ISABELLA BANK CORP
Form 10-Q
November 07, 2012
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

x **Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934.**
For the quarterly period ended September 30, 2012

or

¨ **Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934.**
For the transition period from to

Commission File Number: 0-18415

Isabella Bank Corporation

(Exact name of registrant as specified in its charter)

Michigan	**38-2830092**
(State or other jurisdiction of	**(I.R.S. Employer**
incorporation or organization)	**identification No.)**
401 N. Main St, Mt. Pleasant, MI	**48858**
(Address of principal executive offices)	**(Zip code)**

(989) 772-9471

(Registrant s telephone number, including area code)

N/A

(Former name, former address and former fiscal year, if changed since last report)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (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). x 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 accelerated filer , large accelerated filer , and smaller reporting company , in Rule 12b-2 of the Exchange Act (Check One).

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

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

APPLICABLE ONLY TO CORPORATE ISSUERS:

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

Common Stock no par value, 7,620,399 as of October 19, 2012

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ISABELLA BANK CORPORATION

QUARTERLY REPORT ON FORM 10-Q

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PART I FINANCIAL INFORMATION

Item 1 Interim Condensed Consolidated Financial Statements (Unaudited)

INTERIM CONDENSED CONSOLIDATED BALANCE SHEETS

(Dollars in thousands)

	September 30 2012	December 31 2011
ASSETS		
Cash and cash equivalents		
Cash and demand deposits due from banks	$ 19,202	$ 24,514
Interest bearing balances due from banks	5,462	4,076
Total cash and cash equivalents	**24,664**	**28,590**
Certificates of deposit held in other financial institutions	5,675	8,924
Trading securities	1,788	4,710
Available-for-sale securities (amortized cost of $452,536 in 2012 and $414,614 in 2011)	467,414	425,120
Mortgage loans available-for-sale	2,820	3,205
Loans		
Agricultural	83,439	74,645
Commercial	369,366	365,714
Consumer	33,515	31,572
Residential real estate	280,431	278,360
Total loans	**766,751**	**750,291**
Less allowance for loan losses	12,062	12,375
Net loans	**754,689**	**737,916**
Premises and equipment	25,471	24,626
Corporate owned life insurance	22,594	22,075
Accrued interest receivable	6,565	5,848
Equity securities without readily determinable fair values	17,830	17,189
Goodwill and other intangible assets	46,592	46,792
Other assets	13,036	12,930
TOTAL ASSETS	**$ 1,389,138**	**$ 1,337,925**
LIABILITIES AND SHAREHOLDERS EQUITY		
Deposits		
Noninterest bearing	$ 126,362	$ 119,072
NOW accounts	174,350	163,653
Certificates of deposit under $100 and other savings	453,348	440,123
Certificates of deposit over $100	235,431	235,316
Total deposits	**989,491**	**958,164**
Borrowed funds ($0 in 2012 and $5,242 in 2011 at fair value)	226,580	216,136
Accrued interest payable and other liabilities	8,920	8,842
Total liabilities	**1,224,991**	**1,183,142**
Shareholders equity		

Common stock no par value 15,000,000 shares authorized; issued and outstanding 7,611,350 shares (including 25,644 shares held in the Rabbi Trust) in 2012 and 7,589,226 shares (including 16,585 shares held in the Rabbi Trust) in 2011	134,973	134,734
Shares to be issued for deferred compensation obligations	4,925	4,524
Retained earnings	18,178	13,036
Accumulated other comprehensive income	6,071	2,489
Total shareholders equity	**164,147**	**154,783**
TOTAL LIABILITIES AND SHAREHOLDERS EQUITY	**$ 1,389,138**	**$ 1,337,925**

See notes to interim condensed consolidated financial statements.

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INTERIM CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS EQUITY

(Dollars in thousands except per share data)

