

SOUTH STATE Corp  
Form 10-Q  
May 08, 2015  
[Table of Contents](#)

**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

WASHINGTON, D.C. 20549

**FORM 10-Q**

(Mark One)

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

**For the quarterly period ended March 31, 2015**

**OR**

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

**For the transition period from to**

**Commission file number 001-12669**

## **SOUTH STATE CORPORATION**

(Exact name of registrant as specified in its charter)

**South Carolina**

(State or other jurisdiction of incorporation)

**57-0799315**

(IRS Employer Identification No.)

**520 Gervais Street**

**Columbia, South Carolina**

(Address of principal executive offices)

**29201**

(Zip Code)

**(800) 277-2175**

(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, if any, every Interactive Data file required to be submitted and posted pursuant to Rule 405 of Regulation S-T (Section 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 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.

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 ☒

## Edgar Filing: SOUTH STATE Corp - Form 10-Q

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

| Class                          | Outstanding as of April 30, 2015 |
|--------------------------------|----------------------------------|
| Common Stock, \$2.50 par value | 24,184,578                       |

---

Table of Contents

**South State Corporation and Subsidiary**

**March 31, 2015 Form 10-Q**

**INDEX**

|                                                                                                                                | <b>Page</b> |
|--------------------------------------------------------------------------------------------------------------------------------|-------------|
| <b><u>PART I FINANCIAL INFORMATION</u></b>                                                                                     |             |
| <u>Item 1.</u>                                                                                                                 |             |
| <u>Financial Statements</u>                                                                                                    |             |
| <u>Condensed Consolidated Balance Sheets at March 31, 2015, December 31, 2014 and March 31, 2014</u>                           | 1           |
| <u>Condensed Consolidated Statements of Income for the Three Months Ended March 31, 2015 and 2014</u>                          | 2           |
| <u>Condensed Consolidated Statements of Comprehensive Income for the Three Months Ended March 31, 2015 and 2014</u>            | 3           |
| <u>Condensed Consolidated Statements of Changes in Shareholders' Equity for the Three Months Ended March 31, 2015 and 2014</u> | 4           |
| <u>Condensed Consolidated Statements of Cash Flows for the Three Months Ended March 31, 2015 and 2014</u>                      | 5           |
| <u>Notes to Condensed Consolidated Financial Statements</u>                                                                    | 6-48        |
| <u>Item 2.</u>                                                                                                                 |             |
| <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>                                   | 49-70       |
| <u>Item 3.</u>                                                                                                                 |             |
| <u>Quantitative and Qualitative Disclosures About Market Risk</u>                                                              | 70          |
| <u>Item 4.</u>                                                                                                                 |             |
| <u>Controls and Procedures</u>                                                                                                 | 70          |
| <b><u>PART II OTHER INFORMATION</u></b>                                                                                        |             |
| <u>Item 1.</u>                                                                                                                 |             |
| <u>Legal Proceedings</u>                                                                                                       | 70          |
| <u>Item 1A.</u>                                                                                                                |             |
| <u>Risk Factors</u>                                                                                                            | 70          |
| <u>Item 2.</u>                                                                                                                 |             |
| <u>Unregistered Sales of Equity Securities and Use of Proceeds</u>                                                             | 71          |
| <u>Item 3.</u>                                                                                                                 |             |
| <u>Defaults Upon Senior Securities</u>                                                                                         | 71          |
| <u>Item 4.</u>                                                                                                                 |             |
| <u>Mine Safety Disclosures</u>                                                                                                 | 71          |
| <u>Item 5.</u>                                                                                                                 |             |
| <u>Other Information</u>                                                                                                       | 71          |
| <u>Item 6.</u>                                                                                                                 |             |
| <u>Exhibits</u>                                                                                                                | 72          |



Table of Contents**PART I FINANCIAL INFORMATION****Item 1. FINANCIAL STATEMENTS****South State Corporation and Subsidiary****Condensed Consolidated Balance Sheets***(Dollars in thousands, except par value)*

|                                                                                                                                                                                             | March 31,<br>2015<br>(Unaudited) | December 31,<br>2014<br>(Note 1) | March 31,<br>2014<br>(Unaudited) |
|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------------------|----------------------------------|----------------------------------|
| <b>ASSETS</b>                                                                                                                                                                               |                                  |                                  |                                  |
| Cash and cash equivalents:                                                                                                                                                                  |                                  |                                  |                                  |
| Cash and due from banks                                                                                                                                                                     | \$ 457,130                       | \$ 229,901                       | \$ 361,816                       |
| Interest-bearing deposits with banks                                                                                                                                                        | 7,696                            | 7,456                            | 4,690                            |
| Federal funds sold and securities purchased under agreements to resell                                                                                                                      | 165,908                          | 180,512                          | 246,109                          |
| Total cash and cash equivalents                                                                                                                                                             | 630,734                          | 417,869                          | 612,615                          |
| Investment securities:                                                                                                                                                                      |                                  |                                  |                                  |
| Securities held to maturity (fair value of \$10,232, \$10,233, and \$11,427, respectively)                                                                                                  | 9,659                            | 9,659                            | 10,891                           |
| Securities available for sale, at fair value                                                                                                                                                | 808,396                          | 806,766                          | 793,124                          |
| Other investments                                                                                                                                                                           | 9,031                            | 10,518                           | 10,518                           |
| Total investment securities                                                                                                                                                                 | 827,086                          | 826,943                          | 814,533                          |
| Loans held for sale                                                                                                                                                                         | 87,342                           | 61,934                           | 57,609                           |
| Loans:                                                                                                                                                                                      |                                  |                                  |                                  |
| Acquired credit impaired (covered of \$172,870, \$182,464, and \$263,735, respectively; non-covered of \$693,634, \$736,938, and \$850,028, respectively), net of allowance for loan losses | 866,504                          | 919,402                          | 1,113,763                        |
| Acquired non-credit impaired (covered of \$8,591, \$9,376, and \$8,246, respectively; non-covered of \$1,238,758, \$1,318,623, and \$1,503,955, respectively)                               | 1,247,349                        | 1,327,999                        | 1,512,201                        |
| Non-acquired                                                                                                                                                                                | 3,586,405                        | 3,467,826                        | 2,979,958                        |
| Less allowance for non-acquired loan losses                                                                                                                                                 | (33,538)                         | (34,539)                         | (34,669)                         |
| Loans, net                                                                                                                                                                                  | 5,666,720                        | 5,680,688                        | 5,571,253                        |
| FDIC receivable for loss share agreements                                                                                                                                                   | 16,713                           | 22,161                           | 60,484                           |
| Other real estate owned (covered of \$12,026, \$16,227, and \$29,003, respectively; non-covered of \$24,070, \$26,499, and \$35,144, respectively)                                          | 36,096                           | 42,726                           | 64,147                           |
| Premises and equipment, net                                                                                                                                                                 | 171,565                          | 171,772                          | 187,127                          |
| Bank owned life insurance                                                                                                                                                                   | 99,751                           | 99,140                           | 97,314                           |
| Deferred tax assets                                                                                                                                                                         | 40,629                           | 42,692                           | 67,997                           |
| Mortgage servicing rights                                                                                                                                                                   | 21,510                           | 21,601                           | 20,925                           |
| Core deposit and other intangibles                                                                                                                                                          | 47,223                           | 49,239                           | 57,568                           |
| Goodwill                                                                                                                                                                                    | 317,688                          | 317,688                          | 317,688                          |
| Other assets                                                                                                                                                                                | 58,525                           | 71,774                           | 61,715                           |
| Total assets                                                                                                                                                                                | \$ 8,021,582                     | \$ 7,826,227                     | \$ 7,990,975                     |
| <b>LIABILITIES AND SHAREHOLDERS EQUITY</b>                                                                                                                                                  |                                  |                                  |                                  |
| Deposits:                                                                                                                                                                                   |                                  |                                  |                                  |

# Edgar Filing: SOUTH STATE Corp - Form 10-Q

|                                                                                                                                                   |    |           |    |           |    |           |
|---------------------------------------------------------------------------------------------------------------------------------------------------|----|-----------|----|-----------|----|-----------|
| Noninterest-bearing                                                                                                                               | \$ | 1,757,302 | \$ | 1,639,953 | \$ | 1,585,055 |
| Interest-bearing                                                                                                                                  |    | 4,876,355 |    | 4,821,092 |    | 5,049,496 |
| Total deposits                                                                                                                                    |    | 6,633,657 |    | 6,461,045 |    | 6,634,551 |
| Federal funds purchased and securities sold under agreements to repurchase                                                                        |    | 276,774   |    | 221,541   |    | 254,985   |
| Other borrowings                                                                                                                                  |    | 55,003    |    | 101,210   |    | 100,963   |
| Other liabilities                                                                                                                                 |    | 48,584    |    | 57,511    |    | 66,313    |
| Total liabilities                                                                                                                                 |    | 7,014,018 |    | 6,841,307 |    | 7,056,812 |
| Shareholders' equity:                                                                                                                             |    |           |    |           |    |           |
| Preferred stock - \$.01 par value; authorized 10,000,000 shares; no shares issued and outstanding                                                 |    |           |    |           |    |           |
| Common stock - \$2.50 par value; authorized 40,000,000 shares; 24,156,759, 24,150,702, and 24,118,243 shares issued and outstanding, respectively |    | 60,392    |    | 60,377    |    | 60,296    |
| Surplus                                                                                                                                           |    | 702,648   |    | 701,764   |    | 698,079   |
| Retained earnings                                                                                                                                 |    | 241,526   |    | 223,156   |    | 179,842   |
| Accumulated other comprehensive income (loss)                                                                                                     |    | 2,998     |    | (377)     |    | (4,054)   |
| Total shareholders' equity                                                                                                                        |    | 1,007,564 |    | 984,920   |    | 934,163   |
| Total liabilities and shareholders' equity                                                                                                        | \$ | 8,021,582 | \$ | 7,826,227 | \$ | 7,990,975 |

The Accompanying Notes are an Integral Part of the Financial Statements.

Table of Contents

## South State Corporation and Subsidiary

## Condensed Consolidated Statements of Income (unaudited)

*(Dollars in thousands, except per share data)*

|                                                                            | Three Months Ended<br>March 31, |           |
|----------------------------------------------------------------------------|---------------------------------|-----------|
|                                                                            | 2015                            | 2014      |
| <b>Interest income:</b>                                                    |                                 |           |
| Loans, including fees                                                      | \$ 78,848                       | \$ 81,959 |
| Investment securities:                                                     |                                 |           |
| Taxable                                                                    | 3,661                           | 3,881     |
| Tax-exempt                                                                 | 1,078                           | 1,156     |
| Federal funds sold and securities purchased under agreements to resell     | 411                             | 460       |
| Total interest income                                                      | 83,998                          | 87,456    |
| <b>Interest expense:</b>                                                   |                                 |           |
| Deposits                                                                   | 2,003                           | 2,401     |
| Federal funds purchased and securities sold under agreements to repurchase | 96                              | 101       |
| Other borrowings                                                           | 850                             | 1,488     |
| Total interest expense                                                     | 2,949                           | 3,990     |
| Net interest income                                                        | 81,049                          | 83,466    |
| Provision for loan losses                                                  | 818                             | 849       |
| Net interest income after provision for loan losses                        | 80,231                          | 82,617    |
| <b>Noninterest income:</b>                                                 |                                 |           |
| Service charges on deposit accounts                                        | 8,108                           | 8,988     |
| Bankcard services income                                                   | 7,599                           | 7,105     |
| Mortgage banking income                                                    | 6,626                           | 3,291     |
| Trust and investment services income                                       | 4,934                           | 4,543     |
| Amortization of FDIC indemnification assets, net                           | (3,207)                         | (7,078)   |
| Other                                                                      | 2,445                           | 3,699     |
| Total noninterest income                                                   | 26,505                          | 20,548    |
| <b>Noninterest expense:</b>                                                |                                 |           |
| Salaries and employee benefits                                             | 40,987                          | 39,093    |
| Net occupancy expense                                                      | 5,237                           | 5,608     |
| Information services expense                                               | 3,958                           | 4,398     |
| Furniture and equipment expense                                            | 3,145                           | 3,744     |
| OREO expense and loan related                                              | 3,014                           | 4,203     |
| Amortization of intangibles                                                | 2,016                           | 2,104     |
| Bankcard expense                                                           | 1,980                           | 2,256     |
| Supplies, printing and postage expense                                     | 1,612                           | 1,583     |
| Professional fees                                                          | 1,409                           | 1,262     |
| FDIC assessment and other regulatory charges                               | 1,184                           | 1,576     |
| Advertising and marketing                                                  | 888                             | 1,007     |
| Merger and branding related expense                                        |                                 | 5,985     |
| Other                                                                      | 5,055                           | 4,597     |
| Total noninterest expense                                                  | 70,485                          | 77,416    |
| <b>Earnings:</b>                                                           |                                 |           |
| Income before provision for income taxes                                   | 36,251                          | 25,749    |
| Provision for income taxes                                                 | 12,325                          | 8,832     |
| <b>Net income</b>                                                          | \$ 23,926                       | \$ 16,917 |
| Preferred stock dividends                                                  |                                 | 1,073     |
| <b>Net income available to common shareholders</b>                         | \$ 23,926                       | \$ 15,844 |
| <b>Earnings per common share:</b>                                          |                                 |           |

# Edgar Filing: SOUTH STATE Corp - Form 10-Q

|                                                    |    |        |    |        |
|----------------------------------------------------|----|--------|----|--------|
| Basic                                              | \$ | 1.00   | \$ | 0.66   |
| Diluted                                            | \$ | 0.99   | \$ | 0.66   |
| Dividends per common share                         | \$ | 0.23   | \$ | 0.19   |
| <b>Weighted-average common shares outstanding:</b> |    |        |    |        |
| Basic                                              |    | 23,943 |    | 23,873 |
| Diluted                                            |    | 24,201 |    | 24,116 |

The Accompanying Notes are an Integral Part of the Financial Statements.

Table of Contents

**South State Corporation and Subsidiary**

**Condensed Consolidated Statements of Comprehensive Income (unaudited)**

*(Dollars in thousands)*

|                                                                                               | <b>Three Months Ended<br/>March 31,</b> |             |
|-----------------------------------------------------------------------------------------------|-----------------------------------------|-------------|
|                                                                                               | <b>2015</b>                             | <b>2014</b> |
| Net income                                                                                    | \$ 23,926                               | \$ 16,917   |
| Other comprehensive income:                                                                   |                                         |             |
| Unrealized gains on securities:                                                               |                                         |             |
| Unrealized holding gains arising during period                                                | 5,275                                   | 9,158       |
| Tax effect                                                                                    | (2,012)                                 | (3,492)     |
| Net of tax amount                                                                             | 3,263                                   | 5,666       |
| Unrealized gains (losses) on derivative financial instruments qualifying as cash flow hedges: |                                         |             |
| Unrealized holding losses arising during period                                               | (121)                                   | (71)        |
| Tax effect                                                                                    | 46                                      | 27          |
| Reclassification adjustment for losses included in interest expense                           | 76                                      | 76          |
| Tax effect                                                                                    | (29)                                    | (29)        |
| Net of tax amount                                                                             | (28)                                    | 3           |
| Changes in pension plan obligation:                                                           |                                         |             |
| Reclassification adjustment for changes included in net income                                | 226                                     |             |
| Tax effect                                                                                    | (86)                                    |             |
| Net of tax amount                                                                             | 140                                     |             |
| Other comprehensive income, net of tax                                                        | 3,375                                   | 5,669       |
| Comprehensive income                                                                          | \$ 27,301                               | \$ 22,586   |

The Accompanying Notes are an Integral Part of the Financial Statements.

[Table of Contents](#)
**South State Corporation and Subsidiary**
**Condensed Consolidated Statements of Changes in Shareholders' Equity (unaudited)**
**Three months ended March 31, 2015 and 2014**
*(Dollars in thousands, except per share data)*

|                                                                          | Preferred Stock |        | Common Stock |           | Surplus    | Retained Earnings | Accumulated Other Comprehensive Income (Loss) | Total        |
|--------------------------------------------------------------------------|-----------------|--------|--------------|-----------|------------|-------------------|-----------------------------------------------|--------------|
|                                                                          | Shares          | Amount | Shares       | Amount    |            |                   |                                               |              |
| Balance, December 31, 2013                                               | 65,000          | \$ 1   | 24,104,124   | \$ 60,260 | \$ 762,354 | \$ 168,577        | \$ (9,723)                                    | \$ 981,469   |
| Comprehensive income                                                     |                 |        |              |           |            | 16,917            | 5,669                                         | 22,586       |
| Cash dividends on Series A preferred stock at annual dividend rate of 9% |                 |        |              |           |            | (1,073)           |                                               | (1,073)      |
| Cash dividends declared on common stock at \$0.19 per share              |                 |        |              |           |            | (4,579)           |                                               | (4,579)      |
| Stock options exercised                                                  |                 |        | 4,660        | 12        | 117        |                   |                                               | 129          |
| Restricted stock awards                                                  |                 |        | 13,592       | 34        | (34)       |                   |                                               |              |
| Repurchase of Series A preferred stock                                   | (65,000)        | (1)    |              |           | (64,999)   |                   |                                               | (65,000)     |
| Common stock repurchased                                                 |                 |        | (4,133)      | (10)      | (243)      |                   |                                               | (253)        |
| Share-based compensation expense                                         |                 |        |              |           | 884        |                   |                                               | 884          |
| Balance, March 31, 2014                                                  |                 | \$     | 24,118,243   | \$ 60,296 | \$ 698,079 | \$ 179,842        | \$ (4,054)                                    | \$ 934,163   |
| Balance, December 31, 2014                                               |                 | \$     | 24,150,702   | \$ 60,377 | \$ 701,764 | \$ 223,156        | \$ (377)                                      | \$ 984,920   |
| Comprehensive income                                                     |                 |        |              |           |            | 23,926            | 3,375                                         | 27,301       |
| Cash dividends declared on common stock at \$0.23 per share              |                 |        |              |           |            | (5,556)           |                                               | (5,556)      |
| Stock options exercised                                                  |                 |        | 21,000       | 53        | 614        |                   |                                               | 667          |
| Restricted stock awards                                                  |                 |        | 907          | 2         | (2)        |                   |                                               |              |
| Common stock repurchased                                                 |                 |        | (15,850)     | (40)      | (941)      |                   |                                               | (981)        |
| Share-based compensation expense                                         |                 |        |              |           | 1,213      |                   |                                               | 1,213        |
| Balance, March 31, 2015                                                  |                 | \$     | 24,156,759   | \$ 60,392 | \$ 702,648 | \$ 241,526        | \$ 2,998                                      | \$ 1,007,564 |

The Accompanying Notes are an Integral Part of the Financial Statements.

Table of Contents**South State Corporation and Subsidiary****Condensed Consolidated Statements of Cash Flows (unaudited)***(Dollars in thousands)*

|                                                                                                                            | <b>Three Months Ended<br/>March 31,</b> |             |
|----------------------------------------------------------------------------------------------------------------------------|-----------------------------------------|-------------|
|                                                                                                                            | <b>2015</b>                             | <b>2014</b> |
| Cash flows from operating activities:                                                                                      |                                         |             |
| Net income                                                                                                                 | \$ 23,926                               | \$ 16,917   |
| Adjustments to reconcile net income to net cash provided by operating activities:                                          |                                         |             |
| Depreciation and amortization                                                                                              | 5,353                                   | 5,367       |
| Provision for loan losses                                                                                                  | 818                                     | 849         |
| Deferred income taxes                                                                                                      | (17)                                    | 2,303       |
| Share-based compensation expense                                                                                           | 1,213                                   | 884         |
| Amortization on FDIC indemnification asset                                                                                 | 3,207                                   | 7,078       |
| Accretion of discount related to performing acquired loans                                                                 | (1,600)                                 | (2,954)     |
| (Gain) loss on sale of premises and equipment                                                                              | 44                                      | (4)         |
| Gain on sale of OREO                                                                                                       | (207)                                   | (2,712)     |
| Net amortization of premium on investment securities                                                                       | 1,178                                   | 998         |
| OREO write downs                                                                                                           | 2,215                                   | 3,001       |
| Originations and purchases of mortgage loans for sale                                                                      | (241,740)                               | (141,939)   |
| Proceeds from sales of mortgage loans for sale                                                                             | 217,101                                 | 132,935     |
| Net change in:                                                                                                             |                                         |             |
| Accrued interest receivable                                                                                                | 111                                     | (2,385)     |
| Prepaid assets                                                                                                             | (243)                                   | 2,105       |
| FDIC Loss Share Receivable                                                                                                 | 2,241                                   | 18,884      |
| Accrued interest payable                                                                                                   | (1,147)                                 | (534)       |
| Accrued income taxes                                                                                                       | 11,067                                  | 10,725      |
| Miscellaneous assets and liabilities                                                                                       | (6,321)                                 | (19,817)    |
| Net cash provided by operating activities                                                                                  | 17,199                                  | 31,701      |
| Cash flows from investing activities:                                                                                      |                                         |             |
| Proceeds from maturities and calls of investment securities held to maturity                                               |                                         | 1,535       |
| Proceeds from maturities and calls of investment securities available for sale                                             | 42,301                                  | 29,157      |
| Proceeds from calls of other investment securities                                                                         | 1,392                                   |             |
| Proceeds from sales of other investment securities                                                                         | 95                                      | 2,868       |
| Purchases of investment securities available for sale                                                                      | (39,836)                                | (27,413)    |
| Purchases of other investments                                                                                             |                                         | (6,186)     |
| Net decrease in loans                                                                                                      | 8,214                                   | 46,276      |
| Net cash received from acquisitions                                                                                        |                                         | 749         |
| Purchases of premises and equipment                                                                                        | (3,264)                                 | (5,389)     |
| Proceeds from sale of OREO                                                                                                 | 11,158                                  | 13,070      |
| Proceeds from sale of premises and equipment                                                                               | 25                                      | 6           |
| Net cash provided by investing activities                                                                                  | 20,085                                  | 54,673      |
| Cash flows from financing activities:                                                                                      |                                         |             |
| Net increase in deposits                                                                                                   | 172,612                                 | 75,156      |
| Net increase in federal funds purchased and securities sold under agreements to repurchase and other short-term borrowings | 55,233                                  | 43,584      |
| Repayment of other borrowings                                                                                              | (46,394)                                | (1,184)     |
| Preferred stock repurchase                                                                                                 |                                         | (65,000)    |
| Common stock repurchase                                                                                                    | (981)                                   | (253)       |
| Dividends paid on preferred stock                                                                                          |                                         | (1,073)     |
| Dividends paid on common stock                                                                                             | (5,556)                                 | (4,579)     |

# Edgar Filing: SOUTH STATE Corp - Form 10-Q

|                                                  |            |            |
|--------------------------------------------------|------------|------------|
| Stock options exercised                          | 667        | 129        |
| Net cash provided by financing activities        | 175,581    | 46,780     |
| Net increase in cash and cash equivalents        | 212,865    | 133,154    |
| Cash and cash equivalents at beginning of period | 417,869    | 479,461    |
| Cash and cash equivalents at end of period       | \$ 630,734 | \$ 612,615 |

## **Supplemental Disclosures:**

### Cash Flow Information:

#### Cash paid for:

|              |          |          |
|--------------|----------|----------|
| Interest     | \$ 4,098 | \$ 4,540 |
| Income taxes | \$ 1,670 | \$ 421   |

## **Schedule of Noncash Investing Transactions:**

|                                                                                                                                                                     |          |           |
|---------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------|-----------|
| Real estate acquired in full or in partial settlement of loans (covered of \$2,423 and \$6,822, respectively; and non-covered of \$4,113 and \$5,766, respectively) | \$ 6,536 | \$ 12,588 |
|---------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------|-----------|

The Accompanying Notes are an Integral Part of the Financial Statements.

Table of Contents

**South State Corporation and Subsidiary**

**Notes to Condensed Consolidated Financial Statements (unaudited)**

**Note 1 Basis of Presentation**

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and disclosures required by accounting principles generally accepted in the United States ( GAAP ) for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Certain prior period information has been reclassified to conform to the current period presentation, and these reclassifications had no impact on net income or equity as previously reported. Operating results for the three months ended March 31, 2015 are not necessarily indicative of the results that may be expected for the year ending December 31, 2015.

The condensed consolidated balance sheet at December 31, 2014 has been derived from the audited financial statements at that date but does not include all of the information and disclosures required by GAAP for complete financial statements.

**Note 2 Summary of Significant Accounting Policies**

The information contained in the consolidated financial statements and accompanying notes included in the Company's Annual Report on Form 10-K for the year ended December 31, 2014, as filed with the Securities and Exchange Commission (the SEC ) on February 27, 2015, should be referenced when reading these unaudited condensed consolidated financial statements. Unless otherwise mentioned or unless the context requires otherwise, references herein to South State, the Company we, us, our or similar references mean South State Corporation and consolidated subsidiaries. References to the Bank means South State Bank, a South Carolina banking corporation.

***Subsequent Events***

The Company has evaluated subsequent events for accounting and disclosure purposes through the date the financial statements are issued.

**Note 3 Recent Accounting and Regulatory Pronouncements**

In February 2015, the Financial Accounting Standards Board ( FASB ) issued Accounting Standards Update ( ASU ) 2015-02, *Amendments to the Consolidation Analysis* ( ASU 2015-02 ). This ASU affects reporting entities that are required to evaluate whether they should consolidate certain legal entities. Specifically, the amendments: (1) modify the evaluation of whether limited partnerships and similar legal entities are variable

## Edgar Filing: SOUTH STATE Corp - Form 10-Q

interest entities ( VIEs ) or voting interest entities; (2) eliminate the presumption that a general partner should consolidate a limited partnership; (3) affect the consolidation analysis of reporting entities that are involved with VIEs, particularly those that have fee arrangements and related party relationships; and (4) provide a scope exception from consolidation guidance for reporting entities with interests in legal entities that are required to comply with or operate in accordance with requirements that are similar to those in Rule 2a-7 of the Investment Company Act of 1940 for registered money market funds. ASU No. 2015-02 is effective for interim and annual reporting periods beginning after December 15, 2015. The Company is currently evaluating the impact of adopting the new guidance on the consolidated financial statements, but does not expect it to have a material impact.

In November 2014, the FASB issued ASU 2014-16, *Derivatives and Hedging (Topic 815): Determining Whether the Host Contract in a Hybrid Financial Instrument Issued in the Form of a Share Is More Akin to Debt or to Equity*, a consensus of the FASB Emerging Issues Task Force ( ASU 2014-16 ). This ASU clarifies how current U.S. GAAP should be interpreted in subjectively evaluating the economic characteristics and risks of a host contract in a hybrid financial instrument that is issued in the form of a share. ASU 2014-16 is effective for public business entities for annual periods and interim periods within those annual periods, beginning after December 15, 2015. The adoption of ASU 2014-16 is not expected to have a material impact on the Company's financial statements.

Table of Contents

**Note 3 Recent Accounting and Regulatory Pronouncements (Continued)**

In August 2014, the FASB issued ASU 2014-14: *Receivables Troubled Debt Restructurings by Creditors (Subtopic 310-40) Classification of Certain Government Guaranteed Mortgage Loans upon Foreclosure* ( ASU 2014-14 ). ASU 2014-14 provides clarifying guidance related to how creditors classify government-guaranteed loans upon foreclosure. ASU 2014-14 requires that a mortgage loan be derecognized and a separate receivable be recognized upon foreclosure if certain conditions are met. Upon foreclosure, the separate receivable should be measured based on the amount of the loan balance (principal and interest) expected to be recovered from the guarantor. ASU 2014-14 became effective for the Company on January 1, 2015 and did not have an impact on the Company's financial statements.

In June 2014, the FASB issued ASU 2014-12, *Compensation Stock Compensation (Topic 718): Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved after the Requisite Service Period, a consensus of the FASB Emerging Issues Task Force* ( ASU 2014-12 ). ASU 2014-12 requires that a performance target that affects vesting and that could be achieved after the requisite service period be treated as a performance condition. ASU 2014-12 is effective for annual periods and interim periods within those annual periods, beginning after December 15, 2015. An entity may apply the standards (1) prospectively to all share-based payment awards that are granted or modified on or after the effective date, or (2) retrospectively to all awards with performance targets that are outstanding as of the beginning of the earliest annual period presented in the financial statements and to all new or modified awards thereafter. Earlier application is permitted. The adoption of ASU 2014-12 is not expected to have a material impact on the Company's financial statements.

In June 2014, the FASB issued ASU 2014-11, *Transfers and Servicing (Topic 860): Repurchase-to-Maturity Transactions, Repurchase Financings, and Disclosures* ( ASU 2014-11 ). ASU 2014-11 aligns the accounting for repurchase to maturity transactions and repurchase agreements executed as a repurchase financing with the accounting for other typical repurchase agreements. Going forward, these transactions would all be accounted for as secured borrowings. ASU 2014-11 became effective for the Company on January 1, 2015 and did not have a significant impact on the Company's financial statements.

In May 2014, the FASB issued ASU 2014-09, *Revenue from Contracts with Customers, Topic 606* ( ASU 2014-09 ). The new standard's core principle is that a company will recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which the company expects to be entitled in exchange for those goods or services. In doing so, companies will need to use more judgment and make more estimates than under existing guidance. These may include identifying performance obligations in the contract, estimating the amount of variable consideration to include in the transaction price and allocating the transaction price to each separate performance obligation. ASU 2014-09 is effective for annual reporting periods beginning after December 15, 2016 (although the FASB recently proposed a one-year deferral of the effective date), including interim periods within that reporting period. The amendments can be applied retrospectively to each prior reporting period or retrospectively with the cumulative effect of initially applying this new guidance recognized at the date of initial application. The Company is currently evaluating the provisions of ASU 2014-09 to determine the potential impact the new standard will have to the Company's financial statements.

In January 2014, the FASB issued ASU 2014-04, *Receivables Troubled Debt Restructurings by Creditors (Subtopic 310-40): Reclassification of Residential Real Estate Collateralized Consumer Mortgage Loans upon Foreclosure, a consensus of the FASB Emerging Issues Task Force* ( ASU 2014-04 ). ASU 2014-04 clarifies that an in-substance foreclosure occurs, and a creditor is considered to have received physical possession of residential real estate property collateralizing a consumer mortgage loan, upon either (i) the creditor obtaining legal title to the residential real estate property upon completion of a foreclosure or (ii) the borrower conveying all interest in the residential real estate property to the creditor to satisfy the loan through completion of a deed in lieu of foreclosure or similar legal agreement. ASU 2014-04 also requires disclosure of both the amount of foreclosed residential real estate property held by the creditor and the recorded investment in loans collateralized by residential real estate property that are in the process of foreclosure. ASU 2014-04 became effective for the Company on January 1, 2015 and, other than additional disclosures regarding residential real estate foreclosures and properties in process of foreclosure, did not have a significant impact on

the Company's financial statements.

In January 2014, the FASB issued ASU No. 2014-01, *Accounting for Investments in Qualified Affordable Housing Projects* (ASU 2014-01). ASU 2014-01 amends FASB ASC 323, *Investments - Equity Method and Joint Ventures*, to permit reporting entities to make an accounting policy election to account for their investments in qualified affordable housing projects using the proportional amortization method if certain conditions are met. Under the proportional amortization method, an entity amortizes the initial cost of the investment in proportion to the tax credits and other tax benefits received and recognizes the net investment performance in the income statement as a component of income tax expense (benefit). ASU 2014-02 became effective for the Company on January 1, 2015 and did not have a significant impact on the Company's financial statements (see Note 20).

## Table of Contents

### Note 4 Mergers and Acquisitions

The following mergers and acquisitions are referenced throughout this Form 10-Q:

- Community Bank & Trust ( CBT ) January 29, 2010 Federal Deposit Insurance Corporation ( FDIC ) purchase and assumption agreement
- Habersham Bank ( Habersham ) February 18, 2011 FDIC purchase and assumption agreement
- BankMeridian, N.A. ( BankMeridian ) July 29, 2011 FDIC purchase and assumption agreement
- Peoples Bancorporation, Inc. ( Peoples ) April 24, 2012 Whole bank acquisition
- The Savannah Bancorp, Inc. ( Savannah ) December 13, 2012 Whole bank acquisition
- Former First Financial Holdings, Inc. ( FFHI ) July 26, 2013 Whole bank acquisition with FDIC purchase and assumption agreements of Cape Fear Bank ( Cape Fear ) April 10, 2009 and Plantation Federal Bank ( Plantation ) April 27, 2012

FDIC purchase and assumption agreement means that only certain assets and liabilities were acquired by the bank from the FDIC. A whole bank acquisition means that the two parties in the transaction agreed to the transaction, and there was no involvement of the FDIC. A whole bank acquisition with FDIC purchase and assumption agreements means that the two parties in the transaction agreed to the merger, and there were existing FDIC purchase and assumption agreements.

### Note 5 Investment Securities

The following is the amortized cost and fair value of investment securities held to maturity:

| (Dollars in thousands)          | Amortized<br>Cost | Gross<br>Unrealized<br>Gains | Gross<br>Unrealized<br>Losses | Fair<br>Value |
|---------------------------------|-------------------|------------------------------|-------------------------------|---------------|
| <b>March 31, 2015:</b>          |                   |                              |                               |               |
| State and municipal obligations | \$ 9,659          | \$ 573                       | \$                            | \$ 10,232     |
| <b>December 31, 2014:</b>       |                   |                              |                               |               |
| State and municipal obligations | \$ 9,659          | \$ 574                       | \$                            | \$ 10,233     |
| <b>March 31, 2014:</b>          |                   |                              |                               |               |

Edgar Filing: SOUTH STATE Corp - Form 10-Q

|                                 |    |        |    |     |    |     |    |        |
|---------------------------------|----|--------|----|-----|----|-----|----|--------|
| State and municipal obligations | \$ | 10,891 | \$ | 538 | \$ | (2) | \$ | 11,427 |
|---------------------------------|----|--------|----|-----|----|-----|----|--------|

Table of Contents
**Note 5 Investment Securities (Continued)**

The following is the amortized cost and fair value of investment securities available for sale:

| (Dollars in thousands)               | Amortized<br>Cost | Gross<br>Unrealized<br>Gains | Gross<br>Unrealized<br>Losses | Fair<br>Value |
|--------------------------------------|-------------------|------------------------------|-------------------------------|---------------|
| <b>March 31, 2015:</b>               |                   |                              |                               |               |
| Government-sponsored entities debt * | \$ 134,296        | \$ 384                       | \$ (477)                      | 134,203       |
| State and municipal obligations      | 132,043           | 4,638                        | (165)                         | 136,516       |
| Mortgage-backed securities **        | 524,785           | 10,005                       | (366)                         | 534,424       |
| Corporate stocks                     | 3,161             | 592                          | (500)                         | 3,253         |
|                                      | \$ 794,285        | \$ 15,619                    | \$ (1,508)                    | \$ 808,396    |
| <b>December 31, 2014:</b>            |                   |                              |                               |               |
| Government-sponsored entities debt * | \$ 149,720        | \$ 191                       | \$ (1,714)                    | 148,197       |
| State and municipal obligations      | 133,635           | 4,141                        | (195)                         | 137,581       |
| Mortgage-backed securities **        | 511,414           | 7,572                        | (1,040)                       | 517,946       |
| Corporate stocks                     | 3,161             | 573                          | (692)                         | 3,042         |
|                                      | \$ 797,930        | \$ 12,477                    | \$ (3,641)                    | \$ 806,766    |
| <b>March 31, 2014:</b>               |                   |                              |                               |               |
| Government-sponsored entities debt * | \$ 141,900        | \$ 406                       | \$ (4,705)                    | 137,601       |
| State and municipal obligations      | 140,840           | 2,462                        | (1,664)                       | 141,638       |
| Mortgage-backed securities **        | 507,159           | 5,896                        | (2,676)                       | 510,379       |
| Corporate stocks                     | 3,161             | 612                          | (267)                         | 3,506         |
|                                      | \$ 793,060        | \$ 9,376                     | \$ (9,312)                    | \$ 793,124    |

\* - The Company's government-sponsored entities holdings are comprised of debt securities offered by Federal Home Loan Mortgage Corporation ( FHLMC ) or Freddie Mac, Federal National Mortgage Association ( FNMA ) or Fannie Mae, FHLB, and Federal Farm Credit Banks ( FFCB ). Also included in the Company's government-sponsored entities are debt securities offered by the Small Business Administration ( SBA ), which have the full faith and credit backing of the United States Government.

