent interest rate risk. Average interest rates are shocked by plus or minus 100, 200, and 300 basis points (“bp”), although we may elect not to use particular scenarios that we determined are impractical in a current rate environment. It is management’s goal to structure the balance sheet so that net interest earnings at risk over a 12-month period and the economic value of equity at risk do not exceed policy guidelines at the various interest rate shock levels.

We augment our interest rate shock analysis with alternative external interest rate scenarios on a quarterly basis. These alternative interest rate scenarios may include non-parallel rate ramps.

*Analysis.* Measures of net interest income at risk produced by simulation analysis are indicators of an institution’s short-term performance in alternative rate environments. These measures are typically based upon a relatively brief period, usually one year. They do not necessarily indicate the long-term prospects or economic value of the institution.

**ESTIMATED CHANGES IN NET INTEREST INCOME<sup>(1)</sup>**

Changes in Interest Rates	+300 bp	+200 bp	+100 bp	-100 bp
Policy Limit	-10.0%	-7.5 %	-5.0 %	-5.0 %
December 31, 2014	2.7 %	4.0 %	-1.1 %	-2.9 %
December 31, 2013	11.0 %	10.7 %	7.4 %	-1.8 %

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The Net Interest Income at Risk position improved for the month ended December 2014, when compared to the same period in 2013 for all rising rate scenarios. Our largest exposure is when rates decline 100 basis points, with a measure of -2.9%, which remains within our policy limit of -5.0%. The year-over-year unfavorable variance is primarily attributable to lower levels of overnight funds, offset by higher investments and performing loan portfolios. All measures of net interest income at risk are within our prescribed policy limits.

The measures of equity value at risk indicate our ongoing economic value by considering the effects of changes in interest rates on all of our cash flows, and discounting the cash flows to estimate the present value of assets and liabilities. The difference between these discounted values of the assets and liabilities is the economic value of equity, which in theory approximates the fair value of our net assets.

### ESTIMATED CHANGES IN ECONOMIC VALUE OF EQUITY<sup>(1)</sup>

Changes in Interest Rates	+300 bp	+200 bp	+100 bp	-100 bp
Policy Limit	-12.5%	-10.0%	-7.5%	-7.5%
December 31, 2014	-2.1 %	1.0 %	-3.3 %	-8.3 %
December 31, 2013	0.8 %	3.8 %	4.0 %	-5.9 %

The unfavorable variance year over year in all scenarios was attributable to a shift in mix of assets from overnight funds to securities and the loan portfolio, and a more conservative set of rising rate deposit pricing and decay assumptions. Management continuously works to hone and validate these assumptions as historical data is gathered and current market conditions change.

<sup>(1)</sup>Down 200 and 300 rate scenarios have been excluded due to the current historically low interest rate environment.

## LIQUIDITY AND CAPITAL RESOURCES

### Liquidity

In general terms, liquidity is a measurement of our ability to meet our cash needs. Our objective in managing our liquidity is to maintain our ability to fund our operational needs, loan commitments, purchase securities or repay deposits and other liabilities in accordance with their terms, without an adverse impact on our current or future earnings. Our liquidity strategy is guided by policies that are formulated and monitored by our ALCO and senior management, and which take into account the marketability of assets, the sources and stability of funding and the level of unfunded commitments. We regularly evaluate all of our various funding sources with an emphasis on accessibility,

stability, reliability and cost-effectiveness. For the years ended December 31, 2014 and 2013, our principal source of funding has been our clients' deposits, supplemented by our short-term and long-term borrowings, primarily from securities sold under repurchase agreements, federal funds purchased and FHLB borrowings. We believe that the cash generated from operations, our borrowing capacity and our access to capital resources are sufficient to meet our future operating capital and funding requirements.

As of December 31, 2014, we have the ability to generate \$896.4 million in additional liquidity through all of our available resources. In addition to the primary borrowing outlets mentioned above, we also have the ability to generate liquidity by borrowing from the Federal Reserve Discount Window and through brokered deposits. Management recognizes the importance of maintaining liquidity and has developed a Contingent Liquidity Plan, which addresses various liquidity stress levels and our response and action based on the level of severity. We periodically test our credit facilities for access to the funds, but also understand that as the severity of the liquidity level increases certain credit facilities may no longer be available. A liquidity stress test is completed quarterly based on events that could potentially occur at the Bank with the results reported to ALCO, MROC, EROC and the Board of Directors. The liquidity available to us is considered sufficient to meet our ongoing needs.

We view our investment portfolio as a liquidity source and have the option to pledge the portfolio as collateral for borrowings or deposits, and/or sell selected securities. The portfolio consists of debt issued by the U.S. Treasury, U.S. governmental agencies, and municipal governments. The weighted-average life of the portfolio is 2.17 years and as of year-end had a net unrealized pre-tax gain of \$0.5 million.

Our average overnight funds (defined as funds sold plus interest bearing deposits with other banks less funds purchased) position was \$288.6 million during the fourth quarter of 2014 compared to an average net overnight funds sold position of \$317.6 million in the prior quarter and an average overnight funds sold position of \$411.6 million in the fourth quarter of 2013. The decrease when compared to both prior periods reflects the increase in our investment and loan portfolios.

Although we have experienced loan growth in 2014, we continue to work on lowering the level of overnight funds by adding to our investment portfolio with short-duration, high quality securities and reducing deposit balances. We offer to our clients a fully-insured money market account which is provided by a third party and can serve as an alternative investment for some of our higher balance depositors while at the same time allowing us to maintain the account relationship. Until such time that attractive investment alternatives arise, we will continue to execute these strategies as well as seek other initiatives in an effort to better deploy our overnight fund balances.

Capital expenditures are expected to approximate \$5.0 million over the next 12 months, which consist primarily of ATM replacements, furniture and fixtures, and technology purchases. Management believes that these capital expenditures will be funded with existing resources without impairing our ability to meet our ongoing obligations.

## **Borrowings**

At December 31, 2014, advances from the FHLB consisted of \$33.1 million in outstanding debt consisting of 33 notes. In 2014, the Bank made FHLB advance payments totaling \$8.9 million, which includes seven advances that matured or were paid off. No new FHLB advances were obtained in 2014. The FHLB notes are collateralized by a blanket floating lien on all of our 1-4 family residential mortgage loans, commercial real estate mortgage loans, and home equity mortgage loans.

We have issued two junior subordinated deferrable interest notes to wholly owned Delaware statutory trusts. The first note for \$30.9 million was issued to CCBG Capital Trust I in November 2004. The second note for \$32.0 million was issued to CCBG Capital Trust II in May 2005. See Note 9 in the Notes to Consolidated Financial Statements for additional information on these borrowings. The interest payment for the CCBG Capital Trust I borrowing is due quarterly and adjusts quarterly to a variable rate of 3-month LIBOR plus a margin of 1.90%. This note matures on December 31, 2034. The interest payment for the CCBG Capital Trust II borrowing is due quarterly and will adjust annually to a variable rate of 3-month LIBOR plus a margin of 1.80%. This note matures on June 15, 2035. The proceeds of these borrowings were used to partially fund acquisitions.

## **Table 15**

### **CONTRACTUAL CASH OBLIGATIONS**

Table 15 sets forth certain information about contractual cash obligations at December 31, 2014.

(Dollars in Thousands)	Payments Due By Period				Total
	< 1 Yr	> 1 – 3 Yrs	> 3 – 5 Yrs	> 5 Yrs	
Federal Home Loan Bank Advances	\$4,765	\$9,344	\$12,367	\$6,635	\$33,111
Subordinated Notes Payable	—	—	—	62,887	62,887
Operating Lease Obligations	536	897	429	3,234	5,096
Time Deposit Maturities	165,989	25,990	1,876	1,726	195,581
Total Contractual Cash Obligations	\$171,290	\$36,231	\$14,672	\$74,482	\$296,675

### Capital

Shareowners' equity totaled \$272.5 million at December 31, 2014 compared to \$276.4 million at December 31, 2013. During 2014, shareowners' equity decreased \$3.9 million, or 1.4%. During the year, shareowners' equity was positively impacted by net income of \$9.3 million, stock compensation accretion of \$1.3 million, and net adjustments totaling \$0.3 million related to transactions under our stock compensation plans. Shareowners' equity was reduced by common stock dividends of \$1.6 million, share repurchases totaling \$0.3 million, and a \$12.9 million increase in the accumulated other comprehensive loss for our pension plan.

Shareowners' equity as of December 31, for each of the last three years is presented below:

(Dollars in Thousands)	2014	2013	2012
Common Stock	\$174	\$174	\$172
Additional Paid-in Capital	42,569	41,152	38,707
Retained Earnings	251,306	243,614	237,569
Subtotal	294,049	284,940	276,448
Accumulated Other Comprehensive Loss, Net of Tax	(21,509 )	(8,540 )	(29,559 )
Total Shareowners' Equity	\$272,540	\$276,400	\$246,889

We continue to maintain a strong capital position. The ratio of shareowners' equity to total assets at year-end was 10.37%, 10.58%, and 9.37%, in 2014, 2013, and 2012, respectively. Management believes our strong capital base offered protection during the course of the last economic downturn and provides sufficient capacity to meet our strategic objectives.

We are subject to risk-based capital guidelines that measure capital relative to risk-weighted assets and off-balance sheet financial instruments. Capital guidelines issued by the Federal Reserve require bank holding companies to have a minimum total risk-based capital ratio of 8.00%, with at least half of the total capital in the form of Tier I Capital. As of December 31, 2014, we exceeded these capital guidelines with a total risk-based capital ratio of 17.76% and a Tier I capital ratio of 16.67%, compared to 17.94% and 16.56%, respectively, in 2013. As allowed by Federal Reserve capital guidelines the trust preferred securities issued by CCBG Capital Trust I and CCBG Capital Trust II are included as Tier I Capital in our capital calculations previously noted. See Note 9 in the Notes to Consolidated Financial Statements for additional information on our two trust preferred security offerings. See Note 14 in the Notes to Consolidated Financial Statements for additional information as to our capital adequacy.

The federal banking regulators issued new capital rules establishing a new comprehensive capital framework for U.S. banking organizations which will become effective January 1, 2015 (subject to a phase-in period) (the "Basel III Capital Rules"). Refer to the Regulatory Considerations – Capital Regulations section on page 14 for a detailed discussion of the new Basel III capital requirements. Upon implementation of the new capital standards, we believe that we will meet all capital adequacy requirements under the Basel III Capital Rules on a fully phased-in basis as if such requirements were currently in effect.

A leverage ratio is also used in connection with the risk-based capital standards and is defined as Tier I Capital divided by average assets. The minimum leverage ratio under this standard is 4% for the highest-rated bank holding companies which are not undertaking significant expansion programs. A higher standard may be required for other companies, depending upon their regulatory ratings and expansion plans. On December 31, 2014, we had a leverage ratio of 10.99% compared to 10.46% in 2013.



At December 31, 2014, our common stock had a book value of \$15.53 per diluted share compared to \$15.85 at December 31, 2013. Book value is impacted by the net unrealized gains and losses on investment securities available-for-sale. At December 31, 2014, the net unrealized gain was \$59,000 compared to a \$132,000 net unrealized loss at December 31, 2013. The aforementioned net unrealized gain of \$59,000 reflects a \$322,000 gain on available for sale securities and \$263,000 in unamortized loss related to the transfer of securities to HTM in 2013. Book value is also impacted by the recording of our unfunded pension liability through other comprehensive income in accordance with Accounting Standards Codification Topic 715. At December 31, 2014, the net pension liability reflected in other comprehensive loss was \$21.6 million compared to \$8.4 million at December 31, 2013. The increase in our unfunded pension liability was primarily due to (1) a decrease in the plan discount rate (attributable to lower long-term rates at the end of 2014), which drives an increase in pension liabilities, and (2) the incorporation of recent changes to the mortality tables used to calculate pension liabilities.

In February 2014, our Board of Directors authorized the repurchase of up to 1,500,000 shares of our outstanding common stock. Repurchases may be made in the open market or in privately negotiated transactions; however, we are not obligated to repurchase any specified number of shares. During 2014, we repurchased 19,600 shares of our outstanding common stock at an average price of \$13.69 per share under the plan.

We offer an Associate Incentive Plan under which certain associates are eligible to earn equity-based awards based upon achieving established performance goals. In 2014, 76,547 shares were earned under this plan of which 3,200 shares were issued in 2014 and 73,347 were issued in January 2015. In 2013, 66,137 shares were earned under this plan of which 3,100 were issued in 2013 and 63,037 were issued in January 2014.

We also offer stock purchase plans, which permit our associates and directors to purchase shares at a 10% discount. In 2014, 39,562 shares, valued at approximately \$0.6 million (before 10% discount), were issued under these plans. In 2013, we issued 96,946 shares, valued at approximately \$1.1 million (before 10% discount).

## **Dividends**

Adequate capital and financial strength is paramount to our stability and the stability of our subsidiary bank. Cash dividends declared and paid should not place unnecessary strain on our capital levels. When determining the level of dividends the following factors are considered:

- Compliance with state and federal laws and regulations;
- Our capital position and our ability to meet our financial obligations;
- Projected earnings and asset levels; and
- The ability of the Bank and us to fund dividends.

## **Inflation**

The impact of inflation on the banking industry differs significantly from that of other industries in which a large portion of total resources are invested in fixed assets such as property, plant and equipment.

Assets and liabilities of financial institutions are virtually all monetary in nature, and therefore are primarily impacted by interest rates rather than changing prices. While the general level of inflation underlies most interest rates, interest rates react more to changes in the expected rate of inflation and to changes in monetary and fiscal policy. Net interest income and the interest rate spread are good measures of our ability to react to changing interest rates and are discussed in further detail in the section entitled "Results of Operations."

## **OFF-BALANCE SHEET ARRANGEMENTS**

We do not currently engage in the use of derivative instruments to hedge interest rate risks. However, we are a party to financial instruments with off-balance sheet risks in the normal course of business to meet the financing needs of our clients.

At December 31, 2014, we had \$312.1 million in commitments to extend credit and \$8.3 million in standby letters of credit. Commitments to extend credit are agreements to lend to a client so long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments may expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. Standby letters of credit are conditional commitments issued by us to guarantee the performance of a client to a third party. We use the same credit policies in establishing commitments and issuing letters of credit as we do for on-balance sheet instruments.

If commitments arising from these financial instruments continue to require funding at historical levels, management does not anticipate that such funding will adversely impact our ability to meet on-going obligations. In the event these commitments require funding in excess of historical levels, management believes current liquidity, investment security maturities, available advances from the FHLB and Federal Reserve Bank provide a sufficient source of funds to meet these commitments.

## FOURTH QUARTER 2014 – FINANCIAL RESULTS

### Results of Operations

We realized net income of \$1.9 million, or \$0.11 per diluted share for the fourth quarter of 2014, compared to net income of \$2.1 million, or \$0.12 per diluted share for the third quarter of 2014. The decline in earnings reflects a \$0.3 million decrease in noninterest income, an increase in the loan loss provision of \$0.2 million, and higher income taxes of \$0.1 million that were partially offset by higher net interest income of \$0.1 million and lower noninterest expense of \$0.3 million.

Tax equivalent net interest income for the fourth quarter of 2014 was \$19.1 million compared to \$19.0 million for the third quarter of 2014. During the fourth quarter we realized a positive shift in our earning asset mix due to growth in the investment and loan portfolios. Unfavorable asset repricing continued through the quarter and was only partially offset by a slight reduction in the cost of funds. The net interest margin for the fourth quarter of 2014 was 3.43%, an increase of one basis point over the third quarter of 2014 driven growth in our investment and loan portfolios.

The provision for loan losses for the fourth quarter of 2014 was \$0.6 million compared to \$0.4 million for the third quarter of 2014 driven by a higher level loan charge-offs. Net charge-offs for the fourth quarter of 2014 totaled \$2.2 million, or 0.61% (annualized) of average loans, compared to \$1.9 million, or 0.52% (annualized), for the third quarter of 2014.

Noninterest income for the fourth quarter of 2014 totaled \$13.1 million, a \$0.3 million, or 2.2%, decrease from the third quarter of 2014. The decrease reflects lower deposit fees of \$0.2 million, wealth management fees of \$0.1 million, mortgage banking fees of \$0.1 million, and data processing fees of \$0.1 million that were partially offset by higher other income of \$0.2 million. Deposit fees declined due to a lower level of overdraft fees. Lower trade activity by our retail brokerage clients drove the reduction in wealth management fees. The decrease in mortgage banking fees was generally attributable to a seasonal slowdown in home purchase activity in our markets. The reduction in data processing fees is related to the loss of a government processing contract during 2014. Higher bank owned life insurance income and working capital finance fees drove the increase in other income.

Noninterest expense for the fourth quarter of 2014 totaled \$28.3 million, a decrease of \$0.3 million, or 1.0%, from the third quarter of 2014 reflective of lower OREO expense of \$0.4, occupancy expense of \$0.2 million and other expense of \$0.2 million, partially offset by a higher compensation expense of \$0.5 million. The decline in OREO expense was primarily attributable lower property carrying costs. Lower maintenance and repair costs for our premises and lower utility costs drove the reduction in occupancy expense. The reduction in other expense was primarily attributable to a decline in legal fees and advertising costs. The higher level of compensation expense was primarily attributable to an increase in stock compensation expense reflective of a higher level of performance for our stock incentive plans.

## Discussion of Financial Condition

Average earning assets were \$2.213 billion for the fourth quarter of 2014, an increase of \$3.4 million, or 0.2%, over the third quarter of 2014, attributable to a higher level of total deposits. Growth in both the loan and investment portfolios led to a more favorable earning asset mix.

Average loans were \$1.427 billion for the fourth quarter of 2014, a \$5.4 million, or 0.4%, increase over the third quarter of 2014 continuing growth in period end loans for four consecutive quarters. The growth continues to be driven primarily by the consumer portfolio while the commercial real estate portfolio declined.

Nonperforming assets (nonaccrual loans and OREO) totaled \$52.4 million at December 31, 2014, a decrease of \$12.8 million from September 30, 2014. Nonaccrual loans totaled \$16.8 million at December 31, 2014, a decrease of \$6.7 million from September 30, 2014. Nonaccrual loan additions totaled \$5.8 million in the fourth quarter of 2014 compared to \$4.8 million for the third quarter of 2014. The balance of OREO totaled \$35.7 million at December 31, 2014, a decrease of \$6.0 million from September 30, 2014. For the fourth quarter of 2014, we added properties totaling \$3.2 million, sold properties totaling \$7.9 million, recorded valuation adjustments totaling \$0.9 million, and realized miscellaneous adjustments of \$0.4 million. Nonperforming assets represented 2.00% of total assets at December 31, 2014 compared to 2.61% at September 30, 2014.

Average total deposits were \$2.077 billion for the fourth quarter of 2014, an increase of \$14.5 million, or 0.7%, over the third quarter of 2014. The higher level of deposits reflects higher noninterest bearing deposits and savings accounts, partially offset by declines in money markets and certificates of deposit. The seasonal inflow of public funds started in the fourth quarter of 2014 and will continue through the first quarter of 2015. Deposit levels remain strong and our mix of deposits continues to improve as higher cost certificates of deposit are replaced with lower rate non-maturity deposits and noninterest bearing demand accounts. Average borrowings increased by \$4.0 million attributable to higher repurchase agreement balances.

Equity capital was \$272.5 million as of December 31, 2014, compared to \$283.3 million as of September 30, 2014. Our leverage ratio was 10.99% and 10.97% for these periods. Further, our risk-adjusted capital ratio was 17.76% at December 31, 2014 compared to 18.08% at September 30, 2014, significantly exceeding the 10.0% threshold to be designated as “well-capitalized” under the risk-based regulatory guidelines. At December 31, 2014, our tangible common equity ratio was 7.38%, compared to 8.22% at September 30, 2014. The decline in equity and certain capital ratios in the fourth quarter of 2014 were due to an unfavorable adjustment in the pension component of our other comprehensive income. The unfavorable adjustment reflects (1) a decrease in the plan discount rate (attributable to lower long-term rates at the end of 2014), which drives an increase in pension liabilities, and (2) the incorporation of recent changes to the mortality tables used to calculate pension liabilities.

## ACCOUNTING POLICIES

### Critical Accounting Policies

The consolidated financial statements and accompanying Notes to Consolidated Financial Statements are prepared in accordance with accounting principles generally accepted in the United States of America, which require us to make various estimates and assumptions (see Note 1 in the Notes to Consolidated Financial Statements). We believe that, of our significant accounting policies, the following may involve a higher degree of judgment and complexity.

*Allowance for Loan Losses.* The allowance for loan losses is a reserve established through a provision for loan losses charged to expense, which represents management’s best estimate of probable losses within the existing portfolio of loans. The allowance is the amount considered adequate to absorb losses inherent in the loan portfolio based on management’s evaluation of credit risk as of the balance sheet date.