	Common Stock Shares Outstanding	Common Stock	Shares to be Issued for Deferred Compensation Obligations	Retained Earnings	Accumulated Other Comprehensive (Loss) Income	Totals
Balance, January 1, 2011	**7,550,074**	**$ 133,592**	**$ 4,682**	**$ 8,596**	**$ (1,709)**	**$ 145,161**
Comprehensive income				7,499	6,608	14,107
Issuance of common stock	90,049	1,891				1,891
Common stock issued for deferred compensation obligations	14,842	266	(254)			12
Share based payment awards under equity compensation plan			486			486
Common stock purchased for deferred compensation obligations		(356)				(356)
Common stock repurchased pursuant to publicly announced repurchase plan	(76,708)	(1,391)				(1,391)
Cash dividends ($0.57 per share)				(4,331)		(4,331)
Balance, September 30, 2011	**7,578,257**	**$ 134,002**	**$ 4,914**	**$ 11,764**	**$ 4,899**	**$ 155,579**
Balance, January 1, 2012	**7,589,226**	**134,734**	**4,524**	**13,036**	**2,489**	**$ 154,783**
Comprehensive income				9,695	3,582	13,277
Issuance of common stock	85,227	2,025				2,025
Common stock transferred from the Rabbi Trust to satisfy deferred compensation obligations		95	(95)			
Share based payment awards under equity compensation plan			496			496
Common stock purchased for deferred compensation obligations		(361)				(361)
Common stock repurchased pursuant to publicly announced repurchase plan	(63,103)	(1,520)				(1,520)
Cash dividends ($0.60 per share)				(4,553)		(4,553)
Balance, September 30, 2012	**7,611,350**	**$ 134,973**	**$ 4,925**	**$ 18,178**	**$ 6,071**	**$ 164,147**

See notes to interim condensed consolidated financial statements.

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INTERIM CONDENSED CONSOLIDATED STATEMENTS OF INCOME

(Dollars in thousands except per share data)

	Three Months Ended September 30		Nine Months Ended September 30	
	2012	2011	2012	2011
Interest income				
Loans, including fees	$ 10,918	$ 11,365	$ 32,707	$ 34,190
Investment securities				
Taxable	1,878	1,800	5,755	5,149
Nontaxable	1,232	1,201	3,652	3,569
Trading account securities	15	45	79	143
Federal funds sold and other	121	121	363	388
Total interest income	**14,164**	**14,532**	**42,556**	**43,439**
Interest expense				
Deposits	2,203	2,725	7,083	8,286
Borrowings	1,036	1,345	3,289	3,938
Total interest expense	**3,239**	**4,070**	**10,372**	**12,224**
Net interest income	**10,925**	**10,462**	**32,184**	**31,215**
Provision for loan losses	200	963	1,100	2,383
Net interest income after provision for loan losses	**10,725**	**9,499**	**31,084**	**28,832**
Noninterest income				
Service charges and fees	1,543	1,341	4,800	4,434
Gain on sale of mortgage loans	422	111	1,080	293
Net loss on trading securities	(9)	(24)	(41)	(51)
Net gain on borrowings measured at fair value		42	33	159
Gain on sale of available-for-sale investment securities	116		1,119	
Other	687	389	1,853	950
Total noninterest income	**2,759**	**1,859**	**8,844**	**5,785**
Noninterest expenses				
Compensation and benefits	5,130	4,814	15,663	14,565
Occupancy	649	633	1,889	1,892
Furniture and equipment	1,113	1,151	3,373	3,384
Other	2,236	1,915	6,682	6,038
Available-for-sale impairment loss				
Total other-than-temporary impairment loss			486	
Portion of loss reported in other comprehensive income			(204)	
Net available-for-sale impairment loss			282	
Total noninterest expenses	**9,128**	**8,513**	**27,889**	**25,879**
Income before federal income tax expense	**4,356**	**2,845**	**12,039**	**8,738**
Federal income tax expense	899	334	2,344	1,239

NET INCOME	**$ 3,457**	**$ 2,511**	**$ 9,695**	**$ 7,499**
Earnings per share				
Basic	**$ 0.45**	**$ 0.33**	**$ 1.28**	**$ 0.99**
Diluted	**$ 0.44**	**$ 0.32**	**$ 1.24**	**$ 0.97**
Cash dividends per basic share	**$ 0.20**	**$ 0.19**	**$ 0.60**	**$ 0.57**

See notes to interim condensed consolidated financial statements.

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INTERIM CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(Dollars in thousands)

	Three Months Ended September 30		Nine Months Ended September 30	
	2012	2011	2012	2011
Net income	**$ 3,457**	**$ 2,511**	**$ 9,695**	**$ 7,499**
Unrealized holding gains on available-for-sale securities:				
Unrealized holding gains arising during the period	2,990	4,721	5,209	10,050
Reclassification adjustment for net realized gains included in net income	(116)		(1,119)	
Reclassification adjustment for impairment loss included in net income			282	
Net unrealized gains	2,874	4,721	4,372	10,050
Tax effect	(763)	(1,835)	(790)	(3,442)
Other comprehensive income, net of tax	2,111	2,886	3,582	6,608
COMPREHENSIVE INCOME	**$ 5,568**	**$ 5,397**	**$ 13,277**	**$ 14,107**

See notes to interim condensed consolidated financial statements.