\*\* - All of the mortgage-backed securities are issued by government-sponsored entities; there are no private-label holdings.

The following is the amortized cost and fair value of other investment securities:

| (Dollars in thousands)                    | Amortized<br>Cost | Gross<br>Unrealized<br>Gains | Gross<br>Unrealized<br>Losses | Fair<br>Value |
|-------------------------------------------|-------------------|------------------------------|-------------------------------|---------------|
| <b>March 31, 2015:</b>                    |                   |                              |                               |               |
| Federal Home Loan Bank stock              | \$ 7,389          | \$                           | \$                            | 7,389         |
| Investment in unconsolidated subsidiaries | 1,642             |                              |                               | 1,642         |
|                                           | \$ 9,031          | \$                           | \$                            | \$ 9,031      |
| <b>December 31, 2014:</b>                 |                   |                              |                               |               |
| Federal Home Loan Bank stock              | \$ 7,484          | \$                           | \$                            | 7,484         |
| Investment in unconsolidated subsidiaries | 3,034             |                              |                               | 3,034         |
|                                           | \$ 10,518         | \$                           | \$                            | \$ 10,518     |

Edgar Filing: SOUTH STATE Corp - Form 10-Q

**March 31, 2014:**

|                                           |    |        |    |    |    |        |
|-------------------------------------------|----|--------|----|----|----|--------|
| Federal Home Loan Bank stock              | \$ | 7,484  | \$ | \$ | \$ | 7,484  |
| Investment in unconsolidated subsidiaries |    | 3,034  |    |    |    | 3,034  |
|                                           | \$ | 10,518 | \$ | \$ | \$ | 10,518 |

Table of Contents**Note 5 Investment Securities (Continued)**

The amortized cost and fair value of debt securities at March 31, 2015 by contractual maturity are detailed below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without prepayment penalties.

| (Dollars in thousands)                 | Securities<br>Held to Maturity |               | Securities<br>Available for Sale |               |
|----------------------------------------|--------------------------------|---------------|----------------------------------|---------------|
|                                        | Amortized<br>Cost              | Fair<br>Value | Amortized<br>Cost                | Fair<br>Value |
| Due in one year or less                | \$                             | \$            | \$ 6,127                         | \$ 6,168      |
| Due after one year through five years  | 985                            | 1,007         | 38,286                           | 38,676        |
| Due after five years through ten years | 8,674                          | 9,225         | 221,614                          | 226,097       |
| Due after ten years                    |                                |               | 528,258                          | 537,455       |
|                                        | \$ 9,659                       | \$ 10,232     | \$ 794,285                       | \$ 808,396    |

Information pertaining to the Company's securities with gross unrealized losses at March 31, 2015, December 31, 2014 and March 31, 2014, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position is as follows:

| (Dollars in thousands)               | Less Than Twelve Months       |               | Twelve Months or More         |               |
|--------------------------------------|-------------------------------|---------------|-------------------------------|---------------|
|                                      | Gross<br>Unrealized<br>Losses | Fair<br>Value | Gross<br>Unrealized<br>Losses | Fair<br>Value |
| <b>March 31, 2015:</b>               |                               |               |                               |               |
| <b>Securities Available for Sale</b> |                               |               |                               |               |
| Government-sponsored entities debt   | \$ 58                         | \$ 19,933     | \$ 419                        | \$ 32,555     |
| State and municipal obligations      | 4                             | 1,186         | 161                           | 5,593         |
| Mortgage-backed securities           | 29                            | 18,299        | 337                           | 23,040        |
| Corporate Stocks                     |                               |               | 500                           | 1,730         |
|                                      | \$ 91                         | \$ 39,418     | \$ 1,417                      | \$ 62,918     |

**December 31, 2014:****Securities Available for Sale**

|                                    |        |           |          |            |
|------------------------------------|--------|-----------|----------|------------|
| Government-sponsored entities debt | \$ 98  | \$ 22,896 | \$ 1,616 | \$ 82,798  |
| State and municipal obligations    | 3      | 1,444     | 192      | 8,269      |
| Mortgage-backed securities         | 266    | 61,508    | 774      | 55,960     |
| Corporate stocks                   |        |           | 692      | 1,538      |
|                                    | \$ 367 | \$ 85,848 | \$ 3,274 | \$ 148,565 |

**March 31, 2014:****Securities Held to Maturity**

|                                 |      |        |    |    |
|---------------------------------|------|--------|----|----|
| State and municipal obligations | \$ 2 | \$ 499 | \$ | \$ |
|---------------------------------|------|--------|----|----|

**Securities Available for Sale**

|                                    |          |           |        |          |
|------------------------------------|----------|-----------|--------|----------|
| Government-sponsored entities debt | \$ 4,176 | \$ 81,116 | \$ 529 | \$ 9,409 |
| State and municipal obligations    | 1,079    | 62,307    | 585    | 14,400   |
| Mortgage-backed securities         | 2,551    | 187,215   | 125    | 4,288    |
| Corporate stocks                   | 267      | 1,964     |        |          |

Edgar Filing: SOUTH STATE Corp - Form 10-Q

|    |       |    |         |    |       |    |        |
|----|-------|----|---------|----|-------|----|--------|
| \$ | 8,073 | \$ | 332,602 | \$ | 1,239 | \$ | 28,097 |
|----|-------|----|---------|----|-------|----|--------|

Table of Contents**Note 5 Investment Securities (Continued)**

Management evaluates securities for other-than-temporary impairment ( OTTI ) on at least a quarterly basis, and more frequently when economic or market concerns warrant such evaluation. Consideration is given to (1) the financial condition and near-term prospects of the issuer, (2) the outlook for receiving the contractual cash flows of the investments, (3) the length of time and the extent to which the fair value has been less than cost, (4) 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 or for a debt security whether it is more-likely-than-not that the Company will be required to sell the debt security prior to recovering its fair value, and (5) the anticipated outlook for changes in the general level of interest rates. All securities available for sale in an unrealized loss position as of March 31, 2015 continue to perform as scheduled. As part of the Company's evaluation of its intent and ability to hold investments for a period of time sufficient to allow for any anticipated recovery in the market, the Company considers its investment strategy, cash flow needs, liquidity position, capital adequacy and interest rate risk position. The Company does not currently intend to sell the securities within the portfolio and it is not more-likely-than-not that the Company will be required to sell the debt securities; therefore, management does not consider these investments to be other-than-temporarily impaired at March 31, 2015. Management continues to monitor all of these securities with a high degree of scrutiny. There can be no assurance that the Company will not conclude in future periods that conditions existing at that time indicate some or all of these securities may be sold or are other than temporarily impaired, which would require a charge to earnings in such periods.

**Note 6 Loans and Allowance for Loan Losses**

The following is a summary of non-acquired loans:

| <b>(Dollars in thousands)</b>                   | <b>March 31,<br/>2015</b> | <b>December 31,<br/>2014</b> | <b>March 31,<br/>2014</b> |
|-------------------------------------------------|---------------------------|------------------------------|---------------------------|
| Non-acquired loans:                             |                           |                              |                           |
| Commercial non-owner occupied real estate:      |                           |                              |                           |
| Construction and land development               | \$ 358,108                | \$ 364,221                   | \$ 319,441                |
| Commercial non-owner occupied                   | 364,727                   | 333,590                      | 285,145                   |
| Total commercial non-owner occupied real estate | 722,835                   | 697,811                      | 604,586                   |
| Consumer real estate:                           |                           |                              |                           |
| Consumer owner occupied                         | 854,283                   | 786,778                      | 595,652                   |
| Home equity loans                               | 290,488                   | 283,934                      | 263,057                   |
| Total consumer real estate                      | 1,144,771                 | 1,070,712                    | 858,709                   |
| Commercial owner occupied real estate           | 925,192                   | 907,913                      | 845,728                   |
| Commercial and industrial                       | 407,990                   | 405,923                      | 333,574                   |
| Other income producing property                 | 154,360                   | 150,928                      | 158,186                   |
| Consumer                                        | 195,451                   | 189,317                      | 147,710                   |
| Other loans                                     | 35,806                    | 45,222                       | 31,465                    |
| Total non-acquired loans                        | 3,586,405                 | 3,467,826                    | 2,979,958                 |
| Less allowance for loan losses                  | (33,538)                  | (34,539)                     | (34,669)                  |
| Non-acquired loans, net                         | \$ 3,552,867              | \$ 3,433,287                 | \$ 2,945,289              |

# Table of Contents

## Note 6 Loans and Allowance for Loan Losses (Continued)

The following is a summary of acquired non-credit impaired loans accounted for under FASB ASC Topic 310-20, net of related discount:

| (Dollars in thousands)                          | March 31,<br>2015 | December 31,<br>2014 | March 31,<br>2014 |
|-------------------------------------------------|-------------------|----------------------|-------------------|
| FASB ASC Topic 310-20 acquired loans:           |                   |                      |                   |
| Commercial non-owner occupied real estate:      |                   |                      |                   |
| Construction and land development               | \$ 19,598         | \$ 24,099            | \$ 39,181         |
| Commercial non-owner occupied                   | 44,772            | 49,476               | 52,625            |
| Total commercial non-owner occupied real estate | 64,370            | 73,575               | 91,806            |
| Consumer real estate:                           |                   |                      |                   |
| Consumer owner occupied                         | 612,917           | 646,375              | 732,564           |
| Home equity loans                               | 221,535           | 234,949              | 256,963           |
| Total consumer real estate                      | 834,452           | 881,324              | 989,527           |
| Commercial owner occupied real estate           | 56,167            | 62,065               | 71,607            |
| Commercial and industrial                       | 35,592            | 41,130               | 44,183            |
| Other income producing property                 | 61,415            | 65,139               | 73,753            |
| Consumer                                        | 195,353           | 204,766              | 241,325           |
| Total FASB ASC Topic 310-20 acquired loans      | \$ 1,247,349      | \$ 1,327,999         | \$ 1,512,201      |

In accordance with FASB ASC Topic 310-30, the Company aggregated acquired loans that have common risk characteristics into pools of loan categories as described in the table below. The following is a summary of acquired credit impaired loans accounted for under FASB ASC Topic 310-30 (identified as credit impaired at the time of acquisition), net of related discount:

| (Dollars in thousands)                                    | March 31,<br>2015 | December 31,<br>2014 | March 31,<br>2014 |
|-----------------------------------------------------------|-------------------|----------------------|-------------------|
| FASB ASC Topic 310-30 acquired loans:                     |                   |                      |                   |
| Commercial loans greater than or equal to \$1 million-CBT | \$ 15,477         | \$ 15,813            | \$ 21,479         |
| Commercial real estate                                    | 302,592           | 325,109              | 402,505           |
| Commercial real estate construction and development       | 61,456            | 65,262               | 98,060            |
| Residential real estate                                   | 368,633           | 390,244              | 444,115           |
| Consumer                                                  | 80,656            | 85,449               | 99,545            |
| Commercial and industrial                                 | 42,343            | 44,804               | 58,973            |
| Single pay                                                | 64                | 86                   | 132               |
| Total FASB ASC Topic 310-30 acquired loans                | 871,221           | 926,767              | 1,124,809         |
| Less allowance for loan losses                            | (4,717)           | (7,365)              | (11,046)          |
| FASB ASC Topic 310-30 acquired loans, net                 | \$ 866,504        | \$ 919,402           | \$ 1,113,763      |

Table of Contents
**Note 6 Loans and Allowance for Loan Losses (Continued)**

Contractual loan payments receivable, estimates of amounts not expected to be collected, other fair value adjustments and the resulting carrying values of acquired credit impaired loans as of March 31, 2015, December 31, 2014 and March 31, 2014 are as follows:

| (Dollars in thousands)              | March 31,<br>2015 | December 31,<br>2014 | March 31,<br>2014 |
|-------------------------------------|-------------------|----------------------|-------------------|
| Contractual principal and interest  | \$ 1,173,550      | \$ 1,337,703         | \$ 1,568,978      |
| Non-accretable difference           | (85,300)          | (104,110)            | (212,934)         |
| Cash flows expected to be collected | 1,088,250         | 1,233,593            | 1,356,044         |
| Accretable yield                    | (217,029)         | (306,826)            | (231,235)         |
| Carrying value                      | \$ 871,221        | \$ 926,767           | \$ 1,124,809      |
| Allowance for acquired loan losses  | \$ (4,717)        | \$ (7,365)           | \$ (11,046)       |

Income on acquired credit impaired loans that are not impaired at the acquisition date is recognized in the same manner as loans impaired at the acquisition date. A portion of the fair value discount on acquired non-impaired loans has been ascribed as an accretable difference that is accreted into interest income over the estimated remaining life of the loans. The remaining nonaccretable difference represents cash flows not expected to be collected.

The following are changes in the carrying value of acquired credit impaired loans:

| (Dollars in thousands)                                                       | Three Months Ended March 31,<br>2015 | Three Months Ended March 31,<br>2014 |
|------------------------------------------------------------------------------|--------------------------------------|--------------------------------------|
| Balance at beginning of period                                               | \$ 919,402                           | \$ 1,216,080                         |
| Net reductions for payments, foreclosures, and accretion                     | (55,546)                             | (102,889)                            |
| Change in the allowance for loan losses on acquired loans                    | 2,648                                | 572                                  |
| Balance at end of period, net of allowance for loan losses on acquired loans | \$ 866,504                           | \$ 1,113,763                         |

The table below reflects refined accretable yield balance for acquired credit impaired loans:

| (Dollars in thousands)                                                        | Three Months Ended March 31,<br>2015 | Three Months Ended March 31,<br>2014 |
|-------------------------------------------------------------------------------|--------------------------------------|--------------------------------------|
| Balance at beginning of period                                                | \$ 306,826                           | \$ 250,340                           |
| Accretion                                                                     | (25,692)                             | (28,767)                             |
| Reclass of nonaccretable difference due to improvement in expected cash flows | 5,948                                | 10,750                               |
| Other changes, net                                                            | (70,053)                             | (1,088)                              |
| Balance at end of period                                                      | \$ 217,029                           | \$ 231,235                           |

## Edgar Filing: SOUTH STATE Corp - Form 10-Q

During the recast in the first quarter of 2015, the accretable yield balance declined significantly by \$64.1 million. This decline was primarily the result of an increase in the assumed prepayment speed of certain acquired loan pools from the FFHI acquisition. The actual cash flows were faster than what had been previously expected (assumed) and required an adjustment in the assumed prepayment speed used to forecast expected cash flows. The result was a decrease in the accretable yield balance, however, there was no impairment since this only changed the timing of the receipt of future cash on these pools of loans (expect to receive cash sooner).

Table of Contents

**Note 6 Loans and Allowance for Loan Losses (Continued)**

Our loan loss policy adheres to generally accepted accounting principles in the United States as well as interagency guidance. The allowance for loan losses is based upon estimates made by management. We maintain an allowance for loan losses at a level that we believe is appropriate to cover estimated credit losses on individually evaluated loans that are determined to be impaired as well as estimated credit losses inherent in the remainder of our loan portfolio. Arriving at the allowance involves a high degree of management judgment and results in a range of estimated losses. We regularly evaluate the adequacy of the allowance through our internal risk rating system, outside credit review, and regulatory agency examinations to assess the quality of the loan portfolio and identify problem loans. The evaluation process also includes our analysis of current economic conditions, composition of the loan portfolio, past due and nonaccrual loans, concentrations of credit, lending policies and procedures, and historical loan loss experience. While management uses available information to recognize losses on loans, future additions to the allowance may be necessary based on, among other factors, changes in economic conditions in our markets. In addition, regulatory agencies, as an integral part of their examination process, periodically review our allowances for losses on loans. These agencies may require management to recognize additions to the allowances based on their judgments about information available to them at the time of their examination. Because of these and other factors, it is possible that the allowances for losses on loans may change. The provision for loan losses is charged to expense in an amount necessary to maintain the allowance at an appropriate level.

The allowance for loan losses on non-acquired loans consists of general and specific reserves. The general reserves are determined by applying loss percentages to the portfolio that are based on historical loss experience for each class of loans and management's evaluation and risk grading of the loan portfolio. Additionally, the general economic and business conditions affecting key lending areas, credit quality trends, collateral values, loan volumes and concentrations, seasoning of the loan portfolio, the findings of internal and external credit reviews and results from external bank regulatory examinations are included in this evaluation. Currently, these adjustments are applied to the non-acquired loan portfolio when estimating the level of reserve required. The specific reserves are determined on a loan-by-loan basis based on management's evaluation of our exposure for each credit, given the current payment status of the loan and the value of any underlying collateral. These are loans classified by management as doubtful or substandard. For such loans that are also classified as impaired, an allowance is established when the discounted cash flows (or collateral value or observable market price) of the impaired loan is lower than the carrying value of that loan. Generally, the need for specific reserve is evaluated on impaired loans, and once a specific reserve is established for a loan, a charge off of that amount occurs in the quarter subsequent to the establishment of the specific reserve. Loans that are determined to be impaired are provided a specific reserve, if necessary, and are excluded from the calculation of the general reserves.

With the FFHI acquisition, the Company segregated the loan portfolio into performing loans ( non-credit impaired ) and acquired credit impaired loans. The performing loans and revolving type loans are accounted for under FASB ASC 310-20, with each loan being accounted for individually. The allowance for loan losses on these loans will be measured and recorded consistent with non-acquired loans. The acquired credit impaired loans will follow the description in the next paragraph.

In determining the acquisition date fair value of acquired credit impaired loans, and in subsequent accounting, the Company generally aggregates purchased loans into pools of loans with common risk characteristics. Expected cash flows at the acquisition date in excess of the fair value of loans are recorded as interest income over the life of the loans using a level yield method if the timing and amount of the future cash flows of the pool is reasonably estimable. Subsequent to the acquisition date, increases in cash flows over those expected at the acquisition date are reclassified from the non-accretable difference to accretable difference and recognized as interest income prospectively. Decreases in expected cash flows after the acquisition date are recognized by recording an allowance for loan losses. Management analyzes the acquired loan pools using various assessments of risk to determine an expected loss. The expected loss is derived based upon a loss given default based upon the collateral type and/or detailed review by loan officers and the probability of default that is determined based upon historical data at the loan level. Trends are reviewed in terms of accrual status, past due status, and weighted-average grade of the loans within each of the accounting pools. In addition, the relationship between the change in the unpaid principal balance and change in the mark is assessed to correlate the directional consistency of the expected loss for each pool. Offsetting the impact of the provision established for acquired loans covered under FDIC loss share agreements, the receivable from the FDIC is adjusted to reflect the indemnified portion of the post-acquisition exposure with a corresponding credit to the provision for loan losses.



Table of Contents**Note 6 Loans and Allowance for Loan Losses (Continued)**

An aggregated analysis of the changes in allowance for loan losses is as follows:

| (Dollars in thousands)                                                    | Non-acquired<br>Loans | Acquired<br>Non-credit<br>Impaired Loans | Acquired<br>Credit Impaired<br>Loans | Total     |
|---------------------------------------------------------------------------|-----------------------|------------------------------------------|--------------------------------------|-----------|
| <b>Three months ended March 31, 2015:</b>                                 |                       |                                          |                                      |           |
| Balance at beginning of period                                            | \$ 34,539             | \$                                       | \$ 7,365                             | \$ 41,904 |
| Loans charged-off                                                         | (996)                 | (1,811)                                  |                                      | (2,807)   |
| Recoveries of loans previously charged off                                | 1,050                 | 25                                       |                                      | 1,075     |
| Net charge-offs                                                           | 54                    | (1,786)                                  |                                      | (1,732)   |
| Provision (benefit) for loan losses                                       | (1,055)               | 1,786                                    | 66                                   | 797       |
| Benefit attributable to FDIC loss share agreements                        |                       |                                          | 21                                   | 21        |
| Total provision for loan losses charged to operations                     | (1,055)               | 1,786                                    | 87                                   | 818       |
| Provision for loan losses recorded through the FDIC loss share receivable |                       |                                          | (21)                                 | (21)      |
| Reduction due to loan removals                                            |                       |                                          | (2,714)                              | (2,714)   |
| Balance at end of period                                                  | \$ 33,538             | \$                                       | \$ 4,717                             | \$ 38,255 |
| <b>Three months ended March 31, 2014:</b>                                 |                       |                                          |                                      |           |
| Balance at beginning of period                                            | \$ 34,331             | \$                                       | \$ 11,618                            | \$ 45,949 |
| Loans charged-off                                                         | (1,370)               |                                          |                                      | (1,370)   |
| Recoveries of loans previously charged off                                | 1,038                 |                                          |                                      | 1,038     |
| Net charge-offs                                                           | (332)                 |                                          |                                      | (332)     |
| Provision for loan losses                                                 | 670                   |                                          | 304                                  | 974       |
| Benefit attributable to FDIC loss share agreements                        |                       |                                          | (125)                                | (125)     |
| Total provision for loan losses charged to operations                     | 670                   |                                          | 179                                  | 849       |
| Provision for loan losses recorded through the FDIC loss share receivable |                       |                                          | 125                                  | 125       |
| Reduction due to loan removals                                            |                       |                                          | (876)                                | (876)     |
| Balance at end of period                                                  | \$ 34,669             | \$                                       | \$ 11,046                            | \$ 45,715 |

Table of Contents**Note 6 Loans and Allowance for Loan Losses (Continued)**

The following tables present a disaggregated analysis of activity in the allowance for loan losses and loan balances for non-acquired loans:

| (Dollars in thousands)                             | Construction<br>& Land<br>Development | Commercial<br>Non-owner<br>Occupied | Commercial<br>Owner<br>Occupied | Consumer<br>Owner<br>Occupied | Home<br>Equity | Other<br>Commercial<br>& Industrial | Income<br>Producing<br>Property | Consumer   | Other<br>Loans | Total        |
|----------------------------------------------------|---------------------------------------|-------------------------------------|---------------------------------|-------------------------------|----------------|-------------------------------------|---------------------------------|------------|----------------|--------------|
| <b>Three months ended<br/>March 31, 2015</b>       |                                       |                                     |                                 |                               |                |                                     |                                 |            |                |              |
| <b>Allowance for loan losses:</b>                  |                                       |                                     |                                 |                               |                |                                     |                                 |            |                |              |
| Balance,<br>December 31, 2014                      | \$ 5,666                              | \$ 3,154                            | \$ 8,415                        | \$ 6,866                      | \$ 2,829       | \$ 3,561                            | \$ 2,232                        | \$ 1,367   | \$ 449         | \$ 34,539    |
| Charge-offs                                        | (45)                                  | (11)                                | (6)                             |                               | (86)           | (139)                               | (2)                             | (707)      |                | (996)        |
| Recoveries                                         | 40                                    | 8                                   | 7                               | 25                            | 43             | 599                                 | 11                              | 317        |                | 1,050        |
| Provision (benefit)                                | (262)                                 | (20)                                | (545)                           | 150                           | (1)            | (561)                               | (261)                           | 445        |                | (1,055)      |
| Balance, March 31, 2015                            | \$ 5,399                              | \$ 3,131                            | \$ 7,871                        | \$ 7,041                      | \$ 2,785       | \$ 3,460                            | \$ 1,980                        | \$ 1,422   | \$ 449         | \$ 33,538    |
| <b>Loans individually evaluated for impairment</b> |                                       |                                     |                                 |                               |                |                                     |                                 |            |                |              |
|                                                    | \$ 697                                | \$ 35                               | \$ 70                           | \$ 123                        | \$ 1           | \$ 16                               | \$ 485                          | \$ 2       | \$             | \$ 1,429     |
| <b>Loans collectively evaluated for impairment</b> |                                       |                                     |                                 |                               |                |                                     |                                 |            |                |              |
|                                                    | \$ 4,702                              | \$ 3,096                            | \$ 7,801                        | \$ 6,918                      | \$ 2,784       | \$ 3,444                            | \$ 1,495                        | \$ 1,420   | \$ 449         | \$ 32,109    |
| <b>Loans:</b>                                      |                                       |                                     |                                 |                               |                |                                     |                                 |            |                |              |
| <b>Loans individually evaluated for impairment</b> |                                       |                                     |                                 |                               |                |                                     |                                 |            |                |              |
|                                                    | \$ 5,407                              | \$ 3,765                            | \$ 8,297                        | \$ 7,093                      | \$ 250         | \$ 906                              | \$ 4,667                        | \$ 63      | \$             | \$ 30,448    |
| <b>Loans collectively evaluated for impairment</b> |                                       |                                     |                                 |                               |                |                                     |                                 |            |                |              |
|                                                    | 352,701                               | 360,962                             | 916,895                         | 847,190                       | 290,238        | 407,084                             | 149,693                         | 195,388    | 35,806         | 3,555,957    |
| Total non-acquired loans                           | \$ 358,108                            | \$ 364,727                          | \$ 925,192                      | \$ 854,283                    | \$ 290,488     | \$ 407,990                          | \$ 154,360                      | \$ 195,451 | \$ 35,806      | \$ 3,586,405 |
| <b>Three months ended<br/>March 31, 2014</b>       |                                       |                                     |                                 |                               |                |                                     |                                 |            |                |              |
| <b>Allowance for loan losses:</b>                  |                                       |                                     |                                 |                               |                |                                     |                                 |            |                |              |
| Balance,<br>December 31, 2013                      | \$ 6,789                              | \$ 3,677                            | \$ 7,767                        | \$ 6,069                      | \$ 2,782       | \$ 3,592                            | \$ 2,509                        | \$ 937     | \$ 209         | \$ 34,331    |
| Charge-offs                                        | (92)                                  | (144)                               | (216)                           | (78)                          | (143)          | (60)                                | (86)                            | (551)      |                | (1,370)      |
| Recoveries                                         | 145                                   | 331                                 | 6                               | 203                           | 13             | 90                                  | 6                               | 244        |                | 1,038        |
| Provision (benefit)                                | (520)                                 | (421)                               | 760                             | (72)                          | 269            | (181)                               | 419                             | 475        | (59)           | 670          |
| Balance, March 31, 2014                            | \$ 6,322                              | \$ 3,443                            | \$ 8,317                        | \$ 6,122                      | \$ 2,921       | \$ 3,441                            | \$ 2,848                        | \$ 1,105   | \$ 150         | \$ 34,669    |
| <b>Loans individually evaluated for impairment</b> |                                       |                                     |                                 |                               |                |                                     |                                 |            |                |              |
|                                                    | \$ 563                                | \$ 39                               | \$ 106                          | \$ 72                         | \$ 1           | \$ 21                               | \$ 617                          | \$ 2       | \$             | \$ 1,421     |

Edgar Filing: SOUTH STATE Corp - Form 10-Q

|                                                   |    |       |    |       |    |       |    |       |    |       |    |       |    |       |    |       |    |     |    |        |
|---------------------------------------------------|----|-------|----|-------|----|-------|----|-------|----|-------|----|-------|----|-------|----|-------|----|-----|----|--------|
| Loans collectively<br>evaluated for<br>impairment | \$ | 5,759 | \$ | 3,404 | \$ | 8,211 | \$ | 6,050 | \$ | 2,920 | \$ | 3,420 | \$ | 2,231 | \$ | 1,103 | \$ | 150 | \$ | 33,248 |
|---------------------------------------------------|----|-------|----|-------|----|-------|----|-------|----|-------|----|-------|----|-------|----|-------|----|-----|----|--------|

**Loans:**

|                                                   |    |       |    |       |    |        |    |       |    |    |    |       |    |       |    |    |    |  |    |        |
|---------------------------------------------------|----|-------|----|-------|----|--------|----|-------|----|----|----|-------|----|-------|----|----|----|--|----|--------|
| Loans individually<br>evaluated for<br>impairment | \$ | 6,150 | \$ | 4,153 | \$ | 12,798 | \$ | 2,550 | \$ | 48 | \$ | 1,536 | \$ | 6,498 | \$ | 89 | \$ |  | \$ | 33,822 |
|---------------------------------------------------|----|-------|----|-------|----|--------|----|-------|----|----|----|-------|----|-------|----|----|----|--|----|--------|

|                                                   |  |         |  |         |  |         |  |         |  |         |  |         |  |         |  |         |  |        |  |           |
|---------------------------------------------------|--|---------|--|---------|--|---------|--|---------|--|---------|--|---------|--|---------|--|---------|--|--------|--|-----------|
| Loans collectively<br>evaluated for<br>impairment |  | 313,291 |  | 280,992 |  | 832,930 |  | 593,102 |  | 263,009 |  | 332,038 |  | 151,688 |  | 147,621 |  | 31,465 |  | 2,946,136 |
|---------------------------------------------------|--|---------|--|---------|--|---------|--|---------|--|---------|--|---------|--|---------|--|---------|--|--------|--|-----------|

|                             |    |         |    |         |    |         |    |         |    |         |    |         |    |         |    |         |    |        |    |           |
|-----------------------------|----|---------|----|---------|----|---------|----|---------|----|---------|----|---------|----|---------|----|---------|----|--------|----|-----------|
| Total non-acquired<br>loans | \$ | 319,441 | \$ | 285,145 | \$ | 845,728 | \$ | 595,652 | \$ | 263,057 | \$ | 333,574 | \$ | 158,186 | \$ | 147,710 | \$ | 31,465 | \$ | 2,979,958 |
|-----------------------------|----|---------|----|---------|----|---------|----|---------|----|---------|----|---------|----|---------|----|---------|----|--------|----|-----------|

Table of Contents**Note 6 Loans and Allowance for Loan Losses (Continued)**

The following tables present a disaggregated analysis of activity in the allowance for loan losses and loan balances for acquired non-credit impaired loans:

|                                                            | Construction<br>& Land Development | Commercial<br>Non-owner<br>Occupied | Commercial<br>Owner<br>Occupied | Consumer<br>Owner<br>Occupied | Home<br>Equity    | Commercial<br>& Industrial | Other Income<br>Producing<br>Property | Consumer          | Total               |
|------------------------------------------------------------|------------------------------------|-------------------------------------|---------------------------------|-------------------------------|-------------------|----------------------------|---------------------------------------|-------------------|---------------------|
| <b>(Dollars in thousands)</b>                              |                                    |                                     |                                 |                               |                   |                            |                                       |                   |                     |
| <b>Three months<br/>ended March 31,<br/>2015</b>           |                                    |                                     |                                 |                               |                   |                            |                                       |                   |                     |
| <b>Allowance for loan<br/>losses:</b>                      |                                    |                                     |                                 |                               |                   |                            |                                       |                   |                     |
| Balance,<br>December 31, 2014                              | \$                                 | \$                                  | \$                              | \$                            | \$                | \$                         | \$                                    | \$                | \$                  |
| Charge-offs                                                |                                    |                                     |                                 | (328)                         | (1,050)           | (103)                      | (4)                                   | (326)             | (1,811)             |
| Recoveries                                                 | 1                                  |                                     |                                 | 5                             | 3                 | 5                          | 1                                     | 10                | 25                  |
| Provision (benefit)                                        | (1)                                |                                     |                                 | 323                           | 1,047             | 98                         | 3                                     | 316               | 1,786               |
| Balance, March 31,<br>2015                                 | \$                                 | \$                                  | \$                              | \$                            | \$                | \$                         | \$                                    | \$                | \$                  |
| <b>Loans individually<br/>evaluated for<br/>impairment</b> | \$                                 | \$                                  | \$                              | \$                            | \$                | \$                         | \$                                    | \$                | \$                  |
| <b>Loans collectively<br/>evaluated for<br/>impairment</b> | \$                                 | \$                                  | \$                              | \$                            | \$                | \$                         | \$                                    | \$                | \$                  |
| <b>Loans:</b>                                              |                                    |                                     |                                 |                               |                   |                            |                                       |                   |                     |
| Loans individually<br>evaluated for<br>impairment          | \$                                 | \$                                  | \$                              | \$                            | \$                | \$                         | \$                                    | \$                | \$                  |
| Loans collectively<br>evaluated for<br>impairment          | 19,598                             | 44,772                              | 56,167                          | 612,917                       | 221,535           | 35,592                     | 61,415                                | 195,353           | 1,247,349           |
| <b>Total non-acquired<br/>loans</b>                        | <b>\$ 19,598</b>                   | <b>\$ 44,772</b>                    | <b>\$ 56,167</b>                | <b>\$ 612,917</b>             | <b>\$ 221,535</b> | <b>\$ 35,592</b>           | <b>\$ 61,415</b>                      | <b>\$ 195,353</b> | <b>\$ 1,247,349</b> |

As of March 31, 2014, the Company had not recorded an allowance for loan losses for acquired non-credit impaired loans.