The allowance for loan losses includes allowance allocations calculated in accordance with U.S. GAAP. The level of the allowance reflects management’s continuing evaluation of specific credit risks, loss experience, loan portfolio quality, economic conditions and unidentified losses inherent in the current loan portfolio, as well as trends in the foregoing. This evaluation is inherently subjective, as it requires estimates that are susceptible to significant revision as information becomes available.

The Company’s allowance for loan losses consists of two components: (i) specific reserves established for probable losses on impaired loans; and (ii) general reserves for non-homogenous loans not deemed impaired and homogenous loan pools based on, but not limited to, historical loan loss experience, current economic and market conditions, levels of past due loans, and levels of problem loans.

Our financial results are affected by the changes in and the absolute level of the allowance for loan losses. This estimation process is judgmental and requires an estimate of the loss severity rates that we apply to our unimpaired loan portfolio. In the event that estimated loss severity rates for our unimpaired loan portfolio increased by 10%, the allowance for loan losses would increase by approximately \$0.9 million.

*Goodwill.* Goodwill represents the excess of the cost of acquired businesses over the fair market value of their identifiable net assets. We perform an impairment review on an annual basis or more frequently if events or changes in circumstances indicate that the carrying value may not be recoverable. Adverse changes in the economic environment, declining operations, or other factors could result in a decline in the estimated implied fair value of goodwill. If the estimated implied fair value of goodwill is less than the carrying amount, a loss would be recognized to reduce the carrying amount to the estimated implied fair value.

We evaluate goodwill for impairment on an annual basis, using a two-step process. Step One compares the estimated fair value of the reporting unit to its carrying amount. We have determined that we have one reporting unit which consists of the Company as a whole, thus the carrying amount of the reporting unit is the net book value of the Company, including goodwill. If the carrying amount of the reporting unit exceeds its estimated fair value, Step Two is performed by comparing the fair value of the reporting unit's implied goodwill to the carrying value of goodwill. If the carrying value of the reporting unit's goodwill exceeds the estimated fair value, an impairment charge is recorded equal to the excess.

Given the Company's net book value exceeded its market capitalization as of the annual impairment testing date, we proceeded with Step One of the annual goodwill impairment test. We first estimated the fair value of the reporting unit utilizing a market approach that was supplemented with a reconciliation of the resulting equity value of the Company with our market capitalization. The market approach utilized the guideline company valuation ("GLC") method to determine the overall equity valuation. A book and tangible book multiple was developed to determine a market value of equity on a controlling basis. A control premium was then applied to the minority value to calculate a Step One value indication for the Company. The multiples that resulted from the GLC method were validated by comparing to peer companies. Based on the valuation developed as part of Step One, the estimated fair value of our reporting unit exceeded the carrying value of goodwill and therefore, no Step Two was required. For Step One of the impairment testing, change in economic conditions and observable bank purchase transactions can impact the outcome of the market valuation approach.

*Pension Assumptions.* We have a defined benefit pension plan for the benefit of substantially all of our associates. Our funding policy with respect to the pension plan is to contribute amounts to the plan sufficient to meet minimum funding requirements as set by law. Pension expense, which is included in the Consolidated Statements of Operations in noninterest expense as “Compensation,” is determined by an external actuarial valuation based on assumptions that are evaluated annually as of December 31, the measurement date for the pension obligation. The Consolidated Statements of Financial Condition reflect an accrued pension benefit cost due to funding levels and unrecognized actuarial amounts. The most significant assumptions used in calculating the pension obligation are the weighted-average discount rate used to determine the present value of the pension obligation, the weighted-average expected long-term rate of return on plan assets, and the assumed rate of annual compensation increases. These assumptions are re-evaluated annually with the external actuaries, taking into consideration both current market conditions and anticipated long-term market conditions.

The weighted-average discount rate is determined by matching the anticipated defined pension plan cash flows to a long-term corporate Aa-rated bond index and solving for the underlying rate of return, which investing in such securities would generate. This methodology is applied consistently from year-to-year. The discount rate utilized in 2014 was 5.00%. The estimated impact to 2014 pension expense of a 25 basis point increase or decrease in the discount rate would have been a decrease and increase of approximately \$662,000 and \$695,000, respectively. We anticipate using a 4.15% discount rate in 2015.

The weighted-average expected long-term rate of return on plan assets is determined based on the current and anticipated future mix of assets in the plan. The assets currently consist of equity securities, U.S. Government and Government agency debt securities, and other securities (typically temporary liquid funds awaiting investment). The weighted-average expected long-term rate of return on plan assets utilized for 2014 was 7.5%. The estimated impact to 2014 pension expense of a 25 basis point increase or decrease in the rate of return would have been an approximate \$250,000 increase or decrease, respectively. We anticipate using a rate of return on plan assets for 2015 of 7.5%.

The assumed rate of annual compensation increases of 3.25% in 2014 reflected expected trends in salaries and the employee base. We anticipate using a compensation increase of 3.25% for 2015 reflecting current market trends.

Detailed information on the pension plan, the actuarially determined disclosures, and the assumptions used are provided in Note 12 of the Notes to Consolidated Financial Statements.

### **Recent Accounting Pronouncements**

*The Financial Accounting Standards Board, the SEC, and other regulatory bodies have enacted new accounting pronouncements and standards that either have impacted our results in prior years presented, or will likely impact our results in 2015. Please refer to Note 1 of the Notes to our Consolidated Financial Statements.*



**ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURE ABOUT MARKET RISK**

See “Financial Condition - Market Risk and Interest Rate Sensitivity” in Management’s Discussion and Analysis of Financial Condition and Results of Operations, above, which is incorporated herein by reference.

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**Item 8. Financial Statements and Supplementary Data****Table 16****QUARTERLY FINANCIAL DATA (Unaudited)**

(Dollars in Thousands, Except Per Share Data)	2014				2013		
	Fourth	Third	Second	First	Fourth	Third	Second
Summary of Operations:							
Interest Income	\$ 19,871	\$ 19,766	\$ 19,348	\$ 19,236	\$ 20,076	\$ 20,250	\$ 20,698
Interest Expense	852	868	910	950	1,080	1,050	1,103
Net Interest Income	19,019	18,898	18,438	18,286	18,996	19,200	19,595
Provision for Loan Losses	623	424	499	359	397	555	1,450
Net Interest Income After Provision for Loan Losses	18,396	18,474	17,939	17,927	18,599	18,645	18,145
Noninterest Income	13,053	13,351	13,347	12,785	13,825	14,026	13,731
Noninterest Expense	28,309	28,607	29,076	28,366	29,647	30,153	30,464
Income Before Income Taxes	3,140	3,218	2,210	2,346	2,777	2,518	1,412
Income Tax Expense (Benefit)	1,219	1,103	737	(1,405 )	5	927	569
Net Income	\$ 1,921	\$ 2,115	\$ 1,473	\$ 3,751	\$ 2,772	\$ 1,591	\$ 843
Net Interest Income (FTE)	\$ 19,124	\$ 19,020	\$ 18,567	\$ 18,424	\$ 19,141	\$ 19,355	\$ 19,744
Per Common Share:							
Net Income Basic	\$ 0.11	\$ 0.12	\$ 0.08	\$ 0.22	\$ 0.16	\$ 0.09	\$ 0.05
Net Income Diluted	0.11	0.12	0.08	0.22	0.16	0.09	0.05
Cash Dividends Declared	0.03	0.02	0.02	0.02	0.00	0.00	0.00
Diluted Book Value	15.53	16.18	16.08	16.02	15.85	14.44	14.36

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Market Price:

High	16.00	14.98	14.71	14.59	12.69	13.08	12.64
Low	13.00	13.26	12.60	11.56	11.33	11.06	10.12
Close	15.54	13.54	14.53	13.28	11.77	11.78	11.53

Selected  
Average  
Balances:

Loans, Net	\$ 1,426,756	\$ 1,421,327	\$ 1,411,988	\$ 1,395,506	\$ 1,414,909	\$ 1,436,039	\$ 1,456,904
Earning Assets	2,212,781	2,209,429	2,260,885	2,268,320	2,206,286	2,201,390	2,206,694
Total Assets	2,549,736	2,530,571	2,578,993	2,598,307	2,553,653	2,558,395	2,564,528
Deposits	2,077,365	2,062,881	2,109,563	2,124,960	2,050,870	2,059,498	2,067,647
Shareowners' Equity	286,029	284,130	282,346	279,729	253,999	251,617	250,485
Common Equivalent Average Shares:							
Basic	17,433	17,440	17,427	17,399	17,341	17,336	17,319
Diluted	17,530	17,519	17,488	17,439	17,423	17,396	17,355

Performance  
Ratios:

Return on Average Assets	0.30	%	0.33	%	0.23	%	0.59	%	0.43	%	0.25	%	0.13	%
Return on Average Equity	2.66		2.95		2.09		5.44		4.33		2.51		1.35	
Net Interest Margin (FTE)	3.43		3.42		3.29		3.29		3.45		3.49		3.59	
Noninterest Income as % of Operating Revenue	40.70		41.40		41.99		41.15		42.12		42.21		41.20	
Efficiency Ratio	88.16		88.44		91.15		91.02		90.22		90.42		91.07	

Asset Quality:

Allowance for Loan Losses	\$ 17,539		\$ 19,093		\$ 20,543		\$ 22,110		\$ 23,095		\$ 25,010		\$ 27,294	
Allowance for Loan Losses to Loans	1.22	%	1.34	%	1.45	%	1.57	%	1.65	%	1.75	%	1.89	%
Nonperforming Assets ("NPA's")	52,449		65,208		68,249		78,594		85,035		94,700		96,653	
NPA's to Total Assets	2.00		2.61		2.66		2.98		3.26		3.77		3.77	
NPA's to Loans + ORE	3.55		4.45		4.67		5.42		5.87		6.38		6.44	
Allowance to Non-Performing Loans	104.60		81.31		80.03		63.98		62.48		60.00		65.66	
Net Charge-Offs to Average	0.61		0.52		.059		0.39		0.65		0.78		0.54	

Loans

Capital Ratios:

Tier I Capital	16.67	%	16.88	%	16.85	%	16.85	%	16.56	%	15.60	%	15.36	%
Total Capital	17.76		18.08		18.10		18.10		17.94		16.97		16.73	
Tangible Capital	7.38		8.22		7.93		7.66		7.58		6.84		6.64	
Leverage	10.99		10.97		10.70		10.47		10.46		10.16		10.07	

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**CONSOLIDATED FINANCIAL STATEMENTS**

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Report of Independent Registered Certified Public Accounting Firm

The Board of Directors and Shareowners of

Capital City Bank Group, Inc.

We have audited the accompanying consolidated statements of financial condition of Capital City Bank Group, Inc. as of December 31, 2014 and 2013, and the related consolidated statements of operations, comprehensive income, changes in shareowners' equity, and cash flows for each of the three years in the period ended December 31, 2014. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

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

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), Capital City Bank Group, Inc.'s internal control over financial reporting as of December 31, 2014, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 framework) and our report dated March 6, 2015 expressed an unqualified opinion thereon.

Tampa, Florida

March 6, 2015



**CAPITAL CITY BANK GROUP, INC.****CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION**

(Dollars in Thousands)	As of December 31,	
	2014	2013
<b>ASSETS</b>		
Cash and Due From Banks	\$55,467	\$55,209
Federal Funds Sold and Interest Bearing Deposits	329,589	474,719
Total Cash and Cash Equivalents	385,056	529,928
Investment Securities, Available for Sale, at fair value	341,548	251,420
Investment Securities, Held to Maturity, at amortized cost (fair value of \$163,412 and \$146,961)	163,581	148,211
Total Investment Securities	505,129	399,631
Loans Held For Sale	10,688	11,065
Loans, Net of Unearned Income	1,431,374	1,388,604
Allowance for Loan Losses	(17,539 )	(23,095 )
Loans, Net	1,413,835	1,365,509
Premises and Equipment, Net	101,899	103,385
Goodwill	84,811	84,811
Other Intangible Assets	—	32
Other Real Estate Owned	35,680	48,071
Other Assets	90,071	69,471
Total Assets	\$2,627,169	\$2,611,903
<b>LIABILITIES</b>		
Deposits:		
Noninterest Bearing Deposits	\$659,115	\$641,463
Interest Bearing Deposits	1,487,679	1,494,785
Total Deposits	2,146,794	2,136,248
Short-Term Borrowings	49,425	51,321
Subordinated Notes Payable	62,887	62,887
Other Long-Term Borrowings	31,097	38,043
Other Liabilities	64,426	47,004
Total Liabilities	2,354,629	2,335,503
<b>SHAREOWNERS' EQUITY</b>		
Preferred Stock, \$.01 par value; 3,000,000 shares authorized; no shares issued and outstanding	—	—
Common Stock, \$.01 par value; 90,000,000 shares authorized; 17,447,223 and 17,360,960 shares issued and outstanding at December 31, 2014 and December 31, 2013, respectively	174	174
Additional Paid-In Capital	42,569	41,152
Retained Earnings	251,306	243,614



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Accumulated Other Comprehensive Loss, Net of Tax	(21,509 )	(8,540 )
Total Shareowners' Equity	272,540	276,400
Total Liabilities and Shareowners' Equity	\$2,627,169	\$2,611,903

*The accompanying Notes to Consolidated Financial Statements are an integral part of these statements.*

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**CAPITAL CITY BANK GROUP, INC.****CONSOLIDATED STATEMENTS OF OPERATIONS**

(Dollars in Thousands, Except Per Share Data)	For the Years Ended December 31,		
	2014	2013	2012
<b>INTEREST INCOME</b>			
Loans, including Fees	\$ 73,402	\$ 78,184	\$ 85,394
Investment Securities:			
Taxable	3,394	2,345	2,912
Tax Exempt	492	546	428
Funds Sold	933	1,077	946
Total Interest Income	78,221	82,152	89,680
<b>INTEREST EXPENSE</b>			
Deposits	1,099	1,431	2,108
Short-Term Borrowings	78	235	196
Subordinated Notes Payable	1,328	1,420	1,477
Other Long-Term Borrowings	1,075	1,330	1,587
Total Interest Expense	3,580	4,416	5,368
<b>NET INTEREST INCOME</b>			
	74,641	77,736	84,312
Provision for Loan Losses	1,905	3,472	16,166
Net Interest Income After Provision for Loan Losses	72,736	74,264	68,146
<b>NONINTEREST INCOME</b>			
Deposit Fees	24,320	25,254	25,792
Bank Card Fees	10,892	10,786	10,783
Wealth Management Fees	7,808	8,179	7,181
Mortgage Banking Fees	3,082	3,534	3,600
Data Processing Fees	1,543	2,674	2,713
Securities Transactions	1	3	—
Other	4,890	4,681	4,500
Total Noninterest Income	52,536	55,111	54,569
<b>NONINTEREST EXPENSE</b>			
Compensation	62,215	66,127	64,242
Occupancy, Net	17,818	17,331	18,055
Intangible Amortization	32	210	431
Other Real Estate Owned, Net	6,811	8,234	10,812
Other	27,482	29,503	30,403
Total Noninterest Expense	114,358	121,405	123,943
<b>INCOME (LOSS) BEFORE INCOME TAXES</b>			
	10,914	7,970	(1,228 )
Income Tax Expense (Benefit)	1,654	1,925	(1,336 )
<b>NET INCOME</b>	<b>\$ 9,260</b>	<b>\$ 6,045</b>	<b>\$ 108</b>

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BASIC NET INCOME PER SHARE	\$0.53	\$0.35	\$0.01
DILUTED NET INCOME PER SHARE	\$0.53	\$0.35	\$0.01
Average Basic Common Shares Outstanding	17,425	17,325	17,205
Average Diluted Common Shares Outstanding	17,488	17,399	17,220

*The accompanying Notes to Consolidated Financial Statements are an integral part of these statements.*

**CAPITAL CITY BANK GROUP, INC.****CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**

(Dollars in Thousands)	For the Years Ended December 31,		
	2014	2013	2012
NET INCOME	\$ 9,260	\$ 6,045	\$ 108
Other comprehensive income (loss), before tax:			
Investment Securities:			
Change in net unrealized gain/loss on securities available for sale	250	(1,252 )	(786 )
Unrealized losses on securities transferred from available for sale to held to maturity	—	(523 )	—
Amortization of unrealized losses on securities transferred from available for sale to held to maturity	70	25	—
Reclassification adjustment for net gain included in net income	1	3	—
Reclassification adjustment for impairment loss realized in net income	—	600	—
Total Investment Securities	321	(1,147 )	(786 )
Benefit Plans:			
Reclassification adjustment for amortization of prior service cost	473	504	548
Reclassification adjustment for amortization of net loss	705	4,079	3,021
Current year actuarial (loss) gain	(22,603 )	30,784	(12,587 )
Total Benefit Plans	(21,425 )	35,367	(9,018 )
Other comprehensive (loss) income, before tax:	(21,104 )	34,220	(9,804 )
Deferred tax benefit (expense) related to other comprehensive income	8,135	(13,201 )	3,774
Other comprehensive (loss) income, net of tax	(12,969 )	21,019	(6,030 )
<b>TOTAL COMPREHENSIVE (LOSS) INCOME</b>	<b>\$ (3,709 )</b>	<b>\$ 27,064</b>	<b>\$ (5,922 )</b>

*The accompanying Notes to Consolidated Financial Statements are an integral part of these statements.*

**CAPITAL CITY BANK GROUP, INC.****CONSOLIDATED STATEMENTS OF CHANGES IN SHAREOWNERS' EQUITY**

(Dollars in Thousands, Except Per Share Data)	Shares Outstanding	Common Stock	Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Loss, Net of Taxes	Total
Balance, January 1, 2012	17,160,274	\$ 172	\$ 37,838	\$237,461	\$ (23,529 )	\$251,942
Net Income		—	—	108	—	108
Other Comprehensive Loss, Net of Tax		—	—	—	(6,030 )	(6,030 )
Stock Compensation Expense		—	262	—	—	262
Impact of Transactions Under Compensation Plans, net	72,106	—	607	—	—	607
Balance, December 31, 2012	17,232,380	172	38,707	237,569	(29,559 )	246,889
Net Income		—	—	6,045	—	6,045
Other Comprehensive Loss, Net of Tax		—	—	—	21,019	21,019
Stock Compensation Expense		—	1,296	—	—	1,296
Impact of Transactions Under Compensation Plans, net	128,580	2	1,149	—	—	1,151
Balance, December 31, 2013	17,360,960	174	41,152	243,614	(8,540 )	276,400
Net Income		—	—	9,260	—	9,260
Other Comprehensive Income, Net of Tax		—	—	—	(12,969 )	(12,969 )
Cash Dividends (\$0.09 per share)		—	—	(1,568 )	—	(1,568 )
Stock Compensation Expense		—	1,349	—	—	1,349
Impact of Transactions Under Compensation Plans, net	105,863	—	337	—	—	337
Repurchase of Common Stock	(19,600 )	—	(269 )	—	—	(269 )
Balance, December 31, 2014	17,447,223	\$ 174	\$ 42,569	\$251,306	\$ (21,509 )	\$272,540

*The accompanying Notes to Consolidated Financial Statements are an integral part of these statements.*

**CAPITAL CITY BANK GROUP, INC.****CONSOLIDATED STATEMENTS OF CASH FLOWS**

(Dollars in Thousands)	For the Years Ended December 31,		
	2014	2013	2012
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>			
Net Income	\$9,260	\$6,045	\$108
Adjustments to Reconcile Net Income to Cash Provided by Operating Activities:			
Provision for Loan Losses	1,905	3,472	16,166
Depreciation	6,490	6,396	6,759
Amortization of Premiums, Discounts, and Fees, net	4,717	4,756	3,358
Amortization of Intangible Assets	32	210	431
Gain on Securities Transactions	(1 )	(3 )	—
Impairment Loss on Security	—	600	—
Net Decrease in Loans Held-for-Sale	377	3,124	7,036
Stock Compensation	1,349	1,296	262
Deferred Income Taxes	4,779	1,805	(2,805 )
Loss on Sales and Write-Downs of Other Real Estate Owned	4,462	4,573	6,314
Loss on Sale or Disposal of Premises and Equipment	113	—	—
Net (Increase) Decrease in Other Assets	(12,353 )	5,087	5,665
Net Increase (Decrease) in Other Liabilities	4,021	(2,510 )	13,417
Net Cash Provided By Operating Activities	25,151	34,851	56,711
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>			
Securities Held to Maturity:			
Purchases	(56,249 )	(95,946 )	—
Payments, Maturities, and Calls	39,335	9,768	—
Securities Available for Sale:			
Purchases	(210,858 )	(149,111 )	(141,863 )
Sales	—	7,506	805
Payments, Maturities, and Calls	117,281	118,142	146,862
Net (Increase) Decrease in Loans	(64,975 )	84,969	59,751
Purchase of Bank Owned Life Insurance	(13,085 )	—	—
Proceeds From Sales of Other Real Estate Owned	23,201	25,270	25,636
Purchases of Premises and Equipment, net	(5,117 )	(2,689 )	(2,860 )
Net Cash (Used In) Provided by Investing Activities	(170,467 )	(2,091 )	88,331
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>			
Net Increase (Decrease) in Deposits	10,546	(8,748 )	(27,523 )
Net Decrease in Short-Term Borrowings	(3,955 )	(542 )	(3,121 )
Proceeds from Other Long-Term Borrowings	—	1,303	12,591
Repayment of Other Long-Term Borrowings	(4,888 )	(5,691 )	(3,154 )
Dividends Paid	(1,568 )	—	—
Payments to Repurchase Common Stock	(269 )	—	—
Issuance of Common Stock Under Compensation Plans	578	1,114	583
Net Cash Provided By (Used In) Financing Activities	444	(12,564 )	(20,624 )

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NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS	(144,872)	20,196	124,418
Cash and Cash Equivalents at Beginning of Year	529,928	509,732	385,314
Cash and Cash Equivalents at End of Year	\$385,056	\$529,928	\$509,732
Supplemental Cash Flow Disclosures:			
Interest Paid	\$3,562	\$6,012	\$6,662
Income Taxes Paid (Refunded)	\$2,655	\$(3,202)	\$(3,799)
Noncash Investing and Financing Activities:			
Transfer of Securities Available for Sale to Held to Maturity	\$—	\$62,488	\$—
Loans Transferred to Other Real Estate Owned	\$15,271	\$24,488	\$22,777
Transfer of Current Portion of Long-Term Borrowings	\$2,059	\$4,428	\$7,184

*The accompanying Notes to Consolidated Financial Statements are an integral part of these statements.*

*Notes to Consolidated Financial Statements*

**Note 1**

**SIGNIFICANT ACCOUNTING POLICIES**

**Nature of Operations**

Capital City Bank Group, Inc. (“CCBG” or the “Company”) provides a full range of banking and banking-related services to individual and corporate clients through its subsidiary, Capital City Bank, with banking offices located in Florida, Georgia, and Alabama. The Company is subject to competition from other financial institutions, is subject to regulation by certain government agencies and undergoes periodic examinations by those regulatory authorities.

