

1ST SOURCE CORP  
Form 10-Q  
April 22, 2010

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2010

OR

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

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

Commission file number 0-6233

(Exact name of registrant as specified in its charter)

INDIANA  
(State or other jurisdiction of  
incorporation or organization)

35-1068133  
(I.R.S. Employer  
Identification No.)

100 North Michigan Street South Bend, Indiana 46601  
(Address of principal executive offices) (Zip Code)

(574) 235-2000  
(Registrant's telephone number, including area code)

Not Applicable  
(Former name, former address and former fiscal year, if changed since last report.)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.  Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).  Yes  No

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

Large accelerated filer	<input type="radio"/>	Accelerated filer	<input checked="" type="radio"/>
Non-accelerated filer	<input type="radio"/>	Smaller reporting company	<input type="radio"/>

(Do not check if a 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

Number of shares of common stock outstanding as of April 16, 2010 – 24,286,688 shares

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## CERTIFICATIONS

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1st SOURCE CORPORATION  
CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION  
(Unaudited - Dollars in thousands, except share amounts)

	March 31, 2010	December 31, 2009
<b>ASSETS</b>		
Cash and due from banks	\$53,518	\$72,872
Federal funds sold and interest bearing deposits with other banks	71,139	141,166
Investment securities available-for-sale (amortized cost of \$878,403 and \$893,439 at March 31, 2010 and December 31, 2009, respectively)	888,862	901,638
Other investments	21,012	21,012
Trading account securities	130	125
Mortgages held for sale	23,067	26,649
<b>Loans and leases - net of unearned discount</b>		
Commercial and agricultural loans	546,826	546,222
Auto, light truck and environmental equipment	364,445	349,741
Medium and heavy duty truck	200,228	204,545
Aircraft financing	608,643	617,384
Construction equipment financing	303,866	313,300
Loans secured by real estate	977,667	952,223
Consumer loans	104,440	109,735
Total loans and leases	3,106,115	3,093,150
Reserve for loan and lease losses	(87,827 )	(88,236 )
Net loans and leases	3,018,288	3,004,914
Equipment owned under operating leases, net	92,226	97,004
Net premises and equipment	37,556	37,907
Goodwill and intangible assets	89,949	90,222
Accrued income and other assets	149,365	148,591
Total assets	\$4,445,112	\$4,542,100
<b>LIABILITIES</b>		
<b>Deposits:</b>		
Noninterest bearing	\$457,645	\$450,608
Interest bearing	3,081,485	3,201,856
Total deposits	3,539,130	3,652,464
Federal funds purchased and securities sold under agreements to repurchase	111,788	123,787
Other short-term borrowings	29,358	26,323
Long-term debt and mandatorily redeemable securities	24,847	19,761
Subordinated notes	89,692	89,692
Accrued expenses and other liabilities	71,240	59,753
Total liabilities	3,866,055	3,971,780
<b>SHAREHOLDERS' EQUITY</b>		
Preferred stock; no par value Authorized 10,000,000 shares; issued 111,000 at March 31, 2010,		

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and at December 31, 2009	105,254	104,930
Common stock; no par value		
Authorized 40,000,000 shares; issued 25,643,506 at March 31, 2010, and at December 31, 2009	350,272	350,269
Retained earnings	147,381	142,407
Cost of common stock in treasury (1,356,818 shares at March 31, 2010, and 1,532,483 shares at December 31, 2009)	(30,348 )	(32,380 )
Accumulated other comprehensive income	6,498	5,094
Total shareholders' equity	579,057	570,320
Total liabilities and shareholders' equity	\$4,445,112	\$4,542,100

The accompanying notes are a part of the consolidated financial statements.