[Table of Contents](#)
**Note 6 Loans and Allowance for Loan Losses (Continued)**

The following tables present a disaggregated analysis of activity in the allowance for loan losses and loan balances for acquired credit impaired loans:

| (Dollars in thousands)                                                                    | Commercial<br>Loans Greater<br>Than or Equal<br>to \$1 Million-CB | Commercial<br>Real Estate-<br>Development<br>Real Estate | Commercial<br>Real Estate-<br>Construction and<br>Residential | Commercial<br>Consumer and Industrial | Commercial<br>Single Pay | Total      |
|-------------------------------------------------------------------------------------------|-------------------------------------------------------------------|----------------------------------------------------------|---------------------------------------------------------------|---------------------------------------|--------------------------|------------|
| <b>Three months ended</b>                                                                 |                                                                   |                                                          |                                                               |                                       |                          |            |
| <b>March 31, 2015</b>                                                                     |                                                                   |                                                          |                                                               |                                       |                          |            |
| <b>Allowance for loan losses:</b>                                                         |                                                                   |                                                          |                                                               |                                       |                          |            |
| Balance, December 31, 2014                                                                | \$ 135                                                            | \$ 1,444                                                 | \$ 336                                                        | \$ 4,387                              | \$ 275                   | \$ 7,365   |
| Provision for loan losses<br>before benefit attributable to<br>FDIC loss share agreements |                                                                   | 3                                                        | 9                                                             | 19                                    | 158                      | 66         |
| Benefit attributable to FDIC<br>loss share agreements                                     |                                                                   |                                                          |                                                               | (107)                                 | 127                      | 21         |
| Total provision for loan<br>losses charged to operations                                  |                                                                   | 3                                                        | 9                                                             | 19                                    | 51                       | 87         |
| Provision for loan losses<br>recorded through the FDIC<br>loss share receivable           |                                                                   |                                                          |                                                               | 107                                   | (127)                    | (21)       |
| Reduction due to loan<br>removals                                                         | (199)                                                             | (898)                                                    | 55                                                            | (1,086)                               | (189)                    | (2,714)    |
| Balance, March 31, 2015                                                                   | \$ (64)                                                           | \$ 549                                                   | \$ 400                                                        | \$ 3,320                              | \$ 244                   | \$ 4,717   |
| Loans individually evaluated<br>for impairment                                            | \$                                                                | \$                                                       | \$                                                            | \$                                    | \$                       | \$         |
| Loans collectively evaluated<br>for impairment                                            | \$ (64)                                                           | \$ 549                                                   | \$ 400                                                        | \$ 3,320                              | \$ 244                   | \$ 4,717   |
| <b>Loans:*</b>                                                                            |                                                                   |                                                          |                                                               |                                       |                          |            |
| Loans individually evaluated<br>for impairment                                            | \$                                                                | \$                                                       | \$                                                            | \$                                    | \$                       | \$         |
| Loans collectively evaluated<br>for impairment                                            | 15,477                                                            | 302,592                                                  | 61,456                                                        | 368,633                               | 80,656                   | 871,221    |
| Total acquired loans                                                                      | \$ 15,477                                                         | \$ 302,592                                               | \$ 61,456                                                     | \$ 368,633                            | \$ 80,656                | \$ 871,221 |
| <b>Three months ended</b>                                                                 |                                                                   |                                                          |                                                               |                                       |                          |            |
| <b>March 31, 2014</b>                                                                     |                                                                   |                                                          |                                                               |                                       |                          |            |
| <b>Allowance for loan losses:</b>                                                         |                                                                   |                                                          |                                                               |                                       |                          |            |
| Balance, December 31, 2013                                                                | \$ 303                                                            | \$ 1,816                                                 | \$ 2,244                                                      | \$ 5,132                              | \$ 538                   | \$ 11,618  |
| Provision for loan losses<br>before benefit attributable to<br>FDIC loss share agreements | (3)                                                               | 126                                                      | 289                                                           | 141                                   | (112)                    | 304        |
| Benefit attributable to FDIC<br>loss share agreements                                     | 5                                                                 | (116)                                                    | (112)                                                         | (138)                                 | 140                      | (125)      |
| Total provision for loan<br>losses charged to operations                                  | 2                                                                 | 10                                                       | 177                                                           | 3                                     | (11)                     | 179        |
| Provision for loan losses<br>recorded through the FDIC<br>loss share receivable           | (5)                                                               | 116                                                      | 112                                                           | 138                                   | (140)                    | 125        |

Edgar Filing: SOUTH STATE Corp - Form 10-Q

|                                             |    |        |            |           |            |           |           |        |              |
|---------------------------------------------|----|--------|------------|-----------|------------|-----------|-----------|--------|--------------|
| Reduction due to loan removals              |    | 11     | (4)        | (561)     | (83)       | (16)      | (220)     | (3)    | (876)        |
| Balance, March 31, 2014                     | \$ | 311    | \$ 1,938   | \$ 1,972  | \$ 5,190   | \$ 410    | \$ 1,119  | \$ 106 | \$ 11,046    |
| Loans individually evaluated for impairment | \$ | \$     | \$         | \$        | \$         | \$        | \$        | \$     | \$           |
| Loans collectively evaluated for impairment | \$ | 311    | \$ 1,938   | \$ 1,972  | \$ 5,190   | \$ 410    | \$ 1,119  | \$ 106 | \$ 11,046    |
| <b>Loans:*</b>                              |    |        |            |           |            |           |           |        |              |
| Loans individually evaluated for impairment | \$ | \$     | \$         | \$        | \$         | \$        | \$        | \$     | \$           |
| Loans collectively evaluated for impairment |    | 21,479 | 402,505    | 98,060    | 444,115    | 99,545    | 58,973    | 132    | 1,124,809    |
| Total acquired loans                        | \$ | 21,479 | \$ 402,505 | \$ 98,060 | \$ 444,115 | \$ 99,545 | \$ 58,973 | \$ 132 | \$ 1,124,809 |

---

\* The carrying value of acquired credit impaired loans includes a non-accretable difference which is primarily associated with the assessment of credit quality of acquired loans.

# Table of Contents

## Note 6 Loans and Allowance for Loan Losses (Continued)

As part of the ongoing monitoring of the credit quality of the Company's loan portfolio, management tracks certain credit quality indicators, including trends related to (i) the level of classified loans, (ii) net charge-offs, (iii) non-performing loans (see details below), and (iv) the general economic conditions of the markets that we serve.

The Company utilizes a risk grading matrix to assign a risk grade to each of its loans. A description of the general characteristics of the risk grades is as follows:

- **Pass** These loans range from minimal credit risk to average, however, still acceptable credit risk.
- **Special mention** A special mention loan has potential weaknesses that deserve management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan or the institution's credit position at some future date.
- **Substandard** A substandard loan is inadequately protected by the current sound worth and paying capacity of the obligor or of the collateral pledged, if any. Loans so classified must have a well-defined weakness, or weaknesses, that may jeopardize the liquidation of the debt. A substandard loan is characterized by the distinct possibility that the Bank will sustain some loss if the deficiencies are not corrected.
- **Doubtful** A doubtful loan has all of the weaknesses inherent in one classified as substandard with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of the currently existing facts, conditions and values, highly questionable and improbable.

The following table presents the credit risk profile by risk grade of commercial loans for non-acquired loans:

|                        | Construction & Development |                      |                   | Commercial Non-owner Occupied |                      |                   | Commercial Owner Occupied |                      |                   |
|------------------------|----------------------------|----------------------|-------------------|-------------------------------|----------------------|-------------------|---------------------------|----------------------|-------------------|
|                        | March 31,<br>2015          | December 31,<br>2014 | March 31,<br>2014 | March 31,<br>2015             | December 31,<br>2014 | March 31,<br>2014 | March 31,<br>2015         | December 31,<br>2014 | March 31,<br>2014 |
| (Dollars in thousands) |                            |                      |                   |                               |                      |                   |                           |                      |                   |
| Pass                   | \$ 330,871                 | \$ 337,641           | \$ 284,775        | \$ 344,435                    | \$ 307,450           | \$ 253,863        | \$ 880,425                | \$ 858,220           | \$ 799,450        |
| Special mention        | 16,621                     | 15,466               | 19,692            | 15,522                        | 20,596               | 24,523            | 30,547                    | 34,737               | 25,850            |
| Substandard            | 10,616                     | 11,114               | 14,974            | 4,770                         | 5,544                | 6,759             | 14,220                    | 14,956               | 20,428            |
| Doubtful               |                            |                      |                   |                               |                      |                   |                           |                      |                   |
|                        | \$ 358,108                 | \$ 364,221           | \$ 319,441        | \$ 364,727                    | \$ 333,590           | \$ 285,145        | \$ 925,192                | \$ 907,913           | \$ 845,728        |

| Commercial & Industrial |                      |                   | Other Income Producing Property |                      |                   | Commercial Total  |                      |                   |
|-------------------------|----------------------|-------------------|---------------------------------|----------------------|-------------------|-------------------|----------------------|-------------------|
| March 31,<br>2015       | December 31,<br>2014 | March 31,<br>2014 | March 31,<br>2015               | December 31,<br>2014 | March 31,<br>2014 | March 31,<br>2015 | December 31,<br>2014 | March 31,<br>2014 |

# Edgar Filing: SOUTH STATE Corp - Form 10-Q

|                 |            |            |            |            |            |            |              |              |              |
|-----------------|------------|------------|------------|------------|------------|------------|--------------|--------------|--------------|
| Pass            | \$ 401,032 | \$ 397,555 | \$ 321,466 | \$ 139,821 | \$ 135,400 | \$ 139,373 | \$ 2,096,584 | \$ 2,036,266 | \$ 1,798,927 |
| Special mention | 5,405      | 6,718      | 10,098     | 9,977      | 10,333     | 8,530      | 78,072       | 87,850       | 88,693       |
| Substandard     | 1,553      | 1,650      | 2,010      | 4,562      | 5,195      | 10,283     | 35,721       | 38,459       | 54,454       |
| Doubtful        |            |            |            |            |            |            |              |              |              |
|                 | \$ 407,990 | \$ 405,923 | \$ 333,574 | \$ 154,360 | \$ 150,928 | \$ 158,186 | \$ 2,210,377 | \$ 2,162,575 | \$ 1,942,074 |

# Edgar Filing: SOUTH STATE Corp - Form 10-Q

## Table of Contents

### Note 6 Loans and Allowance for Loan Losses (Continued)

The following table presents the credit risk profile by risk grade of consumer loans for non-acquired loans:

| (Dollars in thousands) | Consumer Owner Occupied |                   |                | Home Equity    |                   |                | Consumer       |                   |                |
|------------------------|-------------------------|-------------------|----------------|----------------|-------------------|----------------|----------------|-------------------|----------------|
|                        | March 31, 2015          | December 31, 2014 | March 31, 2014 | March 31, 2015 | December 31, 2014 | March 31, 2014 | March 31, 2015 | December 31, 2014 | March 31, 2014 |
| Pass                   | \$ 814,701              | \$ 746,847        | \$ 549,663     | \$ 274,727     | \$ 269,844        | \$ 248,561     | \$ 194,151     | \$ 188,049        | \$ 146,538     |
| Special mention        | 21,431                  | 22,129            | 26,618         | 9,336          | 8,047             | 9,093          | 842            | 764               | 826            |
| Substandard            | 18,151                  | 17,802            | 19,371         | 6,403          | 6,021             | 5,380          | 458            | 504               | 346            |
| Doubtful               |                         |                   |                | 22             | 22                | 23             |                |                   |                |
|                        | \$ 854,283              | \$ 786,778        | \$ 595,652     | \$ 290,488     | \$ 283,934        | \$ 263,057     | \$ 195,451     | \$ 189,317        | \$ 147,710     |

|                 | Other          |                   |                | Consumer Total |                   |                |
|-----------------|----------------|-------------------|----------------|----------------|-------------------|----------------|
|                 | March 31, 2015 | December 31, 2014 | March 31, 2014 | March 31, 2015 | December 31, 2014 | March 31, 2014 |
| Pass            | \$ 35,806      | \$ 45,222         | \$ 31,465      | \$ 1,319,385   | \$ 1,249,962      | \$ 976,227     |
| Special mention |                |                   |                | 31,609         | 30,940            | 36,537         |
| Substandard     |                |                   |                | 25,012         | 24,327            | 25,097         |
| Doubtful        |                |                   |                | 22             | 22                | 23             |
|                 | \$ 35,806      | \$ 45,222         | \$ 31,465      | \$ 1,376,028   | \$ 1,305,251      | \$ 1,037,884   |

The following table presents the credit risk profile by risk grade of total non-acquired loans:

| (Dollars in thousands) | Total Non-acquired Loans |                   |                |
|------------------------|--------------------------|-------------------|----------------|
|                        | March 31, 2015           | December 31, 2014 | March 31, 2014 |
| Pass                   | \$ 3,415,969             | \$ 3,286,228      | \$ 2,775,154   |
| Special mention        | 109,681                  | 118,790           | 125,230        |
| Substandard            | 60,733                   | 62,786            | 79,551         |
| Doubtful               | 22                       | 22                | 23             |
|                        | \$ 3,586,405             | \$ 3,467,826      | \$ 2,979,958   |

The following table presents the credit risk profile by risk grade of commercial loans for acquired non-credit impaired loans:

| (Dollars in thousands) | Construction & Development |                   |                | Commercial Non-owner Occupied |                   |                | Commercial Owner Occupied |                   |                |
|------------------------|----------------------------|-------------------|----------------|-------------------------------|-------------------|----------------|---------------------------|-------------------|----------------|
|                        | March 31, 2015             | December 31, 2014 | March 31, 2014 | March 31, 2015                | December 31, 2014 | March 31, 2014 | March 31, 2015            | December 31, 2014 | March 31, 2014 |
| Pass                   | \$ 18,703                  | \$ 22,456         | \$ 38,150      | \$ 37,903                     | \$ 42,572         | \$ 50,127      | \$ 55,093                 | \$ 61,040         | \$ 69,637      |
| Special mention        | 122                        | 816               | 106            | 184                           | 6,039             | 1,510          | 329                       | 265               | 315            |
| Substandard            | 773                        | 827               | 925            | 6,685                         | 865               | 988            | 745                       | 760               | 1,655          |
| Doubtful               |                            |                   |                |                               |                   |                |                           |                   |                |
|                        | \$ 19,598                  | \$ 24,099         | \$ 39,181      | \$ 44,772                     | \$ 49,476         | \$ 52,625      | \$ 56,167                 | \$ 62,065         | \$ 71,607      |

Commercial & Industrial

Other Income Producing Property

Commercial Total

# Edgar Filing: SOUTH STATE Corp - Form 10-Q

|                 | March 31,<br>2015 | December 31,<br>2014 | March 31,<br>2014 | March 31,<br>2015 | December 31,<br>2014 | March 31,<br>2014 | March 31,<br>2015 | December 31,<br>2014 | March 31,<br>2014 |
|-----------------|-------------------|----------------------|-------------------|-------------------|----------------------|-------------------|-------------------|----------------------|-------------------|
| Pass            | \$ 34,482         | \$ 39,780            | \$ 42,192         | \$ 59,990         | \$ 63,090            | \$ 69,465         | \$ 206,171        | \$ 228,938           | \$ 269,571        |
| Special mention | 406               | 448                  | 942               | 445               | 896                  | 2,333             | 1,486             | 8,464                | 5,206             |
| Substandard     | 704               | 902                  | 1,049             | 980               | 1,153                | 1,955             | 9,887             | 4,507                | 6,572             |
| Doubtful        |                   |                      |                   |                   |                      |                   |                   |                      |                   |
|                 | \$ 35,592         | \$ 41,130            | \$ 44,183         | \$ 61,415         | \$ 65,139            | \$ 73,753         | \$ 217,544        | \$ 241,909           | \$ 281,349        |

# Table of Contents

## Note 6 Loans and Allowance for Loan Losses (Continued)

The following table presents the credit risk profile by risk grade of consumer loans for acquired non-credit impaired loans:

| (Dollars in thousands) | Consumer Owner Occupied |                   |                |                | Home Equity       |                | Consumer       |                   |                |
|------------------------|-------------------------|-------------------|----------------|----------------|-------------------|----------------|----------------|-------------------|----------------|
|                        | March 31, 2015          | December 31, 2014 | March 31, 2014 | March 31, 2015 | December 31, 2014 | March 31, 2014 | March 31, 2015 | December 31, 2014 | March 31, 2014 |
| Pass                   | \$ 605,813              | \$ 639,555        | \$ 729,165     | \$ 207,419     | \$ 222,653        | \$ 241,895     | \$ 192,309     | \$ 201,636        | \$ 239,336     |
| Special mention        | 1,544                   | 1,241             | 334            | 6,353          | 4,491             | 4,627          | 596            | 619               | 465            |
| Substandard            | 5,560                   | 5,579             | 3,065          | 7,763          | 7,805             | 10,441         | 2,448          | 2,511             | 1,524          |
| Doubtful               |                         |                   |                |                |                   |                |                |                   |                |
|                        | \$ 612,917              | \$ 646,375        | \$ 732,564     | \$ 221,535     | \$ 234,949        | \$ 256,963     | \$ 195,353     | \$ 204,766        | \$ 241,325     |

| (Dollars in thousands) | Consumer Total |                   |                |
|------------------------|----------------|-------------------|----------------|
|                        | March 31, 2015 | December 31, 2014 | March 31, 2014 |
| Pass                   | \$ 1,005,541   | \$ 1,063,844      | \$ 1,210,396   |
| Special mention        | 8,493          | 6,351             | 5,426          |
| Substandard            | 15,771         | 15,895            | 15,030         |
| Doubtful               |                |                   |                |
|                        | \$ 1,029,805   | \$ 1,086,090      | \$ 1,230,852   |

The following table presents the credit risk profile by risk grade of total acquired non-credit loans:

| (Dollars in thousands) | Total Acquired Non-credit Impaired Loans |                   |                |
|------------------------|------------------------------------------|-------------------|----------------|
|                        | March 31, 2015                           | December 31, 2014 | March 31, 2014 |
| Pass                   | \$ 1,211,712                             | \$ 1,292,782      | \$ 1,479,967   |
| Special mention        | 9,979                                    | 14,815            | 10,632         |
| Substandard            | 25,658                                   | 20,402            | 21,602         |
| Doubtful               |                                          |                   |                |
|                        | \$ 1,247,349                             | \$ 1,327,999      | \$ 1,512,201   |

The following table presents the credit risk profile by risk grade of acquired credit impaired loans (identified as credit-impaired at the time of acquisition), net of the related discount (this table should be read in conjunction with the allowance for acquired credit impaired loan losses table found on page 18):

| (Dollars in thousands) | Commercial Loans Greater Than<br>or Equal to \$1 million-CBT |                      |                   |                   | Commercial Real Estate |                   |                   | Commercial Real Estate<br>Construction and Development |                   |  |
|------------------------|--------------------------------------------------------------|----------------------|-------------------|-------------------|------------------------|-------------------|-------------------|--------------------------------------------------------|-------------------|--|
|                        | March 31,<br>2015                                            | December 31,<br>2014 | March 31,<br>2014 | March 31,<br>2015 | December 31,<br>2014   | March 31,<br>2014 | March 31,<br>2015 | December 31,<br>2014                                   | March 31,<br>2014 |  |
|                        |                                                              |                      |                   |                   |                        |                   |                   |                                                        |                   |  |
| Pass                   | \$ 11,175                                                    | \$ 11,248            | \$ 11,761         | \$ 196,116        | \$ 208,269             | \$ 232,060        | \$ 26,468         | \$ 26,855                                              | \$ 34,992         |  |
| Special mention        | 1,040                                                        | 1,030                | 1,054             | 35,154            | 35,896                 | 37,932            | 13,723            | 9,539                                                  | 13,183            |  |
| Substandard            | 3,262                                                        | 3,535                | 8,664             | 71,322            | 80,944                 | 132,513           | 21,265            | 28,868                                                 | 49,885            |  |
| Doubtful               |                                                              |                      |                   |                   |                        |                   |                   |                                                        |                   |  |
|                        | \$ 15,477                                                    | \$ 15,813            | \$ 21,479         | \$ 302,592        | \$ 325,109             | \$ 402,505        | \$ 61,456         | \$ 65,262                                              | \$ 98,060         |  |

# Edgar Filing: SOUTH STATE Corp - Form 10-Q

|                 | Residential Real Estate |                      |                   | Consumer          |                      |                   | Commercial & Industrial |                      |                   |
|-----------------|-------------------------|----------------------|-------------------|-------------------|----------------------|-------------------|-------------------------|----------------------|-------------------|
|                 | March 31,<br>2015       | December 31,<br>2014 | March 31,<br>2014 | March 31,<br>2015 | December 31,<br>2014 | March 31,<br>2014 | March 31,<br>2015       | December 31,<br>2014 | March 31,<br>2014 |
| Pass            | \$ 179,855              | \$ 190,931           | \$ 190,158        | \$ 6,417          | \$ 7,493             | \$ 7,058          | \$ 23,703               | \$ 25,530            | \$ 33,036         |
| Special mention | 71,798                  | 73,699               | 81,960            | 27,897            | 29,087               | 37,072            | 5,328                   | 5,317                | 3,670             |
| Substandard     | 116,980                 | 125,614              | 171,925           | 46,342            | 48,869               | 55,415            | 13,312                  | 13,957               | 22,267            |
| Doubtful        |                         |                      | 72                |                   |                      |                   |                         |                      |                   |
|                 | \$ 368,633              | \$ 390,244           | \$ 444,115        | \$ 80,656         | \$ 85,449            | \$ 99,545         | \$ 42,343               | \$ 44,804            | \$ 58,973         |

|                 | Single Pay        |                      |                   | Total Acquired Credit Impaired Loans |                      |                   |
|-----------------|-------------------|----------------------|-------------------|--------------------------------------|----------------------|-------------------|
|                 | March 31,<br>2015 | December 31,<br>2014 | March 31,<br>2014 | March 31,<br>2015                    | December 31,<br>2014 | March 31,<br>2014 |
| Pass            | \$ 48             | \$ 58                | \$ 54             | \$ 443,782                           | \$ 470,384           | \$ 509,119        |
| Special mention |                   |                      |                   | 154,940                              | 154,568              | 174,871           |
| Substandard     | 16                | 28                   | 78                | 272,499                              | 301,815              | 440,747           |
| Doubtful        |                   |                      |                   |                                      |                      | 72                |
|                 | \$ 64             | \$ 86                | \$ 132            | \$ 871,221                           | \$ 926,767           | \$ 1,124,809      |

Table of Contents**Note 6 Loans and Allowance for Loan Losses (Continued)**

The risk grading of acquired credit impaired loans is determined utilizing a loan's contractual balance, while the amount recorded in the financial statements and reflected above is the carrying value. In an FDIC-assisted acquisition, covered acquired loans are initially recorded at their fair value, including a credit discount due to the high concentration of substandard and doubtful loans. In addition to the credit discount and the allowance for loan losses on covered acquired loans, the Company's risk of loss is mitigated by the FDIC loss share arrangement.

The following table presents an aging analysis of past due loans, segregated by class for non-acquired loans:

| (Dollars in thousands)            | 30-59 Days<br>Past Due | 60-89 Days<br>Past Due | 90+ Days<br>Past Due | Total<br>Past<br>Due | Current      | Total<br>Loans |
|-----------------------------------|------------------------|------------------------|----------------------|----------------------|--------------|----------------|
| <b>March 31, 2015</b>             |                        |                        |                      |                      |              |                |
| Commercial real estate:           |                        |                        |                      |                      |              |                |
| Construction and land development | \$ 855                 | \$ 261                 | \$ 964               | \$ 2,080             | \$ 356,028   | \$ 358,108     |
| Commercial non-owner occupied     | 105                    | 110                    | 1,680                | 1,895                | 362,832      | 364,727        |
| Commercial owner occupied         | 2,211                  | 626                    | 4,536                | 7,373                | 917,819      | 925,192        |
| Consumer real estate:             |                        |                        |                      |                      |              |                |
| Consumer owner occupied           | 1,157                  | 981                    | 3,268                | 5,406                | 848,877      | 854,283        |
| Home equity loans                 | 1,126                  | 101                    | 601                  | 1,828                | 288,660      | 290,488        |
| Commercial and industrial         | 203                    | 170                    | 454                  | 827                  | 407,163      | 407,990        |
| Other income producing property   | 54                     | 308                    | 988                  | 1,350                | 153,010      | 154,360        |
| Consumer                          | 381                    | 135                    | 153                  | 669                  | 194,782      | 195,451        |
| Other loans                       | 60                     | 40                     | 36                   | 136                  | 35,670       | 35,806         |
|                                   | \$ 6,152               | \$ 2,732               | \$ 12,680            | \$ 21,564            | \$ 3,564,841 | \$ 3,586,405   |
| <b>December 31, 2014</b>          |                        |                        |                      |                      |              |                |
| Commercial real estate:           |                        |                        |                      |                      |              |                |
| Construction and land development | \$ 318                 | \$ 439                 | \$ 1,354             | \$ 2,111             | \$ 362,110   | \$ 364,221     |
| Commercial non-owner occupied     | 1,197                  |                        | 1,432                | 2,629                | 330,961      | 333,590        |
| Commercial owner occupied         | 1,106                  | 95                     | 5,403                | 6,604                | 901,309      | 907,913        |
| Consumer real estate:             |                        |                        |                      |                      |              |                |
| Consumer owner occupied           | 1,946                  | 501                    | 2,746                | 5,193                | 781,585      | 786,778        |
| Home equity loans                 | 679                    | 443                    | 519                  | 1,641                | 282,293      | 283,934        |
| Commercial and industrial         | 760                    | 123                    | 107                  | 990                  | 404,933      | 405,923        |
| Other income producing property   | 570                    | 114                    | 1,319                | 2,003                | 148,925      | 150,928        |
| Consumer                          | 512                    | 243                    | 120                  | 875                  | 188,442      | 189,317        |
| Other loans                       | 65                     | 46                     | 62                   | 173                  | 45,049       | 45,222         |
|                                   | \$ 7,153               | \$ 2,004               | \$ 13,062            | \$ 22,219            | \$ 3,445,607 | \$ 3,467,826   |
| <b>March 31, 2014</b>             |                        |                        |                      |                      |              |                |
| Commercial real estate:           |                        |                        |                      |                      |              |                |
| Construction and land development | \$ 1,289               | \$ 236                 | \$ 2,069             | \$ 3,594             | \$ 315,847   | \$ 319,441     |
| Commercial non-owner occupied     | 1,092                  |                        | 2,791                | 3,883                | 281,262      | 285,145        |
| Commercial owner occupied         | 2,051                  | 923                    | 4,333                | 7,307                | 838,421      | 845,728        |

# Edgar Filing: SOUTH STATE Corp - Form 10-Q

## Consumer real estate:

|                                 |          |          |           |           |              |              |
|---------------------------------|----------|----------|-----------|-----------|--------------|--------------|
| Consumer owner occupied         | 1,826    | 484      | 3,559     | 5,869     | 589,783      | 595,652      |
| Home equity loans               | 843      | 144      | 685       | 1,672     | 261,385      | 263,057      |
| Commercial and industrial       | 316      | 437      | 403       | 1,156     | 332,418      | 333,574      |
| Other income producing property | 114      | 493      | 2,339     | 2,946     | 155,240      | 158,186      |
| Consumer                        | 195      | 44       | 79        | 318       | 147,392      | 147,710      |
| Other loans                     | 44       | 22       | 32        | 98        | 31,367       | 31,465       |
|                                 | \$ 7,770 | \$ 2,783 | \$ 16,290 | \$ 26,843 | \$ 2,953,115 | \$ 2,979,958 |

Table of Contents
**Note 6 Loans and Allowance for Loan Losses (Continued)**

The following table presents an aging analysis of past due loans, segregated by class for acquired non-credit impaired loans:

| (Dollars in thousands)            | 30-59 Days<br>Past Due | 60-89 Days<br>Past Due | 90+ Days<br>Past Due | Total<br>Past<br>Due | Current      | Total<br>Loans |
|-----------------------------------|------------------------|------------------------|----------------------|----------------------|--------------|----------------|
| <b>March 31, 2015</b>             |                        |                        |                      |                      |              |                |
| Commercial real estate:           |                        |                        |                      |                      |              |                |
| Construction and land development | \$                     | \$                     | \$                   | \$                   | \$           | \$             |
|                                   |                        |                        |                      |                      | 19,598       | 19,598         |
| Commercial non-owner occupied     |                        |                        |                      |                      | 44,772       | 44,772         |
| Commercial owner occupied         | 49                     |                        | 38                   | 87                   | 56,080       | 56,167         |
| Consumer real estate:             |                        |                        |                      |                      |              |                |
| Consumer owner occupied           | 107                    | 328                    | 3,311                | 3,746                | 609,171      | 612,917        |
| Home equity loans                 | 570                    | 525                    | 1,042                | 2,137                | 219,398      | 221,535        |
| Commercial and industrial         | 6                      |                        | 221                  | 227                  | 35,365       | 35,592         |
| Other income producing property   | 77                     |                        | 89                   | 166                  | 61,249       | 61,415         |
| Consumer                          | 289                    | 211                    | 561                  | 1,061                | 194,292      | 195,353        |
|                                   | \$ 1,098               | \$ 1,064               | \$ 5,262             | \$ 7,424             | \$ 1,239,925 | \$ 1,247,349   |
| <b>December 31, 2014</b>          |                        |                        |                      |                      |              |                |
| Commercial real estate:           |                        |                        |                      |                      |              |                |
| Construction and land development | \$ 17                  | \$                     | 40                   | 57                   | 24,042       | 24,099         |
| Commercial non-owner occupied     |                        |                        |                      |                      | 49,476       | 49,476         |
| Commercial owner occupied         | 414                    |                        | 38                   | 452                  | 61,613       | 62,065         |
| Consumer real estate:             |                        |                        |                      |                      |              |                |
| Consumer owner occupied           | 443                    | 241                    | 1,566                | 2,250                | 644,125      | 646,375        |
| Home equity loans                 | 1,451                  | 866                    | 972                  | 3,289                | 231,660      | 234,949        |
| Commercial and industrial         | 14                     | 250                    | 117                  | 381                  | 40,749       | 41,130         |
| Other income producing property   | 97                     |                        | 88                   | 185                  | 64,954       | 65,139         |
| Consumer                          | 885                    | 341                    | 843                  | 2,069                | 202,697      | 204,766        |
|                                   | \$ 3,321               | \$ 1,698               | \$ 3,664             | \$ 8,683             | \$ 1,319,316 | \$ 1,327,999   |
| <b>March 31, 2014</b>             |                        |                        |                      |                      |              |                |
| Commercial real estate:           |                        |                        |                      |                      |              |                |
| Construction and land development | \$ 428                 | \$                     | 295                  | 723                  | 38,458       | 39,181         |
| Commercial non-owner occupied     |                        |                        |                      |                      | 52,625       | 52,625         |
| Commercial owner occupied         |                        | 371                    | 248                  | 619                  | 70,988       | 71,607         |
| Consumer real estate:             |                        |                        |                      |                      |              |                |
| Consumer owner occupied           | 2,277                  | 45                     | 1,674                | 3,996                | 728,568      | 732,564        |
| Home equity loans                 | 846                    | 339                    | 1,018                | 2,203                | 254,760      | 256,963        |
| Commercial and industrial         | 211                    |                        | 166                  | 377                  | 43,806       | 44,183         |
| Other income producing property   |                        |                        | 334                  | 334                  | 73,419       | 73,753         |
| Consumer                          | 1,316                  | 144                    | 239                  | 1,699                | 239,626      | 241,325        |
|                                   | \$ 5,078               | \$ 899                 | \$ 3,974             | \$ 9,951             | \$ 1,502,250 | \$ 1,512,201   |



Table of Contents**Note 6 Loans and Allowance for Loan Losses (Continued)**

The following table presents an aging analysis of past due loans, segregated by class for acquired credit impaired loans:

| (Dollars in thousands)                                    | 30-59 Days<br>Past Due | 60-89 Days<br>Past Due | 90+ Days<br>Past Due | Total<br>Past<br>Due | Current      | Total<br>Loans |
|-----------------------------------------------------------|------------------------|------------------------|----------------------|----------------------|--------------|----------------|
| <b>March 31, 2015</b>                                     |                        |                        |                      |                      |              |                |
| Commercial loans greater than or equal to \$1 million-CBT | \$                     | \$                     | \$ 2,659             | \$ 2,659             | \$ 12,818    | \$ 15,477      |
| Commercial real estate                                    | 6,548                  | 1,069                  | 14,522               | 22,139               | 280,453      | 302,592        |
| Commercial real estate construction and development       | 136                    | 196                    | 6,363                | 6,695                | 54,761       | 61,456         |
| Residential real estate                                   | 4,737                  | 3,747                  | 14,113               | 22,597               | 346,036      | 368,633        |
| Consumer                                                  | 1,174                  | 286                    | 2,178                | 3,638                | 77,018       | 80,656         |
| Commercial and industrial                                 | 714                    | 193                    | 4,997                | 5,904                | 36,439       | 42,343         |
| Single pay                                                |                        |                        |                      |                      | 64           | 64             |
|                                                           | \$ 13,309              | \$ 5,491               | \$ 44,832            | \$ 63,632            | \$ 807,589   | \$ 871,221     |
| <b>December 31, 2014</b>                                  |                        |                        |                      |                      |              |                |
| Commercial loans greater than or equal to \$1 million-CBT | \$                     | \$                     | \$ 2,896             | \$ 2,896             | \$ 12,917    | \$ 15,813      |
| Commercial real estate                                    | 4,350                  | 723                    | 15,866               | 20,939               | 304,170      | 325,109        |
| Commercial real estate construction and development       | 1,750                  | 452                    | 8,204                | 10,406               | 54,856       | 65,262         |
| Residential real estate                                   | 7,194                  | 2,856                  | 15,471               | 25,521               | 364,723      | 390,244        |
| Consumer                                                  | 2,241                  | 1,106                  | 2,614                | 5,961                | 79,488       | 85,449         |
| Commercial and industrial                                 | 451                    | 196                    | 3,413                | 4,060                | 40,744       | 44,804         |
| Single pay                                                |                        |                        |                      |                      | 86           | 86             |
|                                                           | \$ 15,986              | \$ 5,333               | \$ 48,464            | \$ 69,783            | \$ 856,984   | \$ 926,767     |
| <b>March 31, 2014</b>                                     |                        |                        |                      |                      |              |                |
| Commercial loans greater than or equal to \$1 million-CBT | \$ 766                 | \$                     | \$ 6,917             | \$ 7,683             | \$ 13,796    | \$ 21,479      |
| Commercial real estate                                    | 3,993                  | 3,461                  | 23,038               | 30,492               | 372,013      | 402,505        |
| Commercial real estate construction and development       | 1,145                  | 1,311                  | 13,220               | 15,676               | 82,384       | 98,060         |
| Residential real estate                                   | 12,038                 | 1,827                  | 20,452               | 34,317               | 409,798      | 444,115        |
| Consumer                                                  | 2,335                  | 593                    | 1,562                | 4,490                | 95,055       | 99,545         |
| Commercial and industrial                                 | 4,640                  | 875                    | 4,682                | 10,197               | 48,776       | 58,973         |
| Single pay                                                |                        |                        | 47                   | 47                   | 85           | 132            |
|                                                           | \$ 24,917              | \$ 8,067               | \$ 69,918            | \$ 102,902           | \$ 1,021,907 | \$ 1,124,809   |

Table of Contents
**Note 6 Loans and Allowance for Loan Losses (Continued)**

The following is a summary of information pertaining to impaired non-acquired and acquired loans accounted for under FASB ASC Topic 310-20:

| (Dollars in thousands)            | Unpaid<br>Contractual<br>Principal<br>Balance | Recorded<br>Investment<br>With No<br>Allowance | Gross<br>Recorded<br>Investment<br>With<br>Allowance | Total<br>Recorded<br>Investment | Related<br>Allowance |
|-----------------------------------|-----------------------------------------------|------------------------------------------------|------------------------------------------------------|---------------------------------|----------------------|
| <b>March 31, 2015</b>             |                                               |                                                |                                                      |                                 |                      |
| Commercial real estate:           |                                               |                                                |                                                      |                                 |                      |
| Construction and land development | \$ 8,074                                      | \$ 1,577                                       | \$ 3,830                                             | \$ 5,407                        | \$ 697               |
| Commercial non-owner occupied     | 5,131                                         | 2,509                                          | 1,256                                                | 3,765                           | 35                   |
| Commercial owner occupied         | 11,406                                        | 5,136                                          | 3,161                                                | 8,297                           | 70                   |
| Consumer real estate:             |                                               |                                                |                                                      |                                 |                      |
| Consumer owner occupied           | 8,026                                         | 4,505                                          | 2,588                                                | 7,093                           | 123                  |
| Home equity loans                 | 349                                           | 199                                            | 51                                                   | 250                             | 1                    |
| Commercial and industrial         | 1,644                                         | 323                                            | 583                                                  | 906                             | 16                   |
| Other income producing property   | 5,473                                         | 124                                            | 4,543                                                | 4,667                           | 485                  |
| Consumer                          | 107                                           |                                                | 63                                                   | 63                              | 2                    |
| Other loans                       |                                               |                                                |                                                      |                                 |                      |
| Total impaired loans              | \$ 40,210                                     | \$ 14,373                                      | \$ 16,075                                            | \$ 30,448                       | \$ 1,429             |
| <b>December 31, 2014</b>          |                                               |                                                |                                                      |                                 |                      |
| Commercial real estate:           |                                               |                                                |                                                      |                                 |                      |
| Construction and land development | \$ 7,414                                      | \$ 1,528                                       | \$ 3,324                                             | \$ 4,852                        | \$ 475               |
| Commercial non-owner occupied     | 4,920                                         | 2,539                                          | 1,071                                                | 3,610                           | 77                   |
| Commercial owner occupied         | 12,508                                        | 5,546                                          | 3,614                                                | 9,160                           | 172                  |
| Consumer real estate:             |                                               |                                                |                                                      |                                 |                      |
| Consumer owner occupied           | 3,393                                         |                                                | 2,966                                                | 2,966                           | 144                  |
| Home equity loans                 | 131                                           |                                                | 31                                                   | 31                              | 1                    |
| Commercial and industrial         | 1,625                                         | 336                                            | 572                                                  | 908                             | 41                   |
| Other income producing property   | 6,280                                         | 360                                            | 5,138                                                | 5,498                           | 646                  |
| Consumer                          | 95                                            |                                                | 60                                                   | 60                              | 2                    |
| Other loans                       |                                               |                                                |                                                      |                                 |                      |
| Total impaired loans              | \$ 36,366                                     | \$ 10,309                                      | \$ 16,776                                            | \$ 27,085                       | \$ 1,558             |
| <b>March 31, 2014</b>             |                                               |                                                |                                                      |                                 |                      |
| Commercial real estate:           |                                               |                                                |                                                      |                                 |                      |
| Construction and land development | \$ 8,607                                      | \$ 1,916                                       | \$ 4,234                                             | \$ 6,150                        | \$ 563               |
| Commercial non-owner occupied     | 4,948                                         | 1,479                                          | 2,674                                                | 4,153                           | 39                   |
| Commercial owner occupied         | 16,690                                        | 8,641                                          | 4,157                                                | 12,798                          | 106                  |
| Consumer real estate:             |                                               |                                                |                                                      |                                 |                      |
| Consumer owner occupied           | 2,895                                         |                                                | 2,550                                                | 2,550                           | 72                   |
| Home equity loans                 | 118                                           |                                                | 48                                                   | 48                              | 1                    |

# Edgar Filing: SOUTH STATE Corp - Form 10-Q

|                                 |           |           |           |           |          |
|---------------------------------|-----------|-----------|-----------|-----------|----------|
| Commercial and industrial       | 2,174     | 802       | 734       | 1,536     | 21       |
| Other income producing property | 6,891     | 1,246     | 5,252     | 6,498     | 617      |
| Consumer                        | 114       |           | 89        | 89        | 2        |
| Other loans                     |           |           |           |           |          |
| Total impaired loans            | \$ 42,437 | \$ 14,084 | \$ 19,738 | \$ 33,822 | \$ 1,421 |

Acquired credit impaired loans are accounted for in pools as shown on page 18 rather than being individually evaluated for impairment; therefore, the table above excludes acquired credit impaired loans.