**Basis of Presentation**

The consolidated financial statements include the accounts of Capital City Bank Group, Inc. (“CCBG”), and its wholly owned subsidiary, Capital City Bank (“CCB” or the “Bank” and together with CCBG, the “Company”). All material inter-company transactions and accounts have been eliminated.

The Company, which operates a single reportable business segment that is comprised of commercial banking within the states of Florida, Georgia, and Alabama, follows accounting principles generally accepted in the United States of America and reporting practices applicable to the banking industry. The principles which materially affect the financial position, results of operations and cash flows are summarized below.

The Company determines whether it has a controlling financial interest in an entity by first evaluating whether the entity is a voting interest entity or a variable interest entity under accounting principles generally accepted in the United States of America. Voting interest entities are entities in which the total equity investment at risk is sufficient to enable the entity to finance itself independently and provide the equity holders with the obligation to absorb losses, the right to receive residual returns and the right to make decisions about the entity’s activities. The Company consolidates voting interest entities in which it has all, or at least a majority of, the voting interest. As defined in applicable accounting standards, variable interest entities (“VIE’s”) are entities that lack one or more of the characteristics of a voting interest entity. A controlling financial interest in an entity is present when an enterprise has a variable interest, or a combination of variable interests, that will absorb a majority of the entity’s expected losses, receive a majority of the entity’s expected residual returns, or both. The enterprise with a controlling financial interest, known as the primary beneficiary, consolidates the VIE. CCBG’s wholly owned subsidiaries, CCBG Capital Trust I (established November 1, 2004) and CCBG Capital Trust II (established May 24, 2005) are VIEs for which the



Company is not the primary beneficiary. Accordingly, the accounts of these entities are not included in the Company's consolidated financial statements.

Certain previously reported amounts have been reclassified to conform to the current year's presentation. The Company has evaluated subsequent events for potential recognition and/or disclosure through the date the consolidated financial statements included in this Annual Report on Form 10-K were filed with the United States Securities and Exchange Commission.

### **Use of Estimates**

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could vary from these estimates. Material estimates that are particularly susceptible to significant changes in the near-term relate to the determination of the allowance for loan losses, pension expense, income taxes, loss contingencies, and valuation of goodwill and other intangibles and their respective analysis of impairment.

### **Cash and Cash Equivalents**

Cash and cash equivalents include cash and due from banks, interest-bearing deposits in other banks, and federal funds sold. Generally, federal funds are purchased and sold for one-day periods and all other cash equivalents have a maturity of 90 days or less. The Company is required to maintain average reserve balances with the Federal Reserve Bank based upon a percentage of deposits. The average amounts of these required reserve balances for the years ended December 31, 2014 and 2013 were \$13.2 million and \$17.6 million, respectively.

### **Investment Securities**

Securities are classified as held to maturity and carried at amortized cost when the Company has the positive intent and ability to hold them until maturity. Securities to be held for indefinite periods of time are classified as available for sale and carried at fair value, with the unrealized holding gains and losses reported as a component of other comprehensive income, net of tax. The Company determines the appropriate classification of securities at the time of purchase. Securities with limited marketability, such as stock in the Federal Reserve Bank and the Federal Home Loan Bank, are carried at cost. Securities transferred from available for sale to held to maturity are recorded at fair value at the time of transfer. The respective gain or loss is reclassified as a separate component of other comprehensive income and amortized as an adjustment to interest income over the remaining life of the security.



Interest income includes amortization of purchase premiums and discounts. Realized gains and losses are derived from the amortized cost of the security sold. Declines in the fair value of held-to-maturity and available-for-sale securities below their cost that are deemed to be other than temporary are reflected in earnings as realized losses. In estimating other-than-temporary impairment losses, the Company considers, among other things, (i) the length of time and the extent to which the fair value has been less than cost, (ii) the financial condition and near-term prospects of the issuer and (iii) the intent and ability of the Company to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value.

### **Loans Held For Sale**

Certain residential mortgage loans are originated for sale in the secondary mortgage loan market. Additionally, certain other loans are periodically identified to be sold. The Company has the ability and intent to sell these loans and they are classified as loans held for sale and carried at the lower of cost or estimated fair value. Fair value is determined on the basis of rates quoted in the respective secondary market for the type of loan held for sale. Loans are generally sold with servicing released at a premium or discount from the carrying amount of the loans. Such premium or discount is recognized as mortgage banking revenue at the date of sale. Fixed commitments are generally used at the time loans are originated or identified for sale to mitigate interest rate risk. The fair value of fixed commitments to originate and sell loans held for sale is not material.

### **Loans**

Loans are stated at the principal amount outstanding, net of unearned income. Interest income is accrued on the effective yield method based on outstanding balances, and includes loan late fees. Fees charged to originate loans and direct loan origination costs are deferred and amortized over the life of the loan as a yield adjustment.

The Company defines loans as past due when one full payment is past due or a contractual maturity is over 30 days late. The accrual of interest is generally suspended on loans more than 90 days past due with respect to principal or interest. When a loan is placed on nonaccrual status, all previously accrued and uncollected interest is reversed against current income. Interest income on nonaccrual loans is recognized when the ultimate collectability is no longer considered doubtful. Loans are returned to accrual status when the principal and interest amounts contractually due are brought current or when future payments are reasonably assured.

Loan charge-offs on commercial and investor real estate loans are recorded when the facts and circumstances of the individual loan confirm the loan is not fully collectible and the loss is reasonably quantifiable. Factors considered in making these determinations are the borrower's and any guarantor's ability and willingness to pay, the status of the account in bankruptcy court (if applicable), and collateral value. Charge-off decisions for consumer loans are dictated by the Federal Financial Institutions Examination Council's (FFIEC) Uniform Retail Credit Classification and Account Management Policy which establishes standards for the classification and treatment of consumer loans, which

generally require charge-off after 120 days of delinquency.

### **Allowance for Loan Losses**

The allowance for loan losses is a reserve established through a provision for loan losses charged to expense, which represents management's best estimate of probable losses within the existing portfolio of loans. The allowance is that amount considered adequate to absorb losses inherent in the loan portfolio based on management's evaluation of credit risk as of the balance sheet date.

The allowance for loan losses includes allowance allocations calculated in accordance with FASB ASC Topic 310 – Receivables and ASC Topic 450 - Contingencies. The level of the allowance reflects management's continuing evaluation of specific credit risks, loan loss experience, current loan portfolio quality, present economic conditions and unidentified losses inherent in the current loan portfolio, as well as trends in the foregoing. This evaluation is inherently subjective, as it requires estimates that are susceptible to significant revision as more information becomes available.

The Company's allowance for loan losses consists of two components: (i) specific reserves established for probable losses on impaired loans; and (ii) general reserve for non-homogenous loans not deemed impaired and homogenous loan pools based on, but not limited to, historical loan loss experience, current economic conditions, levels of past due loans, and levels of problem loans.

Loans are deemed to be impaired when, based on current information and events, it is probable that the Company will not be able to collect all amounts due (principal and interest payments), according to the contractual terms of the loan agreement. Loans to borrowers who are experiencing financial difficulties and whose loans were modified with concessions are classified as troubled debt restructurings and measured for impairment. Loans to borrowers that have filed Chapter 7 bankruptcy, but continue to perform as agreed are classified as troubled debt restructurings and measured for impairment.

## **Long-Lived Assets**

Premises and equipment is stated at cost less accumulated depreciation, computed on the straight-line method over the estimated useful lives for each type of asset with premises being depreciated over a range of 10 to 40 years, and equipment being depreciated over a range of 3 to 10 years. Additions, renovations and leasehold improvements to premises are capitalized and depreciated over the lesser of the useful life or the remaining lease term. Repairs and maintenance are charged to noninterest expense as incurred.

Intangible assets, other than goodwill, consist of core deposit intangible assets and client relationship assets that were recognized in connection with various acquisitions. Core deposit intangible assets are amortized on the straight-line method over various periods, with the majority being amortized over an average of 5 to 10 years. Other identifiable intangibles are amortized on the straight-line method over their estimated useful lives. At December 31, 2014, all of the Company's core deposit intangible and client relationship assets were fully amortized.

Long-lived assets are evaluated for impairment if circumstances suggest that their carrying value may not be recoverable, by comparing the carrying value to estimated undiscounted cash flows. If the asset is deemed impaired, an impairment charge is recorded equal to the carrying value less the fair value.

## **Bank Owned Life Insurance (BOLI)**

The Company, through its subsidiary bank, has purchased life insurance policies on certain key officers. Bank owned life insurance is recorded at the amount that can be realized under the insurance contract at the balance sheet date, which is the cash surrender value adjusted for other charges or other amounts due that are probable at settlement.

## **Goodwill**

Goodwill represents the excess of the cost of businesses acquired over the fair value of the net assets acquired. In accordance with FASB ASC Topic 350, the Company determined it has one goodwill reporting unit. Goodwill is tested for impairment at least annually or on an interim basis if an event occurs or circumstances change that would more likely than not reduce the fair value of the reporting unit below its carrying value. See Note 5 – Intangible Assets for additional information.

## **Other Real Estate Owned**

Assets acquired through, or in lieu of, loan foreclosure are held for sale and are initially recorded at the lower of cost or fair value less estimated selling costs, establishing a new cost basis. Subsequent to foreclosure, valuations are periodically performed by management and the assets are carried at the lower of carrying amount or fair value less cost to sell. The valuation of foreclosed assets is subjective in nature and may be adjusted in the future because of changes in economic conditions. Revenue and expenses from operations and changes in value are included in noninterest expense.

### **Loss Contingencies**

Loss contingencies, including claims and legal actions arising in the ordinary course of business are recorded as liabilities when the likelihood of loss is probable and an amount or range of loss can be reasonably estimated.

### **Revenue Recognition**

The Company recognizes revenue as it is earned based on contractual terms, as transactions occur, or as services are provided and collectability is reasonably assured. Certain specific policies include the following:

*Deposit Fees.* Deposit fees are primarily overdraft and insufficient fund fees and monthly transaction-based fees. These fees are recognized as earned or as transactions occur and services are provided.

*Bank Card Fees.* Bank card fees primarily include interchange income from client use of consumer and business debit cards. Interchange income is a fee paid by a merchant bank to the card-issuing bank through the interchange network. Interchange fees are set by the credit card associations and are based on cardholder purchase volumes. The Company records interchange income as transactions occur.

## **Income Taxes**

Income tax expense is the total of the current year income tax due or refundable and the change in deferred tax assets and liabilities (excluding deferred tax assets and liabilities related to business combinations or components of other comprehensive income). Deferred tax assets and liabilities are the expected future tax amounts for the temporary differences between carrying amounts and tax bases of assets and liabilities, computed using enacted tax rates. A valuation allowance, if needed, reduces deferred tax assets to the expected amount most likely to be realized. Realization of deferred tax assets is dependent upon the generation of a sufficient level of future taxable income and recoverable taxes paid in prior years.

The Company files a consolidated federal income tax return and each subsidiary files a separate state income tax return.

## **Earnings Per Common Share**

Basic earnings per common share is based on net income divided by the weighted-average number of common shares outstanding during the period excluding non-vested stock. Diluted earnings per common share include the dilutive effect of stock options and non-vested stock awards granted using the treasury stock method. A reconciliation of the weighted-average shares used in calculating basic earnings per common share and the weighted average common shares used in calculating diluted earnings per common share for the reported periods is provided in Note 13 — Earnings Per Share.

## **Comprehensive Income**

Comprehensive income includes all changes in shareowners' equity during a period, except those resulting from transactions with shareowners. Besides net income, other components of the Company's comprehensive income include the after tax effect of changes in the net unrealized gain/loss on securities available for sale and changes in the funded status of defined benefit and supplemental executive retirement plans. Comprehensive income is reported in the accompanying Consolidated Statements of Comprehensive Income and Changes in Shareowners' Equity.

## **Stock Based Compensation**

Compensation cost is recognized for share based awards issued to employees, based on the fair value of these awards at the date of grant. The market price of the Company's common stock at the date of the grant is used for restricted

stock awards. For stock option awards, a Black-Scholes model is utilized to estimate the fair value of the options. Compensation cost is recognized over the requisite service period, generally defined as the vesting period.

## **NEW AUTHORITATIVE ACCOUNTING GUIDANCE**

*ASU 2014-01 “Investments – Equity Method and Joint Ventures (Topic 323) – Accounting for Investments in Qualified Affordable Housing Projects.”* ASU 2014-01 provides guidance related to the accounting for investments in qualified affordable housing projects. The guidance allows the holder of low income housing tax credit (“LIHTC”) investments to apply a proportional amortization method that would recognize the cost of the investment as a part of income tax expense, provided that the investment meets certain criteria. The guidance is silent regarding statement of financial position classification, although it would not be appropriate to classify the investment as a deferred tax asset. The decision to apply the proportional amortization method is an accounting policy election. Entities may also elect to continue to account for these investments using the equity method. The guidance will be applied retrospectively and is effective for fiscal years, and interim periods within those years, beginning after December 15, 2014. Early adoption is permitted. The Company does not believe this pronouncement will have a significant impact on its financial statements.

*ASU 2014-04 “Receivables – Troubled Debt Restructurings by Creditors (Topic 310-40) – Reclassification of Residential Real Estate Collateralized Consumer Loans Upon Foreclosure.”* ASU 2014-04 provides guidance regarding the reclassification of residential real estate collateralized consumer mortgage loans upon foreclosures. The guidance requires reclassification of a consumer mortgage loan to other real estate owned upon obtaining legal title to the residential property, which could occur either through foreclosure or through a deed in lieu of foreclosure or similar legal agreement. The existence of a borrower redemption right will not prevent the lender from reclassifying a loan to real estate once the lender obtains legal title to the property. In addition, entities are required to disclose the amount of foreclosed residential real estate properties and the recorded investment in residential real estate mortgage loans in the process of foreclosure on both an interim and annual basis. The guidance may be applied prospectively or on a modified retrospective basis in fiscal years, and interim periods within those fiscal years, beginning after December 15, 2014. Early adoption is permitted. The Company does not believe this pronouncement will have a significant impact on its financial statements.



*ASU 2014-09, "Revenue from Contracts with Customers (Topic 606)."* ASU 2014-09 implements a common revenue standard that clarifies the principles for recognizing revenue. The core principle of ASU 2014-09 is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. To achieve that core principle, an entity should apply the following steps: (i) identify the contract(s) with a customer, (ii) identify the performance obligations in the contract, (iii) determine the transaction price, (iv) allocate the transaction price to the performance obligations in the contract and (v) recognize revenue when (or as) the entity satisfies a performance obligation. ASU 2014-09 is effective for the Company on January 1, 2017. The Company does not believe this pronouncement will have a significant impact on its financial statements.

*ASU 2014-14, "Receivables-Troubled Debt Restructurings by Creditors (Topic 310-40) – Classification of Certain Government-Guaranteed Mortgage Loans Upon Foreclosure."* ASU 2014-14 requires that a mortgage loan be derecognized and that a separate other receivable be recognized upon foreclosure if the following conditions are met: (i) the loan has a government guarantee that is not separable from the loan before foreclosure, (ii) at the time of foreclosure, the creditor has the intent to convey the real estate property to the guarantor and make a claim on the guarantee, and the creditor has the ability to recover that claim, (iii) at the time of foreclosure, any amount of the claim that is determined on the basis of the fair value of the real estate is fixed. The guidance may be applied prospectively or on a modified retrospective basis in fiscal years, and interim periods within those fiscal years, beginning after December 15, 2014. The Company does not believe that this pronouncement will have a significant impact on its financial statements.

*ASU 2015-01, "Income Statement - Extraordinary and Unusual Items (Subtopic 225-20) – Simplifying Income Statement Presentation by Eliminating the Concept of Extraordinary Items."* ASU 2015-01 eliminates from U.S. GAAP the concept of extraordinary items, which, among other things, required an entity to segregate extraordinary items considered to be unusual and infrequent from the results of ordinary operations and show the item separately in the income statement, net of tax, after income from continuing operations. ASU 2015-01 is effective for the Company beginning January 1, 2016, though early adoption is permitted. ASU 2015-01 is not expected to have a significant impact on the Company's financial statements.

*ASU 2015-02, "Consolidation (Topic 810) – Amendments to the Consolidation Analysis."* ASU 2015-02 is comprised of three Subtopics. Subtopic 810-10 provides guidance on general consolidation issues, as well as guidance related to variable interest entities and consolidation of entities controlled by contract. Subtopic 810-20 provides guidance related to the potential consolidation of partnerships and similar interests. Subtopic 810-30 provides guidance on whether and how a sponsor should consolidate a research and development arrangement. ASU 2015-02 is effective for the Company beginning December 15, 2015, though early adoption is permitted. ASU 2015-02 is not expected to have a significant impact on the Company's financial statements.

**Note 2****INVESTMENT SECURITIES**

*Investment Portfolio Composition.* The amortized cost and related market value of investment securities at December 31 were as follows:

	<b>2014</b>				<b>2013</b>			
	Amortized Cost	Unrealized Gains	Unrealized Losses	Market Value	Amortized Cost	Unrealized Gain	Unrealized Losses	Market Value
<b>Available for Sale</b>								
U.S. Government Treasury	\$ 185,830	\$ 220	\$ 19	\$ 186,031	\$ 71,791	\$ 82	\$ 40	\$ 71,833
U.S. Government Agency	95,950	289	142	96,097	75,275	127	256	75,146
States and Political Subdivisions	48,405	65	82	48,388	91,605	167	19	91,753
Mortgage-Backed Securities	2,094	193	—	2,287	2,583	212	—	2,795
Equity Securities <sup>(1)</sup>	8,745	—	—	8,745	9,893	—	—	9,893
<b>Total</b>	<b>\$ 341,024</b>	<b>\$ 767</b>	<b>\$ 243</b>	<b>\$ 341,548</b>	<b>\$ 251,147</b>	<b>\$ 588</b>	<b>\$ 315</b>	<b>\$ 251,420</b>
<b>Held to Maturity</b>								
U.S. Government Treasury	\$ 76,179	\$ 144	\$ 6	\$ 76,317	\$ 43,533	\$ 84	\$ 38	\$ 43,579
U.S. Government Agency	19,807	29	19	19,817	15,794	38	22	15,810
States and Political Subdivisions	26,717	36	6	26,747	33,216	53	4	33,265
Mortgage-Backed Securities	40,878	33	380	40,531	55,668	12	1,373	54,307
<b>Total</b>	<b>\$ 163,581</b>	<b>\$ 242</b>	<b>\$ 411</b>	<b>\$ 163,412</b>	<b>\$ 148,211</b>	<b>\$ 187</b>	<b>\$ 1,437</b>	<b>\$ 146,961</b>
<b>Total Investment Securities</b>	<b>\$ 504,605</b>	<b>\$ 1,009</b>	<b>\$ 654</b>	<b>\$ 504,960</b>	<b>\$ 399,358</b>	<b>\$ 775</b>	<b>\$ 1,752</b>	<b>\$ 398,381</b>

<sup>(1)</sup> *Includes Federal Home Loan Bank and Federal Reserve Bank stock recorded at cost of \$3.9 million and \$4.8 million, respectively, at December 31, 2014 and \$5.0 million and \$4.8 million, respectively, at December 31, 2013.*

During the third quarter of 2013, the Company transferred certain securities from available for sale to held to maturity. Transfers of securities into the held to maturity categories from available for sale are made at fair value on the date of the transfer. The securities had an aggregate fair value of \$63.0 million with an aggregate net unrealized loss of \$523,000 on the date of the transfer. The net unamortized, unrealized loss on the transferred securities included in accumulated other comprehensive income in the accompanying balance sheet as of December 31, 2014 totaled \$428,000. This amount will be amortized out of accumulated other comprehensive income over the remaining life of the underlying securities as an adjustment of the yield on those securities.