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INTERIM CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Dollars in thousands)

	Nine Months Ended September 30 2012	2011
OPERATING ACTIVITIES		
Net income	$ 9,695	$ 7,499
Reconciliation of net income to net cash provided by operations:		
Provision for loan losses	1,100	2,383
Impairment of foreclosed assets	17	45
Depreciation	1,802	1,909
Amortization and impairment of originated mortgage servicing rights	582	606
Amortization of acquisition intangibles	200	229
Net amortization of available-for-sale securities	1,683	1,117
Available-for-sale security impairment loss	282	
Gain on sale of available-for-sale securities	(1,119)	
Net unrealized losses on trading securities	41	51
Net gain on sale of mortgage loans	(1,080)	(293)
Net unrealized gains on borrowings measured at fair value	(33)	(159)
Increase in cash value of corporate owned life insurance	(519)	(428)
Share-based payment awards under equity compensation plan	496	486
Origination of loans held for sale	(69,503)	(31,225)
Proceeds from loan sales	70,968	29,724
Net changes in operating assets and liabilities which provided (used) cash:		
Trading securities	2,881	900
Accrued interest receivable	(717)	(1,067)
Other assets	(1,994)	423
Accrued interest payable and other liabilities	78	792
Net cash provided by operating activities	**14,860**	**12,992**
INVESTING ACTIVITIES		
Net change in certificates of deposit held in other financial institutions	3,249	6,159
Activity in available-for-sale securities		
Sales	40,677	3,000
Maturities and calls	58,598	49,117
Purchases	(138,043)	(128,339)
Loan principal originations, net	(19,461)	(18,923)
Proceeds from sales of foreclosed assets	1,446	1,625
Purchases of premises and equipment	(2,647)	(1,576)
Purchases of corporate owned life insurance		(4,000)
Net cash used in investing activities	**(56,181)**	**(92,937)**

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INTERIM CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (continued)

(Dollars in thousands)

	Nine Months Ended September 30	
	2012	2011
FINANCING ACTIVITIES		
Acceptances and withdrawals of deposits, net	31,327	65,102
Increase in other borrowed funds	10,477	22,130
Cash dividends paid on common stock	(4,553)	(4,331)
Proceeds from issuance of common stock	2,025	1,637
Common stock repurchased	(1,520)	(1,125)
Common stock purchased for deferred compensation obligations	(361)	(356)
Net cash provided by financing activities	**37,395**	**83,057**
(DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS	**(3,926)**	**3,112**
Cash and cash equivalents at beginning of period	28,590	18,109
CASH AND CASH EQUIVALENTS AT END OF PERIOD	**$ 24,664**	**$ 21,221**
SUPPLEMENTAL CASH FLOWS INFORMATION:		
Interest paid	$ 10,526	$ 12,292
Federal income taxes paid	1,467	672
SUPPLEMENTAL NONCASH INFORMATION:		
Transfers of loans to foreclosed assets	$ 1,588	$ 1,681
Common stock issued for deferred compensation obligations		254
Common stock repurchased from the Rabbi Trust		(266)

See notes to interim condensed consolidated financial statements.

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NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands except per share amounts)

NOTE 1 - BASIS OF PRESENTATION

As used in these Notes as well as in the Management s Discussion and Analysis of Financial Condition and Results of Operations, references to Isabella, we, our, us, and similar terms refer to the consolidated entity consisting of Isabella Bank Corporation and its subsidiaries. Isabella Ban Corporation refers solely to the parent holding company, and Isabella Bank refers to Isabella Bank Corporation s subsidiary, Isabella Bank.

The acronyms and abbreviations identified below are used in the Notes to the Interim Condensed Consolidated Financial Statements as well as in the Management s Discussion and Analysis of Financial Condition and Results of Operations. You may find it helpful to refer back to this page as you read this report.