Table of Contents
**Note 6 Loans and Allowance for Loan Losses (Continued)**

The following summarizes the average investment in impaired loans, non-acquired and acquired loans accounted for under FASB ASC Topic 310-20, and interest income recognized on these loans:

| (Dollars in thousands)            | Three Months Ended March 31,               |                               |                                            |                               |
|-----------------------------------|--------------------------------------------|-------------------------------|--------------------------------------------|-------------------------------|
|                                   | 2015                                       |                               | 2014                                       |                               |
|                                   | Average<br>Investment in<br>Impaired Loans | Interest Income<br>Recognized | Average<br>Investment in<br>Impaired Loans | Interest Income<br>Recognized |
| Commercial real estate:           |                                            |                               |                                            |                               |
| Construction and land development | \$ 5,129                                   | \$ 24                         | \$ 6,031                                   | \$ 19                         |
| Commercial non-owner occupied     | 3,688                                      | 12                            | 3,633                                      | 16                            |
| Commercial owner occupied         | 8,729                                      | 32                            | 11,783                                     | 41                            |
| Consumer real estate:             |                                            |                               |                                            |                               |
| Consumer owner occupied           | 5,029                                      | 28                            | 1,278                                      | 19                            |
| Home equity loans                 | 140                                        | 2                             | 17                                         |                               |
| Commercial and industrial         | 907                                        | 7                             | 929                                        | 15                            |
| Other income producing property   | 5,082                                      | 36                            | 5,148                                      | 27                            |
| Consumer                          | 62                                         | 1                             | 31                                         | 2                             |
| Other loans                       |                                            |                               |                                            |                               |
| Total Impaired Loans              | \$ 28,766                                  | \$ 142                        | \$ 28,850                                  | \$ 139                        |

The following is a summary of information pertaining to non-acquired nonaccrual loans by class, including restructured loans:

| (Dollars in thousands)                          | March 31,<br>2015 | December 31,<br>2014 | March 31,<br>2014 |
|-------------------------------------------------|-------------------|----------------------|-------------------|
| Commercial non-owner occupied real estate:      |                   |                      |                   |
| Construction and land development               | \$ 2,474          | \$ 2,920             | \$ 5,305          |
| Commercial non-owner occupied                   | 2,193             | 2,325                | 2,886             |
| Total commercial non-owner occupied real estate | 4,667             | 5,245                | 8,191             |
| Consumer real estate:                           |                   |                      |                   |
| Consumer owner occupied                         | 6,877             | 6,015                | 7,840             |
| Home equity loans                               | 1,328             | 1,412                | 1,646             |
| Total consumer real estate                      | 8,205             | 7,427                | 9,486             |
| Commercial owner occupied real estate           | 2,721             | 3,605                | 6,383             |
| Commercial and industrial                       | 513               | 600                  | 857               |
| Other income producing property                 | 1,068             | 1,348                | 4,154             |
| Consumer                                        | 317               | 344                  | 119               |
| Other loans                                     |                   |                      |                   |
| Restructured loans                              | 9,879             | 9,425                | 8,156             |
| Total loans on nonaccrual status                | \$ 27,370         | \$ 27,994            | \$ 37,346         |



Table of Contents
**Note 6 Loans and Allowance for Loan Losses (Continued)**

The following is a summary of information pertaining to acquired non-credit impaired nonaccrual loans by class, including restructured loans:

| <b>(Dollars in thousands)</b>                   | <b>March 31,<br/>2015</b> | <b>December 31,<br/>2014</b> |
|-------------------------------------------------|---------------------------|------------------------------|
| Commercial non-owner occupied real estate:      |                           |                              |
| Construction and land development               | \$                        | \$ 41                        |
| Commercial non-owner occupied                   | 627                       | 645                          |
| Total commercial non-owner occupied real estate | 627                       | 686                          |
| Consumer real estate:                           |                           |                              |
| Consumer owner occupied                         | 3,610                     | 3,685                        |
| Home equity loans                               | 1,411                     | 1,507                        |
| Total consumer real estate                      | 5,021                     | 5,192                        |
| Commercial owner occupied real estate           | 38                        | 38                           |
| Commercial and industrial                       | 225                       | 120                          |
| Other income producing property                 | 308                       | 309                          |
| Consumer                                        | 1,061                     | 1,193                        |
| Restructured loans                              |                           |                              |
| Total loans on nonaccrual status                | \$ 7,280                  | \$ 7,538                     |

As of March 31, 2014, the Company did not have any acquired non-credit impaired nonaccrual loans.

In the course of resolving delinquent loans, the Bank may choose to restructure the contractual terms of certain loans. Any loans that are modified are reviewed by the Bank to determine if a troubled debt restructuring ( TDR or restructured loan ) has occurred. A TDR is a modification in which the Bank grants a concession to a borrower that it would not otherwise consider due to economic or legal reasons related to a borrower's financial difficulties. The concessions granted on TDRs generally include terms to reduce the interest rate, extend the term of the debt obligation, or modify the payment structure on the debt obligation.

The Bank designates loan modifications as TDRs when it grants a concession to the borrower that it would not otherwise consider due to the borrower experiencing financial difficulty (FASB ASC Topic 310-40). Loans on nonaccrual status at the date of modification are initially classified as nonaccrual TDRs. Loans on accruing status at the date of concession are initially classified as accruing TDRs if the note is reasonably assured of repayment and performance is expected in accordance with its modified terms. Such loans may be designated as nonaccrual loans subsequent to the concession date if reasonable doubt exists as to the collection of interest or principal under the restructuring agreement. Nonaccrual TDRs are returned to accruing status when there is economic substance to the restructuring, there is documented credit evaluation of the borrower's financial condition, the remaining balance is reasonably assured of repayment in accordance with its modified terms, and the borrower has demonstrated sustained repayment performance in accordance with the modified terms for a reasonable period of time (generally a minimum of six months).

The following table presents non-acquired and acquired non-credit impaired loans designated as TDRs segregated by class and type of concession that were restructured during the three months ended March 31, 2015 and 2014:

Edgar Filing: SOUTH STATE Corp - Form 10-Q

| (Dollars in thousands)               | Number<br>of loans | Three Months Ended March 31,                                          |                                                                |                    |                                                                       |                                                                |  |
|--------------------------------------|--------------------|-----------------------------------------------------------------------|----------------------------------------------------------------|--------------------|-----------------------------------------------------------------------|----------------------------------------------------------------|--|
|                                      |                    | 2015<br>Pre-<br>Modification<br>Outstanding<br>Recorded<br>Investment | Post-<br>Modification<br>Outstanding<br>Recorded<br>Investment | Number<br>of loans | 2014<br>Pre-<br>Modification<br>Outstanding<br>Recorded<br>Investment | Post-<br>Modification<br>Outstanding<br>Recorded<br>Investment |  |
| Interest rate modification           |                    |                                                                       |                                                                |                    |                                                                       |                                                                |  |
| Consumer owner occupied              | 1                  | \$ 199                                                                | \$ 199                                                         | 1                  | \$ 217                                                                | \$ 217                                                         |  |
| Total interest rate<br>modifications | 1                  | 199                                                                   | 199                                                            | 1                  | 217                                                                   | 217                                                            |  |
| Term modification                    |                    |                                                                       |                                                                |                    |                                                                       |                                                                |  |
| Construction and land<br>development | 2                  | 552                                                                   | 551                                                            |                    |                                                                       |                                                                |  |
| Total term modifications             | 2                  | 552                                                                   | 551                                                            |                    |                                                                       |                                                                |  |
|                                      | 3                  | \$ 751                                                                | \$ 750                                                         | 1                  | \$ 217                                                                | \$ 217                                                         |  |

At March 31, 2015 and 2014, the balance of accruing TDRs was \$6.7 million and \$7.0 million, respectively.

## Table of Contents

### Note 6 Loans and Allowance for Loan Losses (Continued)

The following table presents the changes in status of non-acquired loans restructured within the previous 12 months as of March 31, 2015 by type of concession:

| (Dollars in thousands)     | Paying Under<br>Restructured Terms |                        | Converted to Nonaccrual |                        | Foreclosures and Defaults |                        |
|----------------------------|------------------------------------|------------------------|-------------------------|------------------------|---------------------------|------------------------|
|                            | Number<br>of Loans                 | Recorded<br>Investment | Number<br>of Loans      | Recorded<br>Investment | Number<br>of Loans        | Recorded<br>Investment |
| Interest rate modification | 7                                  | \$ 1,135               | 2                       | \$ 177                 |                           | \$                     |
| Term modification          | 4                                  | 1,834                  | 1                       | 474                    |                           |                        |
|                            | 11                                 | \$ 2,969               | 3                       | \$ 651                 |                           | \$                     |

The amount of specific reserve associated with non-acquired restructured loans was \$1.2 million at March 31, 2015, none of which was related to restructured loans that had subsequently defaulted. The Company had \$1,000 remaining availability under commitments to lend additional funds on these restructured loans at March 31, 2015.

### Note 7 FDIC Indemnification Asset

The following table provides changes in FDIC indemnification asset:

| (Dollars in thousands)                          | Three Months Ended March 31, |           |
|-------------------------------------------------|------------------------------|-----------|
|                                                 | 2015                         | 2014      |
| Balance at beginning of period                  | \$ 22,161                    | \$ 86,447 |
| Increase (decrease) in expected losses on loans | (21)                         | 125       |
| Additional losses (recoveries) on OREO          | (1,240)                      | (643)     |
| Reimbursable expenses                           | 348                          | 676       |
| Amortization of discounts and premiums, net     | (3,207)                      | (7,078)   |
| Reimbursements from FDIC                        | (1,328)                      | (19,043)  |
| Balance at end of period                        | \$ 16,713                    | \$ 60,484 |

The FDIC indemnification asset is measured separately from the related covered assets. At March 31, 2015, the projected cash flows related to the FDIC indemnification asset for losses on assets acquired were approximately \$12.1 million less than the current carrying value. This amount is being recognized as amortization (in non-interest income) over the shorter of the underlying asset's remaining life or remaining term of the loss share agreements. Subsequent to March 31, 2015, the Company expects to receive \$2.8 million from loss share claims filed, including reimbursable expenses.

Included in the FDIC indemnification asset is an expected true up with the FDIC related to both the BankMeridian and Plantation acquisitions. This amount is determined each reporting period and at March 31, 2015 was estimated to be approximately \$4.1 million related to the BankMeridian acquisition at the end of the loss share agreement (July 2021) and \$3.1 million related to the Plantation acquisition at the end of

## Edgar Filing: SOUTH STATE Corp - Form 10-Q

the loss share agreement (April 2017). The actual payment to the FDIC will be determined at the end of the loss sharing agreement term for each of the five FDIC-assisted acquisitions and is based on the negative bid, expected losses, intrinsic loss estimate, and assets covered under loss share. There was no true up expected from the CBT, Cape Fear, or Habersham FDIC-assisted transactions as of March 31, 2015.

Effective March 31, 2015, the Commercial Shared-Loss Agreement with the FDIC for CBT expired and losses on assets covered under this agreement are no longer claimable after filing the first quarter of 2015 commercial loss share certificate. The carrying value of commercial loans and OREO no longer covered under the CBT loss share agreement totaled \$49.0 million and \$2.3 million, respectively. The Commercial Shared-Loss Agreement for Cape Fear expired June 30, 2014 and losses on assets covered under this agreement are no longer claimable.

# Table of Contents

## Note 8 Other Real Estate Owned

The following is a summary of information pertaining to OREO at March 31, 2015:

| (Dollars in thousands)     | OREO      | Covered<br>OREO | Total     |
|----------------------------|-----------|-----------------|-----------|
| Balance, December 31, 2014 | \$ 26,499 | \$ 16,227       | \$ 42,726 |
| Additions                  | 4,113     | 2,423           | 6,536     |
| Write-downs                | (813)     | (1,402)         | (2,215)   |
| Sold                       | (5,729)   | (5,222)         | (10,951)  |
| Balance, March 31, 2015    | \$ 24,070 | \$ 12,026       | \$ 36,096 |

The following is a summary of information pertaining to OREO at March 31, 2014:

| (Dollars in thousands)     | OREO      | Covered<br>OREO | Total     |
|----------------------------|-----------|-----------------|-----------|
| Balance, December 31, 2013 | \$ 37,398 | \$ 27,520       | \$ 64,918 |
| Additions                  | 5,766     | 6,822           | 12,588    |
| Write-downs                | (2,228)   | (773)           | (3,001)   |
| Sold                       | (5,792)   | (4,566)         | (10,358)  |
| Balance, March 31, 2014    | \$ 35,144 | \$ 29,003       | \$ 64,147 |

The covered OREO above is covered pursuant to the FDIC loss share agreements and is presented net of the related fair value discount. At March 31, 2015, there were 178 properties included in OREO, with 123 uncovered and 55 covered by loss share agreements with the FDIC. At March 31, 2014, there were 452 properties included in OREO, with 217 uncovered and 235 covered by loss share agreements with the FDIC. At March 31, 2015, the Company had \$4.6 million in residential real estate included in OREO and \$14.8 million in residential real estate consumer mortgage loans in the process of foreclosure.

## Note 9 Deposits

The Company's total deposits are comprised of the following:

| (Dollars in thousands)               | March 31,<br>2015 | December 31,<br>2014 | March 31,<br>2014 |
|--------------------------------------|-------------------|----------------------|-------------------|
| Certificates of deposit              | \$ 1,187,908      | \$ 1,237,140         | \$ 1,452,935      |
| Interest-bearing demand deposits     | 3,009,005         | 2,927,820            | 2,915,756         |
| Non-interest bearing demand deposits | 1,757,302         | 1,639,953            | 1,585,055         |
| Savings deposits                     | 677,056           | 655,132              | 678,650           |
| Other time deposits                  | 2,386             | 1,000                | 2,155             |
| Total deposits                       | \$ 6,633,657      | \$ 6,461,045         | \$ 6,634,551      |

At March 31, 2015, December 31, 2014, and March 31, 2014, the Company had \$139.5 million, \$128.5 million, and \$150.3 million in certificates of deposits greater than \$250,000, respectively. At March 31, 2015, December 31, 2014, and March 31, 2014, the Company had \$19.9 million, \$23.4 million and \$30.4 million, in traditional, out-of-market brokered deposits, respectively.

**Note 10 Retirement Plans**

The Company and the Bank provide certain retirement benefits to their employees in the form of a non-contributory defined benefit pension plan and an employees' savings plan. The non-contributory defined benefit pension plan covers all employees hired on or before December 31, 2005, who have attained age 21, and who have completed a year of eligible service. Employees hired on or after January 1, 2006 are not eligible to participate in the non-contributory defined benefit pension plan, but are eligible to participate in the employees' savings plan. On this date, a new benefit formula applies only to participants who have not attained age 45 or who do not have five years of service.

Table of Contents**Note 10 Retirement Plans (Continued)**

Effective July 1, 2009, the Company suspended the accrual of benefits for pension plan participants under the non-contributory defined benefit plan. The pension plan remained suspended as of March 31, 2015.

The components of net periodic pension expense recognized are as follows:

| (Dollars in thousands)                 | Three Months Ended |       |      |       |
|----------------------------------------|--------------------|-------|------|-------|
|                                        | March 31,          |       |      |       |
|                                        | 2015               |       | 2014 |       |
| Interest cost                          | \$                 | (254) | \$   | (277) |
| Expected return on plan assets         |                    | 518   |      | 487   |
| Recognized net actuarial loss          |                    | (226) |      | (165) |
| Net periodic pension benefit (expense) | \$                 | 38    | \$   | 45    |

The Company did not contribute to the pension plan for the three months ended March 31, 2015, and does not expect to make any additional contributions during the remainder of 2015. The plans assets currently exceed the projected benefit obligation of the plan, and no additional contributions are required for 2015.

Electing employees are eligible to participate in the employees' savings plan, under the provisions of Internal Revenue Code Section 401(k), after attaining age 21. Plan participants elect to contribute portions of their annual base compensation as a before tax contribution. Employer contributions may be made from current or accumulated net profits. Participants may elect to contribute 1% to 50% of annual base compensation as a before tax contribution. Employees participating in the plan receive a 100% matching of their 401(k) plan contribution, up to 5% of their salary. Effective January 1, 2015, employees are eligible for an additional 1% discretionary matching contribution contingent upon achievement of the Company's 2015 financial goals and payable the first quarter of 2016. The Company expensed \$1.3 million and \$1.2 million for the 401(k) plan during the three months ended March 31, 2015 and 2014, respectively.

Employees can enter the savings plan on or after the first day of each month. The employee may enter into a salary deferral agreement at any time to select an alternative deferral amount or to elect not to defer in the plan. If the employee does not elect an investment allocation, the plan administrator will select a retirement-based portfolio according to the employee's number of years until normal retirement age. The plan's investment valuations are generally provided on a daily basis.

**Note 11 Earnings Per Share**

Basic earnings per share are calculated by dividing net income available to common shareholders by the weighted-average shares of common stock outstanding during each period, excluding non-vested shares. The Company's diluted earnings per share are based on the weighted-average shares of common stock outstanding during each period plus the maximum dilutive effect of common stock issuable upon exercise of stock options or vesting of restricted shares. The weighted-average number of shares and equivalents are determined after giving retroactive effect to

stock dividends and stock splits.

# Table of Contents

## **Note 11 Earnings Per Share (Continued)**

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

| (Dollars and shares in thousands)           | Three Months Ended<br>March 31, |           |
|---------------------------------------------|---------------------------------|-----------|
|                                             | 2015                            | 2014      |
| Basic earnings per common share:            |                                 |           |
| Net income available to common shareholders | \$ 23,926                       | \$ 15,844 |
| Weighted-average basic common shares        | 23,943                          | 23,873    |
| Basic earnings per common share             | \$ 1.00                         | \$ 0.66   |
| Diluted earnings per share:                 |                                 |           |
| Net income available to common shareholders | \$ 23,926                       | \$ 15,844 |
| Weighted-average basic common shares        | 23,943                          | 23,873    |
| Effect of dilutive securities               | 258                             | 243       |
| Weighted-average dilutive shares            | 24,201                          | 24,116    |
| Diluted earnings per common share           | \$ 0.99                         | \$ 0.66   |

The calculation of diluted earnings per common share excludes outstanding stock options for which the results would have been anti-dilutive under the treasury stock method as follows:

| (Dollars in thousands)   | Three Months Ended<br>March 31, |                 |
|--------------------------|---------------------------------|-----------------|
|                          | 2015                            | 2014            |
| Number of shares         | 48,927                          | 22,497          |
| Range of exercise prices | \$61.42-\$66.32                 | \$61.49-\$66.32 |

## **Note 12 Share-Based Compensation**

The Company's 2004 and 2012 share-based compensation programs are long-term retention programs intended to attract, retain, and provide incentives for key employees and non-employee directors in the form of incentive and non-qualified stock options, restricted stock, and restricted stock units (RSUs).

### *Stock Options*

## Edgar Filing: SOUTH STATE Corp - Form 10-Q

With the exception of non-qualified stock options granted to directors under the 2004 and 2012 plans, which in some cases may be exercised at any time prior to expiration and in some other cases may be exercised at intervals less than a year following the grant date, incentive stock options granted under the plans may not be exercised in whole or in part within a year following the date of the grant, as these incentive stock options become exercisable in 25% increments pro rata over the four-year period following the grant date. The options are granted at an exercise price at least equal to the fair value of the common stock at the date of grant and expire ten years from the date of grant. No options were granted under the 2004 plan after January 26, 2012, and the 2004 plan is closed other than for any options still unexercised and outstanding. The 2012 plan is the only plan from which new share-based compensation grants may be issued. It is the Company's policy to grant options out of the 1,684,000 shares registered under the 2012 plan, of which no more than 817,476 shares can be granted as restricted stock or RSUs.

[Table of Contents](#)
**Note 12 Share-Based Compensation (Continued)**

Activity in the Company's stock option plans is summarized in the following table. All information has been retroactively adjusted for stock dividends and stock splits.

| Options                                                           | Number of<br>Shares | Weighted-<br>Average<br>Exercise<br>Price | Weighted-<br>Average<br>Remaining<br>Contractual<br>Life (Yrs.) | Aggregate<br>Intrinsic<br>Value (000 \$) |
|-------------------------------------------------------------------|---------------------|-------------------------------------------|-----------------------------------------------------------------|------------------------------------------|
| Outstanding at January 1, 2015                                    | 294,342             | \$ 35.91                                  |                                                                 |                                          |
| Granted                                                           | 26,430              | 61.74                                     |                                                                 |                                          |
| Exercised                                                         | (21,000)            | 31.74                                     |                                                                 |                                          |
| Outstanding at March 31, 2015                                     | 299,772             | 38.48                                     | 4.95                                                            | \$ 8,967                                 |
| Exercisable at March 31, 2015                                     | 241,491             | 34.28                                     | 4.01                                                            | \$ 8,236                                 |
| Weighted-average fair value of<br>options granted during the year | \$ 25.08            |                                           |                                                                 |                                          |

The fair value of options is estimated at the date of grant using the Black-Scholes option pricing model and expensed over the options' vesting periods. The following weighted-average assumptions were used in valuing options issued:

|                         | 2015        | March 31,<br>2014 |
|-------------------------|-------------|-------------------|
| Dividend yield          | 1.40%       | 1.27%             |
| Expected life           | 8.5 years   | 6.3 years         |
| Expected volatility     | 40.9%-40.9% | 43.8%-44.7%       |
| Risk-free interest rate | 1.79%       | 2.10%             |

As of March 31, 2015, there was \$1.2 million of total unrecognized compensation cost related to nonvested stock option grants under the plans. The cost is expected to be recognized over a weighted-average period of 1.83 years as of March 31, 2015. The total fair value of shares vested during the three months ended March 31, 2015 was \$386,000.

**Restricted Stock**

The Company from time-to-time also grants shares of restricted stock to key employees and non-employee directors. These awards help align the interests of these employees and directors with the interests of the shareholders of the Company by providing economic value directly related to increases in the value of the Company's stock. The value of the stock awarded is established as the fair market value of the stock at the time of the grant. The Company recognizes expenses, equal to the total value of such awards, ratably over the vesting period of the stock grants. Restricted stock grants to employees typically cliff vest after four years. Grants to non-employee directors typically vest within a 12-month

period.

Table of Contents**Note 12 Share-Based Compensation (Continued)**

Nonvested restricted stock for the three months ended March 31, 2015 is summarized in the following table. All information has been retroactively adjusted for stock dividends and stock splits.

| <b>Restricted Stock</b>      | <b>Shares</b> | <b>Weighted-Average Grant-Date Fair Value</b> |
|------------------------------|---------------|-----------------------------------------------|
| Nonvested at January 1, 2015 | 228,907       | \$ 37.44                                      |
| Granted                      | 907           | 63.19                                         |
| Vested                       | (36,068)      | 33.88                                         |
| Nonvested at March 31, 2015  | 193,746       | 38.22                                         |

As of March 31, 2015, there was \$3.7 million of total unrecognized compensation cost related to nonvested restricted stock granted under the plans. This cost is expected to be recognized over a weighted-average period of 2.49 years as of March 31, 2015. The total fair value of shares vested during the three months ended March 31, 2015 was \$1.3 million.

*Restricted Stock Units*

The Company from time-to-time also grants performance RSUs to key employees. These awards help align the interests of these employees with the interests of the shareholders of the Company by providing economic value directly related to the performance of the Company. Performance RSU grants contain a three year performance period. The Company communicates threshold, target, and maximum performance RSU awards and performance targets to the applicable key employees at the beginning of a performance period. Dividends are not paid in respect to the awards during the performance period. The value of the RSUs awarded is established as the fair market value of the stock at the time of the grant. The Company recognizes expenses on a straight-line basis typically over three years based upon the probable performance target that will be met. For the three months ended March 31, 2015, the Company accrued for 85% of the RSUs granted, based on Management's expectations of performance.

Nonvested RSUs for the three months ended March 31, 2015 is summarized in the following table.

| <b>Restricted Stock Units</b> | <b>Shares</b> | <b>Weighted-Average Grant-Date Fair Value</b> |
|-------------------------------|---------------|-----------------------------------------------|
| Nonvested at January 1, 2015  | 79,308        | \$ 55.92                                      |
| Granted                       | 38,456        | 68.10                                         |
| Nonvested at March 31, 2015   | 117,764       | 59.90                                         |

## Edgar Filing: SOUTH STATE Corp - Form 10-Q

As of March 31, 2015, there was \$4.8 million of total unrecognized compensation cost related to nonvested RSUs granted under the plan. This cost is expected to be recognized over a weighted-average period of 1.73 years as of March 31, 2015. There were no shares vested during the three months ended March 31, 2015.

### **Note 13 Commitments and Contingent Liabilities**

In the normal course of business, the Company makes various commitments and incurs certain contingent liabilities, which are not reflected in the accompanying financial statements. The commitments and contingent liabilities include guarantees, commitments to extend credit, and standby letters of credit. At March 31, 2015, commitments to extend credit and standby letters of credit totaled \$1.3 billion. The Company does not anticipate any material losses as a result of these transactions.

The Company has been named as defendant in various legal actions, arising from its normal business activities, in which damages in various amounts are claimed. The Company is also exposed to litigation risk related to the prior business activities of banks acquired through whole bank acquisitions as well as banks from which assets were acquired and liabilities assumed in FDIC-assisted transactions. Although the amount of any ultimate liability with respect to such matters cannot be determined, in the opinion of management, any such liability will not have a material effect on the Company's consolidated financial statements.

Table of Contents

**Note 14 Fair Value**

FASB ASC 820, *Fair Value Measurements and Disclosures*, defines fair value, establishes a framework for measuring fair value under accounting principles generally accepted in the United States, and enhances disclosures about fair value measurements. FASB ASC 820 clarifies that fair value should be based on the assumptions market participants would use when pricing an asset or liability and establishes a fair value hierarchy that prioritizes the information used to develop those assumptions.

The Company utilizes fair value measurements to record fair value adjustments to certain assets and liabilities and to determine fair value disclosures. Available for sale securities, derivative contracts, and mortgage servicing rights are recorded at fair value on a recurring basis. Additionally, from time to time, the Company may be required to record at fair value other assets on a nonrecurring basis, such as impaired loans, OREO, and certain other assets. These nonrecurring fair value adjustments typically involve application of lower of cost or market accounting or write-downs of individual assets.

FASB ASC 820 establishes a three-tier fair value hierarchy which prioritizes the inputs used in measuring fair value as follows:

- Level 1      Observable inputs such as quoted prices in active markets;
- Level 2      Inputs, other than the quoted prices in active markets, that are observable either directly or indirectly; and
- Level 3      Unobservable inputs in which there is little or no market data, which require the reporting entity to develop its own assumptions.

The following is a description of valuation methodologies used for assets recorded at fair value.

*Investment Securities*

Securities available for sale are valued on a recurring basis at quoted market prices where available. If quoted market prices are not available, fair values are based on quoted market prices of comparable securities. Level 1 securities include those traded on an active exchange, such as the New York Stock Exchange and The NASDAQ Stock Market, or U.S. Treasury securities that are traded by dealers or brokers in active over-the-counter markets and money market funds. Level 2 securities include mortgage-backed securities and debentures issued by government sponsored entities, municipal bonds and corporate debt securities. Securities held to maturity are valued at quoted market prices or dealer quotes similar to securities available for sale. The carrying value of FHLB stock approximates fair value based on the redemption provisions.

*Mortgage Loans Held for Sale*

Mortgage loans held for sale are carried at the fair market value. The fair values of mortgage loans held for sale are based on commitments on hand from investors within the secondary market for loans with similar characteristics. As such, the fair value adjustments for mortgage loans held for sale are recurring Level 2.

*Loans*

The Company does not record loans at fair value on a recurring basis. However, from time to time, a loan may be considered impaired and an allowance for loan losses may be established. Loans for which it is probable that payment of interest and principal will not be made in accordance with the contractual terms of the loan agreement are considered impaired. Once a loan is identified as individually impaired, management measures impairment using estimated fair value methodologies. The fair value of impaired loans is estimated using one of several methods, including collateral value, market value of similar debt, enterprise value, liquidation value and discounted cash flows. Those impaired loans not requiring an allowance represent loans for which the fair value of the expected repayments or collateral exceed the recorded investments in such loans. At March 31, 2015, substantially all of the impaired loans were evaluated based on the fair value of the collateral because such loans were considered collateral dependent. Impaired loans, where an allowance is established based on the fair value of collateral; require classification in the fair value hierarchy. When the fair value of the collateral is based on an observable market price or a current appraised value, the Company considers the impaired loan as nonrecurring Level 2. When an appraised value is not available or management determines the fair value of the collateral is further impaired below the appraised value and there is no observable market price, the Company considers the impaired loan as nonrecurring Level 3.

Table of Contents

**Note 14 Fair Value (Continued)**

*Other Real Estate Owned ( OREO )*

Typically non-covered OREO, consisting of properties obtained through foreclosure or in satisfaction of loans, is reported at fair value, determined on the basis of current appraisals, comparable sales, and other estimates of value obtained principally from independent sources, adjusted for estimated selling costs (Level 2). However, both non-covered and covered OREO are considered Level 3 in the fair value hierarchy because management has qualitatively applied a discount due to the size, supply of inventory, and the incremental discounts applied to the appraisals. Management also considers other factors, including changes in absorption rates, length of time the property has been on the market and anticipated sales values, which have resulted in adjustments to the collateral value estimates indicated in certain appraisals. At the time of foreclosure, any excess of the loan balance over the fair value of the real estate held as collateral is treated as a charge against the allowance for loan losses. Gains or losses on sale and generally any subsequent adjustments to the value are recorded as a component of OREO expense, net of any FDIC indemnification proceeds in the case of covered OREO.

*Derivative Financial Instruments*

Fair value is estimated using pricing models of derivatives with similar characteristics; accordingly, the derivatives are classified within Level 2 of the fair value hierarchy (see Note 16 Derivative Financial Instruments for additional information).

*Mortgage servicing rights ( MSRs )*

The estimated fair value of MSRs is obtained through an independent derivatives dealer analysis of future cash flows. The evaluation utilizes assumptions market participants would use in determining fair value including market discount rates, prepayment speeds, servicing income, servicing costs, default rates and other market driven data, as well as the market's perception of future interest rate movements. MSRs are classified as Level 3.