Securities with an amortized cost of \$337.9 million and \$258.5 million at December 31, 2014 and December 31, 2013, respectively, were pledged to secure public deposits and for other purposes.

The Bank, as a member of the Federal Home Loan Bank of Atlanta (“FHLB”), is required to own capital stock in the FHLB based generally upon the balances of residential and commercial real estate loans, and FHLB advances. FHLB stock which is included in other securities is pledged to secure FHLB advances. No ready market exists for this stock, and it has no quoted market value; however, redemption of this stock has historically been at par value.

*Investment Sales.* The total proceeds from the sale of investment securities and the gross realized gains and losses from the sale of such securities for each of the last three years are as follows:

<i>(Dollars in Thousands)</i>	Year	Total Proceeds	Gross Realized Gains	Gross Realized Losses
	2014	\$ —	\$ —	\$ —
	2013	7,506	3	—
	2012	\$ 805	\$ —	\$ —

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*Maturity Distribution.* As of December 31, 2014, the Company's investment securities had the following maturity distribution based on contractual maturity. Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations. Mortgage-backed securities and certain amortizing U.S. government agency securities are shown separately since they are not due at a certain maturity date.

(Dollars in Thousands)	Available for Sale		Held to Maturity	
	Amortized Cost	Market Value	Amortized Cost	Market Value
Due in one year or less	\$45,747	\$45,780	\$17,957	\$17,983
Due after one through five years	213,639	213,786	104,745	104,898
Mortgage-Backed Securities	2,094	2,287	40,879	40,531
U.S. Government Agency	70,799	70,950	—	—
Equity Securities	8,745	8,745	—	—
Total	\$341,024	\$341,548	\$163,581	\$163,412

*Other Than Temporarily Impaired Securities.* The following table summarizes the investment securities with unrealized losses at December 31, aggregated by major security type and length of time in a continuous unrealized loss position:

(Dollars in Thousands)	Less Than 12 Months		Greater Than 12 Months		Total	
	Market Value	Unrealized Losses	Market Value	Unrealized Losses	Market Value	Unrealized Losses
<b>2014</b>						
<b>Available for Sale</b>						
U.S. Government Treasury	\$35,838	\$ 19	\$—	\$ —	\$35,838	\$ 19
U.S. Government Agency	18,160	54	18,468	88	36,628	142
States and Political Subdivisions	16,497	77	505	5	17,002	82
Total	70,495	150	18,973	93	89,468	243
<b>Held to Maturity</b>						
U.S. Government Treasury	15,046	6	—	—	15,046	6
U.S. Government Agency	10,002	19	—	—	10,002	19
States and Political Subdivisions	3,788	6	—	—	3,788	6
Mortgage-Backed Securities	15,066	149	18,155	231	33,221	380
Total	\$43,902	\$ 180	\$18,155	\$ 231	\$62,057	\$ 411
<b>2013</b>						
<b>Available for Sale</b>						
U.S. Government Treasury	\$24,924	\$ 40	\$—	\$ —	\$24,924	\$ 40
U.S. Government Agency	40,944	235	4,842	21	45,786	256
States and Political Subdivisions	4,101	7	511	12	4,612	19
Total	69,969	282	5,353	33	75,322	315
<b>Held to Maturity</b>						

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U.S. Government Treasury	10,054	38	—	—	10,054	38
U.S. Government Agency	5,676	22	—	—	5,676	22
States and Political Subdivisions	3,316	4	—	—	3,316	4
Mortgage-Backed Securities	44,031	1,373	—	—	44,031	1,373
Total	\$63,077	\$ 1,437	\$—	\$ —	\$63,077	\$ 1,437

Management evaluates securities for other than temporary impairment at least quarterly, and more frequently when economic or market concerns warrant such evaluation. Consideration is given to: 1) the length of time and the extent to which the fair value has been less than amortized cost, 2) the financial condition and near-term prospects of the issuer, and 3) the intent and ability of the Company to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in cost. In analyzing an issuer's financial condition, management considers whether the securities are issued by the federal government or its agencies, whether downgrades by rating agencies have occurred, regulatory issues, and analysts' reports.

Approximately \$19.0 million of investment securities with an unrealized loss of approximately \$93,000 have been in a loss position for greater than 12 months. These debt securities are in a loss position because they were acquired when the general level of interest rates was lower than that on December 31, 2014. The Company believes that the unrealized losses in these debt securities are temporary in nature and that the full principal will be collected as anticipated. Because the declines in the market value of these investments are attributable to changes in interest rates and not credit quality and because the Company has the present ability and intent to hold these investments until there is a recovery in fair value, which may be at maturity, the Company does not consider these investments to be other-than-temporarily impaired at December 31, 2014.

**NOTE 3 – LOANS, NET**

*Loan Portfolio Composition.* The composition of the loan portfolio at December 31 was as follows:

(Dollars in Thousands)	2014	2013
Commercial, Financial and Agricultural	\$ 136,925	\$ 126,607
Real Estate – Construction	41,596	31,012
Real Estate – Commercial Mortgage	510,120	533,871
Real Estate – Residential <sup>(1)</sup>	295,969	309,692
Real Estate – Home Equity	229,572	227,922
Consumer	217,192	159,500
Loans, Net of Unearned Income	\$ 1,431,374	\$ 1,388,604

<sup>(1)</sup> *Includes loans in process with outstanding balances of \$7.4 million and \$6.8 million for 2014 and 2013, respectively.*

Net deferred fees included in loans were \$1.5 million at December 31, 2014 and December 31, 2013.

The Company has pledged a blanket floating lien on all 1-4 family residential mortgage loans, commercial real estate mortgage loans, and home equity loans to support available borrowing capacity at the FHLB of Atlanta and has pledged a blanket floating lien on all consumer loans, commercial loans, and construction loans to support available borrowing capacity at the Federal Reserve Bank of Atlanta.

*Nonaccrual Loans.* Loans are generally placed on nonaccrual status if principal or interest payments become 90 days past due and/or management deems the collectability of the principal and/or interest to be doubtful. Loans are returned to accrual status when the principal and interest amounts contractually due are brought current or when future payments are reasonably assured.

The following table presents the recorded investment in nonaccrual loans and loans past due over 90 days and still on accrual by class of loans at December 31:

(Dollars in Thousands)	2014		2013	
	Nonaccrual	90 + Days	Nonaccrual	90 + Days
Commercial, Financial and Agricultural	\$ 507	—	\$ 188	—
Real Estate – Construction	424	—	426	—
Real Estate – Commercial Mortgage	5,806	—	25,227	—

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Real Estate – Residential	6,737	—	6,440	—
Real Estate – Home Equity	2,544	—	4,084	—
Consumer	751	—	599	—
Total	\$16,769	—	\$36,964	—

*Loan Portfolio Aging.* A loan is defined as a past due loan when one full payment is past due or a contractual maturity is over 30 days past due (“DPD”).

The following table presents the aging of the recorded investment in past due loans by class of loans at December 31,

	30-59 DPD	60-89 DPD	90 + DPD	Total Past Due	Total Current	Total Loans
<i>(Dollars in Thousands)</i>						
2014						
Commercial, Financial and Agricultural	\$352	\$155	\$ —	\$ 507	\$135,911	\$136,925
Real Estate – Construction	690	—	—	690	40,482	41,596
Real Estate – Commercial Mortgage	1,701	569	—	2,270	502,044	510,120
Real Estate – Residential	682	1,147	—	1,829	287,403	295,969
Real Estate – Home Equity	689	85	—	774	226,254	229,572
Consumer	625	97	—	722	215,719	217,192
Total	\$4,739	\$2,053	\$ —	\$ 6,792	\$1,407,813	\$1,431,374
2013						
Commercial, Financial and Agricultural	\$258	\$100	\$ —	\$ 358	\$126,062	\$126,607
Real Estate – Construction	—	—	—	—	30,587	31,012
Real Estate – Commercial Mortgage	1,548	672	—	2,220	506,424	533,871
Real Estate – Residential	1,647	1,090	—	2,737	300,514	309,692
Real Estate – Home Equity	848	212	—	1,060	222,778	227,922
Consumer	1,127	244	—	1,371	157,529	159,500
Total	\$5,428	\$2,318	\$ —	\$ 7,746	\$1,343,894	\$1,388,604

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*Allowance for Loan Losses.* The allowance for loan losses is a reserve established through a provision for loan losses charged to expense, which represents management's best estimate of probable losses within the existing portfolio of loans. Loans are charged-off to the allowance when losses are deemed to be probable and reasonably quantifiable.

The following table details the activity in the allowance for loan losses by portfolio class for the years ended December 31. Allocation of a portion of the allowance to one category of loans does not preclude its availability to absorb losses in other categories.

	Commercial,		Real	Real	Real	Real		Total
	Financial,	Real	Estate	Commercial	Estate	Equity	Unallocated	
(Dollars in Thousands)	Agriculture	Construction	Mortgage	Residential	Equity	Consumer	Unallocated	Total
<b>2014</b>								
Beginning Balance	\$ 699	\$ 1,580	\$ 7,710	\$ 9,073	\$ 3,051	\$ 982	\$ —	\$23,095
Provision for Loan Losses	742	(718 )	897	(1,145 )	1,069	1,060	—	1,905
Charge-Offs	(871 )	(28 )	(3,788 )	(2,160 )	(1,379 )	(1,820 )	—	(10,046)
Recoveries	214	9	468	752	141	1,001	—	2,585
Net Charge-Offs	(657 )	(19 )	(3,320 )	(1,408 )	(1,238 )	(819 )	—	(7,461 )
Ending Balance	\$ 784	\$ 843	\$ 5,287	\$ 6,520	\$ 2,882	\$ 1,223	\$ —	\$17,539
<b>2013</b>								
Beginning Balance	\$ 1,253	\$ 2,856	\$ 11,081	\$ 8,678	\$ 2,945	\$ 1,327	\$ 1,027	\$29,167
Provision for Loan Losses	(15 )	(207 )	(83 )	3,392	971	441	(1,027 )	3,472
Charge-Offs	(748 )	(1,070 )	(3,651 )	(3,835 )	(1,159 )	(1,751 )	—	(12,214)
Recoveries	209	1	363	838	294	965	—	2,670
Net Charge-Offs	(539 )	(1,069 )	(3,288 )	(2,997 )	(865 )	(786 )	—	(9,544 )
Ending Balance	\$ 699	\$ 1,580	\$ 7,710	\$ 9,073	\$ 3,051	\$ 982	\$ —	\$23,095
<b>2012</b>								
Beginning Balance	\$ 1,534	\$ 1,133	\$ 10,660	\$ 12,518	\$ 2,392	\$ 1,887	\$ 911	\$31,035
Provision for Loan Losses	251	2,309	5,770	4,588	3,050	82	116	16,166
Charge-Offs	(822 )	(629 )	(6,031 )	(9,719 )	(2,896 )	(2,125 )	—	(22,222)
Recoveries	290	43	682	1,291	399	1,483	—	4,188
Net Charge-Offs	(532 )	(586 )	(5,349 )	(8,428 )	(2,497 )	(642 )	—	(18,034)
Ending Balance	\$ 1,253	\$ 2,856	\$ 11,081	\$ 8,678	\$ 2,945	\$ 1,327	\$ 1,027	\$29,167



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The following table details the amount of the allowance for loan losses by portfolio class at December 31, disaggregated on the basis of the Company's impairment methodology.

(Dollars in Thousands)	Commercial, Financial, Agricultural	Real Estate Construction	Real Estate Commercial Mortgage	Real Estate Residential	Real Estate Home Equity	Consumer	Unallocated	Total
<b>2014</b>								
Period-end amount								
Allocated to:								
Loans Individually Evaluated for Impairment	\$ 293	\$ —	\$ 2,733	\$ 2,113	\$ 638	\$ 5	\$ —	\$ 5,782
Loans Collectively Evaluated for Impairment	491	843	2,554	4,407	2,244	1,218	—	11,757
Ending Balance	\$ 784	\$ 843	\$ 5,287	\$ 6,520	\$ 2,882	\$ 1,223	\$ —	\$ 17,539
<b>2013</b>								
Period-end amount								
Allocated to:								
Loans Individually Evaluated for Impairment	\$ 75	\$ 66	\$ 4,336	\$ 2,047	\$ 682	\$ 23	\$ —	\$ 7,229
Loans Collectively Evaluated for Impairment	624	1,514	3,374	7,026	2,369	959	—	15,866
Ending Balance	\$ 699	\$ 1,580	\$ 7,710	\$ 9,073	\$ 3,051	\$ 982	\$ —	\$ 23,095
<b>2012</b>								
Period-end amount								
Allocated to:								
Loans Individually Evaluated for Impairment	\$ 210	\$ 714	\$ 6,641	\$ 2,778	\$ 546	\$ 32	\$ —	\$ 10,921
Loans Collectively Evaluated for Impairment	1,043	2,142	4,440	5,900	2,399	1,295	1,027	18,246
Ending Balance	\$ 1,253	\$ 2,856	\$ 11,081	\$ 8,678	\$ 2,945	\$ 1,327	\$ 1,027	\$ 29,167

The Company's recorded investment in loans as of December 31 related to each balance in the allowance for loan losses by portfolio class and disaggregated on the basis of the Company's impairment methodology was as follows:

(Dollars in Thousands)	Commercial, Financial, Agricultural	Real Estate Construction	Real Estate Commercial Mortgage	Real Estate Residential	Real Estate Home Equity	Consumer	Unallocated	Total
<b>2014</b>								

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Individually Evaluated for Impairment	\$ 1,040	\$ 401	\$ 32,242	\$ 20,120	\$ 3,074	\$ 216	\$ —	\$ 57,093
Collectively Evaluated for Impairment	135,885	41,195	477,878	275,849	226,498	216,976	—	1,374,281
Total	\$ 136,925	\$ 41,596	\$ 510,120	\$ 295,969	\$ 229,572	\$ 217,192	\$ —	\$ 1,431,374

**2013**

Individually Evaluated for Impairment	\$ 1,580	\$ 557	\$ 49,973	\$ 20,470	\$ 3,359	\$ 355	\$ —	\$ 76,294
Collectively Evaluated for Impairment	125,027	30,455	483,898	289,222	224,563	159,145	—	1,312,310
Total	\$ 126,607	\$ 31,012	\$ 533,871	\$ 309,692	\$ 227,922	\$ 159,500	\$ —	\$ 1,388,604

**2012**

Individually Evaluated for Impairment	\$ 2,325	\$ 4,232	\$ 74,650	\$ 23,030	\$ 3,858	\$ 687	\$ —	\$ 108,782
Collectively Evaluated for Impairment	137,525	33,280	538,975	298,956	232,405	157,190	—	1,398,331
Total	\$ 139,850	\$ 37,512	\$ 613,625	\$ 321,986	\$ 236,263	\$ 157,877	\$ —	\$ 1,507,113

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*Impaired Loans.* Loans are deemed to be impaired when, based on current information and events, it is probable that the Company will not be able to collect all amounts due (principal and interest payments), according to the contractual terms of the loan agreement. Loans, for which the terms have been modified, and for which the borrower is experiencing financial difficulties, are considered troubled debt restructurings and classified as impaired.

The following table presents loans individually evaluated for impairment by class of loans at December 31:

<i>(Dollars in Thousands)</i>	Unpaid Principal Balance	Recorded Investment With No Allowance	Recorded Investment With Allowance	Related Allowance
2014				
Commercial, Financial and Agricultural	\$ 1,040	\$ 189	\$ 851	\$ 293
Real Estate – Construction	401	401	—	—
Real Estate – Commercial Mortgage	32,242	11,984	20,258	2,733
Real Estate – Residential	20,120	5,492	14,628	2,113
Real Estate – Home Equity	3,074	758	2,316	638
Consumer	216	3	213	5
Total	\$ 57,093	\$ 18,827	\$ 38,266	\$ 5,782
2013				
Commercial, Financial and Agricultural	\$ 1,580	\$ 443	\$ 1,137	\$ 75
Real Estate – Construction	557	—	557	66
Real Estate – Commercial Mortgage	49,973	19,860	30,113	4,336
Real Estate – Residential	20,470	4,330	16,140	2,047
Real Estate – Home Equity	3,359	646	2,713	682
Consumer	355	90	265	23
Total	\$ 76,294	\$ 25,369	\$ 50,925	\$ 7,229

Nonaccrual loans include both smaller balance homogenous loans that are collectively evaluated for impairment and individually classified impaired loans. Therefore, the sum of nonaccrual loans and accruing troubled debt restructurings will differ from the total impaired amount.

The following table summarizes the average recorded investment and interest income recognized for each of the last three years by class of impaired loans:

<i>(Dollars in Thousands)</i>	2014		2013		2012	
	Average Recorded Investment	Total Interest Income	Average Recorded Investment	Total Interest Income	Average Recorded Investment	Total Interest Income
Commercial, Financial and Agricultural	\$ 1,175	\$ 62	\$ 2,861	\$ 140	\$ 2,018	\$ 81

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Real Estate – Construction	471	4	1,181	7	4,443	70
Real Estate – Commercial Mortgage	30,760	1,725	60,043	2,062	70,701	2,113
Real Estate – Residential	16,394	1,070	21,238	860	28,680	853
Real Estate – Home Equity	2,329	72	4,037	72	3,540	95
Consumer	215	9	501	10	229	3
Total	\$51,344	\$2,942	\$89,861	\$3,151	\$109,611	\$3,215

*Credit Risk Management.* The Company has adopted comprehensive lending policies, underwriting standards and loan review procedures designed to maximize loan income within an acceptable level of risk. Management and the Board of Directors review and approve these policies and procedures on a regular basis (at least annually).

Reporting systems have been implemented to monitor loan originations, loan quality, concentrations of credit, loan delinquencies and nonperforming loans and potential problem loans. Management and the Credit Risk Oversight Committee periodically review our lines of business to monitor asset quality trends and the appropriateness of credit policies. In addition, total borrower exposure limits are established and concentration risk is monitored. As part of this process, the overall composition of the portfolio is reviewed to gauge diversification of risk, client concentrations, industry group, loan type, geographic area, or other relevant classifications of loans. Specific segments of the loan portfolio are monitored and reported to the Board on a quarterly basis and have strategic plans in place to supplement Board approved credit policies governing exposure limits and underwriting standards. Detailed below are the types of loans within the Company’s loan portfolio and risk characteristics unique to each.

Commercial, Financial, and Agricultural – Loans in this category are primarily made based on identified cash flows of the borrower with consideration given to underlying collateral and personal or other guarantees. Lending policy establishes debt service coverage ratio limits that require a borrower’s cash flow to be sufficient to cover principal and interest payments on all new and existing debt. The majority of these loans are secured by the assets being financed or other business assets such as accounts receivable, inventory, or equipment. Collateral values are determined based upon third party appraisals and evaluations. Loan to value ratios at origination are governed by established policy guidelines.

Real Estate Construction – Loans in this category consist of short-term construction loans, revolving and non-revolving credit lines and construction/permanent loans made to individuals and investors to finance the acquisition, development, construction or rehabilitation of real property. These loans are primarily made based on identified cash flows of the borrower or project and generally secured by the property being financed, including 1-4 family residential properties and commercial properties that are either owner-occupied or investment in nature. These properties may include either vacant or improved property. Construction loans are generally based upon estimates of costs and value associated with the completed project. Collateral values are determined based upon third party appraisals and evaluations. Loan to value ratios at origination are governed by established policy guidelines. The disbursement of funds for construction loans is made in relation to the progress of the project and as such these loans are closely monitored by on-site inspections.