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1st SOURCE CORPORATION  
CONSOLIDATED STATEMENTS OF INCOME  
(Unaudited - Dollars in thousands, except per share amounts)

	Three Months Ended March 31,	
	2010	2009
Interest income:		
Loans and leases	\$42,270	\$44,597
Investment securities, taxable	5,401	4,036
Investment securities, tax-exempt	1,467	1,710
Other	274	333
Total interest income	49,412	50,676
Interest expense:		
Deposits	12,405	17,606
Short-term borrowings	188	349
Subordinated notes	1,647	1,647
Long-term debt and mandatorily redeemable securities	270	352
Total interest expense	14,510	19,954
Net interest income	34,902	30,722
Provision for loan and lease losses	4,388	7,785
Net interest income after provision for loan and lease losses	30,514	22,937
Noninterest income:		
Trust fees	3,745	3,804
Service charges on deposit accounts	4,620	4,746
Mortgage banking income	777	2,570
Insurance commissions	1,465	1,516
Equipment rental income	6,745	6,147
Other income	2,689	2,235
Investment securities and other investment gains (losses)	881	(469)
Total noninterest income	20,922	20,549
Noninterest expense:		
Salaries and employee benefits	18,810	20,086
Net occupancy expense	2,487	2,601
Furniture and equipment expense	2,800	3,481
Depreciation - leased equipment	5,364	4,956
Professional fees	1,514	1,062
Supplies and communication	1,369	1,567
FDIC and other insurance	1,674	1,550
Business development and marketing expense	567	485
Loan and lease collection and repossession expense	1,106	559
Other expense	1,419	2,293
Total noninterest expense	37,110	38,640

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Income before income taxes	14,326	4,846
Income tax expense (benefit)	4,647	(1,405 )
Net income	9,679	6,251
Preferred stock dividends and discount accretion	(1,711 )	(1,313 )
Net income available to common shareholders	\$7,968	\$4,938
Per common share		
Basic net income per common share	\$0.33	\$0.20
Diluted net income per common share	\$0.33	\$0.20
Dividends	\$0.15	\$0.14
Basic weighted average common shares outstanding	24,210,242	24,150,200
Diluted weighted average common shares outstanding	24,215,506	24,191,610

The accompanying notes are a part of the consolidated financial statements.

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1st SOURCE  
CORPORATION  
CONSOLIDATED STATEMENTS OF  
SHAREHOLDERS' EQUITY  
(Unaudited - Dollars in thousands, except per share  
amounts)

	Total	Preferred Stock	Common Stock	Retained Earnings	Cost of Common Stock in Treasury	Accumulated Other Comprehensive Income (Loss), Net
Balance at January 1, 2009	\$453,664	\$0	\$342,982	\$136,877	\$(32,019 )	\$ 5,824
Comprehensive Income, net of tax:						
Net Income	6,251	-	-	6,251	-	-
Change in unrealized appreciation of available-for-sale securities, net of tax	(853 )	-	-	-	-	(853 )
Total Comprehensive Income	5,398	-	-	-	-	-
Issuance of 78,194 common shares under stock based compensation awards, including related tax effects	1,566	-	-	687	879	-
Issuance of preferred stock	103,725	103,725	-	-	-	-
Preferred stock discount accretion	-	265	-	(265 )	-	-
Issuance of warrants to purchase common stock	7,275	-	7,275	-	-	-
Preferred stock dividend (paid and/or accrued)	(1,048 )	-	-	(1,048 )	-	-
Common stock dividend (\$0.14 per share)	(3,381 )	-	-	(3,381 )	-	-
Stock based compensation	3	-	3	-	-	-
Balance at March 31, 2009	\$567,202	\$103,990	\$350,260	\$139,121	\$(31,140 )	\$ 4,971
Balance at January 1, 2010	\$570,320	\$104,930	\$350,269	\$142,407	\$(32,380 )	\$ 5,094
Comprehensive Income, net of tax:						
Net Income	9,679	-	-	9,679	-	-
Change in unrealized appreciation of available-for-sale securities, net of tax	1,404	-	-	-	-	1,404
Total Comprehensive Income	11,083	-	-	-	-	-



Issuance of 182,934 common shares under stock based compensation awards, including related tax effects	2,778	-	-	632	2,146	-
Cost of 7,269 shares of common stock acquired for treasury	(114 )	-	-	-	(114 )	-
Preferred stock discount accretion	-	324	-	(324 )	-	-
Preferred stock dividend (paid and/or accrued)	(1,387 )	-	-	(1,387 )	-	-
Common stock dividend (\$0.15 per share)	(3,626 )	-	-	(3,626 )	-	-
Stock based compensation	3	-	3	-	-	-
Balance at March 31, 2010	\$579,057	\$105,254	\$350,272	\$147,381	\$(30,348 )	\$ 6,498

The accompanying notes are a part of the consolidated financial statements.