Table of Contents**Note 14 Fair Value (Continued)***Assets and Liabilities Recorded at Fair Value on a Recurring Basis*

The tables below present the recorded amount of assets and liabilities measured at fair value on a recurring basis.

| (Dollars in thousands)              | Fair Value | Quoted Prices<br>In Active<br>Markets<br>for Identical<br>Assets<br>(Level 1) | Significant<br>Other<br>Observable<br>Inputs<br>(Level 2) | Significant<br>Unobservable<br>Inputs<br>(Level 3) |
|-------------------------------------|------------|-------------------------------------------------------------------------------|-----------------------------------------------------------|----------------------------------------------------|
| <b>March 31, 2015:</b>              |            |                                                                               |                                                           |                                                    |
| <b>Assets</b>                       |            |                                                                               |                                                           |                                                    |
| Derivative financial instruments    | \$ 3,160   | \$                                                                            | \$ 3,160                                                  | \$                                                 |
| Loans held for sale                 | 87,342     |                                                                               | 87,342                                                    |                                                    |
| Securities available for sale:      |            |                                                                               |                                                           |                                                    |
| Government-sponsored entities debt  | 134,203    |                                                                               | 134,203                                                   |                                                    |
| State and municipal obligations     | 136,516    |                                                                               | 136,516                                                   |                                                    |
| Mortgage-backed securities          | 534,424    |                                                                               | 534,424                                                   |                                                    |
| Corporate stocks                    | 3,253      | 3,028                                                                         | 225                                                       |                                                    |
| Total securities available for sale | 808,396    | 3,028                                                                         | 805,368                                                   |                                                    |
| Mortgage servicing rights           | 21,510     |                                                                               |                                                           | 21,510                                             |
|                                     | \$ 920,407 | \$ 3,028                                                                      | \$ 895,869                                                | \$ 21,510                                          |
| <b>Liabilities</b>                  |            |                                                                               |                                                           |                                                    |
| Derivative financial instruments    | \$ 1,608   | \$                                                                            | \$ 1,608                                                  | \$                                                 |
| <b>December 31, 2014:</b>           |            |                                                                               |                                                           |                                                    |
| <b>Assets</b>                       |            |                                                                               |                                                           |                                                    |
| Derivative financial instruments    | \$ 2,148   | \$                                                                            | \$ 2,148                                                  | \$                                                 |
| Loans held for sale                 | 61,934     |                                                                               | 61,934                                                    |                                                    |
| Securities available for sale:      |            |                                                                               |                                                           |                                                    |
| Government-sponsored entities debt  | \$ 148,197 | \$                                                                            | \$ 148,197                                                | \$                                                 |
| State and municipal obligations     | 137,581    |                                                                               | 137,581                                                   |                                                    |
| Mortgage-backed securities          | 517,946    |                                                                               | 517,946                                                   |                                                    |
| Corporate stocks                    | 3,042      | 2,817                                                                         | 225                                                       |                                                    |
| Total securities available for sale | 806,766    | 2,817                                                                         | 803,949                                                   |                                                    |
| Mortgage servicing rights           | 21,601     |                                                                               |                                                           | 21,601                                             |
|                                     | \$ 892,449 | \$ 2,817                                                                      | \$ 868,031                                                | \$ 21,601                                          |
| <b>Liabilities</b>                  |            |                                                                               |                                                           |                                                    |
| Derivative financial instruments    | \$ 1,341   | \$                                                                            | \$ 1,341                                                  | \$                                                 |
| <b>March 31, 2014:</b>              |            |                                                                               |                                                           |                                                    |
| <b>Assets</b>                       |            |                                                                               |                                                           |                                                    |
| Derivative financial instruments    | \$ 752     | \$                                                                            | \$ 752                                                    | \$                                                 |
| Loans held for sale                 | 57,609     |                                                                               | 57,609                                                    |                                                    |
| Securities available for sale:      |            |                                                                               |                                                           |                                                    |
| Government-sponsored entities debt  | 137,601    |                                                                               | 137,601                                                   |                                                    |
| State and municipal obligations     | 141,638    |                                                                               | 141,638                                                   |                                                    |
| Mortgage-backed securities          | 510,379    |                                                                               | 510,379                                                   |                                                    |

# Edgar Filing: SOUTH STATE Corp - Form 10-Q

|                                     |            |          |            |           |  |        |
|-------------------------------------|------------|----------|------------|-----------|--|--------|
| Corporate stocks                    | 3,506      | 3,281    | 225        |           |  |        |
| Total securities available for sale | 793,124    | 3,281    | 789,843    |           |  |        |
| Mortgage servicing rights           | 20,925     |          |            |           |  | 20,925 |
|                                     | \$ 872,410 | \$ 3,281 | \$ 848,204 | \$ 20,925 |  |        |
| <b>Liabilities</b>                  |            |          |            |           |  |        |
| Derivative financial instruments    | \$ 1,461   | \$       | \$ 1,461   | \$        |  |        |

Table of Contents**Note 14 Fair Value (Continued)***Changes in Level 1, 2 and 3 Fair Value Measurements*

When a determination is made to classify a financial instrument within Level 3 of the valuation hierarchy, the determination is based upon the significance of the unobservable factors to the overall fair value measurement. However, since Level 3 financial instruments typically include, in addition to the unobservable or Level 3 components, observable components (that is, components that are actively quoted and can be validated to external sources), the gains and losses below include changes in fair value due in part to observable factors that are part of the valuation methodology.

There were no changes in hierarchy classifications of Level 3 assets or liabilities for the three months ended March 31, 2015. A reconciliation of the beginning and ending balances of Level 3 assets and liabilities recorded at fair value on a recurring basis for the three months ended March 31, 2015 and 2014 is as follows:

| <b>(Dollars in thousands)</b>  | <b>Assets</b> |                | <b>Liabilities</b> |  |
|--------------------------------|---------------|----------------|--------------------|--|
| Fair value, January 1, 2015    | \$            | <b>21,601</b>  | \$                 |  |
| Mortgage and other loan income |               | <b>(1,673)</b> |                    |  |
| Purchases and issuances        |               | <b>1,582</b>   |                    |  |
| Fair value, March 31, 2015     | \$            | <b>21,510</b>  | \$                 |  |
| Fair value, January 1, 2014    | \$            | 20,729         | \$                 |  |
| Mortgage and other loan income |               | (664)          |                    |  |
| Purchases and issuances        |               | 860            |                    |  |
| Fair value, March 31, 2014     | \$            | 20,925         | \$                 |  |

There were no unrealized losses included in accumulated other comprehensive income related to Level 3 financial assets and liabilities at March 31, 2015 or 2014.

See Note 19 Loan Servicing, Mortgage Obligation, and Loans Held for Sale for information about recurring Level 3 fair value measurements of mortgage servicing rights.

*Assets and Liabilities Recorded at Fair Value on a Nonrecurring Basis*

The tables below present the recorded amount of assets and liabilities measured at fair value on a nonrecurring basis:

**Quoted Prices**

Edgar Filing: SOUTH STATE Corp - Form 10-Q

| (Dollars in thousands)      | Fair Value | In Active<br>Markets<br>for Identical<br>Assets<br>(Level 1) | Significant<br>Other<br>Observable<br>Inputs<br>(Level 2) | Significant<br>Unobservable<br>Inputs<br>(Level 3) |
|-----------------------------|------------|--------------------------------------------------------------|-----------------------------------------------------------|----------------------------------------------------|
| <b>March 31, 2015:</b>      |            |                                                              |                                                           |                                                    |
| OREO                        | \$ 36,096  | \$                                                           | \$                                                        | \$ 36,096                                          |
| Non-acquired impaired loans | 6,636      |                                                              |                                                           | 6,636                                              |
| <b>December 31, 2014:</b>   |            |                                                              |                                                           |                                                    |
| OREO                        | \$ 42,726  | \$                                                           | \$                                                        | \$ 42,726                                          |
| Non-acquired impaired loans | 12,612     |                                                              |                                                           | 12,612                                             |
| <b>March 31, 2014:</b>      |            |                                                              |                                                           |                                                    |
| OREO                        | \$ 64,147  | \$                                                           | \$                                                        | \$ 64,147                                          |
| Non-acquired impaired loans | 4,725      |                                                              |                                                           | 4,725                                              |

Table of Contents**Note 14 Fair Value (Continued)***Quantitative Information about Level 3 Fair Value Measurements as of March 31, 2015*

|                                   | Valuation Technique   | Unobservable Input                               | General Range | Weighted Average |
|-----------------------------------|-----------------------|--------------------------------------------------|---------------|------------------|
| <b>Nonrecurring measurements:</b> |                       |                                                  |               |                  |
| Impaired loans                    | Discounted appraisals | Collateral discounts                             | 0-25%         | 4.53%            |
| OREO                              | Discounted appraisals | Collateral discounts and estimated costs to sell | 0-50%         | 18.45%           |

*Fair Value of Financial Instruments*

The following methods and assumptions were used by the Company in estimating its fair value disclosures for financial instruments. In cases where quoted market prices are not available, fair values are based on estimates using present value or other valuation techniques. Those models are significantly affected by the assumptions used, including the discount rates and estimates of future cash flows. In that regard, the derived fair value estimates cannot be substantiated by comparison to independent markets and, in many cases, could not be realized in immediate settlement of the instrument. The use of different methodologies may have a material effect on the estimated fair value amounts. The fair value estimates presented herein are based on pertinent information available to management as of March 31, 2015, December 31, 2014 and March 31, 2014. Such amounts have not been revalued for purposes of these consolidated financial statements since those dates and, therefore, current estimates of fair value may differ significantly from the amounts presented herein.

The following methods and assumptions were used to estimate the fair value of each class of financial instruments for which it is practicable to estimate that value:

*Cash and Cash Equivalents* The carrying amount is a reasonable estimate of fair value.

*Investment Securities* Securities held to maturity are valued at quoted market prices or dealer quotes. The carrying value of FHLB stock approximates fair value based on the redemption provisions. The carrying value of the Company's investment in unconsolidated subsidiaries approximates fair value. See Note 5 Investment Securities for additional information, as well as page 34 regarding fair value.

*Loans held for sale* The fair values disclosed for loans held for sale are based on commitments from investors for loans with similar characteristics.

*Loans* For variable-rate loans that reprice frequently and with no significant change in credit risk, fair values are based on carrying values. Fair values for certain mortgage loans (e.g., one-to-four family residential) and other consumer loans are estimated using discounted cash flow

## Edgar Filing: SOUTH STATE Corp - Form 10-Q

analyses based on the Company's current rates offered for new loans of the same type, structure and credit quality. Fair values for other loans (e.g., commercial real estate and investment property mortgage loans, commercial and industrial loans) are estimated using discounted cash flow analyses, using interest rates currently being offered by the Company for loans with similar terms to borrowers of similar credit quality. Fair values for non-performing loans are estimated using discounted cash flow analyses or underlying collateral values, where applicable.

*FDIC Receivable for Loss Share Agreements* The fair value is estimated based on discounted future cash flows using current discount rates.

*Deposit Liabilities* The fair values disclosed for demand deposits (e.g., interest and non-interest bearing checking, passbook savings, and certain types of money market accounts) are, by definition, equal to the amount payable on demand at the reporting date (i.e., their carrying amounts). The carrying amounts of variable-rate, fixed-term money market accounts, and certificates of deposit approximate their fair values at the reporting date. Fair values for fixed-rate certificates of deposit are estimated using a discounted cash flow calculation that applies interest rates currently being offered on certificates to a schedule of aggregated expected monthly maturities on time deposits.

*Federal Funds Purchased and Securities Sold Under Agreements to Repurchase* The carrying amount of federal funds purchased, borrowings under repurchase agreements, and other short-term borrowings maturing within ninety days approximate their fair values.

*Other Borrowings* The fair value of other borrowings is estimated using discounted cash flow analysis on the Company's current incremental borrowing rates for similar types of instruments.

*Accrued Interest* The carrying amounts of accrued interest approximate fair value.

Table of Contents

**Note 14 Fair Value (Continued)**

*Derivative Financial Instruments* The fair value of derivative financial instruments (including interest rate swaps) is estimated using pricing models of derivatives with similar characteristics.

*Commitments to Extend Credit, Standby Letters of Credit and Financial Guarantees* The fair values of commitments to extend credit are estimated using the fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the present creditworthiness of the counterparties. For fixed-rate loan commitments, fair value also considers the difference between current levels of interest rates and the committed rates. The fair values of guarantees and letters of credit are based on fees currently charged for similar agreements or on the estimated costs to terminate them or otherwise settle the obligations with the counterparties at the reporting date.

Table of Contents**Note 14 Fair Value (Continued)**

The estimated fair value, and related carrying amount, of the Company's financial instruments are as follows:

| (Dollars in thousands)                                                        | Carrying<br>Amount | Fair<br>Value | Level 1    | Level 2   | Level 3   |
|-------------------------------------------------------------------------------|--------------------|---------------|------------|-----------|-----------|
| <b>March 31, 2015</b>                                                         |                    |               |            |           |           |
| <b>Financial assets:</b>                                                      |                    |               |            |           |           |
| Cash and cash equivalents                                                     | \$ 630,734         | \$ 630,734    | \$ 630,734 | \$        |           |
| Investment securities                                                         | 827,086            | 827,659       | 12,284     | 815,375   |           |
| Loans held for sale                                                           | 87,342             | 87,342        |            | 87,342    |           |
| Loans, net of allowance for loan losses                                       | 5,666,720          | 5,747,502     |            |           | 5,747,502 |
| FDIC receivable for loss share agreements                                     | 16,713             | 6,646         |            |           | 6,646     |
| Accrued interest receivable                                                   | 16,255             | 16,255        |            | 3,637     | 12,618    |
| Mortgage servicing rights                                                     | 21,510             | 21,510        |            |           | 21,510    |
| Interest rate swap non-designated hedge                                       | 178                | 178           |            | 178       |           |
| Other derivative financial instruments<br>(mortgage banking related)          | 2,982              | 2,982         |            | 2,982     |           |
| <b>Financial liabilities:</b>                                                 |                    |               |            |           |           |
| Deposits                                                                      | 6,633,657          | 6,381,486     |            | 6,381,486 |           |
| Federal funds purchased and securities sold<br>under agreements to repurchase | 276,774            | 276,774       |            | 276,774   |           |
| Other borrowings                                                              | 55,003             | 51,623        |            | 51,623    |           |
| Accrued interest payable                                                      | 3,163              | 3,163         |            | 3,163     |           |
| Interest rate swap cash flow hedge                                            | 900                | 900           |            | 900       |           |
| Interest rate swap non-designated hedge                                       | 178                | 178           |            | 178       |           |
| Other derivative financial instruments<br>(mortgage banking related)          | 530                | 530           |            | 530       |           |
| <b>Off balance sheet financial instruments:</b>                               |                    |               |            |           |           |
| Commitments to extend credit                                                  |                    | 18,005        |            | 18,005    |           |
| Standby letters of credit and financial<br>guarantees                         |                    |               |            |           |           |
| <b>December 31, 2014</b>                                                      |                    |               |            |           |           |
| <b>Financial assets:</b>                                                      |                    |               |            |           |           |
| Cash and cash equivalents                                                     | \$ 417,869         | \$ 417,869    | \$ 417,869 | \$        |           |
| Investment securities                                                         | 826,943            | 827,517       | 13,560     | 813,957   |           |
| Loans held for sale                                                           | 61,934             | 61,934        |            | 61,934    |           |
| Loans, net of allowance for loan losses                                       | 5,680,688          | 5,743,111     |            |           | 5,743,111 |
| FDIC receivable for loss share agreements                                     | 22,161             | 7,150         |            |           | 7,150     |
| Accrued interest receivable                                                   | 16,366             | 16,366        |            | 3,443     | 12,923    |
| Mortgage servicing rights                                                     | 21,601             | 21,601        |            |           | 21,601    |
| Interest rate swap non-designated hedge                                       | 172                | 172           |            | 172       |           |
| Other derivative financial instruments<br>(mortgage banking related)          | 1,976              | 1,976         |            | 1,976     |           |
| <b>Financial liabilities:</b>                                                 |                    |               |            |           |           |
| Deposits                                                                      | 6,461,045          | 6,193,580     |            | 6,193,580 |           |
| Federal funds purchased and securities sold<br>under agreements to repurchase | 221,541            | 221,541       |            | 221,541   |           |
| Other borrowings                                                              | 101,210            | 98,534        |            | 98,534    |           |
| Accrued interest payable                                                      | 4,311              | 4,311         |            | 4,311     |           |
| Interest rate swap cash flow hedge                                            | 856                | 856           |            | 856       |           |

Edgar Filing: SOUTH STATE Corp - Form 10-Q

|                                                    |     |        |        |
|----------------------------------------------------|-----|--------|--------|
| Interest rate swap non-designated hedge            | 172 | 172    | 172    |
| Other derivative financial instruments             |     |        |        |
| (mortgage banking related)                         | 313 | 313    | 313    |
| <b>Off balance sheet financial instruments:</b>    |     |        |        |
| Commitments to extend credit                       |     | 14,600 | 14,600 |
| Standby letters of credit and financial guarantees |     |        |        |

Table of Contents**Note 14 Fair Value (Continued)**

| (Dollars in thousands)                                                     | Carrying<br>Amount | Fair<br>Value | Level 1    | Level 2   | Level 3   |
|----------------------------------------------------------------------------|--------------------|---------------|------------|-----------|-----------|
| <b>March 31, 2014</b>                                                      |                    |               |            |           |           |
| <b>Financial assets:</b>                                                   |                    |               |            |           |           |
| Cash and cash equivalents                                                  | \$ 612,615         | \$ 612,615    | \$ 612,615 | \$        | \$        |
| Investment securities                                                      | 814,533            | 815,069       | 13,799     | 801,270   |           |
| Loans held for sale                                                        | 57,609             | 57,609        |            | 57,609    |           |
| Loans, net of allowance for loan losses                                    | 5,571,253          | 5,636,854     |            |           | 5,636,854 |
| FDIC receivable for loss share agreements                                  | 60,484             | 35,255        |            |           | 35,255    |
| Accrued interest receivable                                                | 15,389             | 15,389        |            | 3,963     | 11,426    |
| Mortgage servicing rights                                                  | 20,925             | 20,925        |            |           | 20,925    |
| Interest rate swap non-designated hedge                                    | 178                | 178           |            | 178       |           |
| Other derivative financial instruments (mortgage banking related)          | 574                | 574           |            | 574       |           |
| <b>Financial liabilities:</b>                                              |                    |               |            |           |           |
| Deposits                                                                   | 6,634,551          | 6,370,810     |            | 6,370,810 |           |
| Federal funds purchased and securities sold under agreements to repurchase | 254,985            | 254,985       |            | 254,985   |           |
| Other borrowings                                                           | 100,963            | 102,971       |            | 102,971   |           |
| Accrued interest payable                                                   | 4,854              | 4,854         |            | 4,854     |           |
| Interest rate swap cash flow hedge                                         | 909                | 909           |            | 909       |           |
| Interest rate swap non-designated hedge                                    | 178                | 178           |            | 178       |           |
| Other derivative financial instruments (mortgage banking related)          | 374                | 374           |            | 374       |           |
| <b>Off balance sheet financial instruments:</b>                            |                    |               |            |           |           |
| Commitments to extend credit                                               |                    | 15,494        |            | 15,494    |           |
| Standby letters of credit and financial guarantees                         |                    |               |            |           |           |

**Note 15 Accumulated Other Comprehensive Income (Loss)**

The changes in each components of accumulated other comprehensive income (loss), net of tax, were as follows:

| (Dollars in thousands)                                                  | Benefit<br>Plans | Unrealized Gains<br>and Losses<br>on Securities<br>Available<br>for Sale | Gains and<br>Losses on<br>Cash Flow<br>Hedges | Total    |
|-------------------------------------------------------------------------|------------------|--------------------------------------------------------------------------|-----------------------------------------------|----------|
| <b>Three months ended March 31, 2015</b>                                |                  |                                                                          |                                               |          |
| Balance at December 31, 2014                                            | \$ (5,315)       | \$ 5,467                                                                 | \$ (529)                                      | \$ (377) |
| Other comprehensive income (loss) before reclassifications              |                  | 3,263                                                                    | (75)                                          | 3,188    |
| Amounts reclassified from accumulated other comprehensive income (loss) | 140              |                                                                          | 47                                            | 187      |
| Net comprehensive income (loss)                                         | 140              | 3,263                                                                    | (28)                                          | 3,375    |
| Balance at March 31, 2015                                               | \$ (5,175)       | \$ 8,730                                                                 | \$ (557)                                      | \$ 2,998 |

Edgar Filing: SOUTH STATE Corp - Form 10-Q

**Three months ended March 31, 2014**

|                                                                         |    |         |    |         |    |       |    |         |
|-------------------------------------------------------------------------|----|---------|----|---------|----|-------|----|---------|
| Balance at December 31, 2013                                            | \$ | (3,585) | \$ | (5,573) | \$ | (565) | \$ | (9,723) |
| Other comprehensive income (loss) before reclassifications              |    |         |    | 5,666   |    | (44)  |    | 5,622   |
| Amounts reclassified from accumulated other comprehensive income (loss) |    |         |    |         |    | 47    |    | 47      |
| Net comprehensive income (loss)                                         |    |         |    | 5,666   |    | 3     |    | 5,669   |
| Balance at March 31, 2014                                               | \$ | (3,585) | \$ | 93      | \$ | (562) | \$ | (4,054) |

Table of Contents**Note 15 Accumulated Other Comprehensive Income (Loss) (Continued)**

The table below presents the reclassifications out of accumulated other comprehensive income (loss), net of tax:

| (Dollars in thousands)<br>Accumulated Other Comprehensive<br>Income (Loss) Component | Amount Reclassified from Accumulated<br>Other Comprehensive Income (Loss)<br>Three Months Ended March 31, |       | Income Statement Line Item Affected |
|--------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------|-------|-------------------------------------|
|                                                                                      | 2015                                                                                                      | 2014  |                                     |
| Gains and losses on cash flow hedges:                                                |                                                                                                           |       |                                     |
| Interest rate contracts                                                              | \$ 76                                                                                                     | \$ 76 | Interest expense                    |
|                                                                                      | (29)                                                                                                      | (29)  | Provision for income taxes          |
|                                                                                      | 47                                                                                                        | 47    | Net income                          |
| Amortization of defined benefit<br>pension items:                                    |                                                                                                           |       |                                     |
| Actuarial losses                                                                     | \$ 226                                                                                                    | \$    | Salaries and employee benefits      |
|                                                                                      | (86)                                                                                                      |       | Provision for income taxes          |
|                                                                                      | 140                                                                                                       |       | Net income                          |
| Total reclassifications for the period                                               | \$ 187                                                                                                    | \$ 47 |                                     |

**Note 16 Derivative Financial Instruments*****Cash Flow Hedge of Interest Rate Risk***

The Company utilizes this interest rate swap agreement to convert a portion of its variable-rate debt to a fixed rate (cash flow hedge). During 2009, the Company entered into a forward starting interest rate swap agreement with a notional amount of \$8.0 million to manage interest rate risk due to periodic rate resets on its junior subordinated debt issued by SCBT Capital Trust II, an unconsolidated subsidiary of the Company established for the purpose of issuing trust preferred securities. The Company hedges the variable rate cash flows of subordinated debt against future interest rate increases by using an interest rate swap that effectively fixed the rate on the debt beginning on June 15, 2010, at which time the debt contractually converted from a fixed interest rate to a variable interest rate. This hedge expires on June 15, 2019. The notional amount on which the interest payments are based will not be exchanged. This derivatives contract calls for the Company to pay a fixed rate of 4.06% on \$8.0 million notional amount and receive a variable rate of three-month LIBOR on the \$8.0 million notional amount.

The Company recognized an after-tax unrealized loss on its cash flow hedge in other comprehensive income of \$28,000 for the three months ended March 31, 2015, compared to an after-tax unrealized gain on its cash flow hedge in other comprehensive income of less than \$3,000 for the three months ended March 31, 2014, respectively. The Company recognized a \$900,000 cash flow hedge liability in other liabilities on the balance sheet at March 31, 2015, compared to a \$908,000 liability recognized at March 31, 2014. There was no ineffectiveness in the cash flow hedge during the three months ended March 31, 2015 and 2014.

Credit risk related to the derivative arises when amounts receivable from the counterparty (derivatives dealer) exceed those payable. The Company controls the risk of loss by only transacting with derivatives dealers that are national market makers whose credit ratings are strong. Each party to the interest rate swap is required to provide collateral in the form of cash or securities to the counterparty when the counterparty's

## Edgar Filing: SOUTH STATE Corp - Form 10-Q

exposure to a mark-to-market replacement value exceeds certain negotiated limits. These limits are typically based on current credit ratings and vary with ratings changes. As of March 31, 2015 and 2014, the Company provided \$950,000 and \$1.0 million of collateral, respectively, which is included in cash and cash equivalents on the balance sheet as interest-bearing deposits with banks. Also, the Company has a netting agreement with the counterparty.

### ***Non-designated Hedges of Interest Rate Risk***

#### *Customer Swap*

As of March 31, 2015, the Company has two interest rate swap contracts that were classified as non-designated hedges that were acquired through the merger transaction with Savannah. These derivatives are not designated as hedges and are not speculative in nature. One of the derivatives is an interest rate swap that was executed with a commercial borrower to facilitate a respective risk management strategy and allow the customer to pay a fixed rate of interest to the Company. This interest rate swap was simultaneously hedged by executing an offsetting interest rate swap that was entered into with a derivatives dealer to minimize the net risk exposure to the Company resulting from the transactions and allow the Company to receive a variable rate of interest.

Table of Contents

**Note 16 Derivative Financial Instruments (Continued)**

The interest rate swap contract with the commercial borrower requires the borrower to pay or receive from the Company an amount equal to and offsetting the value of the interest rate swap. If the commercial borrower fails to perform and the market value for the interest rate swap with the derivatives dealer is negative (net liability position), the Company would be obligated to pay the settlement amount for the financial derivative with the dealer. If the market value for the interest rate swap with the derivatives dealer is positive (net asset position), the Company would receive a payment for the settlement amount for the financial derivative with the dealer. The settlement amount is determined by the fluctuation of interest rates.

As the interest rate swaps associated with this program do not meet the strict hedge accounting requirements, changes in the fair value of both the customer swaps and the offsetting swaps are recognized directly in earnings. As of March 31, 2015, the interest rate swaps had an aggregate notional amount of approximately \$3.9 million and the fair value of these two interest rate swap derivatives are recorded in other assets and in other liabilities for \$178,000 on the balance sheet. The net effect of recording the derivatives at fair value through earnings was immaterial to the Company's financial condition and results of operations during 2015.

The Company also has an agreement with the derivatives dealer in this transaction that contains a provision where if the Company defaults on any of its indebtedness, including default where repayment of the indebtedness has not been accelerated by the lender, then the Company could also be declared in default on this derivatives obligation. As of March 31, 2015, the fair value of the interest rate swap derivative with the derivatives dealer was in a net liability position of \$178,000, which excludes any adjustment for nonperformance risk, related to these agreements. As of March 31, 2015, the Company provided \$355,000 of collateral, which is included in cash and cash equivalents on the balance sheet as interest-bearing deposits with banks. If the Company had breached any of these provisions at March 31, 2015, it would have been required to settle its obligations under the agreement at the termination value, \$184,000.

*Mortgage Banking*

The Company also has derivatives contracts that are classified as non-designated hedges. These derivatives contracts are a part of the Company's risk management strategy for its mortgage banking activities. These instruments may include financial forwards, futures contracts, and options written and purchased, which are used to hedge mortgage servicing rights; while when-issued securities are typically used to hedge the mortgage pipeline. Such instruments derive their cash flows, and therefore their values, by reference to an underlying instrument, index or referenced interest rate. The Company does not elect hedge accounting treatment for any of these derivative instruments and as a result, changes in fair value of the instruments (both gains and losses) are recorded in the Company's consolidated statements of income in mortgage banking income.

*Mortgage Servicing Rights*

Derivatives contracts related to mortgage servicing rights are used to help offset changes in fair value and are written in amounts referred to as notional amounts. Notional amounts provide a basis for calculating payments between counterparties but do not represent amounts to be exchanged between the parties, and are not a measure of financial risk. On March 31, 2015, the Company had derivative financial instruments outstanding with notional amounts totaling \$93.0 million related to mortgage servicing rights. The estimated net fair value of the open contracts related to the mortgage servicing rights was recorded as a gain of \$368,000 at March 31, 2015.

*Mortgage Pipeline*

The following table presents the Company's notional value of forward sale commitments and the fair value of those obligations along with the fair value of the mortgage pipeline.

| <b>(Dollars in thousands)</b>                    | <b>March 31, 2015</b> | <b>December 31, 2014</b> | <b>March 31, 2014</b> |
|--------------------------------------------------|-----------------------|--------------------------|-----------------------|
| Mortgage loan pipeline                           | \$ <b>135,542</b>     | \$ 67,201                | \$ 68,433             |
| Expected closures                                | <b>101,657</b>        | 50,760                   | 51,325                |
| Fair Value of mortgage loan pipeline commitments | <b>2,613</b>          | 1,335                    | 490                   |
| Forward commitments                              | <b>154,000</b>        | 81,000                   | 60,000                |
| Fair value of forward commitments                | <b>(530)</b>          | (313)                    | 84                    |

Table of Contents

**Note 17 Capital Ratios**

The Company is subject to regulations with respect to certain risk-based capital ratios. These risk-based capital ratios measure the relationship of capital to a combination of balance sheet and off-balance sheet risks. The values of both balance sheet and off-balance sheet items are adjusted based on the rules to reflect categorical credit risk. In addition to the risk-based capital ratios, the regulatory agencies have also established a leverage ratio for assessing capital adequacy. The leverage ratio is equal to Tier 1 capital divided by total consolidated on-balance sheet assets (minus amounts deducted from Tier 1 capital). The leverage ratio does not involve assigning risk weights to assets.

In July 2013, the Federal Reserve announced its approval of a final rule to implement the regulatory capital reforms developed by the Basel Committee on Banking Supervision ( Basel III ), among other changes required by the Dodd-Frank Wall Street Reform and Consumer Protection Act. The new rules became effective January 1, 2015, subject to a phase-in period for certain aspects of the new rules.

As applied to the Company and the Bank, the new rules include a new minimum ratio of common equity Tier 1 capital ( CET1 ) to risk-weighted assets of 4.5%. The new rules also raise the minimum required ratio of Tier 1 capital to risk-weighted assets from 4% to 6%. The minimum required leverage ratio under the new rules is 4%. The minimum required total capital to risk-weighted assets ratio remains at 8% under the new rules.

In order to avoid restrictions on capital distributions and discretionary bonus payments to executives, under the new rules a covered banking organization will also be required to maintain a capital conservation buffer in addition to its minimum risk-based capital requirements. This buffer will be required to consist solely of common equity Tier 1, and the buffer will apply to all three risk-based measurements (CET1, Tier 1 capital and total capital). The capital conservation buffer will be phased in incrementally over time, beginning January 1, 2016 and becoming fully effective on January 1, 2019, and will ultimately consist of an additional amount of Tier 1 common equity equal to 2.5% of risk-weighted assets.

The Bank is also subject to the regulatory framework for prompt corrective action, which identifies five capital categories for insured depository institutions (well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized, and critically undercapitalized) and is based on specified thresholds for each of the three risk-based regulatory capital ratios (CET1, Tier 1 capital and total capital) and for the leverage ratio.

The following table presents actual and required capital ratios as of March 31, 2015 for the Company and the Bank under the Basel III capital rules. The minimum required capital amounts presented include the minimum required capital levels as of March 31, 2015 based on the phase-in provisions of the Basel III Capital Rules and the minimum required capital levels as of January 1, 2019 when the Basel III Capital Rules have been fully phased-in. Capital levels required to be considered well capitalized are based upon prompt corrective action regulations, as amended to reflect the changes under the Basel III Capital Rules.

| (Dollars in thousands) | Actual         |       | Minimum Capital Required - Basel III Phase-In Schedule |       | Minimum Capital Required - Basel III Fully Phased-In |       | Required to be Considered Well Capitalized |       |
|------------------------|----------------|-------|--------------------------------------------------------|-------|------------------------------------------------------|-------|--------------------------------------------|-------|
|                        | Capital Amount | Ratio | Capital Amount                                         | Ratio | Capital Amount                                       | Ratio | Capital Amount                             | Ratio |

Edgar Filing: SOUTH STATE Corp - Form 10-Q

**March 31, 2015**

Common equity Tier 1 to  
risk-weighted assets:

|                             |    |         |        |    |         |       |    |         |       |    |         |       |
|-----------------------------|----|---------|--------|----|---------|-------|----|---------|-------|----|---------|-------|
| Consolidated                | \$ | 670,750 | 12.26% | \$ | 246,398 | 4.50% | \$ | 383,286 | 7.00% | \$ | 355,908 | 6.50% |
| South State Bank (the Bank) |    | 707,542 | 12.93% |    | 246,287 | 4.50% |    | 383,113 | 7.00% |    | 355,748 | 6.50% |

Tier 1 capital to  
risk-weighted assets:

|                             |  |         |        |  |         |       |  |         |       |  |         |       |
|-----------------------------|--|---------|--------|--|---------|-------|--|---------|-------|--|---------|-------|
| Consolidated                |  | 721,069 | 13.18% |  | 328,531 | 6.00% |  | 465,418 | 8.50% |  | 438,041 | 8.00% |
| South State Bank (the Bank) |  | 707,542 | 12.93% |  | 328,383 | 6.00% |  | 465,209 | 8.50% |  | 437,843 | 8.00% |

Total capital to  
risk-weighted assets:

|                             |  |         |        |  |         |       |  |         |        |  |         |        |
|-----------------------------|--|---------|--------|--|---------|-------|--|---------|--------|--|---------|--------|
| Consolidated                |  | 759,534 | 13.89% |  | 438,041 | 8.00% |  | 574,928 | 10.50% |  | 547,551 | 10.00% |
| South State Bank (the Bank) |  | 746,008 | 13.63% |  | 437,843 | 8.00% |  | 574,669 | 10.50% |  | 547,304 | 10.00% |

Tier 1 capital to average  
assets (leverage ratio):

|                             |  |         |       |  |         |       |  |         |       |  |         |       |
|-----------------------------|--|---------|-------|--|---------|-------|--|---------|-------|--|---------|-------|
| Consolidated                |  | 721,069 | 9.53% |  | 302,558 | 4.00% |  | 302,558 | 4.00% |  | 378,197 | 5.00% |
| South State Bank (the Bank) |  | 707,542 | 9.36% |  | 302,391 | 4.00% |  | 302,391 | 4.00% |  | 377,989 | 5.00% |

Table of Contents**Note 17 Capital Ratios (Continued)**

The following table presents actual and required capital ratios as of December 31, 2014 and March 31, 2014 under the regulatory capital rules then in effect.

| (Dollars in thousands)                             | Actual     |        | Minimum Capital Requirement |       | Required to be Considered Well Capitalized |        |
|----------------------------------------------------|------------|--------|-----------------------------|-------|--------------------------------------------|--------|
|                                                    | Amount     | Ratio  | Amount                      | Ratio | Amount                                     | Ratio  |
| <b>December 31, 2014</b>                           |            |        |                             |       |                                            |        |
| Tier 1 capital to risk-weighted assets:            |            |        |                             |       |                                            |        |
| Consolidated                                       | \$ 713,371 | 13.62% | \$ 209,491                  | 4.00% | n/a                                        | n/a    |
| South State Bank (the Bank)                        | 700,280    | 13.37% | 209,438                     | 4.00% | 314,158                                    | 6.00%  |
| Total capital to risk-weighted assets:             |            |        |                             |       |                                            |        |
| Consolidated                                       | 755,484    | 14.43% | 418,982                     | 8.00% | n/a                                        | n/a    |
| South State Bank (the Bank)                        | 742,393    | 14.18% | 418,877                     | 8.00% | 523,596                                    | 10.00% |
| Tier 1 capital to average assets (leverage ratio): |            |        |                             |       |                                            |        |
| Consolidated                                       | 713,371    | 9.47%  | 301,363                     | 4.00% | n/a                                        | n/a    |
| South State Bank (the Bank)                        | 700,280    | 9.30%  | 301,162                     | 4.00% | 376,452                                    | 5.00%  |
| <b>March 31, 2014</b>                              |            |        |                             |       |                                            |        |
| Tier 1 capital to risk-weighted assets:            |            |        |                             |       |                                            |        |
| Consolidated                                       | \$ 658,325 | 12.78% | \$ 206,124                  | 4.00% | n/a                                        | n/a    |
| South State Bank (the Bank)                        | 647,379    | 12.56% | 206,105                     | 4.00% | 309,158                                    | 6.00%  |
| Total capital to risk-weighted assets:             |            |        |                             |       |                                            |        |
| Consolidated                                       | 704,404    | 13.67% | 412,247                     | 8.00% | n/a                                        | n/a    |
| South State Bank (the Bank)                        | 693,322    | 13.46% | 412,210                     | 8.00% | 515,263                                    | 10.00% |
| Tier 1 capital to average assets (leverage ratio): |            |        |                             |       |                                            |        |
| Consolidated                                       | 658,325    | 8.68%  | 303,317                     | 4.00% | n/a                                        | n/a    |
| South State Bank (the Bank)                        | 647,379    | 8.54%  | 303,115                     | 4.00% | 378,893                                    | 5.00%  |

As of March 31, 2015, December 31, 2014, and March 31, 2014, the capital ratios of the Company and the Bank were well in excess of the minimum regulatory requirements and exceeded the thresholds for the well capitalized regulatory classification.