Real Estate Commercial Mortgage – Loans in this category consists of commercial mortgage loans secured by property that is either owner-occupied or investment in nature. These loans are primarily made based on identified cash flows of the borrower or project with consideration given to underlying real estate collateral and personal guarantees. Lending policy establishes debt service coverage ratios and loan to value ratios specific to the property type. Collateral values are determined based upon third party appraisals and evaluations.

Real Estate Residential – Residential mortgage loans held in the Company’s loan portfolio are made to borrowers that demonstrate the ability to make scheduled payments with full consideration to underwriting factors such as current income, employment status, current assets, and other financial resources, credit history, and the value of the collateral. Collateral consists of mortgage liens on 1-4 family residential properties. Collateral values are determined based upon third party appraisals and evaluations. The Company does not originate sub-prime loans.

Real Estate Home Equity – Home equity loans and lines are made to qualified individuals for legitimate purposes generally secured by senior or junior mortgage liens on owner-occupied 1-4 family homes or vacation homes. Borrower qualifications include favorable credit history combined with supportive income and debt ratio requirements and combined loan to value ratios within established policy guidelines. Collateral values are determined based upon third party appraisals and evaluations.

Consumer Loans – This loan portfolio includes personal installment loans, direct and indirect automobile financing, and overdraft lines of credit. The majority of the consumer loan portfolio consists of indirect and direct automobile loans. Lending policy establishes maximum debt to income ratios, minimum credit scores, and includes guidelines for

verification of applicants' income and receipt of credit reports.

*Credit Quality Indicators.* As part of the ongoing monitoring of the Company's loan portfolio quality, management 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 performance, credit documentation, and current economic/market trends, among other factors. Risk ratings are assigned to each loan and revised as needed through established monitoring procedures for individual loan relationships over a predetermined amount and review of smaller balance homogenous loan pools. The Company uses the definitions noted below for categorizing and managing its criticized loans. Loans categorized as "Pass" do not meet the criteria set forth for the Special Mention, Substandard, or Doubtful categories and are not considered criticized.

**Special Mention** – Loans in this category are presently protected from loss, but weaknesses are apparent which, if not corrected, could cause future problems. Loans in this category may not meet required underwriting criteria and have no mitigating factors. More than the ordinary amount of attention is warranted for these loans.

**Substandard** – Loans in this category exhibit well-defined weaknesses that would typically bring normal repayment into jeopardy. These loans are no longer adequately protected due to well-defined weaknesses that affect the repayment capacity of the borrower. The possibility of loss is much more evident and above average supervision is required for these loans.

**Doubtful** – Loans in this category have all the weaknesses inherent in a loan categorized as Substandard, with the 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 following table presents the risk category of loans by segment at December 31:

<i>(Dollars in Thousands)</i>	<b>Commercial, Financial, Agriculture</b>	<b>Real Estate</b>	<b>Consumer</b>	<b>Total Criticized Loans</b>
<b>2014</b>				
Special Mention	\$ 8,059	\$ 51,060	\$ 114	\$ 59,233
Substandard	2,817	79,167	1,153	83,137
Doubtful	—	—	—	—
Total Criticized Loans	\$ 10,876	\$ 130,227	\$ 1,267	\$ 142,370
<b>2013</b>				
Special Mention	\$ 3,656	\$ 45,870	\$ 115	\$ 49,641
Substandard	4,243	108,990	1,496	114,729
Doubtful	—	900	—	900
Total Criticized Loans	\$ 7,899	\$ 155,760	\$ 1,611	\$ 165,270

*Troubled Debt Restructurings ("TDRs")*. TDRs are loans in which the borrower is experiencing financial difficulty and the Company has granted an economic concession to the borrower that it would not otherwise consider. In these instances, as part of a work-out alternative, the Company will make concessions including the extension of the loan term, a principal moratorium, a reduction in the interest rate, or a combination thereof. The impact of the TDR modifications and defaults are factored into the allowance for loan losses on a loan-by-loan basis as all TDRs are, by definition, impaired loans. Thus, specific reserves are established based upon the results of either a discounted cash flow analysis or the underlying collateral value, if the loan is deemed to be collateral dependent. In the limited circumstances that a loan is removed from TDR classification it is the Company's policy to also remove it from the impaired loan category, but to continue to individually evaluate loan impairment based on the contractual terms specified by the loan agreement.

The following table presents loans classified as TDRs at December 31:

<i>(Dollars in Thousands)</i>	2014		2013	
	Accruing	Nonaccruing	Accruing	Nonaccruing
Commercial, Financial and Agricultural	\$838	\$ 266	\$1,511	\$ —
Real Estate – Construction	—	—	156	—
Real Estate – Commercial Mortgage	26,565	—	24,735	10,308
Real Estate – Residential	14,940	1,622	16,441	458
Real Estate – Home Equity	1,856	356	1,576	241
Consumer	211	—	345	—
Total TDRs	\$44,410	\$ 2,244	\$44,764	\$ 11,007

Loans classified as TDRs during 2014, 2013, and 2012 are presented in the table below. The modifications made during the reporting period involved either an extension of the loan term, a principal moratorium, a reduction in the interest rate, or a combination thereof. The financial impact of these modifications was not material.

	<b>2014</b>		<b>2013</b>		<b>2012</b>	
	<b>Number</b>	<b>Recorded</b>	<b>Number</b>	<b>Recorded</b>	<b>Number</b>	<b>Recorded</b>
<i>(Dollars in Thousands)</i>	<b>of</b>	<b>Investment<sup>(1)</sup></b>	<b>of</b>	<b>Investment<sup>(1)</sup></b>	<b>of</b>	<b>Investment<sup>(1)</sup></b>
	<b>Contracts</b>	<b>(\$)</b>	<b>Contracts</b>	<b>(\$)</b>	<b>Contracts</b>	<b>(\$)</b>
Commercial, Financial and Agricultural	3	\$ 320	4	\$ 337	12	\$ 1,857
Real Estate – Construction	—	—	—	—	6	976
Real Estate – Commercial Mortgage	3	1,769	13	9,653	54	16,011
Real Estate – Residential	11	1,972	18	2,073	68	6,955
Real Estate – Home Equity	10	883	9	587	19	731
Consumer	1	34	6	93	60	656
Total TDRs	28	\$ 4,978	50	\$ 12,743	219	\$ 27,186

<sup>(1)</sup> Recorded investment reflects charge-offs and additional funds advanced at time of restructure, if applicable.



The following table provides information on how TDRs were modified during the periods included.

(Dollars in Thousands)	2014		2013		2012	
	Number of Contracts	Post-Modified Investment Recorded	Number of Contracts	Post-Modified Investment Recorded	Number of Contracts	Post-Modified Investment Recorded
Extended Amortization	10	\$ 1,894	15	4,334	33	8,080
Interest Rate Adjustment	1	156	9	982	1	158
Extended Amortization and Interest Rate Adjustment	8	1,179	17	5,381	53	10,027
Principal Moratorium	—	—	1	1,700	—	—
Other	9	1,749	8	346	132	8,921
Total TDRs	28	\$ 4,978	50	\$ 12,743	219	\$ 27,186

The following table presents loans classified as TDRs for which there was a payment default during the years presented and the loans were modified within the twelve months prior to default.

(Dollars in Thousands)	2014		2013		2012	
	Number of Contracts	Recorded Investment <sup>(1)</sup>	Number of Contracts	Recorded Investment <sup>(1)</sup>	Number of Contracts	Recorded Investment <sup>(1)</sup>
Commercial, Financial and Agricultural	—	\$ —	—	\$ —	—	\$ —
Real Estate – Construction	—	—	—	—	4	713
Real Estate – Commercial Mortgage	1	60	1	73	3	1,001
Real Estate – Residential	2	177	—	—	7	1,906
Real Estate – Home Equity	1	153	1	50	—	—
Consumer	—	—	—	—	1	2
Total TDRs	4	\$ 390	2	\$ 123	15	\$ 3,622

<sup>(1)</sup>Recorded investment reflects charge-offs and additional funds advanced at time of restructure, if applicable.

#### Note 4

#### PREMISES AND EQUIPMENT

The composition of the Company's premises and equipment at December 31 was as follows:

(Dollars in Thousands)	2014	2013
Land	\$24,548	\$24,522

Buildings	111,810	112,706
Fixtures and Equipment	57,579	57,498
Total	193,937	194,726
Accumulated Depreciation	(92,038 )	(91,341 )
Premises and Equipment, Net	\$ 101,899	\$ 103,385

**NOTE 5 - INTANGIBLE ASSETS**

The Company had net intangible assets of \$84.8 million at December 31, 2014 and December 31, 2013. Intangible assets were as follows:

(Dollars in Thousands)	2014		2013	
	Gross Amount	Accumulated Amortization	Gross Amount	Accumulated Amortization
Core Deposit Intangibles	\$47,176	\$ 47,176	\$47,176	\$ 47,176
Goodwill	84,811	—	84,811	—
Customer Relationship Intangible	1,867	1,867	1,867	1,835
Total Intangible Assets	\$133,854	\$ 49,043	\$133,854	\$ 49,011

*Net Core Deposit Intangibles:* As of December 31, 2013, the Company's core deposit intangibles were fully amortized. Amortization expense was \$200,000 and \$19,000 for 2012 and 2013, respectively.

*Goodwill:* As of December 31, 2014 and December 31, 2013, the Company had goodwill, net of accumulated amortization, of \$84.8 million. Goodwill is tested for impairment on an annual basis, or more often if impairment indicators exist. A goodwill impairment test consists of two steps. Step One compares the estimated fair value of the reporting unit to its carrying amount. If the carrying amount exceeds the estimated fair value, Step Two is performed by comparing the fair value of the reporting unit's implied goodwill to the carrying value of goodwill. If the carrying value of the reporting unit's goodwill exceeds the estimated fair value, an impairment charge is recorded equal to the excess.

As of December 31, 2014, the Company's net book value, including goodwill, exceeded its market capitalization, and as such, the Company performed goodwill impairment testing. The Step One test indicated that the carrying amount (including goodwill) of the Company's reporting unit was less than its estimated fair value, therefore, no impairment was recorded. The Company will continue to evaluate goodwill for impairment as defined by ASC Topic 350.

*Other:* As of December 31, 2014 and December 31, 2013, the Company had a customer relationship intangible asset, net of accumulated amortization, of \$0 and \$32,000, respectively. This intangible asset was recorded as a result of the acquisition of trust customer relationships. The Company's customer relationship intangible asset was fully amortized in February 2014. Annual amortization expense during 2014 was approximately \$32,000. Annual amortization expense for 2013 and 2012 was approximately \$191,000.

## Note 6

### OTHER REAL ESTATE OWNED

The following table presents other real estate owned activity as of December 31,

(Dollars in Thousands)	2014	2013	2012
Beginning Balance	\$48,071	\$53,426	\$62,600
Additions	15,271	24,488	22,777
Valuation Write-Downs	(3,142 )	(3,592 )	(3,336 )
Sales	(23,791)	(25,940)	(28,183)
Other	(729 )	(311 )	(432 )
Ending Balance	\$35,680	\$48,071	\$53,426

Net expenses applicable to other real estate owned as of December 31, was as follows:

(Dollars in Thousands)	2014	2013	2012
------------------------	------	------	------

Gains from the Sale of Properties	\$(774 )	\$(1,306)	\$(616 )
Losses from the Sale of Properties	2,094	2,287	3,593
Rental Income from Properties	(523 )	(293 )	(78 )
Property Carrying Costs	2,872	3,954	4,577
Valuation Adjustments	3,142	3,592	3,336
Total	\$6,811	\$8,234	\$10,812

**Note 7****DEPOSITS**

The composition of the Company's interest bearing deposits at December 31 was as follows:

<i>(Dollars in Thousands)</i>	<b>2014</b>	<b>2013</b>
NOW Accounts	\$804,337	\$794,746
Money Market Accounts	254,149	268,449
Savings Deposits	233,612	211,668
Other Time Deposits	195,581	219,922
Total Interest Bearing Deposits	\$1,487,679	\$1,494,785

At December 31, 2014 and 2013, \$2.4 million and \$2.8 million, respectively, in overdrawn deposit accounts were reclassified as loans.

Time deposits that meet or exceed the FDIC insurance limit of \$250,000 totaled \$11.6 million and \$14.1 million at December 31, 2014 and December 31, 2013, respectively.

At December 31, the scheduled maturities of time deposits were as follows:

(Dollars in Thousands)	2014
2015	\$165,989
2016	19,108
2017	6,882
2018	1,876
2019 and thereafter	1,726
Total	\$195,581

Interest expense on deposits for the three years ended December 31, was as follows:

(Dollars in Thousands)	2014	2013	2012
NOW Accounts	\$318	\$482	\$634
Money Market Accounts	190	211	255
Savings Deposits	112	101	87
Time Deposits < \$250,000	463	505	912
Time Deposits > \$250,000	16	132	220
Total	\$1,099	\$1,431	\$2,108

## Note 8

### SHORT-TERM BORROWINGS

Short-term borrowings included the following:

(Dollars in Thousands)	Federal Funds Purchased	Securities Sold Under Repurchase Agreements <sup>(1)</sup>	Other Short-Term Borrowings <sup>(2)</sup>
2014			
Balance at December 31	\$ —	\$ 47,411	\$ 2,014
Maximum indebtedness at any month end	—	47,413	2,035
Daily average indebtedness outstanding	11	42,877	1,514
Average rate paid for the year	0.76	% 0.05	% 3.76
Average rate paid on period-end borrowings	—	% 0.05	% 3.76
2013			
Balance at December 31	\$ —	\$ 47,312	\$ 4,009
Maximum indebtedness at any month end	—	55,261	8,929

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Daily average indebtedness outstanding	11		48,337		5,573	
Average rate paid for the year	0.76	%	0.05	%	3.79	%
Average rate paid on period-end borrowings	—	%	0.05	%	3.25	%

2012

Balance at December 31	\$ —		\$ 40,639		\$ 6,796	
Maximum indebtedness at any month end	—		62,458		6,991	
Daily average indebtedness outstanding	—		47,485		4,679	
Average rate paid for the year	—	%	0.05	%	3.68	%
Average rate paid on period-end borrowings	—	%	0.05	%	3.69	%

<sup>(1)</sup> *Balances are fully collateralized by government treasury or agency securities held in the Company's investment portfolio.*

<sup>(2)</sup> *Comprised of FHLB debt.*

**Note 9****LONG-TERM BORROWINGS**

*Federal Home Loan Bank Advances.* FHLB advances totaled \$31.1 million at December 31, 2014 and \$38.0 million at December 31, 2013. The advances mature at varying dates from 2015 through 2025 and had a weighted-average rate of 3.17% and 3.20% at December 31, 2014 and 2013, respectively. The FHLB advances are collateralized by a blanket floating lien on all 1-4 family residential mortgage loans, commercial real estate mortgage loans, and home equity mortgage loans. Interest on the FHLB advances is paid on a monthly basis.

Scheduled minimum future principal payments on FHLB advances at December 31 were as follows:

(Dollars in Thousands)	2014
2015	\$2,751
2016	2,829
2017	6,515
2018	7,714
2019	4,653
2020 and thereafter	6,635
Total	\$31,097

*Junior Subordinated Deferrable Interest Notes.* The Company has issued two junior subordinated deferrable interest notes to wholly owned Delaware statutory trusts. The first note for \$30.9 million was issued to CCBG Capital Trust I. The second note for \$32.0 million was issued to CCBG Capital Trust II. The two trusts are considered variable interest entities for which the Company is not the primary beneficiary. Accordingly, the accounts of the trusts are not included in the Company's consolidated financial statements. See Note 1 - Summary of Significant Accounting Policies for additional information about the Company's consolidation policy. Details of the Company's transaction with the two trusts are provided below.

In November 2004, CCBG Capital Trust I issued \$30.0 million of trust preferred securities which represent interest in the assets of the trust. The interest payments are due quarterly at 3-month LIBOR plus a margin of 1.90%, adjusted quarterly. The trust preferred securities will mature on December 31, 2034, and are redeemable upon approval of the Federal Reserve in whole or in part at the option of the Company at any time after December 31, 2009 and in whole at any time upon occurrence of certain events affecting their tax or regulatory capital treatment. Distributions on the trust preferred securities are payable quarterly on March 31, June 30, September 30, and December 31 of each year. CCBG Capital Trust I also issued \$928,000 of common equity securities to CCBG. The proceeds of the offering of trust preferred securities and common equity securities were used to purchase a \$30.9 million junior subordinated deferrable interest note issued by the Company, which has terms similar to the trust preferred securities.

In May 2005, CCBG Capital Trust II issued \$31.0 million of trust preferred securities which represent interest in the assets of the trust. The interest payments are due quarterly at 3-month LIBOR plus a margin of 1.80%, adjusted annually. The trust preferred securities will mature on June 15, 2035, and are redeemable upon approval of the Federal Reserve in whole or in part at the option of the Company and in whole at any time upon occurrence of certain events affecting their tax or regulatory capital treatment. Distributions on the trust preferred securities are payable quarterly on March 15, June 15, September 15, and December 15 of each year. CCBG Capital Trust II also issued \$959,000 of common equity securities to CCBG. The proceeds of the offering of trust preferred securities and common equity securities were used to purchase a \$32.0 million junior subordinated deferrable interest note issued by the Company, which has terms substantially similar to the trust preferred securities.

The Company has the right to defer payments of interest on the two notes at any time or from time to time for a period of up to twenty consecutive quarterly interest payment periods. Under the terms of each note, in the event that under certain circumstances there is an event of default under the note or the Company has elected to defer interest on the note, the Company may not, with certain exceptions, declare or pay any dividends or distributions on its capital stock or purchase or acquire any of its capital stock. As of December 31, 2014, the Company has paid all interest payments in full.

The Company has entered into agreements to guarantee the payments of distributions on the trust preferred securities and payments of redemption of the trust preferred securities. Under these agreements, the Company also agrees, on a subordinated basis, to pay expenses and liabilities of the two trusts other than those arising under the trust preferred securities. The obligations of the Company under the two junior subordinated notes, the trust agreements establishing the two trusts, the guarantee and agreement as to expenses and liabilities, in aggregate, constitute a full and unconditional guarantee by the Company of the two trusts' obligations under the two trust preferred security issuances.

Despite the fact that the accounts of CCBG Capital Trust I and CCBG Capital Trust II are not included in the Company's consolidated financial statements, the \$30.0 million and \$31.0 million, respectively, in trust preferred securities issued by these subsidiary trusts are included in the Tier I Capital of Capital City Bank Group, Inc. as allowed by Federal Reserve guidelines.



**Note 10****INCOME TAXES**

The provision for income taxes reflected in the statements of comprehensive income is comprised of the following components:

(Dollars in Thousands)	2014	2013	2012
<b>Current:</b>			
Federal	\$(51 )	\$(75 )	\$1,189
State	(2,916)	195	280
	(2,967)	120	1,469
<b>Deferred:</b>			
Federal	4,270	1,650	(1,260)
State	249	99	(1,597)
Valuation Allowance	102	56	52
	4,621	1,805	(2,805)
<b>Total:</b>			
Federal	4,219	1,575	(71 )
State	(2,667)	294	(1,317)
Valuation Allowance	102	56	52
Total	\$1,654	\$1,925	\$(1,336)

Income taxes provided were different than the tax expense computed by applying the statutory federal income tax rate of 35% to pre-tax income as a result of the following:

(Dollars in Thousands)	2014	2013	2012
Tax Expense at Federal Statutory Rate	\$3,820	\$2,790	\$(430 )
<b>Increases (Decreases) Resulting From:</b>			
Tax-Exempt Interest Income	(327 )	(385 )	(402 )
Change in Reserve for Uncertain Tax Positions	(2,902)	(777 )	(347 )
State Taxes, Net of Federal Benefit	892	191	(856 )
Other	69	50	199
Change in Valuation Allowance	102	56	52
Increase Deferred Tax Liability for Equity Investment	—	—	448
Actual Tax Expense	\$1,654	\$1,925	\$(1,336)

Deferred income tax liabilities and assets result from differences between assets and liabilities measured for financial reporting purposes and for income tax return purposes. These assets and liabilities are measured using the enacted tax rates and laws that are currently in effect. The net deferred tax asset and the temporary differences comprising that balance at December 31, 2014 and 2013 are as follows:

(Dollars in Thousands)	2014	2013
Deferred Tax Assets Attributable to:		
Allowance for Loan Losses	\$6,767	\$8,910
Accrued Pension/SERP	13,547	5,284
State Net Operating Loss and Tax Credit Carry-Forwards	5,012	4,906
Other Real Estate Owned	8,229	9,459
Other	4,226	5,304
Total Deferred Tax Assets	\$37,781	\$33,863

Deferred Tax Liabilities Attributable to:		
Depreciation on Premises and Equipment	\$6,247	\$6,322
Deferred Loan Fees and Costs	2,490	2,446
Intangible Assets	3,719	3,419
Other	612	526
Total Deferred Tax Liabilities	13,068	12,713
Valuation Allowance	1,328	1,226
Net Deferred Tax Asset	\$23,385	\$19,924

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In the opinion of management, it is more likely than not that all of the deferred tax assets, with the exception of the separate state net operating loss carry-forward of CCBG, the separate state net operating loss carry-forwards of an inactive subsidiary, and certain of the Bank's separate state tax credit carry-forwards, will be realized. Accordingly, a valuation allowance for CCBG's separate state net operating loss carry-forward was recorded in 2008 and increased for CCBG's additional state operating loss carry-forward generated in 2009 through 2014. This valuation allowance at year-end 2014 was \$1.1 million. In addition, a valuation allowance for the inactive subsidiary's separate state net operating loss carry-forwards and for certain of the Bank's state tax credit carry-forwards totaled \$0.2 million at year-end 2014. At year-end 2014, the Company had state loss and tax credit carry-forwards of approximately \$5.0 million, which expire at various dates from 2015 through 2033, and federal credit carry-forwards of approximately \$0.5 million that never expire.