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1st SOURCE CORPORATION  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
(Unaudited - Dollars in thousands)

	Three Months Ended March 31,	
	2010	2009
Operating activities:		
Net income	\$ 9,679	\$ 6,251
Adjustments to reconcile net income to net cash provided (used) by operating activities:		
Provision for loan and lease losses	4,388	7,785
Depreciation of premises and equipment	1,182	1,226
Depreciation of equipment owned and leased to others	5,364	4,956
Amortization of investment security premiums and accretion of discounts, net	668	1,662
Amortization of mortgage servicing rights	761	724
Mortgage servicing asset (recovery) impairment	(1 )	565
Deferred income taxes	948	(1,944 )
Investment securities and other investment (gains) losses	(881 )	469
Originations/purchases of loans held for sale, net of principal collected	(50,208 )	(195,322 )
Proceeds from the sales of loans held for sale	54,303	117,411
Net gain on sale of loans held for sale	(512 )	(1,888 )
Change in trading account securities	(5 )	1
Change in interest receivable	75	(1,002 )
Change in interest payable	1,110	2,165
Change in other assets	(1,337 )	665
Change in other liabilities	8,573	(7,896 )
Other	15	587
Net change in operating activities	34,122	(63,585 )
Investing activities:		
Proceeds from sales of investment securities	71,579	98,945
Proceeds from maturities of investment securities	123,734	77,103
Purchases of investment securities	(180,063 )	(384,778 )
Net change in short-term investments	70,026	(1,539 )
Loans sold or participated to others	4,586	3,978
Net change in loans and leases	(22,348 )	76,305
Net change in equipment owned under operating leases	(586 )	(2,119 )
Purchases of premises and equipment	(857 )	(542 )
Net change in investing activities	66,071	(132,647 )
Financing activities:		
Net change in demand deposits, NOW accounts and savings accounts	(69,419 )	59,910
Net change in certificates of deposit	(43,915 )	(26,584 )
Net change in short-term borrowings	(8,964 )	4,966
Proceeds from issuance of long-term debt	5,303	12
Payments on long-term debt	(139 )	(10,186 )
Net proceeds from issuance of treasury stock	2,778	1,566
Acquisition of treasury stock	(114 )	-

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Net proceeds from issuance of preferred stock & common stock warrants	-	111,000
Cash dividends paid on preferred stock	(1,387 )	(339 )
Cash dividends paid on common stock	(3,690 )	(3,440 )
Net change in financing activities	(119,547 )	136,905
Net change in cash and cash equivalents	(19,354 )	(59,327 )
Cash and cash equivalents, beginning of year	72,872	119,771
Cash and cash equivalents, end of period	\$ 53,518	\$ 60,444

The accompanying notes are a part of the consolidated financial statements.

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1ST SOURCE CORPORATION  
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS  
(Unaudited)

Note 1. Basis of Presentation

The accompanying unaudited consolidated financial statements reflect all adjustments (all of which are normal and recurring in nature) which are, in the opinion of management, necessary for a fair presentation of the consolidated financial position, the results of operations, changes in shareholders' equity, and cash flows for the periods presented. These unaudited consolidated financial statements have been prepared according to the rules and regulations of the Securities and Exchange Commission (SEC) and, therefore, certain information and footnote disclosures normally included in financial statements prepared in accordance with U. S. generally accepted accounting principles (GAAP) have been omitted. The Notes to the Consolidated Financial Statements appearing in 1st Source Corporation's Annual Report on Form 10-K (2009 Annual Report), which include descriptions of significant accounting policies, should be read in conjunction with these interim financial statements. The balance sheet at December 31, 2009 has been derived from the audited financial statements at that date but does not include all of the information and footnotes required by U. S. generally accepted accounting principles for complete financial statements. Certain amounts in the prior period consolidated financial statements have been reclassified to conform with the current year presentation.