**Note 18 Goodwill and Other Intangible Assets**

## Edgar Filing: SOUTH STATE Corp - Form 10-Q

The carrying amount of goodwill was \$317.7 million at March 31, 2015. The Company's other intangible assets, consisting of core deposit intangibles, noncompete intangibles, and client list intangibles are included on the face of the balance sheet. The following is a summary of gross carrying amounts and accumulated amortization of other intangible assets:

| (Dollars in thousands)   | March 31,<br>2015 | December 31,<br>2014 | March 31,<br>2014 |
|--------------------------|-------------------|----------------------|-------------------|
| Gross carrying amount    | \$ 75,354         | \$ 75,354            | \$ 77,660         |
| Accumulated amortization | (28,131)          | (26,115)             | (20,092)          |
|                          | \$ 47,223         | \$ 49,239            | \$ 57,568         |

Amortization expense totaled \$2.0 million and \$2.1 million for the three months ended March 31, 2015, and 2014, respectively. Other intangibles are amortized using either the straight-line method or an accelerated basis over their estimated useful lives, with lives generally between two and 15 years. Estimated amortization expense for other intangibles for each of the next five quarters is as follows:

| (Dollars in thousands) |           |
|------------------------|-----------|
| Quarters ending:       |           |
| June 30, 2015          | \$ 1,963  |
| September 30, 2015     | 1,963     |
| December 31, 2015      | 1,948     |
| March 31, 2016         | 1,604     |
| June 30, 2016          | 1,592     |
| Thereafter             | 38,153    |
|                        | \$ 47,223 |

Table of Contents**Note 19 Loan Servicing, Mortgage Origination, and Loans Held for Sale**

As of March 31, 2015, December 31, 2014, and March 31, 2014, the portfolio of residential mortgages serviced for others, which is not included in the accompanying balance sheets, was \$2.4 billion, \$2.3 billion, and \$2.1 billion, respectively. Servicing loans for others generally consists of collecting mortgage payments, maintaining escrow accounts and disbursing payments to investors. The amount of contractually specified servicing fees earned by the Company during the three months ended March 31, 2015 and March 31, 2014 was \$1.5 million and \$1.3 million, respectively. Servicing fees are recorded in mortgage banking income in the Company's consolidated statements of income.

At March 31, 2015, December 31, 2014, and March 31, 2014, mortgage servicing rights (MSRs) were \$21.5 million, \$21.6 million, and \$20.9 million on the Company's consolidated balance sheets, respectively. MSRs are recorded at fair value with changes in fair value recorded as a component of mortgage banking income in the consolidated statements of income. The market value adjustments related to MSRs recorded in mortgage banking income for the three months ended March 31, 2015 and March 31, 2014 was a loss of \$836,000 and a loss of \$208,000, respectively. Since the merger with FFHI, the Company has used various free standing derivative instruments to mitigate the income statement effect of changes in fair value due to changes in market value adjustments and to changes in valuation inputs and assumptions related to MSRs.

The following table presents the changes in the fair value of MSRs and the offsetting hedge.

| (Dollars in thousands)             | Three Months Ended March 31, |          |
|------------------------------------|------------------------------|----------|
|                                    | 2015                         | 2014     |
| Decrease in fair value of MSRs     | \$ (836)                     | \$ (208) |
| Decay of MSRs                      | (837)                        | (456)    |
| Gains related to derivatives       | 1,522                        | 795      |
| Net effect on Statements of Income | \$ (151)                     | \$ 131   |

The following table is an analysis of the activity in the MSRs.

| (Dollars in thousands)                                            | Three Months Ended March 31, |           |
|-------------------------------------------------------------------|------------------------------|-----------|
|                                                                   | 2015                         | 2014      |
| Balance at beginning of the period                                | \$ 21,601                    | \$ 20,729 |
| Additions (deductions):                                           |                              |           |
| Servicing assets that resulted from transfers of financial assets | 1,582                        | 860       |
| Changes in fair value due to valuation inputs or assumptions      | (836)                        | (208)     |
| Decay in fair value:                                              |                              |           |
| Due to increases in principal paydowns or runoff                  | (837)                        | (456)     |
| Carrying value at end of period                                   | \$ 21,510                    | \$ 20,925 |

The fair value of MSRs is highly sensitive to changes in assumptions and fair value is determined by estimating the present value of the asset's future cash flows utilizing market-based prepayment rates, discount rates and other assumptions validated through comparison to trade information, industry surveys and with the use of independent third party appraisals. Changes in prepayment speed assumptions have the most significant impact on the fair value of MSRs. Generally, as interest rates decline, mortgage loan prepayments accelerate due to increased refinance activity, which results in a decrease in the fair value of the MSR. Measurement of fair value is limited to the conditions existing and the assumptions utilized as of a particular point in time, and those assumptions may not be appropriate if they are applied at a different time.



Table of Contents**Note 19 Loan Servicing, Mortgage Origination, and Loans Held for Sale (Continued)**

The characteristics and sensitivity analysis of the MSR are included in the following table.

| (Dollars in thousands)                                | March 31,<br>2015 | December 31,<br>2014 | March 31,<br>2014 |
|-------------------------------------------------------|-------------------|----------------------|-------------------|
| Composition of residential loans serviced for others  |                   |                      |                   |
| Fixed-rate mortgage loans                             | 99.3%             | 99.2%                | 99.0%             |
| Adjustable-rate mortgage loans                        | 0.7%              | 0.8%                 | 1.0%              |
| Total                                                 | 100.0%            | 100.0%               | 100.0%            |
| Weighted average life                                 | 6.09 years        | 6.30 years           | 6.68 years        |
| Constant prepayment rate                              | 12.0%             | 11.4%                | 10.5%             |
| Weighted average discount rate                        | 9.7%              | 9.7%                 | 9.9%              |
| Effect on fair value due to change in interest rates: |                   |                      |                   |
| 25 basis point increase                               | \$ 1,627          | \$ 1,365             | \$ 1,042          |
| 50 basis point increase                               | 3,059             | 2,555                | 1,937             |
| 25 basis point decrease                               | (1,813)           | (1,562)              | (1,218)           |
| 50 basis point decrease                               | (3,654)           | (3,221)              | (2,240)           |

The sensitivity calculations above are hypothetical and should not be considered to be predictive of future performance. Changes in fair value based on adverse changes in assumptions generally cannot be extrapolated because the relationship of the changes in assumptions to fair value may not be linear. Also, in this table, the effects of an adverse variation in a particular assumption on the fair value of the MSRs is calculated without changing any other assumptions, while in reality, changes in one factor may result in changing another, which may magnify or contract the effect of the change.

Custodial escrow balances maintained in connection with the loan servicing were \$14.4 million and \$13.2 million at March 31, 2015 and March 31, 2014.

Mandatory cash forwards and whole loan sales were \$196.0 million and \$115.6 million for the three months ended March 31, 2015 and March 31, 2014, respectively, of which \$147.1 million and \$84.2 million, or 75.1% and 72.3%, respectively, were sold with the servicing rights retained by the company.

Loans held for sale have historically been comprised of residential mortgage loans awaiting sale in the secondary market, which generally settle in 15 to 45 days. Loans held for sale, which consists primarily of residential mortgage loans to be sold in the secondary market, were \$87.3 million, \$61.9 million, and \$57.6 million at March 31, 2015, December 31, 2014, and March 31, 2014, respectively.

**Note 20 Investments in Qualified Affordable Housing Projects**

## Edgar Filing: SOUTH STATE Corp - Form 10-Q

The Company has investments in qualified affordable housing projects ( QAHPs ) that provide low income housing tax credits and operating loss benefits over an extended period. The tax credits and the operating loss tax benefits that are generated by each of the properties are expected to exceed the total value of the investment made by the Company. For the three months ended March 31, 2015, tax credits and other tax benefits of \$459,000 and amortization of \$327,000 were recorded. For the three months ended March 31, 2014, the Company recorded tax credits and other tax benefits of \$357,000 and amortization of \$153,000. At March 31, 2015 and 2014, the Company's carrying value of QAHPs was \$13.1 million and \$13.3 million, respectively, with an original investment of \$19.3 million. The Company has \$5.2 million and \$6.8 million in remaining funding obligations related to these QAHPs recorded in liabilities at March 31, 2015 and 2014, respectively. None of the original investment will be repaid. The investment in QAHPs is being accounted for using the equity method.

Table of Contents

**Note 21 Subsequent Events**

*Branch Initiatives*

On April 22, 2015, South State Bank, a wholly-owned subsidiary of the Company, entered into a Purchase Agreement to purchase 12 South Carolina branch locations and 1 Georgia branch location from Bank of America, N.A. The branches are located in Florence, Greenwood, Orangeburg, Sumter, Newberry, Batesburg-Leesville, Abbeville and Hartsville, South Carolina, as well as Hartwell, Georgia. The bank will be entering six new markets with this transaction and three markets which overlap. The Company expects the transaction to close in the third quarter of 2015, subject to bank regulatory approval and customary closing conditions. South State Bank anticipates assuming approximately \$580 million of deposits, \$3.0 million in loans and 34 ATMs. The Company will also pay a 5.5% deposit premium, on the 30 day average closing balance of deposits prior to closing.

The Company is also consolidating or selling 14 branches and ATM locations over the next two quarters. The total deposits equal approximately \$208 million. One-time costs are expected to be \$4.5 million incurred in the third and fourth quarter of 2015. In addition, the Company has entered into a contract to sell two of the 14 branches with deposits totaling approximately \$32.0 million and \$7.8 million in loans. The Company will receive a 3.5% deposit premium on the 30 day average closing balance of deposits prior to closing. The sale is expected to close in the fourth quarter of 2015, subject to regulatory approval.

Table of Contents

**Item 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

Management's Discussion and Analysis of Financial Condition and Results of Operations relates to the financial statements contained in this Quarterly Report beginning on page 1. For further information, refer to Management's Discussion and Analysis of Financial Condition and Results of Operations appearing in the Annual Report on Form 10-K for the year ended December 31, 2014.

**Overview**

We are a bank holding company headquartered in Columbia, South Carolina, and were incorporated under the laws of South Carolina in 1985. We provide a wide range of banking services and products to our customers through our wholly-owned bank subsidiary, South State Bank (the Bank), a South Carolina-chartered commercial bank that opened for business in 1934. The Bank also operates Minis & Co., Inc. and First Southeast 401k Fiduciaries, both wholly owned registered investment advisors; and First Southeast Investor Services, a wholly owned limited service broker dealer. The Company does not engage in any significant operations other than the ownership of our banking subsidiary.

At March 31, 2015, we had approximately \$8.0 billion in assets and 2,051 full-time equivalent employees. Through the Bank, we provide our customers with checking accounts, NOW accounts, savings and time deposits of various types, brokerage services and alternative investment products such as annuities and mutual funds, trust and asset management services, business loans, agriculture loans, real estate loans, personal use loans, home improvement loans, manufactured housing loans, automobile loans, credit cards, letters of credit, home equity lines of credit, safe deposit boxes, bank money orders, wire transfer services, correspondent banking services, and use of ATM facilities.

We have pursued, and continue to pursue, a growth strategy that focuses on organic growth, supplemented by acquisition of select financial institutions, or branches in certain market areas.

The following discussion describes our results of operations for the three months ended March 31, 2015 as compared to March 31, 2014 and also analyzes our financial condition as of March 31, 2015 as compared to December 31, 2014 and March 31, 2014. Like most financial institutions, we derive most of our income from interest we receive on our loans and investments. Our primary source of funds for making these loans and investments is our deposits, on which we may pay interest. Consequently, one of the key measures of our success is the amount of our net interest income, or the difference between the income on our interest-earning assets, such as loans and investments, and the expense on our interest-bearing liabilities, such as deposits. Another key measure is the spread between the yield we earn on these interest-earning assets and the rate we pay on our interest-bearing liabilities.

Of course, there are risks inherent in all loans, so we maintain an allowance for loan losses (sometimes referred to as ALLL) to absorb probable losses on existing loans that may become uncollectible. We establish and maintain this allowance by charging a provision for loan losses against our operating earnings. In the following section, we have included a detailed discussion of this process.

In addition to earning interest on our loans and investments, we earn income through fees we charge to our customers. We describe the various components of this noninterest income, as well as our noninterest expense, in the following discussion.

The following section also identifies significant factors that have affected our financial position and operating results during the periods included in the accompanying financial statements. We encourage you to read this discussion and analysis in conjunction with the financial statements and the related notes and the other statistical information also included in this report.

## **Recent Events**

### *Branch Initiatives*

On April 22, 2015, South State Bank, a wholly-owned subsidiary of the Company, entered into a Purchase Agreement to purchase 12 South Carolina branch locations and 1 Georgia branch location from Bank of America, N.A. The branches are located in Florence, Greenwood, Orangeburg, Sumter, Newberry, Batesburg-Leesville, Abbeville and Hartsville, South Carolina, as well as Hartwell, Georgia. The bank will be entering six new markets with this transaction and three markets which overlap. The Company expects the transaction to close in the third quarter of 2015, subject to bank regulatory approvals and customary closing conditions.

Table of Contents

South State Bank anticipates assuming approximately \$580 million of deposits, \$3.0 million in loans and 34 ATMs. The Company will also pay a 5.5% deposit premium on the 30 day average closing balance of deposits prior to closing.

The Company is also consolidating or selling 14 branches and ATM locations over the next two quarters. The total deposits equal approximately \$208 million. One-time costs are expected to be \$4.5 million incurred in the third and fourth quarter of 2015. In addition, the Company has entered into a contract to sell two of the 14 branches with deposits totaling approximately \$32.0 million and \$7.8 million in loans. The Company will receive a 3.5% deposit premium on the 30 day average closing balance of deposits prior to closing. The sale is expected to close in the fourth quarter of 2015, subject to regulatory approval.

**Critical Accounting Policies**

We have established various accounting policies that govern the application of accounting principles generally accepted in the United States ( GAAP ) in the preparation of our financial statements. Significant accounting policies are described in Note 1 to the audited consolidated financial statements in our Annual Report on Form 10-K for the year ended December 31, 2014. These policies may involve significant judgments and estimates that have a material impact on the carrying value of certain assets and liabilities. Different assumptions made in the application of these policies could result in material changes in our financial position and results of operations.

***Allowance for Loan Losses***

The allowance for loan losses reflects the estimated losses that will result from the inability of our bank's borrowers to make required loan payments. In determining an appropriate level for the allowance, we identify portions applicable to specific loans as well as providing amounts that are not identified with any specific loan but are derived with reference to actual loss experience, loan types, loan volumes, economic conditions, and industry standards. Changes in these factors may cause our estimate of the allowance to increase or decrease and result in adjustments to the provision for loan losses. See Note 6 Loans and Allowance for Loan Losses in this Form 10-Q, Provision for Loan Losses and Nonperforming Assets in this Management's Discussion and Analysis of Financial Condition and Results of Operation ( MD&A ) and Allowance for Loan Losses in Note 1 to the audited consolidated financial statements in our Annual Report on Form 10-K for the year ended December 31, 2014 for further detailed descriptions of our estimation process and methodology related to the allowance for loan losses.

***Goodwill and Other Intangible Assets***

Goodwill represents the excess of the purchase price over the sum of the estimated fair values of the tangible and identifiable intangible assets acquired less the estimated fair value of the liabilities assumed in a business combination. As of March 31, 2015, December 31, 2014 and March 31, 2014, the balance of goodwill was \$317.7 million. Goodwill has an indefinite useful life and is evaluated for impairment annually or more frequently if events and circumstances indicate that the asset might be impaired. An impairment loss is recognized to the extent that the carrying amount exceeds the asset's fair value. The goodwill impairment analysis is a two-step test. The first step, used to identify potential impairment, involves comparing each reporting unit's estimated fair value to its carrying value, including goodwill. If the estimated fair value of a reporting unit exceeds its carrying value, goodwill is not considered to be impaired. If the carrying value exceeds estimated fair value, there is an indication of potential impairment and the second step is performed to measure the amount of impairment, if any.

If required, the second step involves calculating an implied fair value of goodwill for each reporting unit for which the first step indicated impairment. The implied fair value of goodwill is determined in a manner similar to the amount of goodwill calculated in a business combination, by measuring the excess of the estimated fair value of the reporting unit, as determined in the first step, over the aggregate estimated fair values of the individual assets, liabilities and identifiable intangibles as if the reporting unit was being acquired in a business combination. If the implied fair value of goodwill exceeds the carrying value of goodwill assigned to the reporting unit, there is no impairment. If the carrying value of goodwill assigned to a reporting unit exceeds the implied fair value of the goodwill, an impairment charge is recorded for the excess. An impairment loss cannot exceed the carrying value of goodwill assigned to a reporting unit, and the loss establishes a new basis in the goodwill. Subsequent reversal of goodwill impairment losses is not permitted. Management has determined that the Company has two reporting units.

Our stock price has historically traded above its book value. As of March 31, 2015, book value was \$41.71 per common share. The lowest trading price during the first three months of 2015, as reported by the NASDAQ Global Select Market, was \$58.84 per share, and the stock price closed on March 31, 2015 at \$68.39 per share, which is above book value. In the event our stock was to consistently trade below its book value during the reporting period, we would consider performing an evaluation of the carrying value of goodwill as of the reporting date. Such a circumstance would be one factor in our evaluation that could result in an eventual goodwill impairment charge. We evaluated the carrying value of goodwill as of April 30, 2015, our annual test date,

Table of Contents

and determined that no impairment charge was necessary. Additionally, should our future earnings and cash flows decline and/or discount rates increase, an impairment charge to goodwill and other intangible assets may be required.

Core deposit intangibles, client list intangibles, and noncompetition ( noncompete ) intangibles consist of costs that resulted from the acquisition of other banks from other financial institutions. Core deposit intangibles represent the estimated value of long-term deposit relationships acquired in these transactions. Client list intangibles represent the value of long-term client relationships for the wealth and trust management business. Noncompete intangibles represent the value of key personnel relative to various competitive factors such as ability to compete, willingness or likelihood to compete, and feasibility based upon the competitive environment, and what the Bank could lose from competition. These costs are amortized over the estimated useful lives, such as deposit accounts in the case of core deposit intangible, on a method that we believe reasonably approximates the anticipated benefit stream from this intangible. The estimated useful lives are periodically reviewed for reasonableness.

***Income Taxes and Deferred Tax Assets***

Income taxes are provided for the tax effects of the transactions reported in the accompanying consolidated financial statements and consist of taxes currently due plus deferred taxes related primarily to differences between the basis of available-for-sale securities, allowance for loan losses, accumulated depreciation, net operating loss carryforwards, accretion income, deferred compensation, intangible assets, and pension plan and post-retirement benefits. The deferred tax assets and liabilities represent the future tax return consequences of those differences, which will either be taxable or deductible when the assets and liabilities are recovered or settled. Deferred tax assets and liabilities are reflected at income tax rates applicable to the period in which the deferred tax assets or liabilities are expected to be realized or settled. As changes in tax laws or rates are enacted, deferred tax assets and liabilities are adjusted through the provision for income taxes. The Company files a consolidated federal income tax return with its subsidiary.

The Company recognizes interest and penalties accrued relative to unrecognized tax benefits in its respective federal or state income taxes accounts. As of March 31, 2015, there were no accruals for uncertain tax positions and no accruals for interest and penalties. The Company and its subsidiary file a consolidated United States federal income tax return, as well as income tax returns for its subsidiary in the states of South Carolina, Georgia, North Carolina, Florida, Virginia, Alabama, and Mississippi. The Company's filed income tax returns are no longer subject to examination by taxing authorities for years before 2010.

***Other Real Estate Owned***

Other real estate owned ( OREO ), consisting of properties obtained through foreclosure or through a deed in lieu of foreclosure in satisfaction of loans or through reclassification of former branch sites, is reported at the lower of cost or fair value, determined on the basis of current valuations obtained principally from independent sources, adjusted for estimated selling costs. At the time of foreclosure or initial possession of collateral, any excess of the loan balance over the fair value of the real estate held as collateral is treated as a charge against the allowance for loan losses. Subsequent adjustments to this value are described below.

Subsequent declines in the fair value of OREO below the new cost basis are recorded through valuation adjustments. Significant judgments and complex estimates are required in estimating the fair value of OREO, and the period of time within which such estimates can be considered

## Edgar Filing: SOUTH STATE Corp - Form 10-Q

current is significantly shortened during periods of market volatility. In response to market conditions and other economic factors, management may utilize liquidation sales as part of its problem asset disposition strategy. As a result of the significant judgments required in estimating fair value and the variables involved in different methods of disposition, the net proceeds realized from sales transactions could differ significantly from the current valuations used to determine the fair value of OREO. Management reviews the value of OREO periodically and adjusts the values as appropriate. Revenue and expenses from OREO operations as well as gains or losses on sales and any subsequent adjustments to the value are recorded as OREO expense and loan related expense, a component of non-interest expense, and, for covered OREO, offset with an increase in the FDIC indemnification asset.

### ***Business Combinations, Method of Accounting for Loans Acquired, and FDIC Indemnification Asset***

We account for acquisitions under Financial Accounting Standards Board ( FASB ) Accounting Standards Codification ( ASC ) Topic 805, *Business Combinations*, which requires the use of the acquisition method of accounting. All identifiable assets acquired, including loans, are recorded at fair value. No allowance for loan losses related to the acquired loans is recorded on the acquisition date because the fair value of the loans acquired incorporates assumptions regarding credit risk.

Acquired credit-impaired loans are accounted for under the accounting guidance for loans and debt securities acquired with deteriorated credit quality, found in FASB ASC Topic 310-30, *Receivables Loans and Debt Securities Acquired with Deteriorated Credit Quality*, formerly American Institute of Certified Public Accountants ( AICPA ) Statement of Position (SOP) 03-3,

Table of Contents

*Accounting for Certain Loans or Debt Securities Acquired in a Transfer*, and initially measured at fair value, which includes estimated future credit losses expected to be incurred over the life of the loans. Loans acquired in business combinations with evidence of credit deterioration are considered impaired. Loans acquired through business combinations that do not meet the specific criteria of FASB ASC Topic 310-30, but for which a discount is attributable, at least in part to credit quality, are also accounted for under this guidance. Certain acquired loans, including performing loans and revolving lines of credit (consumer and commercial), are accounted for in accordance with FASB ASC Topic 310-20, where the discount is accreted through earnings based on estimated cash flows over the estimated life of the loan.

In accordance with FASB ASC Topic 805, the FDIC indemnification assets are initially recorded at fair value, and are measured separately from the loan assets and foreclosed assets because the loss sharing agreements are not contractually embedded in them or transferrable with them in the event of disposal. The FDIC indemnification asset is measured at carrying value subsequent to initial measurement. Improved cash flows of the underlying covered assets will result in impairment of the FDIC indemnification asset and amortization through non-interest income over the shorter of the lives of the FDIC indemnification asset or the underlying loans. Impairment of the underlying covered assets will result in improved cash flows of the FDIC indemnification asset and a credit to the provision for loan losses for acquired loans will result.

For further discussion of the Company's loan accounting and acquisitions, see Business Combinations and Method of Accounting for Loans Acquired in our Annual Report on Form 10-K for the year ended December 31, 2014, Note 4 Mergers and Acquisitions to the unaudited condensed consolidated financial statements and Note 6 Loans and Allowance for Loan Losses to the unaudited condensed consolidated financial statements.

**Results of Operations**

We reported consolidated net income available to common shareholders of \$23.9 million, or diluted earnings per share (EPS) of \$0.99, for the first quarter of 2015 as compared to consolidated net income available to common shareholders of \$15.8 million, or diluted EPS of \$0.66, in the comparable period of 2014. The \$8.1 million increase in consolidated net income available to common shareholders was the net result of the following items:

- An increase in noninterest income totaling \$6.0 million, due to a \$3.9 million reduction in the amortization of the FDIC indemnification asset and a \$3.3 million increase in mortgage banking income;
- Noninterest expense declined by \$6.9 million in the first quarter to \$70.5 million compared to the same quarter in 2014. The largest decreases were merger and branding related expenses of \$6.0 million and OREO and loan related expenses of \$1.2 million, which were partially offset by increases in salaries and employee benefits of \$1.9 million;
- An increase in the provision for income taxes of \$3.5 million due to higher pre-tax income; and
- Diluted EPS was \$0.99 compared to \$0.66 in the comparable period in 2014 due to the 51.0% increase in net income available to common shareholders.

Our asset quality related to non-acquired loans continues to be at manageable levels and improved from the end of 2014 and from the March 31, 2014 level. Non-acquired nonperforming assets declined from \$36.5 million at December 31, 2014 to \$34.1 million at March 31, 2015, a \$2.4

## Edgar Filing: SOUTH STATE Corp - Form 10-Q

million decline. Compared to the balance of nonperforming assets at March 31, 2014, nonperforming assets decreased \$15.6 million due to a reduction in nonperforming loans of \$9.9 million and a reduction in non-acquired OREO of \$5.8 million. Our non-acquired OREO decreased by \$1.5 million from the December 31, 2014 to \$6.4 million at March 31, 2015. During the first quarter of 2015, non-acquired classified assets declined by \$3.5 million from December 31, 2014 to \$67.3 million at March 31, 2015. Since March 31, 2014 non-acquired classified assets have declined by \$24.2 million. Annualized net recoveries for the first quarter of 2015 were 0.01%, down from net charge-offs in the first quarter of 2014 of 0.05% and from net charge-offs in the fourth quarter of 2014 of 0.13%.

The allowance for loan losses decreased to 0.94% of total non-acquired loans at March 31, 2015, down from 1.00% at December 31, 2014 and 1.16% at March 31, 2014. The allowance provides 1.22 times coverage of non-acquired nonperforming loans at March 31, 2015, higher than 1.21 times at December 31, 2014, and 0.93 times at March 31, 2014.

During the first quarter of 2015, the Company had net charge-offs related to acquired non-credit impaired loans which totaled \$1.8 million or 0.56% annualized, and accordingly, recorded a provision for loan losses. Additionally, we have \$7.4 million in nonperforming loans from this loan portfolio.

The Company performs ongoing assessments of the estimated cash flows of its acquired credit impaired loan portfolios. In general, increases in cash flow expectations result in a favorable adjustment to interest income over the remaining life of the related loans, and decreases in cash flow expectations result in an immediate recognition of a provision for loans losses, in both cases, net of any adjustments to the receivable from the FDIC for loss sharing for those assets that are covered. When a provision for loan

## Table of Contents

losses (impairments) has been recognized in earlier periods, subsequent improvement in cash flows will result in reversals of those impairments.

These ongoing assessments of the acquired loan portfolio resulted in reduced loan interest accretion due to continued decline in loan balances of both the acquired credit impaired and the acquired non-credit impaired portfolio. The overall credit mark for these loans continued to decline, partially from charge offs and partially from net improvement in expected cash flow. Below is a summary of the first quarter of 2015 assessment of the estimated cash flows of the acquired loan portfolio and the related impact on the indemnification asset:

- Removals from the loan pools due to repayments, charge offs, and transfers to OREO or other assets owned through foreclosures resulted in a decline in acquired loan interest income of \$1.6 million from the fourth quarter of 2014; and compared to the first quarter of 2014, a decline of \$8.1 million in loan interest income primarily from the continued decline in acquired loan balances; and
- The amortization of the indemnification asset also decreased by approximately \$1.0 million compared to the fourth quarter of 2014, and by \$3.9 million compared to the first quarter of 2014. This was primarily the result of the decline in the difference between the net carrying value of the FDIC indemnification asset and projected cash flows of the indemnification asset. In addition, the expiration of the commercial loss share agreement from the CBT FDIC transaction (which began in January of 2010) occurred at March 31, 2015. As a result, we anticipate a decline in this amortization in subsequent quarters.

During the recast in the first quarter of 2015, the accretable yield balance declined significantly by \$64.1 million. This decline was primarily the result of an increase in the assumed prepayment speed of certain acquired loan pools from the FFHI acquisition, and partially offset by decline in expected losses for the acquired credit impaired loans. The actual cash flows were faster than what had been previously expected (assumed) and required an adjustment in the assumed prepayment speed used to forecast expected cash flows, which increases the yield of the acquired loans. The result was a decrease in the accretable yield balance, however, there was no impairment since this only changed the timing of the receipt of future cash on these pools of loans (expect to receive cash sooner). See Note 6 Loans and Allowance for Loan Losses on page 13 for further discussion.

The table below provides an analysis of the total loan portfolio yield which includes both non-acquired and acquired (credit impaired and non-credit impaired loan portfolios). The acquired loan yield continues to increase due to the continued improvement in overall credit quality of this portfolio and the actual cash flows being faster than previously expected.

| (Dollars in thousands)                           | March 31,<br>2015 | Three Months Ended<br>December 31,<br>2014 | March 31,<br>2014 |
|--------------------------------------------------|-------------------|--------------------------------------------|-------------------|
| <b>Average balances:</b>                         |                   |                                            |                   |
| Acquired loans, net of allowance for loan losses | \$ 2,193,825      | \$ 2,298,491                               | \$ 2,737,859      |
| Non-acquired loans                               | 3,513,006         | 3,382,795                                  | 2,909,175         |
| Total loans, excluding held for sale             | \$ 5,706,831      | \$ 5,681,286                               | \$ 5,647,034      |
| <b>Interest income:</b>                          |                   |                                            |                   |
| Noncash interest income on acquired loans        | \$ 1,600          | 2,274                                      | 2,954             |
| Acquired loan interest income                    | 41,318            | \$ 42,231                                  | \$ 48,082         |
| Total acquired loans                             | 42,918            | 44,505                                     | 51,036            |
| Non-acquired loans                               | 35,517            | 34,752                                     | 30,602            |
| Total loans, excluding held for sale             | \$ 78,435         | \$ 79,257                                  | \$ 81,638         |

Edgar Filing: SOUTH STATE Corp - Form 10-Q

|                                      |              |       |       |
|--------------------------------------|--------------|-------|-------|
| <b>Non-TE yield:</b>                 |              |       |       |
| Acquired loans                       | <b>7.93%</b> | 7.68% | 7.56% |
| Non-acquired loans                   | <b>4.10%</b> | 4.08% | 4.27% |
| Total loans, excluding held for sale | <b>5.57%</b> | 5.53% | 5.86% |

## Edgar Filing: SOUTH STATE Corp - Form 10-Q

### Table of Contents

Compared to the balance at December 31, 2014, our non-acquired loan portfolio has increased \$118.6 million, or 13.7% annualized, to \$3.6 billion, driven by increases in most categories. Consumer real estate lending increased by \$74.1 million, or 27.7% annualized; consumer non real estate lending by \$6.1 million, or 13.0% annualized; commercial owner occupied loans by \$17.3 million, or 7.6% annualized; and commercial non-owner occupied by \$31.1 million, or 37.3% annualized. The acquired loan portfolio decreased by \$136.2 million in the first quarter of 2015 due to continued payoffs, charge-offs, and transfers to OREO. Since March 31, 2014, the non-acquired loan portfolio has grown by \$606.4 million, or 20.4%, in most categories. Consumer real estate loans have led the way and increased by \$286.1 million, or 33.3%, in the past year.

Non-taxable equivalent net interest income for the quarter decreased \$2.4 million, or 2.90%, compared to the first quarter of 2014. Non-taxable equivalent net interest margin decreased by 22 basis points to 4.73% from the first quarter of 2014 of 4.95% due to the decrease in yield on most interesting earning assets. Compared to the fourth quarter of 2014, net interest margin (taxable equivalent) increased by six basis points. Interest earning assets yield increased by one basis point primarily from the increase in the yield of the acquired and non-acquired loan portfolios. The rate on interest bearing liabilities decreased by six basis points compared to the fourth quarter of 2014 from a five basis point decrease in the rates on time deposit balances.

Our quarterly efficiency ratio decreased to 65.1%, compared to 69.3% in the fourth quarter of 2014 and from 73.8% in the first quarter of 2014. The decrease in the efficiency ratio compared to the fourth quarter of 2014 was the result of a \$4.2 million reduction in noninterest expense. The reduction in noninterest expense was driven by the \$4.6 million dollar reduction in merger and branding related expenses. The decrease in the efficiency ratio compared to the first quarter of 2014 was the result of a 29.0% increase in noninterest income and a 9.0% decrease in noninterest expense. Compared to the first quarter of 2014, noninterest expense was down by \$6.9 million with a \$6.0 million decrease in merger and branding related expense and a \$1.2 million decrease in OREO and loan related expense, partially offset by a \$1.9 million increase in salary and benefits. Excluding OREO and merger and branding related expenses, the efficiency ratio was 62.3% for the first quarter of 2015, compared to 62.7% for the fourth quarter of 2014 and 64.1% for the first quarter of 2014.

Diluted EPS and basic EPS increased to \$0.99 and \$1.00 for the first quarter of 2015, from the first quarter 2014 amounts of \$0.66 and \$0.66, respectively. This was the result of a 51% increase in net income available to common shareholders.

### *Selected Figures and Ratios*

| (Dollars in thousands)                                 |    | Three Months Ended<br>March 31, |            |
|--------------------------------------------------------|----|---------------------------------|------------|
|                                                        |    | 2015                            | 2014       |
| Return on average assets (annualized)                  |    | 1.23%                           | 0.86%      |
| Return on average common equity (annualized)           |    | 9.73%                           | 6.89%      |
| Return on average equity (annualized)                  |    | 9.73%                           | 6.90%      |
| Return on average tangible common equity (annualized)* |    | 16.21%                          | 12.59%     |
| Return on average tangible equity (annualized)*        |    | 16.21%                          | 12.03%     |
| Dividend payout ratio **                               |    | 23.22%                          | 28.91%     |
| Equity to assets ratio                                 |    | 12.56%                          | 11.69%     |
| Average shareholders common equity (in thousands)      | \$ | 997,473                         | \$ 931,961 |
| Average shareholders equity (in thousands)             | \$ | 997,473                         | \$ 994,073 |

## Edgar Filing: SOUTH STATE Corp - Form 10-Q

\* - Ratio is a non-GAAP financial measure. The section titled Reconciliation of Non-GAAP to GAAP below provides a table that reconciles non-GAAP measures to GAAP measures.

\*\* - See explanation of the dividend payout ratio below.