The Company had no unrecognized tax benefits at December 31, 2014. The unrecognized tax benefits were \$3.2 million and \$4.2 million at December 31, 2013 and December 31, 2012, respectively.

A reconciliation of the beginning and ending unrecognized tax benefit is as follows:

(Dollars in Thousands)	2014	2013	2012
Balance at January 1,	\$3,228	\$4,209	\$4,577
Additions Based on Tax Positions Related to Current Year	—	—	508
Decrease Due to Lapse in Statute of Limitations	—	(981 )	(876 )
Decrease Due to Settlements With Taxing Authorities	(3,228)	—	—
Balance at December 31	\$—	\$3,228	\$4,209

It is the Company's policy to recognize interest and penalties accrued relative to unrecognized tax benefits in their respective federal or state income taxes accounts. The total amounts of interest and penalties recorded in the income statement – income taxes for the years ended December 31, 2014, 2013, and 2012 were \$800,000, \$139,000, and \$108,000, respectively. The amounts accrued for interest and penalties at December 31, 2014 and 2013 were \$0 and \$0.8 million respectively.

The Company and its subsidiaries file a consolidated U.S. federal income tax return, as well as file various returns in states where its banking offices are located. The Company is no longer subject to U.S. federal or state tax examinations for years before 2011.

## Note 11

### STOCK-BASED COMPENSATION

As of December 31, 2014, the Company had three stock-based compensation plans, consisting of the 2011 Associate Incentive Plan (“AIP”), the 2011 Associate Stock Purchase Plan (“ASPP”), and the 2011 Director Stock Purchase Plan (“DSPP”). These plans, which were approved by the shareowners in April 2011, replaced substantially similar plans approved by the shareowners in 2004. Total compensation expense associated with these plans for 2012 through 2014 was \$0.5 million, \$1.4 million, and \$1.9 million, respectively.

*AIP.* The AIP allows the Company’s Board of Directors to award key associates various forms of equity-based incentive compensation. Under the 2011 AIP there were 875,000 shares reserved for issuance. In 2014, the Company, pursuant to the terms and conditions of the AIP, created the 2014 Incentive Plan (“2014 Plan”), under which all participants in the 2014 Plan were eligible to earn performance shares. Awards under the 2014 Plan were tied to internally established performance goals. At base level targets, the grant-date fair value of the shares eligible to be awarded in 2014 was approximately \$0.9 million. For 2014, a total of 50,597 shares were eligible for issuance, but additional shares could be earned if performance exceeded established goals. A total of 73,347 shares were earned for 2014 reflective of goal achievement that exceeded the base level targets. The Company recognized expense of \$1.2 million, \$965,000 and 255,000 for 2014, 2013 and 2012, respectively. After deducting the shares earned in 2014, 774,393 shares remain eligible for issuance under the 2011 AIP.

*Executive Long-Term Incentive Plan (“LTIP”).* Prior to 2007, the Company maintained a stock option program for a key executive officer (William G. Smith, Jr. - Chairman, President and CEO, CCBG). The status of the options granted under this arrangement is detailed in the table provided below. In 2007, the Company replaced its practice of entering into an annual stock option arrangement by establishing a Performance Share Unit Plan under the provisions of the AIP that allows the executive to earn shares based on the compound annual growth rate in diluted earnings per share over a three-year period. The Company recognized \$0.5 million and \$0.3 million in expense for years 2014 and 2013, respectively, under the executive’s LTIP. There was no expense for the year 2012. At the executive’s request, the Compensation Committee, with board approval, exercised its negative discretion option whereby the grant for the three-year period 2012 – 2014 was cancelled and therefore there was no payout.

A summary of the status of the Company's option shares is presented below:

Options	Shares	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term	Aggregate Intrinsic Value
Outstanding at January 1, 2014	60,384	\$ 32.79	\$ 1.9	\$ —
Expired	(23,138)	—	—	—
Outstanding at December 31, 2014	37,246	\$ 32.69	\$ 0.3	\$ —
Exercisable at December 31, 2014	37,246	\$ 32.69	\$ 0.3	\$ —

*DSPP.* The Company's DSPP allows the directors to purchase the Company's common stock at a price equal to 90% of the closing price on the date of purchase. Stock purchases under the DSPP are limited to the amount of the directors' annual retainer and meeting fees. Under the 2011 DSPP there were 150,000 shares reserved for issuance. For 2014, the Company issued 10,932 shares under the DSPP and recognized approximately \$14,000 in expense related to this plan. For 2013, the Company issued 13,348 shares and recognized approximately \$15,000 in expense related to the DSPP. For 2012, the Company issued 25,864 shares and recognized approximately \$21,000 in expense under the DSPP. As of December 31, 2014, there are 86,744 shares eligible for issuance under the 2011 DSPP.

*ASPP.* Under the Company's ASPP, substantially all associates may purchase the Company's common stock through payroll deductions at a price equal to 90% of the lower of the fair market value at the beginning or end of each six-month offering period. Stock purchases under the ASPP are limited to 10% of an associate's eligible compensation, up to a maximum of \$25,000 (fair market value on each enrollment date) in any plan year. Under the 2011 ASPP there were 593,750 shares of common stock reserved for issuance. For 2014, 28,630 shares were acquired under the ASPP and approximately \$64,000 in expense was recognized related to this plan. For 2013, 31,597 shares were acquired and approximately \$69,000 in expense was recognized related to the ASPP. For 2012, 75,257 shares were acquired and approximately \$119,000 in expense was recognized under the ASPP. As of December 31, 2014, 418,320 shares remained eligible for issuance under the ASPP.

Based on the Black-Scholes option pricing model, the weighted average estimated fair value of each of the purchase rights granted under the ASPP was \$2.12 for 2014. For 2013 and 2012, the weighted average fair value purchase right granted was \$2.21 and \$1.61, respectively. In calculating compensation, the fair value of each stock purchase right was estimated on the date of grant using the following weighted average assumptions:

	2014	2013	2012
Dividend yield	0.3 %	— %	— %
Expected volatility	21.5 %	32.0 %	32.0 %
Risk-free interest rate	0.1 %	0.1 %	0.1 %
Expected life (in years)	0.5	0.5	0.5

**Note 12****EMPLOYEE BENEFIT PLANS****Pension Plan**

The Company sponsors a noncontributory pension plan covering substantially all of its associates. Benefits under this plan generally are based on the associate's total years of service and average of the five highest years of compensation during the ten years immediately preceding their departure. The Company's general funding policy is to contribute amounts sufficient to meet minimum funding requirements as set by law and to ensure deductibility for federal income tax purposes.

The following table details on a consolidated basis the changes in benefit obligation, changes in plan assets, the funded status of the plan, components of pension expense, amounts recognized in the Company's consolidated statements of financial condition, and major assumptions used to determine these amounts.

(Dollars in Thousands)	2014	2013	2012
<b>Change in Projected Benefit Obligation:</b>			
Benefit Obligation at Beginning of Year	\$ 115,285	\$ 134,950	\$ 116,173
Service Cost	5,634	6,999	6,397
Interest Cost	5,513	5,566	5,587
Actuarial Loss (Gain)	22,632	(18,965 )	14,156
Benefits Paid	(8,438 )	(12,946 )	(7,138 )
Expenses Paid	(267 )	(319 )	(225 )
Projected Benefit Obligation at End of Year	\$ 140,359	\$ 115,285	\$ 134,950
<b>Change in Plan Assets:</b>			
Fair Value of Plan Assets at Beginning of Year	\$ 103,842	\$ 94,164	\$ 87,844
Actual Return on Plan Assets	8,035	17,943	8,683
Employer Contributions	5,000	5,000	5,000
Benefits Paid	(8,438 )	(12,946 )	(7,138 )
Expenses Paid	(267 )	(319 )	(225 )
Fair Value of Plan Assets at End of Year	\$ 108,172	\$ 103,842	\$ 94,164
<b>Funded Status of Plan and Accrued Liability Recognized at End of Year:</b>			
Other Liabilities	\$ 32,186	\$ 11,442	\$ 40,786
Accumulated Benefit Obligation at End of Year	\$ 119,750	\$ 98,796	\$ 110,985
<b>Components of Net Periodic Benefit Costs:</b>			

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Service Cost	\$5,634	\$6,999	\$6,397
Interest Cost	5,513	5,566	5,587
Expected Return on Plan Assets	(7,487 )	(7,371 )	(6,793 )
Amortization of Prior Service Costs	309	317	359
Net Loss Amortization	1,365	4,316	3,390
Net Periodic Benefit Cost	\$5,334	\$9,827	\$8,940

Weighted-Average Assumptions Used to Determine Benefit Obligation:

Discount Rate	4.15	%	5.00	%	4.25	%
Rate of Compensation Increase	3.25	%	3.25	%	3.75	%
Measurement Date	12/31/14		12/31/13		12/31/12	

Weighted-Average Assumptions Used to Determine Benefit Cost:

Discount Rate	5.00	%	4.25	%	5.00	%
Expected Return on Plan Assets	7.50	%	8.00	%	8.00	%
Rate of Compensation Increase	3.25	%	3.75	%	4.00	%

Amortization Amounts from Accumulated Other Comprehensive Income:

Net Actuarial Loss (Gain)	\$22,083	\$(29,534 )	\$12,265
Prior Service Cost	(309 )	(317 )	(359 )
Net Loss	(1,365 )	(4,316 )	(3,390 )
Deferred Tax (Benefit) Expense	(7,873 )	13,180	(3,285 )
Other Comprehensive Loss (Gain), net of tax	\$12,536	\$(20,987 )	\$5,231

Amounts Recognized in Accumulated Other Comprehensive Income:

Net Actuarial Losses	\$34,665	\$13,947	\$47,800
Prior Service Cost	1,075	1,383	1,700
Deferred Tax Benefit	(13,788 )	(5,914 )	(19,097 )
Accumulated Other Comprehensive Loss, net of tax	\$21,952	\$9,416	\$30,403

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The Company expects to recognize \$3.2 million of the net actuarial loss and \$0.3 million of the prior service cost reflected in accumulated other comprehensive income at December 31, 2014 as a component of net periodic benefit cost during 2015.

*Plan Assets.* The Company's pension plan asset allocation at year-end 2014 and 2013, and the target asset allocation for 2015 are as follows:

	Target	Percentage of Plan				
	Allocation	Assets at Year-End <sup>(1)</sup>				
	2015	2014	2014	2013	2013	
Equity Securities	70	%	74	%	72	%
Debt Securities	25	%	21	%	23	%
Cash and Cash Equivalents	5	%	5	%	5	%
Total	100	%	100	%	100	%

<sup>(1)</sup> Represents asset allocation at year-end which may differ from the average target allocation for the year due to the year-end cash contribution to the plan.

The Company's pension plan assets are overseen by the CCBG Retirement Committee. Capital City Trust Company acts as the investment manager for the plan. The investment strategy is to maximize return on investments while minimizing risk. The Company believes the best way to accomplish this goal is to take a conservative approach to its investment strategy by investing in high-grade equity and debt securities. The overall expected long-term rate of return on assets is a weighted-average expectation for the return on plan assets. The Company considers historical performance data and economic/financial data to arrive at expected long-term rates of return for each asset category.

The major categories of assets in the Company's pension plan as of December 31 are presented in the following table. Assets are segregated by the level of the valuation inputs within the fair value hierarchy established by ASC Topic 820 utilized to measure fair value (see Note 18 – Fair Value Measurements).

(Dollars in Thousands)	2014	2013
Level 1:		
U.S. Government Treasury	\$—	\$768
Equities	23,199	21,564
Mutual Funds	75,421	70,993
Cash and Cash Equivalents	5,626	5,571
Level 2:		
U.S. Government Agency	3,926	4,946
Total Fair Value of Plan Assets	\$108,172	\$103,842



*Expected Benefit Payments.* As of December 31, expected benefit payments related to the defined benefit pension plan were as follows:

(Dollars in Thousands)	2014
2015	\$8,090
2016	8,340
2017	8,969
2018	10,213
2019	10,867
2020 through 2024	54,919
Total	\$101,398

*Contributions.* The following table details the amounts contributed to the pension plan in 2013 and 2014, and the expected amount to be contributed in 2015.

	2013 <sup>(2)</sup>	2014 <sup>(2)</sup>	<b>Expected Range of Contribution 2015<sup>(1)</sup></b>
(Dollars in Thousands)			
Actual Contributions	\$5,000	\$5,000	\$5,000 - \$10,000

<sup>(1)</sup> For 2015, the Company will have the option to make a cash contribution to the plan or utilize pre-funding balances.

<sup>(2)</sup> For the 2012 and 2013 plan years, the Company made the contributions during the 2013 and 2014 calendar years.

<sup>(2)</sup> As of December 31, 2014, no contributions were made for the 2014 plan year.

**Supplemental Executive Retirement Plan**

The Company has a Supplemental Executive Retirement Plan (“SERP”) covering selected executive officers. Benefits under this plan generally are based on the same service and compensation as used for the pension plan, except the benefits are calculated without regard to the limits set by the Internal Revenue Code on compensation and benefits. The net benefit payable from the SERP is the difference between this gross benefit and the benefit payable by the pension plan.

The following table details on a consolidated basis the changes in benefit obligation, the funded status of the plan, components of pension expense, amounts recognized in the Company’s consolidated statements of financial condition, and major assumptions used to determine these amounts.

(Dollars in Thousands)	2014	2013	2012
Change in Projected Benefit Obligation:			
Benefit Obligation at Beginning of Year	\$2,379	\$3,492	\$3,030
Interest Cost	104	137	140
Actuarial Loss (Gain)	520	(1,250 )	322
Projected Benefit Obligation at End of Year	\$3,003	\$2,379	\$3,492
Funded Status of Plan and Accrued Liability Recognized at End of Year:			
Other Liabilities	\$3,003	\$2,379	\$3,492
Accumulated Benefit Obligation at End of Year	\$2,982	\$2,379	\$3,492
Components of Net Periodic Benefit Costs:			
Interest Cost	\$104	\$137	\$140
Amortization of Prior Service Cost	164	187	189
Net Gain Amortization	(661 )	(237 )	(369 )
Net Periodic Benefit Cost	\$(393 )	\$87	\$(40 )
Weighted-Average Assumptions Used to Determine Benefit Obligation:			
Discount Rate	4.15 %	5.00 %	4.25 %
Rate of Compensation Increase	3.25 %	3.25 %	3.75 %
Measurement Date	12/31/14	12/31/13	12/31/12
Weighted-Average Assumptions Used to Determine Benefit Cost:			
Discount Rate	5.00 %	4.25 %	5.00 %
Rate of Compensation Increase	3.25 %	3.75 %	4.00 %
Amortization Amounts from Accumulated Other Comprehensive Income:			
Net Actuarial Loss (Gain)	\$520	\$(1,250 )	\$322
Prior Service Cost	(164 )	(187 )	(189 )
Net Gain	660	237	369
Deferred Tax (Benefit) Expense	(392 )	463	(194 )
Other Comprehensive Loss (Gain), net of tax	\$624	\$(737 )	\$308

Amounts Recognized in Accumulated Other Comprehensive Income:

Net Actuarial Gain	\$ (632 )	\$ (1,812 )	\$ (799 )
Prior Service Cost	7	171	358
Deferred Tax Liability	241	633	170
Accumulated Other Comprehensive Gain, net of tax	\$ (384 )	\$ (1,008 )	\$ (271 )

The Company expects to recognize approximately \$0.4 million of the net actuarial gain and \$7,000 of the prior service cost reflected in accumulated other comprehensive income at December 31, 2014 as a component of net periodic benefit cost during 2015.

*Expected Benefit Payments.* As of December 31, expected benefit payments related to the SERP were as follows:

(Dollars in Thousands)	2014
2015	\$979
2016	522
2017	231
2018	215
2019	230
2020 through 2024	—
Total	\$2,177

#### **401(k) Plan**

The Company has a 401(k) Plan which enables associates to defer a portion of their salary on a pre-tax basis. The plan covers substantially all associates of the Company who meet minimum age requirements. The plan is designed to enable participants to elect to have an amount from 1% to 15% of their compensation withheld in any plan year placed in the 401(k) Plan trust account. Matching contributions of 50% from the Company are made up to 6% of the participant's compensation for eligible associates. During 2014, the Company made matching contributions of \$0.5 million. For the years 2013 and 2012, the Company made matching contributions of \$0.4 million for each respective year. The participant may choose to invest their contributions into twenty-seven investment options available to 401(k) participants, including the Company's common stock. A total of 50,000 shares of CCBG common stock have been reserved for issuance. Shares issued to participants have historically been purchased in the open market.

#### **Other Plans**

The Company has a Dividend Reinvestment and Optional Stock Purchase Plan. A total of 250,000 shares have been reserved for issuance. In recent years, shares for the Dividend Reinvestment and Optional Stock Purchase Plan have been acquired in the open market and, thus, the Company did not issue any shares under this plan in 2014, 2013 and 2012.

#### **Note 13**

#### **EARNINGS PER SHARE**

The following table sets forth the computation of basic and diluted earnings per share:

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(Dollars and Per Share Data in Thousands)	2014	2013	2012
Numerator:			
Net Income	\$9,260	\$6,045	\$108
Denominator:			
Denominator for Basic Earnings Per Share Weighted-Average Shares	17,425	17,325	17,205
Effects of Dilutive Securities Stock Compensation Plans	63	74	15
Denominator for Diluted Earnings Per Share Adjusted Weighted-Average Shares and Assumed Conversions	17,488	17,399	17,220
Basic Earnings Per Share	\$0.53	\$0.35	\$0.01
Diluted Earnings Per Share	\$0.53	\$0.35	\$0.01

Stock options for 37,246 shares of common stock related to an award earned in 2004 were not considered in computing diluted earnings per common share for 2014, 2013, and 2012 because they were anti-dilutive. Stock options for 23,138 shares of common stock, which related to an award earned in 2003 and expired unexercised in 2014, were not considered in computing diluted earnings per common share for 2013 and 2012 because they were anti-dilutive.

**Note 14****REGULATORY MATTERS**

*Regulatory Capital Requirements.* The Company (on a consolidated basis) and the Bank are subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory and possible additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the Company and Bank's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Company and the Bank must meet specific capital guidelines that involve quantitative measures of their assets, liabilities and certain off-balance sheet items as calculated under regulatory accounting practices. The capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors. Prompt corrective action provisions are not applicable to bank holding companies.

Quantitative measures established by regulation to ensure capital adequacy require the Company and the Bank to maintain minimum amounts and ratios (set forth in the following table) of total and Tier 1 capital (as defined in the regulations) to risk-weighted assets (as defined) and of Tier 1 capital (as defined) to average assets (as defined). Management believes, as of December 31, 2014 and 2013, that the Company and the Bank meet all capital adequacy requirements to which they are subject.

As of December 31, 2014, the most recent notification from the Federal Deposit Insurance Corporation categorized the Bank as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized, an institution must maintain minimum total risk-based, Tier 1 risk based and Tier 1 leverage ratios as set forth in the following tables. There are not conditions or events since the notification that management believes have changed the Bank's category. The Company and Bank's actual capital amounts and ratios as of December 31, 2014 and 2013 are also presented in the table.