Note 2. Recent Accounting Pronouncements

**Subsequent Events:** In February 2010, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2010-09 "Subsequent Events (Topic 855) – Amendments to Certain Recognition and Disclosure Requirements." ASU 2010-09 amends the subsequent events disclosure guidance. The amendments include a definition of an SEC filer, requires an SEC filer or conduit bond obligor to evaluate subsequent events through the date the financial statements are issued, and removes the requirement for an SEC filer to disclose the date through which subsequent events have been evaluated. ASU 2010-09 was effective upon issuance except for the use of the issued date for conduit debt obligors. The impact of ASU 2010-09 on our disclosures is reflected in Note 11 - Subsequent Events.

**Fair Value Measurements and Disclosures:** In January 2010, the FASB issued ASU No. 2010-06 "Fair Value Measurements and Disclosures (Topic 820) – Improving Disclosures about Fair Value Measurements." ASU 2010-06 amends the fair value disclosure guidance. The amendments include new disclosures and changes to clarify existing disclosure requirements. ASU 2010-06 was effective for interim and annual reporting periods beginning after December 15, 2009, except for the disclosures about purchases, sales, issuances, and settlements of Level 3 fair value measurements. Those disclosures are effective for fiscal years beginning after December 15, 2010, and for interim periods within those fiscal years. The impact of ASU 2010-06 on our disclosures is reflected in Note 10 - Fair Value Measurements.

**Consolidations:** In December 2009, the FASB issued ASU No. 2009-17 (formerly Statement No. 167), "Consolidations (Topic 810) – Improvements to Financial Reporting for Enterprises involved with Variable Interest Entities". ASU 2009-17 amends the consolidation guidance applicable to variable interest entities. The amendments to the consolidation guidance affect all entities, as well as qualifying special-purpose entities (QSPEs) that are currently excluded from previous consolidation guidance. ASU 2009-17 was effective as of the beginning of the first annual reporting period that begins after November 15, 2009. ASU 2009-17 did not have an impact on our financial condition, results of operations, or disclosures.



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Accounting for Transfers of Financial Assets: In December 2009, the FASB issued ASU No. 2009-16 (formerly Statement No. 166), "Transfers and Servicing (Topic 860) – Accounting for Transfers of Financial Assets". ASU 2009-16 amends the derecognition accounting and disclosure guidance. ASU 2009-16 eliminates the exemption from consolidation for QSPEs and also requires a transferor to evaluate all existing QSPEs to determine whether they must be consolidated. ASU 2009-16 was effective as of the beginning of the first annual reporting period that begins after November 15, 2009. ASU 2009-16 did not have an impact on our financial condition, results of operations, or disclosures.

## Note 3. Investment Securities

Investment securities available-for-sale were as follows:

(Dollars in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
March 31, 2010				
U.S. Treasury and Federal agencies securities	\$355,055	\$1,319	\$(547 )	\$355,827
U.S. States and political subdivisions securities	173,425	5,265	(2,319 )	176,371
Mortgage-backed securities - Federal agencies	322,899	6,201	(1,256 )	327,844
Corporate debt securities	24,048	185	-	24,233
Foreign government securities	1,688	6	-	1,694
Total debt securities	877,115	12,976	(4,122 )	885,969
Marketable equity securities	1,288	1,632	(27 )	2,893
Total investment securities available-for-sale	\$878,403	\$14,608	\$(4,149 )	\$888,862
December 31, 2009				
U.S. Treasury and Federal agencies securities	\$390,189	\$760	\$(1,780 )	