- For the three months ended March 31, 2015, return on average tangible equity increased compared to the same period in 2014. The increase was driven by the 46.6% increase in net income available to common shareholders excluding amortization of intangibles. Similarly, return on average assets increased to 1.23%, compared to the three months ended March 31, 2014, due to the growth in net income.
- Dividend payout ratio decreased to 23.2% for the three months ended March 31, 2015, compared with 28.9% for the three months ended March 31, 2014. The decrease from the comparable period in 2014 primarily reflects the higher net income for the three months ended March 31, 2015, compared to the increase of \$0.04 per share, or 21.1%, in the cash dividends declared per common share. The dividend payout ratio is calculated by dividing total dividends paid during the quarter by the total net income reported for the same period.

## Edgar Filing: SOUTH STATE Corp - Form 10-Q

### Table of Contents

- Equity to assets ratio increased to 12.6% at March 31, 2015, compared with 11.7% at March 31, 2014. The increase in the equity to assets ratio reflects a 0.4% increase in assets, compared to the 7.9% increase in equity, as a result of the Company's retained earnings.
- Quarterly average shareholders' equity increased \$3.4 million, or 0.3%, from the quarter ended March 31, 2014 driven by earnings partially offset by the impact of the redemption of \$65.0 million in preferred stock in March of 2014 and dividends paid to shareholders.

### *Reconciliation of Non-GAAP to GAAP*

| (Dollars in thousands)                                          | 2015       | Three Months Ended<br>March 31, | 2014       |
|-----------------------------------------------------------------|------------|---------------------------------|------------|
| Return on average tangible equity (non-GAAP)                    | 16.21%     |                                 | 12.03%     |
| Effect to adjust for intangible assets                          | -6.48%     |                                 | -5.13%     |
| Return on average equity (GAAP)                                 | 9.73%      |                                 | 6.90%      |
| Adjusted average shareholders' equity (non-GAAP)                | \$ 631,874 |                                 | \$ 616,808 |
| Average intangible assets                                       | 365,599    |                                 | 377,265    |
| Average shareholders' equity (GAAP)                             | \$ 997,473 |                                 | \$ 994,073 |
| Adjusted net income (non-GAAP)                                  | \$ 25,257  |                                 | \$ 18,299  |
| Amortization of intangibles                                     | (2,016)    |                                 | (2,104)    |
| Tax effect                                                      | 685        |                                 | 722        |
| Net income (GAAP)                                               | \$ 23,926  |                                 | \$ 16,917  |
| Return on average common tangible equity (non-GAAP)             | 16.21%     |                                 | 12.59%     |
| Effect to adjust for intangible assets                          | -6.48%     |                                 | -5.70%     |
| Return on average common equity (GAAP)                          | 9.73%      |                                 | 6.89%      |
| Adjusted average common shareholders' equity (non-GAAP)         | \$ 631,874 |                                 | \$ 554,696 |
| Average intangible assets                                       | 365,599    |                                 | 377,265    |
| Average common shareholders' equity (GAAP)                      | \$ 997,473 |                                 | \$ 931,961 |
| Adjusted net income available to common shareholders (non-GAAP) | \$ 25,257  |                                 | \$ 17,226  |
| Amortization of intangibles                                     | (2,016)    |                                 | (2,104)    |
| Tax effect                                                      | 685        |                                 | 722        |
| Net income available to common shareholders (GAAP)              | \$ 23,926  |                                 | \$ 15,844  |

The returns on average tangible equity and average common tangible equity are non-GAAP financial measures. They exclude the effect of the average balance of intangible assets and add back the after-tax amortization of intangibles to GAAP basis net income. Management believes that these non-GAAP measures provide additional useful information, particularly since these measures are widely used by industry analysts following companies with prior merger and acquisition activities. Non-GAAP measures should not be considered as an alternative to any measure of performance or financial condition as promulgated under GAAP, and investors should consider the company's performance and financial condition as reported under GAAP and all other relevant information when assessing the performance or financial condition of the company. Non-GAAP measures have limitations as analytical tools, and investors should not consider them in isolation or as a substitute for analysis of our results of financial condition as reported under GAAP.

### **Net Interest Income and Margin**

*Summary*

Our taxable equivalent ( TE ) net interest margin decreased by 22 basis points from the first quarter of 2014, due primarily to the 28 basis point decline in the yield on interest earning assets, partially offset by a seven basis point decline in the rate on interest bearing liabilities. The net interest margin increased by six basis points from the fourth quarter of 2014 to 4.78%. Yields on average earning assets increased by one basis point from the fourth quarter of 2014, while the rate on average interest bearing liabilities decreased by six basis points.

## Table of Contents

The Company remained in an excess liquidity position during the first quarter of 2015, and the impact represented an estimated 16 basis points reduction in the net interest margin compared to 17 basis points from the fourth quarter of 2014.

Net interest income decreased from the first quarter of 2014 by \$2.4 million. This decrease was primarily driven by the \$544.0 million decrease in the average balance of the acquired loan portfolio, partially offset by a \$603.8 million increase in the average balance of the non-acquired loan portfolio and a \$43.4 million reduction in the average balance of other borrowings due to the redemption of \$46.3 million in trust preferred securities. Certificates of deposit average rate declined by two basis points from the first quarter of 2014 along with the average balance decreasing \$287.8 million. Year-over-year interest expense declined \$1.0 million, and the cost of funds decreased six basis points.

| (Dollars in thousands)                      | Three Months Ended<br>March 31, |           |
|---------------------------------------------|---------------------------------|-----------|
|                                             | 2015                            | 2014      |
| Non-TE net interest income                  | \$ 81,049                       | \$ 83,466 |
| Non-TE yield on interest-earning assets     | 4.90%                           | 5.18%     |
| Non-TE rate on interest-bearing liabilities | 0.23%                           | 0.30%     |
| Non-TE net interest margin                  | 4.73%                           | 4.95%     |
| TE net interest margin                      | 4.78%                           | 5.00%     |

Non-TE net interest income decreased \$2.4 million, or 2.90%, in the first quarter of 2015 compared to the same period in 2014. Some key highlights are outlined below:

- Average interest-earning assets increased 1.5% to \$6.9 billion in the first quarter of 2015 compared to the same period last year due primarily to the increase in investment securities and non-acquired loans.
- Non-TE yield on interest-earning assets for the first quarter of 2015 decreased 28 basis points from the comparable period in 2014. The decrease since the first quarter of 2014 was driven by a 17 basis point decrease in the yield on non-acquired loans and a 22 basis point decrease in the yield on taxable investment securities portfolio. These decreases were partially offset by a 37 basis point increase in the yield of acquired loans. The loan portfolio continues to remix with 63% of the portfolio being comprised of non-acquired loans and 37% being acquired loans. This compares to 53% and 47% one year ago.
- The average cost of interest-bearing liabilities for the first quarter of 2015 decreased seven basis points from the same period in 2014. The decrease since the first quarter of 2014 was in every category of funding, from interest bearing transaction/money market accounts to federal funds purchased and repurchase agreements. This is a reflection of the continuation of the low rate environment. During the first quarter, we redeemed \$46.3 million of 7% fixed rate trust preferred securities. The expected cost of funds on our remaining trust preferred securities, assuming the rate environment remains low, should be approximately 4.70%.
- TE net interest margin decreased by 22 basis points in the first quarter of 2015, compared to the first of 2014.

Table of Contents**Loans**

The following table presents a summary of the loan portfolio by category:

| <b>(Dollars in thousands)</b>                   | <b>March 31,<br/>2015</b> | <b>% of<br/>Total</b> | <b>December 31,<br/>2014</b> | <b>% of<br/>Total</b> | <b>March 31,<br/>2014</b> | <b>% of<br/>Total</b> |
|-------------------------------------------------|---------------------------|-----------------------|------------------------------|-----------------------|---------------------------|-----------------------|
| Acquired loans:                                 |                           |                       |                              |                       |                           |                       |
| Acquired covered loans:                         |                           |                       |                              |                       |                           |                       |
| Commercial non-owner occupied real estate:      |                           |                       |                              |                       |                           |                       |
| Construction and land development               | \$ 18,929                 | 0.3%                  | \$ 20,275                    | 0.4%                  | \$ 37,757                 | 0.7%                  |
| Commercial non-owner occupied                   | 29,961                    | 0.5%                  | 35,035                       | 0.6%                  | 50,814                    | 0.9%                  |
| Total commercial non-owner occupied real estate | 48,890                    | 0.8%                  | 55,310                       | 1.0%                  | 88,571                    | 1.6%                  |
| Consumer real estate:                           |                           |                       |                              |                       |                           |                       |
| Consumer owner occupied                         | 29,708                    | 0.5%                  | 30,304                       | 0.5%                  | 37,111                    | 0.7%                  |
| Home equity loans                               | 33,482                    | 0.6%                  | 35,509                       | 0.6%                  | 34,627                    | 0.6%                  |
| Total consumer real estate                      | 63,190                    | 1.1%                  | 65,813                       | 1.1%                  | 71,738                    | 1.3%                  |
| Commercial owner occupied real estate           | 42,040                    | 0.7%                  | 45,986                       | 0.8%                  | 78,861                    | 1.4%                  |
| Commercial and industrial                       | 8,952                     | 0.2%                  | 9,887                        | 0.2%                  | 11,964                    | 0.2%                  |
| Other income producing property                 | 22,322                    | 0.4%                  | 20,820                       | 0.4%                  | 29,471                    | 0.5%                  |
| Consumer non real estate                        | 562                       | 0.0%                  | 675                          | 0.0%                  | 1,772                     | 0.0%                  |
| Total acquired covered loans                    | 185,956                   | 3.2%                  | 198,491                      | 3.5%                  | 282,377                   | 5.0%                  |
| Acquired non-covered loans:                     |                           |                       |                              |                       |                           |                       |
| Commercial non-owner occupied real estate:      |                           |                       |                              |                       |                           |                       |
| Construction and land development               | 59,437                    | 1.0%                  | 65,959                       | 1.2%                  | 96,981                    | 1.7%                  |
| Commercial non-owner occupied                   | 164,212                   | 2.9%                  | 181,652                      | 3.2%                  | 204,094                   | 3.6%                  |
| Total commercial non-owner occupied real estate | 223,649                   | 3.9%                  | 247,611                      | 4.4%                  | 301,075                   | 5.3%                  |
| Consumer real estate:                           |                           |                       |                              |                       |                           |                       |
| Consumer owner occupied                         | 801,572                   | 14.1%                 | 842,995                      | 14.7%                 | 951,131                   | 16.9%                 |
| Home equity loans                               | 279,866                   | 4.9%                  | 294,589                      | 5.1%                  | 324,686                   | 5.8%                  |
| Total consumer real estate                      | 1,081,438                 | 19.0%                 | 1,137,584                    | 19.8%                 | 1,275,817                 | 22.7%                 |
| Commercial owner occupied real estate           | 164,716                   | 2.9%                  | 176,268                      | 3.1%                  | 200,370                   | 3.6%                  |
| Commercial and industrial                       | 59,251                    | 1.0%                  | 67,028                       | 1.2%                  | 76,016                    | 1.4%                  |
| Other income producing property                 | 129,091                   | 2.3%                  | 139,496                      | 2.4%                  | 160,498                   | 2.9%                  |
| Consumer non real estate                        | 274,469                   | 4.8%                  | 288,288                      | 5.0%                  | 340,857                   | 6.1%                  |
| Total acquired non-covered loans                | 1,932,614                 | 33.9%                 | 2,056,275                    | 35.9%                 | 2,354,633                 | 42.0%                 |
| Total acquired loans                            | 2,118,570                 | 37.1%                 | 2,254,766                    | 39.4%                 | 2,637,010                 | 47.0%                 |
| Non-acquired loans:                             |                           |                       |                              |                       |                           |                       |
| Commercial non-owner occupied real estate:      |                           |                       |                              |                       |                           |                       |
| Construction and land development               | 358,108                   | 6.3%                  | 364,221                      | 6.4%                  | 319,441                   | 5.7%                  |
| Commercial non-owner occupied                   | 364,727                   | 6.4%                  | 333,590                      | 5.8%                  | 285,145                   | 5.1%                  |
| Total commercial non-owner occupied real estate | 722,835                   | 12.7%                 | 697,811                      | 12.2%                 | 604,586                   | 10.8%                 |
| Consumer real estate:                           |                           |                       |                              |                       |                           |                       |
| Consumer owner occupied                         | 854,283                   | 15.0%                 | 786,778                      | 13.7%                 | 595,652                   | 10.6%                 |
| Home equity loans                               | 290,488                   | 5.1%                  | 283,934                      | 5.0%                  | 263,057                   | 4.7%                  |

Edgar Filing: SOUTH STATE Corp - Form 10-Q

|                                       |                     |               |                     |               |                     |               |
|---------------------------------------|---------------------|---------------|---------------------|---------------|---------------------|---------------|
| Total consumer real estate            | <b>1,144,771</b>    | <b>20.1%</b>  | 1,070,712           | 18.7%         | 858,709             | 15.3%         |
| Commercial owner occupied real estate | <b>925,192</b>      | <b>16.2%</b>  | 907,913             | 15.9%         | 845,728             | 15.1%         |
| Commercial and industrial             | <b>407,990</b>      | <b>7.2%</b>   | 405,923             | 7.1%          | 333,574             | 5.9%          |
| Other income producing property       | <b>154,360</b>      | <b>2.7%</b>   | 150,928             | 2.6%          | 158,186             | 2.8%          |
| Consumer non real estate              | <b>195,451</b>      | <b>3.4%</b>   | 189,317             | 3.3%          | 147,710             | 2.6%          |
| Other                                 | <b>35,806</b>       | <b>0.6%</b>   | 45,222              | 0.8%          | 31,465              | 0.5%          |
| Total non-acquired loans              | <b>3,586,405</b>    | <b>62.9%</b>  | 3,467,826           | 60.6%         | 2,979,958           | 53.0%         |
| Total loans (net of unearned income)  | <b>\$ 5,704,975</b> | <b>100.0%</b> | <b>\$ 5,722,592</b> | <b>100.0%</b> | <b>\$ 5,616,968</b> | <b>100.0%</b> |

*Note:* Loan data excludes loans held for sale.

Total loans, net of deferred loan costs and fees (excluding mortgage loans held for sale), increased by \$88.0 million, or 1.6%, at March 31, 2015 as compared to the same period in 2014. Acquired covered loans decreased by \$96.4 million and acquired non-covered loans decreased by \$422.0 million due to principal payments, charge offs, and foreclosures. In addition to the reductions for principal payments, charge offs, and foreclosures, the acquired covered loans will decrease by approximately \$49.0 million in the second quarter of 2015 due to the expiration of the CBT commercial loss share agreement with the FDIC on March

## Edgar Filing: SOUTH STATE Corp - Form 10-Q

### Table of Contents

31, 2015. These loans will be transferred from the covered loan portfolio to the non-covered loan portfolio. Non-acquired loans or legacy loans increased by \$606.4 million, or 20.4%, from March 31, 2014 to March 31, 2015. Non-acquired loans have grown to 62.9% of the total loan portfolio compared to 53.0% at March 31, 2014. The increase was driven by loan growth in almost all categories of non-acquired loans.

| (Dollars in thousands)         | Three Months Ended<br>March 31, |              |
|--------------------------------|---------------------------------|--------------|
|                                | 2015                            | 2014         |
| Average total loans            | \$ 5,706,831                    | \$ 5,647,034 |
| Interest income on total loans | 78,435                          | 81,639       |
| Non-TE yield                   | 5.57%                           | 5.86%        |

Interest earned on loans decreased in the first quarter of 2015 compared to the first quarter of 2014. Some key highlights for the quarter ended March 31, 2015 are outlined below:

- Our non-TE yield on total loans decreased 29 basis points comparing the first quarter of 2015 to 2014 and average total loans increased 1.1%, as compared to the first quarter of 2014. The increase in average total loans was primarily the result of the growth in non-acquired loans during 2015. These new loans, however, are at lower rates and the average yield was 4.10% in the first quarter of 2015 compared to 4.27% in the first quarter of 2014. The acquired loan portfolio effective yield increased to 7.93%, compared to 7.56% in the first quarter of 2014, as a result of improved cash flows in certain pools.
- Acquired covered loans had a balance of \$186.0 million at the end of the first quarter of 2015 compared to \$282.4 million at March 31, 2014.
- Acquired non-covered loans declined by approximately \$422.0 million to \$1.9 billion at the end of the first quarter of 2015 compared to \$2.4 billion at March 31, 2014.
- Non-acquired construction and land development loans increased \$38.7 million, or 12.1%, to \$358.1 million from the ending balance at March 31, 2014.
- Non-acquired commercial non-owner occupied loans increased \$79.6 million, or 27.9%, to \$364.7 million from the ending balance at March 31, 2014.
- Non-acquired consumer real estate loans, including home equity loans, increased \$286.1 million, or 33.3%, to \$1.1 billion from the ending balance at March 31, 2014.
- Non-acquired commercial owner occupied loans increased \$79.5 million, or 9.4%, to \$925.2 million from the ending balance at March 31, 2014.
- Non-acquired commercial and industrial loans increased \$74.4 million, or 22.3%, to \$408.0 million from the ending balance at March 31, 2014.
- Non-acquired consumer non-real estate loans increased \$47.7 million, or 32.30%, to \$195.5 million from the ending balance at March 31, 2014.
- Non-acquired other income producing property loans decreased \$3.8 million, or 2.4%, to \$154.4 million from the ending balance at March 31, 2014.

The balance of mortgage loans held for sale increased \$25.4 million from December 31, 2014 to \$87.3 million at March 31, 2015, and \$29.7 million compared to the balance of mortgage loans held for sale at March 31, 2014 of \$57.6 million.

# Table of Contents

## Investment Securities

We use investment securities, our second largest category of earning assets, to generate interest income through the deployment of excess funds, to provide liquidity, to fund loan demand or deposit liquidation, and to pledge as collateral for public funds deposits and repurchase agreements. At March 31, 2015, investment securities totaled \$827.1 million, compared to \$826.9 million at December 31, 2014 and \$814.5 million at March 31, 2014. In addition, we continue to slowly increase our investment securities portfolio as we identify securities that meet our strategy and objectives. During the quarter, our portfolio remained nearly unchanged from the balance at December 31, 2014.

| (Dollars in thousands)                   | Three Months Ended<br>March 31, |            |
|------------------------------------------|---------------------------------|------------|
|                                          | 2015                            | 2014       |
| Average investment securities            | \$ 815,264                      | \$ 801,263 |
| Interest income on investment securities | 4,739                           | 5,037      |
| Non-TE yield                             | 2.36%                           | 2.55%      |

Interest earned on investment securities decreased 5.9% in the first quarter of 2015 compared to the first quarter of 2014.

The following table provides a summary of the credit ratings for our investment portfolio (including held-to-maturity and available-for-sale securities) at the end of the first quarter of 2015:

| (Dollars in thousands)                | Amortized<br>Cost | Fair<br>Value | Unrealized<br>Gain<br>(Loss) | AAA - A    | BBB | BB or<br>Lower | Not Rated  |
|---------------------------------------|-------------------|---------------|------------------------------|------------|-----|----------------|------------|
| <b>March 31, 2015</b>                 |                   |               |                              |            |     |                |            |
| Government-sponsored<br>entities debt | \$ 134,296        | \$ 134,203    | \$ (93)                      | \$ 134,296 | \$  | \$             | \$         |
| State and municipal<br>obligations    | 141,702           | 146,748       | 5,046                        | 140,965    |     |                | 737        |
| Mortgage-backed<br>securities *       | 524,785           | 534,424       | 9,639                        |            |     |                | 524,785    |
| Corporate stocks                      | 3,161             | 3,253         | 92                           |            |     |                | 3,161      |
|                                       | \$ 803,944        | \$ 818,628    | \$ 14,684                    | \$ 275,261 | \$  | \$             | \$ 528,683 |

\* - Agency mortgage-backed securities ( MBS ) are guaranteed by the issuing GSE as to the timely payments of principal and interest. Except for Government National Mortgage Association ( GNMA ) securities, which have the full faith and credit backing of the United States Government, the GSE alone is responsible for making payments on this guaranty. While the rating agencies have not rated any of the MBS issued, senior debt securities issued by GSEs are rated consistently as Triple-A. Most market participants consider agency MBS as carrying an implied Aaa rating (S&P rating of AA+) because of the guarantees of timely payments and selection criteria of mortgages backing the securities. We do not own any private label mortgage-backed securities.

## Edgar Filing: SOUTH STATE Corp - Form 10-Q

At March 31, 2015, we had 35 securities available for sale in an unrealized loss position, which totaled \$1.5 million. At December 31, 2014, we had 66 securities available for sale in an unrealized loss position, which totaled \$3.6 million. At March 31, 2014, we had 199 securities available for sale in an unrealized loss position, which totaled \$9.3 million.

During the first quarter of 2015 as compared to the first quarter of 2014, the total number of available for sale securities with an unrealized loss position decreased by 164 securities, while the total dollar amount of the unrealized loss decreased by \$7.8 million.

All securities available for sale in an unrealized loss position as of March 31, 2015 continue to perform as scheduled. We have evaluated the cash flows and determined that all contractual cash flows should be received; therefore impairment is temporary because we have the ability to hold these securities within the portfolio until the maturity or until the value recovers, and we believe that it is not likely that we will be required to sell these securities prior to recovery. We continue to monitor all of these securities with a high degree of scrutiny. There can be no assurance that we will not conclude in future periods that conditions existing at that time indicate some or all of these securities are other than temporarily impaired, which would require a charge to earnings in such periods. Any charges for OTTI related to securities available-for-sale would not impact cash flow, tangible capital or liquidity.

As securities are purchased, they are designated as held to maturity or available for sale based upon our intent, which incorporates liquidity needs, interest rate expectations, asset/liability management strategies, and capital requirements. We do not currently hold, nor have we ever held, any securities that are designated as trading securities. Although securities classified as

Table of Contents

available for sale may be sold from time to time to meet liquidity or other needs, it is not our normal practice to trade this segment of the investment securities portfolio. While management generally holds these assets on a long-term basis or until maturity, any short-term investments or securities available for sale could be converted at an earlier point, depending partly on changes in interest rates and alternative investment opportunities.

**Other Investments**

Other investment securities include primarily our investments in Federal Home Loan Bank of Atlanta ( FHLB ) stock with no readily determinable market value. The amortized cost and fair value of all these securities are equal at March 31, 2015. As of March 31, 2015, the investment in FHLB stock represented approximately \$7.4 million, or 0.1% as a percentage of total assets.

***Interest-Bearing Liabilities***

Interest-bearing liabilities include interest-bearing transaction accounts, savings deposits, CDs, other time deposits, federal funds purchased, and other borrowings. Interest-bearing transaction accounts include NOW, HSA, IOLTA, and Market Rate checking accounts.

| (Dollars in thousands)               | Three Months Ended<br>March 31, |              |
|--------------------------------------|---------------------------------|--------------|
|                                      | 2015                            | 2014         |
| Average interest-bearing liabilities | \$ 5,153,328                    | \$ 5,408,276 |
| Interest expense                     | 2,949                           | 3,990        |
| Average rate                         | 0.23%                           | 0.30%        |

The average balance of interest-bearing liabilities decreased in the first quarter of 2015 compared to the first quarter of 2014 due primarily to the decrease in certificates of deposit, other time deposits and other borrowings. The decrease in interest expense in the first quarter was largely driven by the reduction in certificates of deposit, other time deposits and the redemption of \$46.3 million of trust preferred securities at a 7% dividend rate. Rates continued to decline in most categories, with the exception of savings deposit and other borrowings which remained flat. Overall, we experienced a seven basis point decrease in the average rate on all interest-bearing liabilities from the three months ended March 31, 2014. Some key highlights are outlined below:

- Average interest-bearing deposits for the three months ended March 31, 2015 decreased 4.3% from the same period in 2014.
- Interest-bearing deposits decreased 3.4% to \$4.9 billion at March 31, 2015 from the period end balance at March 31, 2014 of \$5.0 billion. This was the result of a \$265.0 million decline in certificates of deposit, which was partially offset by growth in interest-bearing transaction accounts of \$95.7 million. The Company continues to monitor and adjust rates paid on deposit products as part of its strategy to manage its net interest margin.
- The average rate on transaction and money market account deposits for the three months ended March 31, 2015 decreased one basis point from the comparable period in 2014.

## Edgar Filing: SOUTH STATE Corp - Form 10-Q

- Average certificates of deposit and other time deposits decreased 19.2%, down \$287.8 million from the average balance in the first quarter of 2014. Interest expense on certificates of deposit and other time deposits decreased \$325,000 as a result of the decline in average balances and a two basis point decrease in the average rate to 38 basis points for the three months ended March 31, 2015 as compared to the same period in 2014.
- The average rate on other borrowings remained unchanged at 5.94% for the three months ended March 31, 2015 as compared to the same period in 2014.

### ***Noninterest-Bearing Deposits***

Noninterest-bearing deposits are transaction accounts that provide our Bank with interest-free sources of funds. Average noninterest-bearing deposits increased \$207.3 million, or 14.0%, to \$1.7 billion in the first quarter of 2015 compared to \$1.5 billion at March 31, 2014. At March 31, 2015, noninterest-bearing deposits were \$1.8 billion, exceeding the March 31, 2014 balance by \$172.2 million.

### **Provision for Loan Losses and Nonperforming Assets**

The allowance for loan losses is based upon estimates made by management. We maintain an allowance for loan losses at a level that we believe is appropriate to cover estimated credit losses on individually evaluated loans that are determined to be impaired as well as estimated credit losses inherent in the remainder of our loan portfolio. Arriving at the allowance involves a high

Table of Contents

degree of management judgment and results in a range of estimated losses. We regularly evaluate the adequacy of the allowance through our internal risk rating system, outside credit review, and regulatory agency examinations to assess the quality of the loan portfolio and identify problem loans. The evaluation process also includes our analysis of current economic conditions, composition of the loan portfolio, past due and nonaccrual loans, concentrations of credit, lending policies and procedures, and historical loan loss experience. The provision for loan losses is charged to expense in an amount necessary to maintain the allowance at an appropriate level.

The allowance consists of general and specific reserves. The general reserves are determined by applying loss percentages to the portfolio that are based on historical loss experience and management's evaluation and risk grading of the loan portfolio. Additionally, the general economic and business conditions affecting key lending areas, credit quality trends, collateral values, loan volumes and concentrations, seasoning of the loan portfolio, the findings of internal and external credit reviews and results from external bank regulatory examinations are included in this evaluation. The specific reserves are determined on a loan-by-loan basis based on management's evaluation of our exposure for each credit, given the current payment status of the loan and the value of any underlying collateral. These are loans classified by management as nonaccrual and graded doubtful or substandard. For such loans that are also classified as impaired, an allowance is established when the discounted cash flows (or collateral value or observable market price) of the impaired loan is lower than the carrying value of that loan. Generally, the need for a specific reserve is evaluated on impaired loans. Loans for which specific reserves are provided are excluded from the calculation of the general reserves.

With the FFHI business combination, the Company segregated the FFHI acquired loan portfolio into performing loans ( non-credit impaired ) and credit impaired loans. The acquired non-credit impaired loans and acquired revolving type loans are accounted for under FASB ASC 310-20, with each loan being accounted for individually. Acquired credit impaired loans are recorded net of any acquisition accounting discounts and have no allowance for loan losses associated with them at acquisition date. The related discount, if applicable, is accreted into interest income over the remaining contractual life of the loan using the level yield method. Subsequent deterioration in the credit quality of these loans is recognized by recording a provision for loan losses through the income statement, increasing the non-acquired and acquired non-credit impaired allowance for loan losses. The acquired credit impaired loans will follow the description in the next paragraph.

In determining the acquisition date fair value of acquired credit impaired loans, and in subsequent accounting, the Company generally aggregates purchased loans into pools of loans with common risk characteristics. Expected cash flows at the acquisition date in excess of the fair value of loans are recorded as interest income over the life of the loans using a level yield method if the timing and amount of the future cash flows of the pool is reasonably estimable. Subsequent to the acquisition date, increases in cash flows over those expected at the acquisition date are recognized as interest income prospectively. Decreases in expected cash flows after the acquisition date are recognized by recording an allowance for loan losses. Evidence of credit quality deterioration for the loan pools may include information such as increased past-due and nonaccrual levels and migration in the pools to lower loan grades. Offsetting the impact of the provision established for the loan, the receivable from the FDIC is adjusted to reflect the indemnified portion of the post-acquisition exposure with a corresponding credit to the provision for loan losses (For further discussion of the Company's allowance for loan losses on acquired loans, see Note 6 Loans and Allowance for Loan Losses)

During the first quarter of 2015, we decreased the valuation allowance on acquired credit impaired loans by \$2.3 million on certain acquired loan pools due to evidence of credit improvement and expected cash flows during the quarterly review process, which resulted in \$87,000 net provision for loan losses on acquired credit impaired loans (net of the impact of the FDIC loss sharing agreements).

# Edgar Filing: SOUTH STATE Corp - Form 10-Q

## Table of Contents

The following table presents a summary of the changes in the ALLL for the three months ended March 31, 2015 and 2014:

| (Dollars in thousands)                                                                             | Three Months Ended March 31, |                                               |                                           |           |                       |                                           |           |
|----------------------------------------------------------------------------------------------------|------------------------------|-----------------------------------------------|-------------------------------------------|-----------|-----------------------|-------------------------------------------|-----------|
|                                                                                                    | Non-acquired<br>Loans        | 2015<br>Acquired Non-credit<br>Impaired Loans | 2014<br>Acquired Credit<br>Impaired Loans | Total     | Non-acquired<br>Loans | 2014<br>Acquired Credit<br>Impaired Loans | Total     |
| Balance at beginning of period                                                                     | \$ 34,539                    | \$                                            | \$ 7,365                                  | \$ 41,904 | \$ 34,331             | \$ 11,618                                 | \$ 45,949 |
| Loans charged-off                                                                                  | (996)                        | (1,811)                                       |                                           | (2,807)   | (1,370)               |                                           | (1,370)   |
| Recoveries of loans previously charged off                                                         | 1,050                        | 25                                            |                                           | 1,075     | 1,038                 |                                           | 1,038     |
| Net charge-offs                                                                                    | 54                           | (1,786)                                       |                                           | (1,732)   | (332)                 |                                           | (332)     |
| Provision for loan losses                                                                          | (1,055)                      | 1,786                                         | 66                                        | 797       | 670                   | 304                                       | 974       |
| Benefit attributable to FDIC loss share agreements                                                 |                              |                                               | 21                                        | 21        |                       | (125)                                     | (125)     |
| Total provision for loan losses charged to operations                                              | (1,055)                      | 1,786                                         | 87                                        | 818       | 670                   | 179                                       | 849       |
| Provision for loan losses recorded through the FDIC loss share receivable                          |                              |                                               | (21)                                      | (21)      |                       | 125                                       | 125       |
| Reductions due to loan removals                                                                    |                              |                                               | (2,714)                                   | (2,714)   |                       | (876)                                     | (876)     |
| Balance at end of period                                                                           | \$ 33,538                    | \$                                            | \$ 4,717                                  | \$ 38,255 | \$ 34,669             | \$ 11,046                                 | \$ 45,715 |
| Total non-acquired loans:                                                                          |                              |                                               |                                           |           |                       |                                           |           |
| At period end                                                                                      | 3,586,405                    |                                               |                                           |           | 2,979,958             |                                           |           |
| Average                                                                                            | 3,513,006                    |                                               |                                           |           | 2,909,175             |                                           |           |
| Net charge-offs as a percentage of average non-acquired loans (annualized)                         | -0.01%                       |                                               |                                           |           | 0.05%                 |                                           |           |
| Allowance for loan losses as a percentage of period end non-acquired loans                         | 0.94%                        |                                               |                                           |           | 1.16%                 |                                           |           |
| Allowance for loan losses as a percentage of period end non-performing non-acquired loans ( NPLs ) | 121.63%                      |                                               |                                           |           | 92.59%                |                                           |           |

The allowance for loan losses as a percent of non-acquired loans reflects the continued decline due primarily to the decline in our three-year historical charge off rate. Additionally, our classified loans, nonaccrual loans, and non-performing loans declined during the first quarter of 2015 compared to the same quarter in 2014 and to the fourth quarter of 2014. Our overall net charge offs for the quarter on non-acquired loans was negative one basis point annualized, due to recoveries in excess of charge offs, compared to five basis points, or \$332 thousand, a year ago and 13 basis points, or \$1.1 million in the fourth quarter of 2014. The low level of net charge offs may not be sustainable given the remaining uncertainty which exists within the overall economy and markets in which we operate. Excluding acquired assets, nonperforming assets decreased by \$15.6 million during the first quarter of 2015 compared to the first quarter of 2014 and decreased by \$2.4 million from the fourth quarter of 2014. The ratio of the ALLL to cover total nonperforming non-acquired loans increased from 92.6% at March 31, 2014 to 121.6% at March 31, 2015.

We decreased the ALLL compared to the first quarter of 2014 due primarily to the improvement in asset quality metrics during the first quarter of 2015. Compared to the fourth quarter of 2014, the ALLL decreased due primarily to the decline in combined past due and nonaccrual loans, classified assets, and reduced bankruptcies and foreclosures during the first quarter. On an investment purposes general basis, we consider three-year historical loss rates on all loan portfolios, except residential lot loans and lot loans held for where two-year historical loss rates are applied. We also consider economic risk, model risk and operational risk when determining the ALLL. All of these factors are reviewed and adjusted each reporting period to account for management's assessment of loss within the loan portfolio. Overall, the general reserve decreased

## Edgar Filing: SOUTH STATE Corp - Form 10-Q

by \$1.1 million compared to the balance at March 31, 2014 and decreased by \$872,000 from December 31, 2014.

We have adjusted our qualitative factors to account for uncertainty and certain risk inherent in the portfolio that cannot be measured with historical loss rates. We currently view that the low level of net charge offs and historical loss rates may not be indicative of the losses inherent in the overall loan portfolio. Therefore, we have adjusted our qualitative factors to account for the uncertainty which exists in the economy as a whole and within the markets in which we operate.

On a specific reserve basis, the allowance for loan losses decreased \$129,000 from December 31, 2014, with loan balances being evaluated for specific reserves increasing from \$27.1 million to \$30.0 million at March 31, 2015. Specific reserves remained flat from March 31, 2014 to March 31, 2015 at \$1.4 million. However, the loan balances being evaluated for specific reserves decreased from \$33.8 million at March 31, 2014. Our practice, generally, is that once a specific reserve is established for a loan, a charge off occurs in the quarter subsequent to the establishment of the specific reserve.

During the three months ended March 31, 2015, the decline in our total nonperforming assets ( NPAs ) was reflective of improvement in the real estate market and economy as a whole within the markets that we serve.