	<b>Actual</b>		<b>Required For Capital Adequacy Purposes</b>		<b>To Be Well-Capitalized Under Prompt Corrective Action Provisions</b>	
(Dollars in Thousands)	Amount	Ratio	Amount	Ratio	Amount	Ratio
2014						
Tier I Capital:						
CCBG	\$ 269,503	16.67 %	\$ 64,656	4.00 %	*	*
CCB	261,655	16.24 %	64,458	4.00 %	\$ 96,687	6.00 %

Total Capital:

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CCBG	287,042	17.76%	129,313	8.00 %	*	*
CCB	279,194	17.33%	128,916	8.00 %	161,145	10.00 %

Tier I Leverage:

CCBG	269,503	10.99%	98,090	4.00 %	*	*
CCB	261,655	10.70%	97,834	4.00 %	122,293	5.00 %

2013

Tier I Capital:

CCBG	\$ 256,338	16.56%	\$ 62,058	4.00 %	*	*
CCB	256,554	16.59%	61,992	4.00 %	\$92,988	6.00 %

Total Capital:

CCBG	277,618	17.94%	124,116	8.00 %	*	*
CCB	275,927	17.85%	123,984	8.00 %	154,980	10.00 %

Tier I Leverage:

CCBG	256,338	10.46%	98,029	4.00 %	*	*
CCB	256,554	10.48%	97,931	4.00 %	122,414	5.00 %

\*Not applicable to bank holding companies.

*Dividend Restrictions.* In the ordinary course of business, the Company is dependent upon dividends from its banking subsidiary to provide funds for the payment of dividends to shareowners and to provide for other cash requirements. Banking regulations may limit the amount of dividends that may be paid. Approval by regulatory authorities is required if the effect of dividends declared would cause the regulatory capital of the Company's banking subsidiary to fall below specified minimum levels. Approval is also required if dividends declared exceed the net profits of the banking subsidiary for that year combined with the retained net profits for proceeding two years. In 2015, the bank subsidiary may declare dividends without regulatory approval of \$5.1 million plus an additional amount equal to net profits of the Company's subsidiary bank for 2015 up to the date of any such dividend declaration.

*Basel III Capital Rules Effective January 1, 2015.* In July 2013, the Company's primary federal regulator, the Federal Reserve, published final rules (the "Basel III Capital Rules") establishing a new comprehensive capital framework for U.S. banking organizations. The rules implement the Basel Committee's December 2010 framework known as "Basel III" for strengthening international capital standards as well as certain provisions of the Dodd-Frank Act. The Basel III Capital Rules substantially revise the risk-based capital requirements applicable to bank holding companies and depository institutions, including the Company and the Bank, compared to the current U.S. risk-based capital rules. The Basel III Capital Rules define the components of capital and address other issues affecting the numerator in banking institutions' regulatory capital ratios. The Basel III Capital Rules also address risk weights and other issues affecting the denominator in banking institutions' regulatory capital ratios and replace the existing risk-weighting approach, which was derived from the Basel I capital accords of the Basel Committee, with a more risk-sensitive approach based, in part, on the standardized approach in the Basel Committee's 2004 "Basel II" capital accords. The Basel III Capital Rules also implement the requirements of Section 939A of the Dodd-Frank Act to remove references to credit ratings from the federal banking agencies' rules. The Basel III Capital Rules are effective for the Company and the Bank on January 1, 2015 (subject to a phase-in period for certain provisions).



**Note 15****OTHER COMPREHENSIVE INCOME (LOSS)**

FASB Topic ASC 220, "Comprehensive Income" requires that certain transactions and other economic events that bypass the income statement be displayed as other comprehensive income. Total comprehensive income is reported in the consolidated statements of comprehensive income and changes in shareowners' equity.

The following table summarizes the tax effects for each component of other comprehensive income (loss):

(Dollars in Thousands)	Before Tax Amount	Tax (Expense) Benefit	Net of Tax Amount
<b>2014</b>			
Investment Securities:			
Change in net unrealized gain/loss on securities available for sale	\$250	\$(103 )	\$147
Amortization of losses on securities transferred from available for sale to held to maturity	70	(27 )	43
Reclassification adjustment for net gain included in net income	1	—	1
Total Investment Securities	321	(130 )	191
Benefit Plans:			
Reclassification adjustment for amortization of prior service cost	473	(182 )	291
Reclassification adjustment for amortization of net loss	705	(272 )	433
Current year actuarial (loss) gain	(22,603)	8,719	(13,884)
Total Benefit Plans	(21,425)	8,265	(13,160)
<b>Total Other Comprehensive Loss</b>	<b>\$(21,104)</b>	<b>\$8,135</b>	<b>\$(12,969)</b>
<b>2013</b>			
Investment Securities:			
Change in net unrealized gain/loss on securities available for sale	\$(1,252 )	\$483	\$(769 )
Unrealized losses on securities transferred from available for sale to held to maturity	(523 )	202	(321 )
Amortization of losses on securities transferred from available for sale to held to maturity	25	(10 )	15
Reclassification adjustment for net gain included in net income	3	(1 )	2
Reclassification adjustment for impairment loss realized in net income	600	(232 )	368
Total Investment Securities	(1,147 )	442	(705 )
Benefit Plans:			
Reclassification adjustment for amortization of prior service cost	504	(194 )	310
Reclassification adjustment for amortization of net loss	4,079	(1,574 )	2,505
Current year actuarial gain (loss)	30,784	(11,875 )	18,909
Total Benefit Plans	35,367	(13,643 )	21,724

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Total Other Comprehensive Income	\$34,220	\$ (13,201 )	\$21,019
2012			
Investment Securities:			
Change in net unrealized gain/loss on securities available for sale	\$(786 )	\$ 295	\$(491 )
Total Investment Securities	(786 )	295	(491 )
Benefit Plans:			
Reclassification adjustment for amortization of prior service cost	548	(211 )	337
Reclassification adjustment for amortization of net loss	3,021	(1,165 )	1,856
Current year actuarial (loss) gain	(12,587)	4,855	(7,732 )
Total Benefit Plans	(9,018 )	3,479	(5,539 )
Total Other Comprehensive Loss	\$(9,804 )	\$ 3,774	\$(6,030 )
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Accumulated other comprehensive loss was comprised of the following components:

<i>(Dollars in Thousands)</i>	Securities Available for Sale	Retirement Plans	Accumulated Other Comprehensive Loss	
Balance as of January 1, 2014	\$ (132 )	\$ (8,408 )	\$ (8,540 )	
Other comprehensive (loss) income during the period	191	(13,160 )	(12,969 )	
Balance as of December 31, 2014	\$ 59	\$ (21,568 )	\$ (21,509 )	
Balance as of January 1, 2013	\$ 573	\$ (30,132 )	\$ (29,559 )	
Other comprehensive loss during the period	(705 )	21,724	21,019	
Balance as of December 31, 2013	\$ (132 )	\$ (8,408 )	\$ (8,540 )	
Balance as of January 1, 2012	\$ 1,064	\$ (24,593 )	\$ (23,529 )	
Other comprehensive income (loss) during the period	(491 )	(5,539 )	(6,030 )	
Balance as of December 31, 2012	\$ 573	\$ (30,132 )	\$ (29,559 )	

#### **Note 16**

#### **RELATED PARTY TRANSACTIONS**

At December 31, 2014 and 2013, certain officers and directors were indebted to the Company's bank subsidiary in the aggregate amount of \$14.3 million and \$18.3 million, respectively. During 2014, \$8.4 million in new loans were made and repayments totaled \$12.4 million. In the opinion of management, these loans were made on similar terms as loans to other individuals of comparable creditworthiness and were all current at year-end.

Deposits from certain directors, executive officers, and their related interests totaled \$18.8 million and \$24.0 million at December 31, 2014 and 2013, respectively.

Under a lease agreement expiring in 2024, the Bank leases land from a partnership in which several directors and officers have an interest. The lease agreement with Smith Interests General Partnership L.L.P. provides for annual lease payments of approximately \$142,000, to be adjusted for inflation in future years.

#### **Note 17**

#### **OTHER NONINTEREST EXPENSE**

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Components of other noninterest expense in excess of 1% of the sum of total interest income and noninterest income, which are not disclosed separately elsewhere, are presented below for each of the respective years.

(Dollars in Thousands)	2014	2013	2012
Legal Fees	3,187	3,663	4,303
Professional Fees	3,732	4,304	4,882
Telephone	1,903	1,891	1,896
Advertising	1,461	1,719	1,815
Processing Services	6,062	5,396	3,967
Insurance – Other	2,934	4,144	4,104
Postage	1,147 <sup>(1)</sup>	1,309 <sup>(1)</sup>	1,595
Other	7,056	7,077	7,841
Total	\$27,482	\$29,503	\$30,403

<sup>(1)</sup>Amount less than 1% for the current year but was greater than 1% for prior year(s).

**Note 18****COMMITMENTS AND CONTINGENCIES**

*Lending Commitments.* The Company is a party to financial instruments with off-balance sheet risks in the normal course of business to meet the financing needs of its clients. These financial instruments consist of commitments to extend credit and standby letters of credit.

The Company's maximum exposure to credit loss under standby letters of credit and commitments to extend credit is represented by the contractual amount of those instruments. The Company uses the same credit policies in establishing commitments and issuing letters of credit as it does for on-balance sheet instruments. As of December 31, the amounts associated with the Company's off-balance sheet obligations were as follows:

(Dollars in Thousands)	2014			2013		
	Fixed	Variable	Total	Fixed	Variable	Total
Commitments to Extend Credit <sup>(1)</sup>	\$33,633	\$278,438	\$312,071	\$36,927	\$234,342	\$271,269
Standby Letters of Credit	8,307	—	8,307	10,979	—	10,979
Total	\$41,940	\$278,438	\$320,378	\$47,906	\$234,342	\$282,248

<sup>(1)</sup>Commitments include unfunded loans, revolving lines of credit, and other unused commitments.

Commitments to extend credit are agreements to lend to a client so long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements.

Standby letters of credit are conditional commitments issued by the Company to guarantee the performance of a client to a third party. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities. In general, management does not anticipate any material losses as a result of participating in these types of transactions. However, any potential losses arising from such transactions are reserved for in the same manner as management reserves for its other credit facilities.

For both on- and off-balance sheet financial instruments, the Company requires collateral to support such instruments when it is deemed necessary. The Company evaluates each client's creditworthiness on a case-by-case basis. The amount of collateral obtained upon extension of credit is based on management's credit evaluation of the counterparty. Collateral held varies, but may include deposits held in financial institutions; U.S. Treasury securities; other marketable securities; real estate; accounts receivable; property, plant and equipment; and inventory.

*Other Commitments.* In the normal course of business, the Company enters into lease commitments which are classified as operating leases. Rent expense incurred under these leases was approximately \$0.5 million in 2014, \$0.7 million in 2013, and \$0.6 million in 2012. Minimum lease payments under these leases due in each of the five years subsequent to December 31, 2014, are as follows (dollars in millions): 2015, \$0.5; 2016, \$0.5; 2017, \$0.4; 2018, \$0.4, thereafter, \$3.2.

*Contingencies.* The Company is a party to lawsuits and claims arising out of the normal course of business. In management's opinion, there are no known pending claims or litigation, the outcome of which would, individually or in the aggregate, have a material effect on the consolidated results of operations, financial position, or cash flows of the Company.

*Indemnification Obligation.* The Company is a member of the Visa U.S.A. network. Visa U.S.A believes that its member banks are required to indemnify it for potential future settlement of certain litigation (the "Covered Litigation") that relates to several antitrust lawsuits challenging the practices of Visa and MasterCard International. In 2008, the Company, as a member of the Visa U.S.A. network, obtained Class B shares of Visa, Inc. upon its initial public offering. Since its initial public offering, Visa, Inc. has funded a litigation reserve for the Covered Litigation resulting in a reduction in the Class B shares held by the Company. During the first quarter of 2011, the Company sold its remaining Class B shares resulting in a \$3.2 million pre-tax gain. Associated with this sale, the Company entered into a swap contract with the purchaser of the shares that requires a payment to the counterparty in the event that Visa, Inc. makes subsequent revisions to the conversion ratio for its Class B shares. Further information on the swap contract is contained within Note 19 below.

In December 2013, a settlement agreement was approved by the court in resolution of the aforementioned Covered Litigation matter. Visa's share of the settlement is to be paid from the litigation reserve account which was further funded during the third quarter of 2014 resulting in a payment of \$ 161,000 to the counterparty. Fixed charges included in the liability are payable quarterly until the litigation reserve is fully liquidated and at which time the aforementioned swap contract will be terminated. Quarterly payments during 2014 totaled \$212,000. Conversion ratio payments and ongoing fixed quarterly charges are reflected in earnings in the period incurred.

## Note 19

### FAIR VALUE MEASUREMENTS

The fair value of an asset or liability is the price that would be received to sell that asset or paid to transfer that liability in an orderly transaction occurring in the principal market (or most advantageous market in the absence of a principal market) for such asset or liability. In estimating fair value, the Company utilizes valuation techniques that are consistent with the market approach, the income approach and/or the cost approach. Such valuation techniques are consistently applied. Inputs to valuation techniques include the assumptions that market participants would use in pricing an asset or liability. ASC Topic 820 establishes a fair value hierarchy for valuation inputs that gives the highest priority to quoted prices in active markets for identical assets or liabilities and the lowest priority to unobservable inputs. The fair value hierarchy is as follows:

*Level 1 Inputs* - Unadjusted quoted prices in active markets for identical assets or liabilities that the reporting entity has the ability to access at the measurement date.

*Level 2 Inputs* - Inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. These might include quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, inputs other than quoted prices that are observable for the asset or liability (such as interest rates, volatilities, prepayment speeds, credit risks, etc.) or inputs that are derived principally from, or corroborated, by market data by correlation or other means.

*Level 3 Inputs* - Unobservable inputs for determining the fair values of assets or liabilities that reflect an entity's own assumptions about the assumptions that market participants would use in pricing the assets or liabilities.

#### Assets and Liabilities Measured at Fair Value on a Recurring Basis

*Securities Available for Sale.* U.S. Treasury securities and certain U.S. Government Agency securities are reported at fair value utilizing Level 1 inputs. Other securities classified as available for sale are reported at fair value utilizing Level 2 inputs. For these securities, the Company obtains fair value measurements from an independent pricing service. The fair value measurements consider observable data that may include dealer quotes, market spreads, cash flows, the U.S. Treasury yield curve, live trading levels, trade execution data, credit information and the bond's terms and conditions, among other things.

In general, the Company does not purchase securities that have a complicated structure. The Company's entire portfolio consists of traditional investments, nearly all of which are U.S. Treasury obligations, federal agency bullet or mortgage pass-through securities, or general obligation or revenue based municipal bonds. Pricing for such instruments is easily obtained. From time to time, the Company will validate, on a sample basis, prices supplied by the independent pricing service by comparison to prices obtained from third-party sources or derived using internal

models.

*Fair Value Swap.* The Company entered into a stand-alone derivative contract with the purchaser of its Visa Class B shares. The valuation represents the amount due and payable to the counterparty based upon the revised share conversion rate, if any, during the period.

A summary of fair values for assets and liabilities recorded at fair value at December 31 consisted of the following:

(Dollars in Thousands)	Level 1 Inputs	Level 2 Inputs	Level 3 Inputs	Total Fair Value
2014				
Securities Available for Sale:				
U.S. Government Treasury	\$186,031	\$—	\$ —	\$186,031
U.S. Government Agency	—	96,097	—	96,097
States and Political Subdivisions	—	48,388	—	48,388
Mortgage-Backed Securities	—	2,287	—	2,287
Equity Securities	—	8,745	—	8,745
2013				
Securities Available for Sale:				
U.S. Government Treasury	\$71,833	\$—	\$ —	\$71,833
U.S. Government Agency	—	75,146	—	75,146
State and Political Subdivisions	—	91,753	—	91,753
Mortgage-Backed Securities	—	2,795	—	2,795
Equity Securities	—	9,893	—	9,893

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### **Assets Measured at Fair Value on a Non-Recurring Basis**

Certain assets are measured at fair value on a non-recurring basis (i.e., the assets are not measured at fair value on an ongoing basis but are subject to fair value adjustments in certain circumstances). An example would be assets exhibiting evidence of impairment. The following is a description of valuation methodologies used for assets measured on a non-recurring basis.

*Impaired Loans.* Impairment for collateral dependent loans is measured using the fair value of the collateral less selling costs. The fair value of collateral is determined by an independent valuation or professional appraisal in conformance with banking regulations. Collateral values are estimated using Level 3 inputs due to the volatility in the real estate market, and the judgment and estimation involved in the real estate appraisal process. Impaired loans are reviewed and evaluated on at least a quarterly basis for additional impairment and adjusted accordingly. Valuation techniques are consistent with those techniques applied in prior periods. Impaired collateral dependent loans had a carrying value of \$13.6 million with a valuation allowance of \$2.0 million at December 31, 2014 and \$31.5 million and \$3.1 million, respectively, at December 31, 2013.

*Loans Held for Sale.* These loans are carried at the lower of cost or fair value and are adjusted to fair value on a non-recurring basis. Fair value is based on observable markets rates for comparable loan products, which is considered a Level 2 fair value measurement.

*Other Real Estate Owned.* During 2014 and 2013, certain foreclosed assets, upon initial recognition, were measured and reported at fair value through a charge-off to the allowance for loan losses based on the fair value of the foreclosed asset less estimated cost to sell. The fair value of the foreclosed asset is determined by an independent valuation or professional appraisal in conformance with banking regulations. On an ongoing basis, we obtain updated appraisals on foreclosed assets and realize valuation adjustments as necessary. The fair value of foreclosed assets is estimated using Level 3 inputs due to the judgment and estimation involved in the real estate valuation process.

### **Assets and Liabilities Disclosed at Fair Value**

The Company is required to disclose the estimated fair value of financial instruments, both assets and liabilities, for which it is practical to estimate fair value and the following is a description of valuation methodologies used for those assets and liabilities.

*Cash and Short-Term Investments.* The carrying amount of cash and short-term investments is used to approximate fair value, given the short time frame to maturity and as such assets do not present unanticipated credit concerns.

*Securities Held to Maturity.* Securities held to maturity are valued in accordance with the methodology previously noted in the caption “Assets and Liabilities Measured at Fair Value on a Recurring Basis – Securities Available for Sale”.

*Loans.* The loan portfolio is segregated into categories and the fair value of each loan category is calculated using present value techniques based upon projected cash flows and estimated discount rates that reflect the credit, interest rate, and liquidity risks inherent in each loan category. The calculated present values are then reduced by an allocation of the allowance for loan losses against each respective loan category.

*Deposits.* The fair value of Noninterest Bearing Deposits, NOW Accounts, Money Market Accounts and Savings Accounts are the amounts payable on demand at the reporting date. The fair value of fixed maturity certificates of deposit is estimated using present value techniques and rates currently offered for deposits of similar remaining maturities.

*Subordinated Notes Payable.* The fair value of each note is calculated using present value techniques, based upon projected cash flows and estimated discount rates as well as rates being offered for similar obligations.

*Short-Term and Long-Term Borrowings.* The fair value of each note is calculated using present value techniques, based upon projected cash flows and estimated discount rates as well as rates being offered for similar debt.

A summary of estimated fair values of significant financial instruments at December 31 consisted of the following:

(Dollars in Thousands)	2014			
	Carrying Value	Level 1 Inputs	Level 2 Inputs	Level 3 Inputs
<b>ASSETS:</b>				
Cash	\$55,467	\$55,467	\$—	\$—
Short-Term Investments	329,589	329,589	—	—
Investment Securities, Available for Sale	341,548	186,031	155,517	—
Investment Securities, Held to Maturity	163,581	76,317	87,095	—
Loans Held for Sale	10,688	—	10,688	—
Loans, Net of Allowance for Loan Losses	1,413,835	—	—	1,369,314
<b>LIABILITIES:</b>				
Deposits	\$2,146,794	\$—	\$2,146,510	\$—
Short-Term Borrowings	49,425	—	48,760	—
Subordinated Notes Payable	62,887	—	62,887	—
Long-Term Borrowings	31,097	—	32,313	—
(Dollars in Thousands)	2013			
	Carrying Value	Level 1 Inputs	Level 2 Inputs	Level 3 Inputs
<b>ASSETS:</b>				
Cash	\$55,209	\$55,209	\$—	\$—
Short-Term Investments	474,719	474,719	—	—
Investment Securities, Available for Sale	251,420	71,833	179,587	—
Investment Securities, Held to Maturity	148,211	43,579	103,382	—
Loans Held for Sale	11,065	—	11,065	—
Loans, Net of Allowance for Loan Losses	1,365,509	—	—	1,265,827
<b>LIABILITIES:</b>				
Deposits	\$2,136,248	\$—	\$2,136,737	\$—
Short-Term Borrowings	51,321	—	50,754	—
Subordinated Notes Payable	62,887	—	62,886	—
Long-Term Borrowings	38,043	—	39,450	—

All non-financial instruments are excluded from the above table. The disclosures also do not include certain intangible assets such as client relationships, deposit base intangibles and goodwill. Accordingly, the aggregate fair value amounts presented do not represent the underlying value of the Company.