AFS: Available-for-sale
ALLL: Allowance for loan and lease losses
ASC: FASB Accounting Standards Codification
ASU: FASB Accounting Standards Update
ATM: Automated Teller Machine
Directors Plan: Isabella Bank Corporation and Related Companies Deferred Compensation Plan for Directors
Dodd-Frank Act: Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010
FASB: Financial Accounting Standards Board
FDIC: Federal Deposit Insurance Corporation
FFIEC: Federal Financial Institutions Examination Council
FRB: Board of Governors of the Federal Reserve System
FHLB: Federal Home Loan Bank
Freddie Mac: Federal Home Loan Mortgage Corporation
FTE: Fully taxable equivalent
GAAP: U.S. generally accepted accounting principles
IFRS: International Financial Reporting Standards
IRR: Interest Rate Risk
JOBS Act: Jumpstart our Business Startups Act
LIBOR: London Interbank Offered Rate
Moody s: Moody s Investors Service, Inc
N/A: Not applicable
N/M: Not meaningful
OCI: Other comprehensive income (loss)
OMSR: Originated mortgage servicing rights
OREO: Other real estate owned
OTTI: Other-than-temporary impairment
PBO: Projected Benefit Obligation
Rabbi Trust: A trust established to fund the Directors Plan
SEC: U.S. Securities & Exchange Commission
SOX: Sarbanes-Oxley Act of 2002
TDR: Troubled debt restructuring
XBRL: eXtensible Business Reporting Language

The accompanying unaudited interim condensed consolidated financial statements have been prepared in accordance with GAAP for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In our opinion, all adjustments considered necessary for a fair presentation have been included. Operating results for the three and nine month periods ended September 30, 2012 are not necessarily indicative of the results that may be expected for the year ending December 31, 2012. For further information, refer to the consolidated financial statements and footnotes thereto included in our annual report for the year ended December 31, 2011.

The accounting policies are materially the same as those discussed in Note 1 to the Consolidated Financial Statements included in our annual report for the year ended December 31, 2011.

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NOTE 2 - COMPUTATION OF EARNINGS PER SHARE

Basic earnings per share represents income available to common shareholders divided by the weighted average number of common shares outstanding during the period. Diluted earnings per share reflects additional common shares that would have been outstanding if dilutive potential common shares had been issued, as well as any adjustments to income that would result from the assumed issuance. Potential common shares that may be issued relate solely to outstanding shares in the Directors Plan.

Earnings per common share have been computed based on the following:

	Three Months Ended September 30		Nine Months Ended September 30	
	2012	2011	2012	2011
Average number of common shares outstanding for basic calculation	7,600,443	7,577,388	7,595,806	7,568,551
Average potential effect of shares in the Directors Plan (1)	206,233	197,937	203,250	195,360
Average number of common shares outstanding used to calculate diluted earnings per common share	7,806,676	7,775,325	7,799,056	7,763,911
Net income	$ 3,457	$ 2,511	$ 9,695	$ 7,499
Earnings per share				
Basic	**$ 0.45**	**$ 0.33**	**$ 1.28**	**$ 0.99**
Diluted	**$ 0.44**	**$ 0.32**	**$ 1.24**	**$ 0.97**

(1) Exclusive of shares held in the Rabbi Trust

NOTE 3 ACCOUNTING STANDARDS UPDATES

Recently Adopted Accounting Standards Updates

ASU No. 2011-03: Reconsideration of Effective Control for Repurchase Agreements

In April 2011, ASU No. 2011-03 amended ASC Topic 310, Transfers and Servicing to eliminate from the assessment of effective control, the criteria calling for the transferor to have the ability to repurchase or redeem the financial assets on substantially the agreed upon terms, even in the event of the transferee s default. The assessment of effective control should instead focus on the transferor s contractual rights and obligations. The new authoritative guidance was effective for interim and annual periods beginning on or after December 15, 2011 and did not impact our consolidated financial statements.

ASU No. 2011-04: Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRS

In May 2011, ASU No. 2011-04 amended ASC Topic 820, Fair Value Measurement to align fair value measurements and disclosures in GAAP and IFRS. The ASU changes the wording used to describe the requirements in GAAP for measuring fair value and disclosures about fair value.

The ASU clarifies the application of existing fair value measurements and disclosure requirements related to:

The application of highest and best use and valuation premise concepts.

Measuring the fair value of an instrument classified in a reporting entity s stockholders equity.

Disclosure about fair value measurements within Level 3 of the fair value hierarchy.

The ASU also changes particular principles or requirements for measuring fair value and disclosing information measuring fair value and disclosures related to:

Measuring the fair value of financial instruments that are managed within a portfolio.

Application of premiums and discounts in a fair value measurement.

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The new authoritative guidance was effective for interim and annual periods beginning on or after December 15, 2011 and did not have a financial impact but increased the level of disclosures related to fair value measurements in our interim condensed consolidated financial statements in 2012.

ASU No. 2011-05: Presentation of Comprehensive Income

In June 2011, ASU No. 2011-05 amended ASC Topic 220, Comprehensive Income to improve the comparability, consistency, and transparency of financial reporting and to increase the prominence of items reported in other comprehensive income. In addition, to increase the prominence of items reported in other comprehensive income, and to facilitate the convergence of GAAP and IFRS, the FASB eliminated the option to present components of other comprehensive income as part of the statement of changes in shareholders equity.