# Table of Contents

The following table summarizes our NPAs for the past five quarters:

| (Dollars in thousands)                                               | March 31,<br>2015 | December 31,<br>2014 | September 30,<br>2014 | June 30,<br>2014 | March 31,<br>2014 |
|----------------------------------------------------------------------|-------------------|----------------------|-----------------------|------------------|-------------------|
| <b>Non-acquired:</b>                                                 |                   |                      |                       |                  |                   |
| Nonaccrual loans                                                     | \$ 17,491         | \$ 18,569            | \$ 20,419             | \$ 26,546        | \$ 29,190         |
| Accruing loans past due 90 days or more                              | 204               | 522                  | 429                   | 358              | 96                |
| Restructured loans - nonaccrual                                      | 9,879             | 9,425                | 9,633                 | 8,409            | 8,156             |
| Total nonperforming loans                                            | 27,574            | 28,516               | 30,481                | 35,313           | 37,442            |
| Other real estate owned (OREO) (2)                                   | 6,435             | 7,947                | 9,360                 | 9,003            | 12,187            |
| Other nonperforming assets (3)                                       | 65                |                      |                       |                  |                   |
| Total non-acquired nonperforming assets                              | 34,074            | 36,463               | 39,841                | 44,316           | 49,629            |
| <b>Acquired non-credit impaired:</b>                                 |                   |                      |                       |                  |                   |
| Nonaccrual loans                                                     | 7,280             | 7,538                | 5,359                 |                  |                   |
| Accruing loans past due 90 days or more                              | 100               | 108                  | 501                   |                  |                   |
| Total acquired nonperforming loans (1)                               | 7,380             | 7,646                | 5,860                 |                  |                   |
| <b>Acquired OREO and other nonperforming assets:</b>                 |                   |                      |                       |                  |                   |
| Covered OREO (2)                                                     | 12,026            | 16,227               | 18,961                | 21,999           | 29,003            |
| Acquired OREO not covered under loss share (2)                       | 17,635            | 18,552               | 22,929                | 22,732           | 22,957            |
| Other covered nonperforming assets (3)                               | 608               | 694                  | 640                   | 811              | 1,032             |
| Total acquired OREO and other nonperforming assets                   | 30,269            | 35,473               | 42,530                | 45,542           | 52,992            |
| Total nonperforming assets                                           | \$ 71,723         | \$ 79,582            | \$ 88,231             | \$ 89,858        | \$ 102,621        |
| <b>Excluding Acquired Assets</b>                                     |                   |                      |                       |                  |                   |
| Total NPAs as a percentage of total loans and repossessed assets (4) | 0.95%             | 1.05%                | 1.20%                 | 1.39%            | 1.66%             |
| Total NPAs as a percentage of total assets (5)                       | 0.42%             | 0.47%                | 0.51%                 | 0.55%            | 0.62%             |
| Total NPLs as a percentage of total loans (4)                        | 0.77%             | 0.82%                | 0.92%                 | 1.11%            | 1.26%             |
| <b>Including Acquired Assets</b>                                     |                   |                      |                       |                  |                   |
| Total NPAs as a percentage of total loans and repossessed assets (4) | 1.25%             | 1.38%                | 1.54%                 | 1.57%            | 1.81%             |
| Total NPAs as a percentage of total assets                           | 0.89%             | 1.02%                | 1.12%                 | 1.12%            | 1.28%             |
| Total NPLs as a percentage of total loans (4)                        | 0.61%             | 0.63%                | 0.64%                 | 0.62%            | 0.67%             |

(1) Excludes the acquired loans that are contractually past due 90 days or more totaling \$44.8 million, \$48.5 million, \$52.5 million, \$60.3 million, and \$73.9 million as of March 31, 2015, December 31, 2014, September 30, 2015, June 30, 2014, and March 31, 2014, respectively, including the valuation discount. Acquired credit impaired loans are considered to be performing due to the application of the accretion method under FASB ASC Topic 310-30. (For further discussion of the Company's application of the accretion method, see Business Combinations and Method of Accounting for Loans Acquired in our Annual Report on Form 10-K for the year ended December 31, 2014.

(2) Includes certain real estate acquired as a result of foreclosure and property not intended for bank use.

(3) Consists of non-real estate foreclosed assets, such as repossessed vehicles.

(4) Loan data excludes mortgage loans held for sale.

## Edgar Filing: SOUTH STATE Corp - Form 10-Q

(5) For purposes of this calculation, total assets include all assets (both acquired and non-acquired).

Excluding the acquired non-credit impaired loans, total nonperforming loans, including restructured loans, were \$27.6 million, or 0.77% of non-acquired loans, a decrease of \$9.9 million, or 26.4%, from March 31, 2014. The decrease in nonperforming loans was driven primarily by a decrease in commercial nonaccrual loans of \$11.3 million offset by an increase of \$1.7 million in nonaccrual restructured loans.

Nonperforming non-acquired loans, including restructured loans decreased by approximately \$942 thousand during the first quarter of 2015 from the level at December 31, 2014. This decrease was primarily driven by a decrease in commercial nonaccrual loans of \$2.5 million, a decrease in loans 90+ days past due and still accruing of \$318,000, offset by an increase in consumer nonaccrual loans of \$1.4 million and an increase in restructured nonaccrual loans of \$454,000. Recoveries exceeded charge offs this quarter by \$54,000.

## Table of Contents

In February 2015, the Company auctioned approximately 70 OREO assets with a carrying value of \$4.0 million. These assets all had been held in the OREO portfolio for at least twelve months. The assets auctioned included both covered and non-covered assets (relative to loss share agreements). The loss realized totaled approximately \$640,000, net of loss share claims.

At March 31, 2015, non-acquired OREO decreased by \$1.5 million from December 31, 2014. At March 31 2015, non-acquired OREO consisted of 45 properties with an average value of \$143,000, which is significantly lower than the level from December 31, 2014 when we had 72 properties in non-acquired OREO. In the first quarter of 2015, we added 10 properties with an aggregate value of \$1.1 million into non-acquired OREO, and we sold 37 properties with a basis of \$2.0 million in the quarter. We wrote down 16 OREO properties by \$592,000 during the first quarter of 2015. Our non-acquired OREO balance of \$6.4 million at March 31, 2015 is comprised of 43% in the Low Country/Orangeburg region, 33% in the Coastal region (Beaufort to Myrtle Beach), 9% in the Charlotte region, 9% in the Upstate region (Greenville) and 6% primarily related to former branch locations.

## Potential Problem Loans

Potential problem loans (excluding all acquired loans), totaled \$7.4 million, or 0.21%, of total non-acquired loans outstanding at March 31, 2015, compared to \$7.9 million, or 0.26%, of total non-acquired loans outstanding at March 31, 2014, and compared to \$7.6 million, or 0.22% of total non-acquired loans outstanding at December 31, 2014. Potential problem loans related to the acquired non-credit impaired loans totaled \$7.9 million, or 0.63%, of total acquired non-credit impaired loans at March 31, 2015, compared to \$10.4 million, or 0.79%, of total acquired non-credit impaired loans outstanding at December 31, 2014. For the period ended March 31, 2014, there were no acquired non-credit impaired loans that were considered potential problem loans until we completed the evaluation of acquired loans and any related purchase adjustment during the measurement period. All potential problem loans represent those loans where information about possible credit problems of the borrowers has caused management to have serious concern about the borrower's ability to comply with present repayment terms.

## Noninterest Income

| (Dollars in thousands)                              | 2015 | Three Months Ended<br>March 31, |    | 2014    |
|-----------------------------------------------------|------|---------------------------------|----|---------|
|                                                     |      |                                 |    |         |
| Service charges on deposit accounts                 | \$   | 8,108                           | \$ | 8,988   |
| Bankcard services income                            |      | 7,599                           |    | 7,105   |
| Mortgage banking income                             |      | 6,626                           |    | 3,291   |
| Trust and investment services income                |      | 4,934                           |    | 4,543   |
| Amortization of FDIC indemnification assets,<br>net |      | (3,207)                         |    | (7,078) |
| Other                                               |      | 2,445                           |    | 3,699   |
| Total noninterest income                            | \$   | 26,505                          | \$ | 20,548  |

Excluding the amortization on the FDIC indemnification asset, noninterest income increased by \$2.1 million, or 7.6%, during the first three months ended March 31, 2015 as compared to the same period in 2014. The quarterly increase in total noninterest income primarily resulted from the following:

## Edgar Filing: SOUTH STATE Corp - Form 10-Q

- Bankcard services income increased 7.0%, or \$494,000. Debit card income increased 3.5%, or \$210,000, due to organic growth.
- Trust and investment services income increased 8.6%, or \$391,000, driven primarily by the addition of investment services income.
- Mortgage banking income increased \$3.3 million, or 101.3%, driven by a lower interest rate environment which increased the fair value of the held for sale and pipeline portfolios as well as the volume of loan originations.
- Amortization on the FDIC indemnification asset decreased \$3.9 million, or 54.7%, resulting from a smaller difference between the expected cash flows from the FDIC compared to the remaining carrying value of the indemnification asset.
- Service charges on deposit accounts decreased \$880,000 due to changes in customer behavior relative to insufficient funds and overdraft fees.

Table of Contents**Noninterest Expense**

| (Dollars in thousands)                       | Three Months Ended<br>March 31, |           |
|----------------------------------------------|---------------------------------|-----------|
|                                              | 2015                            | 2014      |
| Salaries and employee benefits               | \$ 40,987                       | \$ 39,093 |
| Net occupancy expense                        | 5,237                           | 5,608     |
| Information services expense                 | 3,958                           | 4,398     |
| Furniture and equipment expense              | 3,145                           | 3,744     |
| OREO expense and loan related                | 3,014                           | 4,203     |
| Business development and staff related       | 2,114                           | 1,571     |
| Amortization of intangibles                  | 2,016                           | 2,104     |
| Bankcard expense                             | 1,980                           | 2,256     |
| Supplies, printing and postage               | 1,612                           | 1,583     |
| Professional fees                            | 1,409                           | 1,262     |
| FDIC assessment and other regulatory charges | 1,184                           | 1,576     |
| Advertising and marketing                    | 888                             | 1,007     |
| Merger and branding related expense          |                                 | 5,985     |
| Other                                        | 2,941                           | 3,026     |
| Total noninterest expense                    | \$ 70,485                       | \$ 77,416 |

Noninterest expense decreased \$6.9 million in the first quarter of 2015 as compared to the same period in 2014. The quarterly decrease in total noninterest expense primarily resulted from the following:

- Salary and employee benefits were \$1.9 million higher than last year, due largely to increased mortgage commissions based on higher production.
- Information services expense decreased by \$440,000, driven largely by a reduction in expenses post conversion during the quarter related to certain contract terminations and renegotiations.
- OREO expense and loan related declined from the prior year due to significantly fewer assets with less cost to carry and a decrease in the amount of write downs.
- FDIC assessment and other regulatory charges declined by \$392,000 due to improvement in the financial ratios used to determine our quarterly assessment.
- Advertising and marketing decreased by \$119,000, driven largely by the discretionary nature of this expense.
- Furniture and equipment expense decreased by \$599,000, driven largely by the closing of additional branches during the year and cost savings executed from prior quarters.
- Merger-related expense decreased \$6.0 million due to no merger-related expenses in 2015.

**Income Tax Expense**

Our effective income tax rate decreased to 34.00% for the quarter ended March 31, 2015 compared to 34.30% for the quarter ended March 31, 2014. The lower effective tax rate was attributable primarily to investments in certain qualified tax credit programs.

### Capital Resources

Our ongoing capital requirements have been met primarily through retained earnings, less the payment of cash dividends. As of March 31, 2015, shareholders' equity was \$1.0 billion, an increase of \$22.6 million, or 2.3%, from \$984.9 million at December 31, 2014, and an increase of \$73.4 million, or 7.9%, from \$934.2 million at March 31, 2014. The driving factor for the increase from year-end was net income of \$23.9 million, which was offset by the common dividend paid of \$5.6 million. Accumulated other comprehensive loss changed to a comprehensive gain, during the first quarter 2015, with the increased unrealized gains in the AFS securities portfolio during the quarter of \$3.3 million, net of tax. The increase from the comparable period of 2014 was primarily the result of net income of \$82.4 million and a favorable change in accumulated comprehensive income partially offset by dividends paid to common shareholders. Our common equity-to-assets ratio was 12.56% at March 31, 2015, relatively flat compared to 12.58% at December 31, 2014 and increased from 11.69% at the end of the comparable period of 2014.

Table of Contents

We are subject to regulations with respect to certain risk-based capital ratios. These risk-based capital ratios measure the relationship of capital to a combination of balance sheet and off-balance sheet risks. The values of both balance sheet and off-balance sheet items are adjusted based on the rules to reflect categorical credit risk. In addition to the risk-based capital ratios, the regulatory agencies have also established a leverage ratio for assessing capital adequacy. The leverage ratio is equal to Tier 1 capital divided by total consolidated on-balance sheet assets (minus amounts deducted from Tier 1 capital). The leverage ratio does not involve assigning risk weights to assets.

As disclosed in our Annual Report on Form 10-K for the year ended December 31, 2014, in July 2013, the Federal Reserve announced its approval of a final rule to implement the regulatory capital reforms developed by the Basel Committee on Banking Supervision ( Basel III ), among other changes required by the Dodd-Frank Wall Street Reform and Consumer Protection Act. The new rules became effective January 1, 2015, subject to a phase-in period for certain aspects of the new rules.

The new capital rules framework requires banking organizations to hold more and higher quality capital, which acts as a financial cushion to absorb losses, taking into account the impact of risk. As applied to the Company and the Bank, the new rules include a new minimum ratio of common equity Tier 1 capital ( CET1 ) to risk-weighted assets of 4.5%. The new rules also raise our minimum required ratio of Tier 1 capital to risk-weighted assets from 4% to 6%. Our minimum required leverage ratio under the new rules is 4% (the new rules eliminated an exemption that permitted a minimum leverage ratio of 3% for certain institutions). Our minimum required total capital to risk-weighted assets ratio remains at 8% under the new rules.

In order to avoid restrictions on capital distributions and discretionary bonus payments to executives, under the new rules a covered banking organization will also be required to maintain a capital conservation buffer in addition to its minimum risk-based capital requirements. This buffer will be required to consist solely of common equity Tier 1, and the buffer will apply to all three risk-based measurements (CET1, Tier 1 capital and total capital). The capital conservation buffer will be phased in incrementally over time, beginning January 1, 2016 and becoming fully effective on January 1, 2019, and will ultimately consist of an additional amount of Tier 1 common equity equal to 2.5% of risk-weighted assets.

In terms of quality of capital, the final rule emphasizes common equity Tier 1 capital and implements strict eligibility criteria for regulatory capital instruments. It also changes the methodology for calculating risk-weighted assets to enhance risk sensitivity.

Under the Basel III rules, accumulated other comprehensive income ( AOCI ) is presumptively included in common equity Tier 1 capital and can operate to reduce this category of capital. The final rule provided a one-time opportunity at the end of the first quarter of 2015 for covered banking organizations to opt out of much of this treatment of AOCI, which election the Bank and the Company have made. As a result, the Company and the Bank will retain the pre-existing treatment for AOCI.

The Bank is also subject to the regulatory framework for prompt corrective action, which identifies five capital categories for insured depository institutions (well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized, and critically undercapitalized) and is based on specified thresholds for each of the three risk-based regulatory capital ratios (CET1, Tier 1 capital and total capital) and for the leverage ratio.

The Company's and the Bank's regulatory capital ratios for the following periods are reflected below:

Edgar Filing: SOUTH STATE Corp - Form 10-Q

|                                         | March 31,<br>2015 | December 31,<br>2014 | March 31,<br>2014 |
|-----------------------------------------|-------------------|----------------------|-------------------|
| <b>South State Corporation:</b>         |                   |                      |                   |
| Common equity Tier 1 risk-based capital | 12.26%            | n/a                  | n/a               |
| Tier 1 risk-based capital               | 13.18%            | 13.62%               | 12.78%            |
| Total risk-based capital                | 13.89%            | 14.43%               | 13.67%            |
| Tier 1 leverage                         | 9.53%             | 9.47%                | 8.68%             |
| <b>South State Bank:</b>                |                   |                      |                   |
| Common equity Tier 1 risk-based capital | 12.93%            | n/a                  | n/a               |
| Tier 1 risk-based capital               | 12.93%            | 13.37%               | 12.56%            |
| Total risk-based capital                | 13.63%            | 14.18%               | 13.46%            |
| Tier 1 leverage                         | 9.36%             | 9.30%                | 8.54%             |

Due to the adoption of Basel III for the first quarter of 2015, the March 31, 2015 risk-based capital ratios are not comparable to the December 31, 2014 and March 31, 2014 risk-based capital ratios. The Tier 1 leverage ratio increased compared to December 31, 2014 and March 31, 2014 due to the increase in capital outpacing the increase in our average asset size. Our

Table of Contents

capital ratios are currently well in excess of the minimum standards and continue to be in the well capitalized regulatory classification.

**Liquidity**

Liquidity refers to our ability to generate sufficient cash to meet our financial obligations, which arise primarily from the withdrawal of deposits, extension of credit and payment of operating expenses. Our Asset/Liability Management Committee (ALCO) is charged with monitoring liquidity management policies, which are designed to ensure acceptable composition of asset/liability mix. Two critical areas of focus for ALCO are interest rate sensitivity and liquidity risk management. We have employed our funds in a manner to provide liquidity from both assets and liabilities sufficient to meet our cash needs.

Asset liquidity is maintained by the maturity structure of loans, investment securities and other short-term investments. Management has policies and procedures governing the length of time to maturity on loans and investments. Normally, changes in the earning asset mix are of a longer-term nature and are not utilized for day-to-day corporate liquidity needs.

Our liabilities provide liquidity on a day-to-day basis. Daily liquidity needs are met from deposit levels or from our use of federal funds purchased, securities sold under agreements to repurchase and other short-term borrowings. We engage in routine activities to retain deposits intended to enhance our liquidity position. These routine activities include various measures, such as the following:

- Emphasizing relationship banking to new and existing customers, where borrowers are encouraged and normally expected to maintain deposit accounts with our Bank,
- Pricing deposits, including certificates of deposit, at rate levels that will attract and/or retain balances of deposits that will enhance our Bank's asset/liability management and net interest margin requirements, and
- Continually working to identify and introduce new products that will attract customers or enhance our Bank's appeal as a primary provider of financial services.

Our legacy loan portfolio increased by approximately \$606.4 million, or approximately 20.4%, compared to the balance at March 31, 2014, and by \$118.6 million, or 13.7% annualized, compared to the balance at December 31, 2014. Our investment securities portfolio increased \$12.6 million from first quarter 2014 and by \$143,000 million compared to fourth quarter 2014. Total cash and cash equivalents were \$630.7 million at March 31, 2015 as compared to \$417.9 million at December 31, 2014 and \$612.6 million at March 31, 2014.

At March 31, 2015, December 31, 2014 and March 31, 2014, the Company had \$19.9 million, \$23.4 million and \$30.4 million, respectively, in traditional, out-of-market brokered deposits and \$61.9 million, \$67.5 million, and \$85.5 million, respectively, of reciprocal brokered deposits. Total deposits were \$6.6 billion, relatively flat compared to March 31, 2014, resulting primarily from decreases in certificates of deposit by \$265.0 million offset by increases in core deposits by \$263.9 million. Other borrowings decreased \$46.0 million from the balance at March 31, 2014, due to the redemption of \$46.3 million of trust preferred securities. To the extent that we employ other types of non-deposit funding sources, typically to accommodate retail and correspondent customers, we continue to take in some shorter maturities of such funds. Our current

## Edgar Filing: SOUTH STATE Corp - Form 10-Q

approach may provide an opportunity to sustain a low funding rate or possibly lower our cost of funds but could also increase our cost of funds if interest rates rise.

Our ongoing philosophy is to remain in a liquid position taking into account our current composition of earning assets, asset quality, capital position, and operating results. Our liquid earning assets include federal funds sold, balances at the Federal Reserve Bank, reverse repurchase agreements, and/or other short-term investments. Cyclical and other economic trends and conditions can disrupt our Bank's desired liquidity position at any time. We expect that these conditions would generally be of a short-term nature. Under such circumstances, our Bank's federal funds sold position and any balances at the Federal Reserve Bank serve as the primary sources of immediate liquidity. At March 31, 2015, our Bank had total federal funds credit lines of \$376.0 million with no outstanding advances. If additional liquidity were needed, the Bank would turn to short-term borrowings as an alternative immediate funding source and would consider other appropriate actions such as promotions to increase core deposits or the sale of a portion of our investment portfolio. At March 31, 2015, our Bank had \$159.6 million of credit available at the Federal Reserve Bank's Discount Window, but had no outstanding advances as of the end of the quarter. In addition, we could draw on additional alternative immediate funding sources from lines of credit extended to us from our correspondent banks and/or the FHLB. At March 31, 2015, our Bank had a total FHLB credit facility of \$909.3 million with total outstanding letters of credit consuming \$19.7 million, \$134,000 in outstanding advances and \$234,000 in credit enhancements from participation in the FHLB's Mortgage Partnership Finance Program. The Company had a \$20.0 million unsecured line of credit with U.S. Bank National Association with no outstanding advances. We believe that our liquidity position continues to be adequate and readily available.

## Table of Contents

Our contingency funding plans incorporate several potential stages based on liquidity levels. Also, we review on at least an annual basis our liquidity position and our contingency funding plans with our principal banking regulator. The Company maintains various wholesale sources of funding. If our deposit retention efforts were to be unsuccessful, our Company would utilize these alternative sources of funding. Under such circumstances, depending on the external source of funds, our interest cost would vary based on the range of interest rates charged to our Company. This could increase our Company's cost of funds, impacting net interest margins and net interest spreads.

## Loss Share

The following table presents the expected losses on acquired assets covered under loss share agreements as of March 31, 2015:

| (Dollars in thousands) | FDIC<br>Threshold<br>or ILE | Original<br>Estimated<br>Gross Losses | Original<br>Estimated<br>Covered Losses | Losses<br>Incurred *<br>By FFCH<br>through<br>July 26, 2013 | Losses<br>Incurred **<br>By South State<br>through<br>March 31, 2015 | Remaining<br>Estimated<br>Losses<br>for Loans | OREO<br>Mark ***<br>March 31, 2015 | Projected<br>Total<br>Losses |
|------------------------|-----------------------------|---------------------------------------|-----------------------------------------|-------------------------------------------------------------|----------------------------------------------------------------------|-----------------------------------------------|------------------------------------|------------------------------|
| <b>CBT</b>             | \$ 233,000                  | \$ 340,039                            | \$ 334,082                              | \$                                                          | \$ 314,099                                                           | \$ 1,264                                      | \$ 91                              | \$ 315,454                   |
| <b>Habersham</b>       | 94,000                      | 124,363                               | 119,978                                 |                                                             | 92,218                                                               | 1,461                                         | 295                                | 93,974                       |
| <b>BankMeridian</b>    | 70,827                      | 70,190                                | 67,780                                  |                                                             | 31,019                                                               | 1,666                                         | 1,941                              | 34,626                       |
| <b>Cape Fear ****</b>  | 131,000                     | 12,921                                | 8,213                                   | 76,122                                                      | 4,578                                                                | 562                                           |                                    | 81,262                       |
| <b>Plantation ****</b> | 70,178                      | 24,273                                | 16,176                                  | 35,190                                                      | 12,508                                                               | 3,894                                         | 357                                | 51,949                       |
| <b>Total</b>           | \$ 599,005                  | \$ 571,786                            | \$ 546,229                              | \$ 111,312                                                  | \$ 454,422                                                           | \$ 8,847                                      | \$ 2,684                           | \$ 577,265                   |

\* For Cape Fear and Plantation, claimed or claimable loan and OREO losses excluding expenses, net of revenues, from bank failure date through July 26, 2013.

\*\* Claimed or claimable loan and OREO losses excluding expenses, net of revenues, since bank failure date under South State ownership.

\*\*\* Represents the estimated losses on OREO at period end. These losses have been recognized to record OREO at net realizable value. These losses are claimable from the FDIC upon sale or receipt of a valid appraisal.

\*\*\*\* For Cape Fear and Plantation, the original estimated gross losses and the original estimated covered losses represent estimated losses subsequent to July 26, 2013.

Under the Habersham and BankMeridian loss share agreements, all losses (whether or not they exceed the intrinsic loss estimate ( ILE )) are reimbursable by the FDIC at 80% of the losses and reimbursable expenses paid. During the fourth quarter of 2011, the losses and reimbursable expenses claimed under the CBT loss share agreement exceeded the \$233.0 million threshold and became reimbursable at 95% rather than 80%. Under the loss sharing agreement for Cape Fear, the Bank assumes \$32.4 million of losses and the FDIC reimburses the Bank for 80% of the losses greater than \$32.4 million up to \$110.0 million. On losses exceeding \$110.0 million, the FDIC will reimburse the Bank for 95% of the losses. Under the loss sharing agreement for Plantation, the Bank shares in the losses on certain commercial loans and commercial OREO in three tranches. On losses up to \$55.0 million, the FDIC reimburses the Bank for 80% of all eligible losses; the Bank absorbs losses greater than \$55.0 million up to \$65.0 million; and the FDIC reimburses the Bank for 60% of all eligible losses in excess of \$65.0 million.

Effective March 31, 2015, the Commercial Shared-Loss Agreement with the FDIC for CBT expired and losses on assets covered under this agreement are no longer claimable after filing the first quarter of 2015 commercial loss share certificate. The Commercial Shared-Loss Agreement for Cape Fear expired June 30, 2014 and losses on assets covered under this agreement are no longer claimable.

### **Deposit and Loan Concentrations**

We have no material concentration of deposits from any single customer or group of customers. We have no significant portion of our loans concentrated within a single industry or group of related industries. Furthermore, we attempt to avoid making loans that, in an aggregate amount, exceed 10% of total loans to a multiple number of borrowers engaged in similar business activities. As of March 31, 2015, there were no aggregated loan concentrations of this type. We do not believe there are any material seasonal factors that would have a material adverse effect on us. We do not have foreign loans or deposits.

### **Concentration of Credit Risk**

We consider concentrations of credit to exist when, pursuant to regulatory guidelines, the amounts loaned to a multiple number of borrowers engaged in similar business activities which would cause them to be similarly impacted by general economic conditions represents 25% of total risk-based capital, or \$189.9 million at March 31, 2015. Based on this criteria, the Company had

## Table of Contents

four such credit concentrations for non-acquired loans and acquired non-credit impaired loans at March 31, 2015, including \$322.4 million of loans to lessors of residential buildings, \$402.2 million of loans to lessors of nonresidential buildings (except mini-warehouses), \$213.3 million of loans to religious organizations, and \$247.2 million of loans to offices of physicians, dentists and other health practitioners.

## Cautionary Note Regarding Any Forward-Looking Statements

*Statements included in Management's Discussion and Analysis of Financial Condition and Results of Operations which are not historical in nature are intended to be, and are hereby identified as, forward-looking statements for purposes of the safe harbor provided by Section 27A of the Securities Act of 1933 and Section 21E of the Securities and Exchange Act of 1934. The words may, will, anticipate, should, would, believe, contemplate, expect, estimate, continue, may, and intend, as well as other similar words and expressions of the future, are intended to identify forward-looking statements. We caution readers that forward-looking statements are estimates reflecting our judgment based on current information, and are subject to certain risks and uncertainties that could cause actual results to differ materially from anticipated results. Such risks and uncertainties include, among others, the matters described in Item 1A. Risk Factors of our Annual Report on Form 10-K for the year ended December 31, 2014, and the following:*

- **Credit risk** associated with an obligor's failure to meet the terms of any contract with the Bank or otherwise fail to perform as agreed;
- **Interest rate risk** involving the effect of a change in interest rates on both the Bank's earnings and the market value of the portfolio equity;
- **Liquidity risk** affecting our Bank's ability to meet its obligations when they come due;
- **Price risk** focusing on changes in market factors that may affect the value of financial instruments which are marked-to-market periodically;
- **Merger and merger integration risk** including potential deposit attrition, higher than expected costs, customer loss and business disruption, including, without limitation, potential difficulties in maintaining relationships with key personnel and other integration related-matters, and the potential inability to identify and successfully negotiate and complete additional successful combinations with potential merger or acquisition partners;
- **Transaction risk** arising from problems with service or product delivery;
- **Compliance risk** involving risk to earnings or capital resulting from violations of or nonconformance with laws, rules, regulations, prescribed practices, or ethical standards;
- **Controls and procedures risk**, including the potential failure or circumvention of our controls and procedures or failure to comply with regulations related to controls and procedures;
- **Regulatory change** risk resulting from new laws, rules, regulations, proscribed practices or ethical standards, including the possibility that regulatory agencies may require higher levels of capital above the current regulatory-mandated minimums, including the impact of the capital rules under Basel III and the possibility of changes in accounting principles relating to loan loss recognition;
- **Strategic risk** resulting from adverse business decisions or improper implementation of business decisions;

## Edgar Filing: SOUTH STATE Corp - Form 10-Q

- **Reputation risk** that adversely affects earnings or capital arising from negative public opinion;
- **Terrorist activities risk** that result in loss of consumer confidence and economic disruptions;
- **Cybersecurity risk** related to our dependence on internal computer systems and the technology of outside service providers, as well as the potential impacts of third-party security breaches, subjects us to potential business disruptions or financial losses resulting from deliberate attacks or unintentional events;
- **Noninterest income risk** resulting from the effect of final rules amending Regulation E that prohibit financial institutions from charging consumer fees for paying overdrafts on ATM and one-time debit card transactions, unless the consumer consents or opts-in to the overdraft service for those types of transactions; and
- **Economic downturn risk** resulting in changes in the credit markets, greater than expected non-interest expenses, excessive loan losses and other factors, which risks could be exacerbated by potential negative economic developments resulting from the expiration of the federal tax reductions, and the implementation of federal spending cuts currently scheduled to go into effect.

Additional information with respect to factors that may cause actual results to differ materially from those contemplated by our forward-looking statements may also be included in other reports that the Company files with the Securities and Exchange Commission. The Company cautions that the foregoing list of risk factors is not exclusive and not to place undue reliance on forward-looking statements.

For any forward-looking statements made in this Form 10-Q or in any documents incorporated by reference into this Form 10-Q, we claim the protection of the safe harbor for forward looking statements contained in the Private Securities Litigation Reform Act of 1995. Such forward-looking statements speak only as of the date of this Form 10-Q or the date of any document

Table of Contents

incorporated by reference in Form 10-Q. We do not undertake to update forward looking statements to reflect facts, circumstances, assumptions or events that occur after the date the forward-looking statements are made. All subsequent written and oral forward looking statements by the Company or any person acting on its behalf are expressly qualified in their entirety by the cautionary statements contained or referred to in this Form 10-Q.

**Item 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

We have no material changes in our quantitative and qualitative disclosures about market risk as of March 31, 2015 from that presented in our Annual Report on Form 10-K for the year ended December 31, 2014.

**Item 4. CONTROLS AND PROCEDURES**

*Evaluation of Disclosure Controls and Procedures*

Management, including our Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of our disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) as of the end of the period covered by this report. Based upon that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective to ensure that information required to be disclosed in the reports we file and submit under the Exchange Act is (i) recorded, processed, summarized and reported as and when required and (ii) accumulated and communicated to our management, including our Chief Executive Officer and the Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

The design of any system of controls and procedures is based in part upon certain assumptions about the likelihood of future events. There can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions, regardless of how remote.

*Changes in Internal Control over Financial Reporting*

There has been no change in our internal control over financial reporting during the three months ended March 31, 2015, that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

**PART II OTHER INFORMATION**

**Item 1. LEGAL PROCEEDINGS**

## Edgar Filing: SOUTH STATE Corp - Form 10-Q

As of March 31, 2015 and the date of this form 10-Q, we believe that we are not a party to, nor is any of our property the subject of, any pending material legal proceeding other than those that may occur in the ordinary course of our business.

### Item 1A. RISK FACTORS

Investing in shares of our common stock involves certain risks, including those identified and described in Item 1A. of our Annual Report on Form 10-K for the fiscal year ended December 31, 2014, as well as cautionary statements contained in this Form 10-Q, including those under the caption Cautionary Note Regarding Any Forward-Looking Statements set forth in Part I, Item 2 of this Form 10-Q, risks and matters described elsewhere in this Form 10-Q and in our other filings with the SEC.

# Table of Contents

## Item 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

(a) Not applicable

(b) Not applicable

(c) Issuer Purchases of Registered Equity Securities:

In February 2004, we announced a stock repurchase program with no formal expiration date to repurchase up to 250,000 shares of our common stock. There are 147,872 shares that may yet be purchased under that program. The following table reflects share repurchase activity during the first quarter of 2015:

| Period                   | (a) Total<br>Number of<br>Shares (or<br>Units)<br>Purchased | (b) Average<br>Price Paid per<br>Share (or Unit) | (c) Total<br>Number of<br>Shares (or<br>Units)<br>Purchased as<br>Part of Publicly<br>Announced<br>Plans or<br>Programs | (d) Maximum<br>Number (or<br>Approximate<br>Dollar Value) of<br>Shares (or<br>Units) that May<br>Yet Be<br>Purchased<br>Under the Plans<br>or Programs |
|--------------------------|-------------------------------------------------------------|--------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------|
| January 1 - January 31   | 12,836*                                                     | \$ 61.25                                         |                                                                                                                         | 147,872                                                                                                                                                |
| February 1 - February 28 | 3,014*                                                      | 64.35                                            |                                                                                                                         | 147,872                                                                                                                                                |
| March 1 - March 31       |                                                             |                                                  |                                                                                                                         | 147,872                                                                                                                                                |
| Total                    | 15,850                                                      |                                                  |                                                                                                                         | 147,872                                                                                                                                                |

\* These shares were repurchased under arrangements, authorized by our stock-based compensation plans and Board of Directors, whereby officers or directors may sell previously owned shares to the Company in order to pay for the exercises of stock options or for income taxes owed on vesting shares of restricted stock. These shares are not purchased under the plan to repurchase 250,000 shares announced in February 2004.

## Item 3. DEFAULTS UPON SENIOR SECURITIES

Not applicable.

**Item 4. MINE SAFETY DISCLOSURES**

Not applicable.

**Item 5. OTHER INFORMATION**

Not applicable.

Table of Contents

**Item 6. EXHIBITS**

The exhibits required to be filed as part of this Quarterly Report on Form 10-Q are listed in the Exhibit Index attached hereto and are incorporated by reference.

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

SOUTH STATE CORPORATION  
(Registrant)

Date: May 8, 2015

/s/ Robert R. Hill, Jr.  
Robert R. Hill, Jr.  
Chief Executive Officer  
(Principal Executive Officer)

Date: May 8, 2015

/s/ John C. Pollok  
John C. Pollok  
Senior Executive Vice President,  
Chief Financial Officer, and  
Chief Operating Officer  
(Principal Financial Officer)

Date: May 8, 2015

/s/ Keith S. Rainwater  
Keith S. Rainwater  
Executive Vice President and  
Principal Accounting Officer

Table of Contents

**Exhibit Index**

| <b>Exhibit No.</b> | <b>Description</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                |
|--------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Exhibit 31.1       | Rule 13a-14(a) Certification of Principal Executive Officer                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                       |
| Exhibit 31.2       | Rule 13a-14(a) Certification of Principal Financial Officer                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                       |
| Exhibit 32         | Section 1350 Certifications of Principal Executive Officer and Principal Financial Officer                                                                                                                                                                                                                                                                                                                                                                                                                                                                        |
| Exhibit 101        | The following financial statements from the Quarterly Report on Form 10-Q of South State Corporation for the quarter ended March 31, 2015, formatted in eXtensible Business Reporting Language (XBRL): (i) Condensed Consolidated Balance Sheets, (ii) Condensed Consolidated Statements of Income, (iii) Condensed Consolidated Statements of Comprehensive Income, (iv) Condensed Consolidated Statements of Changes in Shareholders' Equity, (v) Condensed Consolidated Statement of Cash Flows and (vi) Notes to Condensed Consolidated Financial Statements. |