**Note 20****PARENT COMPANY FINANCIAL INFORMATION**

The following are condensed statements of financial condition of the parent company at December 31:

**Parent Company Statements of Financial Condition**

(Dollars in Thousands, Except Per Share Data)	2014	2013
<b>ASSETS</b>		
Cash and Due From Subsidiary Bank	\$11,741	\$6,209
Investment in Subsidiary Bank	329,632	337,809
Other Assets	2,906	3,347
<b>Total Assets</b>	<b>\$344,279</b>	<b>\$347,365</b>
<b>LIABILITIES</b>		
Subordinated Notes Payable	\$62,887	\$62,887
Other Liabilities	8,852	8,078
<b>Total Liabilities</b>	<b>71,739</b>	<b>70,965</b>
<b>SHAREOWNERS' EQUITY</b>		
Preferred Stock, \$.01 par value, 3,000,000 shares authorized; no shares issued and outstanding		
Common Stock, \$.01 par value; 90,000,000 shares authorized; 17,447,223 and 17,360,960 shares issued and outstanding at December 31, 2014 and December 31, 2013, respectively	174	174
Additional Paid-In Capital	42,569	41,152
Retained Earnings	251,306	243,614
Accumulated Other Comprehensive Loss, Net of Tax	(21,509 )	(8,540 )
<b>Total Shareowners' Equity</b>	<b>272,540</b>	<b>276,400</b>
<b>Total Liabilities and Shareowners' Equity</b>	<b>\$344,279</b>	<b>\$347,365</b>

The operating results of the parent company for the three years ended December 31 are shown below:

**Parent Company Statements of Operations**

(Dollars in Thousands)	2014	2013	2012
<b>OPERATING INCOME</b>			
Income Received from Subsidiary Bank:			
Overhead Fees	\$4,468	\$4,417	\$4,536
Dividends	6,000	—	—

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Other Income	138	208	130
Total Operating Income	10,606	4,625	4,666
OPERATING EXPENSE			
Salaries and Associate Benefits	3,156	3,130	2,059
Interest on Subordinated Notes Payable	1,328	1,419	1,477
Professional Fees	1,024	1,491	1,781
Advertising	141	142	140
Legal Fees	243	245	332
Other	624	1,117	478
Total Operating Expense	6,516	7,544	6,267
Earnings (Loss) Before Income Taxes and Equity in Undistributed Earnings of Subsidiary Bank	4,090	(2,919)	(1,601)
Income Tax Benefit	(433 )	(1,036)	(10 )
Earnings (Loss) Before Equity in Undistributed Earnings of Subsidiary Bank	4,523	(1,883)	(1,591)
Equity in Undistributed Earnings of Subsidiary Bank	4,737	7,928	1,699
Net Income	\$9,260	\$6,045	\$108

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The cash flows for the parent company for the three years ended December 31 were as follows:

### Parent Company Statements of Cash Flows

(Dollars in Thousands)	2014	2013	2012
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>			
Net Income	\$9,260	\$6,045	\$108
Adjustments to Reconcile Net Income to Net Cash Provided By (Used In) Operating Activities:			
Equity in Undistributed Earnings of Subsidiary Bank	(4,737 )	(7,928)	(1,699)
Stock Compensation	1,349	1,296	262
Decrease (Increase) in Other Assets	387	339	(491 )
Increase (Decrease) in Other Liabilities	532	(1,755)	2,005
Net Cash Provided By (Used In) Operating Activities	6,791	(2,003)	185
<b>CASH FROM FINANCING ACTIVITIES:</b>			
Dividends Paid	(1,568 )	—	—
Issuance of Common Stock Under Compensation Plans	578	1,151	607
Payments to Repurchase Common Stock	(269 )	—	—
Net Cash (Used In) Provided By in Financing Activities	(1,259 )	1,151	607
Net Increase (Decrease) in Cash	5,532	(852 )	792
Cash at Beginning of Year	6,209	7,061	6,269
Cash at End of Year	\$11,741	\$6,209	\$7,061

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

None.

***Item 9A. Controls and Procedures***

*Evaluation of Disclosure Controls and Procedures.* As of December 31, 2014, the end of the period covered by this Annual Report on Form 10-K, our management, including our Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of our disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934). Based upon that evaluation, our Chief Executive Officer and Chief Financial Officer each concluded that as of December 31, 2014, the end of the period covered by this Annual Report on Form 10-K, we maintained effective disclosure controls and procedures.

*Management's Report on Internal Control Over Financial Reporting.* Our management is responsible for establishing and maintaining effective internal control over financial reporting. Internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with U.S. generally accepted accounting principles.

Under the supervision and with the participation of management, including the Chief Executive Officer and Chief Financial Officer, we conducted an evaluation of the effectiveness of internal control over financial reporting based on the framework in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission in 1992. Based on this evaluation under the framework in Internal Control - Integrated Framework, our management has concluded we maintained effective internal control over financial reporting, as such term is defined in Securities Exchange Act of 1934 Rule 13a-15(f), as of December 31, 2014.

Internal control over financial reporting cannot provide absolute assurance of achieving financial reporting objectives because of its inherent limitations. Internal control over financial reporting is a process that involves human diligence and compliance and is subject to lapses in judgment and breakdowns resulting from human failures. Internal control over financial reporting can also be circumvented by collusion or improper management override. Because of such limitations, there is a risk that material misstatements may not be prevented or detected on a timely basis by internal control over financial reporting. However, these inherent limitations are known features of the financial reporting process. Therefore, it is possible to design into the process safeguards to reduce, though not eliminate, this risk.

Management is also responsible for the preparation and fair presentation of the consolidated financial statements and other financial information contained in this report. The accompanying consolidated financial statements were prepared in conformity with U.S. generally accepted accounting principles and include, as necessary, best estimates and judgments by management.

Ernst & Young LLP, an independent registered certified public accounting firm, has audited our consolidated financial statements as of and for the year ended December 31, 2014, and opined as to the effectiveness of internal control over financial reporting as of December 31, 2014, as stated in its attestation report, which is included herein on page 101.

*Change in Internal Control.* Our management, including the Chief Executive Officer and Chief Financial Officer, has reviewed our internal control. There have been no significant changes in our internal control during our most recently completed fiscal quarter that materially affected, or is likely to materially affect our internal control over financial reporting.

***Item 9B. Other Information***

None.

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Ernst & Young LLP  
One Tampa City Center    Tel: +1 813 225 4800  
Suite 2400                    Fax: +1 813 225 4711  
201 North Franklin Street   ey.com  
Tampa, Florida 33602

Report of Independent Registered Certified Public Accounting Firm

The Board of Directors and Shareowners of

Capital City Bank Group, Inc.

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

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

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

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

deteriorate.

In our opinion, Capital City Bank Group, Inc. maintained, in all material respects, effective internal control over financial reporting as of December 31, 2014, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the 2014 consolidated financial statements of Capital City Bank Group, Inc. and our report dated March 6, 2015 expressed an unqualified opinion thereon.

Tampa, Florida

March 6, 2015

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**Part III*****Item 10. Directors, Executive Officers, and Corporate Governance***

Incorporated herein by reference to the subsection entitled “Codes of Conduct and Ethics” under the section entitled “Corporate Governance,” “Proposal No. 1 - Nominees for Election as Directors,” “Continuing Directors and Executive Officers,” “Share Ownership” and the subsection entitled “Committees of the Board” under the section “Board and Committee Membership” in the Registrant’s Proxy Statement relating to its Annual Meeting of Shareowners to be held April 28, 2015.

***Item 11. Executive Compensation***

Incorporated herein by reference to the sections entitled “Compensation Discussion and Analysis,” “Compensation Committee Report,” “Compensation Committee Interlocks and Insider Participation,” and “Executive Compensation” in the Registrant’s Proxy Statement relating to its Annual Meeting of Shareowners to be held April 28, 2015.

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

The 2011 Associate Incentive Plan, 2011 Associate Stock Purchase Plan, and 2011 Director Stock Purchase Plan were approved by the Registrant’s shareowners. The following table provides certain information regarding the Registrant’s equity compensation plans.

Plan Category	Number of securities to be issued upon exercise of outstanding options, warrants and rights		Weighted-average exercise price of outstanding options, warrants and rights	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a))	
	(a)		(b)	(c)	
Equity Compensation Plans Approved by Securities Holders	37,246	(1)	\$ 32.69	1,279,457	(2)
Equity Compensation Plans Not Approved by Securities Holders	—		—	—	
Total	37,246		\$ 32.69	1,279,457	

(1) Includes 37,246 shares that may be issued upon exercise of outstanding options under the terminated 2005 Associate Incentive Plan.

(2) Consists of 774,393 shares available for issuance under our 2011 Associate Incentive Plan, 418,320 shares available for issuance under our 2011 Associate Stock Purchase Plan, and 86,744 shares available for issuance under our 2011 Director Stock Purchase Plan. Of these plans, the only plan under which options may be granted in the future is our 2011 Associate Incentive Plan.

The other information required by Item 12 of Form 10-K is incorporated by reference from the information contained in the section captioned "Share Ownership" in the Registrant's Proxy Statement relating to its Annual Meeting of Shareowners to be held April 28, 2015.

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

Incorporated herein by reference to the subsections entitled "Procedures for Review, Approval, or Ratification of Related Person Transactions" and "Transactions With Related Persons" under the section entitled "Executive Officers and Transactions with Related Persons" and the subsection entitled "Independent Directors" under the section entitled "Corporate Governance" in the Registrant's Proxy Statement relating to its Annual Meeting of Shareowners to be held April 28, 2015.

***Item 14. Principal Accountant Fees and Services***

Incorporated herein by reference to the section entitled "Audit Fees and Related Matters" in the Registrant's Proxy Statement relating to its Annual Meeting of Shareowners to be held April 28, 2015.

## PART IV

### *Item 15. Exhibits and Financial Statement Schedules*

The following documents are filed as part of this report

#### 1. Financial Statements

Report of Independent Registered Certified Public Accounting Firm  
Consolidated Statements of Financial Condition at the End of Fiscal Years 2014 and 2013  
Consolidated Statements of Operations for Fiscal Years 2014, 2013, and 2012  
Consolidated Statements of Comprehensive Income for Fiscal Years 2014, 2013, and 2012  
Consolidated Statements of Changes in Shareowners' Equity for Fiscal Years 2014, 2013, and 2012  
Consolidated Statements of Cash Flows for Fiscal Years 2014, 2013, and 2012  
Notes to Consolidated Financial Statements

#### 2. Financial Statement Schedules

Other schedules and exhibits are omitted because the required information either is not applicable or is shown in the financial statements or the notes thereto.

#### 3. Exhibits Required to be Filed by Item 601 of Regulation S-K

Reg.  
S-K

Exhibit

Description of Exhibit

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- |     |  |
|-----|--|
| 3.1 | Amended and Restated Articles of Incorporation - incorporated herein by reference to Exhibit 3 of the Registrant's 1996 Proxy Statement (filed 4/11/96) (No. 0-13358).               |
| 3.2 | Amended and Restated Bylaws - incorporated herein by reference to Exhibit 3.2 of the Registrant's Form 8-K (filed 11/30/07) (No. 0-13358).   |
| 4.1 | See Exhibits 3.1, and 3.2 for provisions of Amended and Restated Articles of Incorporation and Amended and Restated Bylaws, which define the rights of the Registrant's shareowners. |
| 4.2 | Capital City Bank Group, Inc. 2011 Director Stock Purchase Plan - incorporated herein by reference to Exhibit 10.2 of the Registrant's Form 8-K (filed 5/2/11) (No. 0-13358).        |

4.3 Capital City Bank Group, Inc. 2011 Associate Stock Purchase Plan - incorporated herein by reference to Exhibit 10.1 of the Registrant's Form 8-K (filed 5/2/11) (No. 0-13358).

4.4 Capital City Bank Group, Inc. 2011 Associate Incentive Plan - incorporated herein by reference to Exhibit 10.3 of the Registrant's Form 8-K (filed 5/2/11) (No. 0-13358).

4.5 In accordance with Regulation S-K, Item 601(b)(4)(iii)(A) certain instruments defining the rights of holders of long-term debt of Capital City Bank Group, Inc. not exceeding 10% of the total assets of Capital City Bank Group, Inc. and its consolidated subsidiaries have been omitted; the Registrant agrees to furnish a copy of any such instruments to the Commission upon request.

10.1 Capital City Bank Group, Inc. 1996 Dividend Reinvestment and Optional Stock Purchase Plan - incorporated herein by reference to Exhibit 10 of the Registrant's Form S-3 (filed 01/30/97) (No. 333-20683).

10.2 Capital City Bank Group, Inc. Supplemental Executive Retirement Plan - incorporated herein by reference to Exhibit 10(d) of the Registrant's Form 10-K (filed 3/27/03) (No. 0-13358).

10.3 Capital City Bank Group, Inc. 401(k) Profit Sharing Plan – incorporated herein by reference to Exhibit 4.3 of Registrant's Form S-8 (filed 09/30/97) (No. 333-36693).

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- 10.5 2006 Stock Option Agreement by and between Capital City Bank Group, Inc. and William G. Smith, Jr., dated March 23, 2006 – incorporated herein by reference to Exhibit 10.1 of the Registrant’s Form 8-K (filed 3/29/06) (No. 0-13358).
- 10.6 Form of Participant Agreement for Long-Term Incentive Plan.\*\*
- 11 Statement re Computation of Per Share Earnings.\*
- 14 Capital City Bank Group, Inc. Code of Ethics for the Chief Financial Officer and Senior Financial Officers - incorporated herein by reference to Exhibit 14 of the Registrant’s Form 8-K (filed 3/11/05) (No. 0-13358).
- 21 Capital City Bank Group, Inc. Subsidiaries, as of December 31, 2014.\*\*
- 23.1 Consent of Independent Registered Certified Public Accounting Firm.\*\*
- 31.1 Certification of CEO pursuant to Securities and Exchange Act Section 302 of the Sarbanes-Oxley Act of 2002.\*\*
- 31.2 Certification of CFO pursuant to Securities and Exchange Act Section 302 of the Sarbanes-Oxley Act of 2002.\*\*
- 32.1 Certification of CEO pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.\*\*
- 32.2 Certification of CFO pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.\*\*
- 101.INS XBRL Instance Document\*\*
- 101.SCH XBRL Taxonomy Extension Schema Document\*\*
- 101.CAL XBRL Taxonomy Extension Calculation Linkbase Document\*\*
- 101.LAB XBRL Taxonomy Extension Label Linkbase Document\*\*
- 101.PRE XBRL Taxonomy Extension Presentation Linkbase Document\*\*
- 101.DEF XBRL Taxonomy Extension Definition Linkbase Document\*\*

Information required to be presented in Exhibit 11 is provided in Note 13 to the consolidated financial statements  
\* under Part II, Item 8 of this Form 10-K in accordance with the provisions of U.S. generally accepted accounting principles.

\*\*Filed electronically herewith.

## Signatures

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on March 6, 2015, on its behalf by the undersigned, thereunto duly authorized.

CAPITAL CITY BANK GROUP, INC.

/s/ William G. Smith, Jr.  
William G. Smith, Jr.  
Chairman, President and Chief Executive Officer  
(Principal Executive Officer)

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed on March 6, 2015 by the following persons in the capacities indicated.

/s/ William G. Smith, Jr.  
William G. Smith, Jr.  
Chairman, President and Chief Executive Officer  
(Principal Executive Officer)

/s/ J. Kimbrough Davis  
J. Kimbrough Davis  
Executive Vice President and Chief Financial Officer  
(Principal Financial and Accounting Officer)

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Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on March 6, 2015, on its behalf by the undersigned, thereunto duly authorized.

Directors:

/s/ DuBose Ausley DuBose Ausley	/s/ J. Everitt Drew J. Everitt Drew
/s/ Thomas A. Barron Thomas A. Barron	/s/ John K. Humphress John K. Humphress
/s/ Allan G. Bense Allan G. Bense	/s/ Lina S. Knox Lina S. Knox
/s/ Frederick Carroll, III Frederick Carroll, III	/s/ Henry Lewis III Henry Lewis III
/s/ Cader B. Cox, III Cader B. Cox, III	/s/ William G. Smith, Jr. William G. Smith, Jr.

**Exhibit Index**

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Exhibit

Description of Exhibit

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- 3.1 Amended and Restated Articles of Incorporation - incorporated herein by reference to Exhibit 3 of the Registrant's 1996 Proxy Statement (filed 4/11/96) (No. 0-13358).
- 3.2 Amended and Restated Bylaws - incorporated herein by reference to Exhibit 3.2 of the Registrant's Form 8-K (filed 11/30/07) (No. 0-13358).
- 4.1 See Exhibits 3.1, and 3.2 for provisions of Amended and Restated Articles of Incorporation and Amended and Restated Bylaws, which define the rights of the Registrant's shareowners.
- 4.2 Capital City Bank Group, Inc. 2011 Director Stock Purchase Plan - incorporated herein by reference to Exhibit 10.2 of the Registrant's Form 8-K (filed 5/2/11) (No. 0-13358).
- 4.3 Capital City Bank Group, Inc. 2011 Associate Stock Purchase Plan - incorporated herein by reference to Exhibit 10.1 of the Registrant's Form 8-K (filed 5/2/11) (No. 0-13358).
- 4.4 Capital City Bank Group, Inc. 2011 Associate Incentive Plan - incorporated herein by reference to Exhibit 10.3 of the Registrant's Form 8-K (filed 5/2/11) (No. 0-13358).
- 4.5 In accordance with Regulation S-K, Item 601(b)(4)(iii)(A) certain instruments defining the rights of holders of long-term debt of Capital City Bank Group, Inc. not exceeding 10% of the total assets of Capital City Bank Group, Inc. and its consolidated subsidiaries have been omitted; the Registrant agrees to furnish a copy of any such instruments to the Commission upon request.
- 10.1 Capital City Bank Group, Inc. 1996 Dividend Reinvestment and Optional Stock Purchase Plan - incorporated herein by reference to Exhibit 10 of the Registrant's Form S-3 (filed 01/30/97) (No. 333-20683).
- 10.2 Capital City Bank Group, Inc. Supplemental Executive Retirement Plan - incorporated herein by reference to Exhibit 10(d) of the Registrant's Form 10-K (filed 3/27/03) (No. 0-13358).
- 10.3 Capital City Bank Group, Inc. 401(k) Profit Sharing Plan – incorporated herein by reference to Exhibit 4.3 of Registrant's Form S-8 (filed 09/30/97) (No. 333-36693).
- 10.5 2006 Stock Option Agreement by and between Capital City Bank Group, Inc. and William G. Smith, Jr., dated March 23, 2006 – incorporated herein by reference to Exhibit 10.1 of the Registrant's Form 8-K (filed 3/29/06) (No. 0-13358).

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- 10.6 Form of Participant Agreement for Long-Term Incentive Plan.\*\*
  - 11 Statement re Computation of Per Share Earnings.\*
  - 14 Capital City Bank Group, Inc. Code of Ethics for the Chief Financial Officer and Senior Financial Officers - incorporated herein by reference to Exhibit 14 of the Registrant's Form 8-K (filed 3/11/05) (No. 0-13358).
  - 21 Capital City Bank Group, Inc. Subsidiaries, as of December 31, 2014.\*\*
  - 23.1 Consent of Independent Registered Certified Public Accounting Firm.\*\*
  - 31.1 Certification of CEO pursuant to Securities and Exchange Act Section 302 of the Sarbanes-Oxley Act of 2002.\*\*
  - 31.2 Certification of CFO pursuant to Securities and Exchange Act Section 302 of the Sarbanes-Oxley Act of 2002.\*\*
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32.1 Certification of CEO pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.\*\*

32.2 Certification of CFO pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.\*\*

101.INS XBRL Instance Document\*\*

101.SCH XBRL Taxonomy Extension Schema Document\*\*

101.CALXBRL Taxonomy Extension Calculation Linkbase Document\*\*

101.LABXBRL Taxonomy Extension Label Linkbase Document\*\*

101.PRE XBRL Taxonomy Extension Presentation Linkbase Document\*\*

101.DEF XBRL Taxonomy Extension Definition Linkbase Document\*\*

Information required to be presented in Exhibit 11 is provided in Note 13 to the consolidated financial statements  
\* under Part II, Item 8 of this Form 10-K in accordance with the provisions of U.S. generally accepted accounting principles.

\*\* Filed electronically herewith.

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