The new authoritative guidance was effective for interim and annual periods beginning on or after December 15, 2011 and did not have an impact on our consolidated financial statements as we have historically elected to present a separate statement of comprehensive income.

Pending Accounting Standards Updates

ASU No. 2012-02: Intangibles Goodwill and Other (Topic 350): Testing Indefinite-Lived Intangible Assets for Impairment

In August, ASU No. 2012-02 amended ASC Topic 350, Goodwill and Other to simplify the testing of intangible assets with indefinite lives. This update will allow for a qualitative assessment of intangible assets with indefinite lives to determine whether or not it is necessary to perform the impairment test described in ASC Topic 350. The new authoritative guidance is effective for fiscal years beginning after September 15, 2012 and is not expected to have any impact on our consolidated financial statements.

NOTE 4 TRADING SECURITIES

Trading securities, at fair value, consist of the following investments at:

	September 30 2012	December 31 2011
States and political subdivisions	$ 1,788	$ 4,710

Included in the net trading losses of $41 during the first nine months of 2012 were $13 of net unrealized trading losses on securities that were held in our trading portfolio as of September 30, 2012. Included in the net trading losses of $51 during the first nine months of 2011 were $45 of net unrealized trading losses on securities that were held in the trading portfolio as of September 30, 2011.

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NOTE 5 AVAILABLE-FOR-SALE SECURITIES

The amortized cost and fair value of AFS securities, with gross unrealized gains and losses, are as follows at:

	September 30, 2012			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Government sponsored enterprises	$ 1,925	$ 32	$	$ 1,957
States and political subdivisions	176,576	9,394	490	185,480
Auction rate money market preferred	3,200		429	2,771
Preferred stocks	6,800	56	496	6,360
Mortgage-backed securities	138,086	4,142		142,228
Collateralized mortgage obligations	125,949	2,773	104	128,618
Total	**$ 452,536**	**$ 16,397**	**$ 1,519**	**$ 467,414**

	December 31, 2011			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Government sponsored enterprises	$ 395	$ 2	$	$ 397
States and political subdivisions	166,832	8,157	51	174,938
Auction rate money market preferred	3,200		1,151	2,049
Preferred stocks	6,800		1,767	5,033
Mortgage-backed securities	140,842	2,807	47	143,602
Collateralized mortgage obligations	96,545	2,556		99,101
Total	**$ 414,614**	**$ 13,522**	**$ 3,016**	**$ 425,120**

The amortized cost and fair value of AFS securities by contractual maturity at September 30, 2012 are as follows:

	Maturing					
	Due in One Year or Less	After One Year But Within Five Years	After Five Years But Within Ten Years	After Ten Years	Securities With Variable Monthly Payments or Continual Call Dates	Total
Government sponsored enterprises	$	$	$ 72	$ 1,853	$	$ 1,925
States and political subdivisions	7,300	37,147	82,543	49,586		176,576
Auction rate money market preferred					3,200	3,200
Preferred stocks					6,800	6,800
Mortgage-backed securities					138,086	138,086
Collateralized mortgage obligations					125,949	125,949
Total amortized cost	**$ 7,300**	**$ 37,147**	**$ 82,615**	**$ 51,439**	**$ 274,035**	**$ 452,536**
Fair value	**$ 7,302**	**$ 38,237**	**$ 88,912**	**$ 52,986**	**$ 279,977**	**$ 467,414**

Expected maturities for government sponsored enterprises and states and political subdivisions may differ from contractual maturities because issuers may have the right to call or prepay obligations.

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As auction rate money market preferred and preferred stocks have continual call dates, they are not reported by a specific maturity group. Because of their variable monthly payments, mortgage-backed securities and collateralized mortgage obligations are not reported by a specific maturity group.

A summary of the activity related to sales of AFS securities was as follows for the nine month period ended September 30, 2012:

Proceeds from sales of securities	$ 40,677
Gross realized gains	$ 1,119
Applicable income tax expense	$ 380

There were no sales of AFS securities in the first nine months of 2011. The cost basis used to determine the realized gains or losses of securities sold was the amortized cost of the individual investment security as of the trade date.

Information pertaining to AFS securities with gross unrealized losses at September 30, 2012 and December 31, 2011 aggregated by investment category and length of time that individual securities have been in a continuous loss position, follows:

	September 30, 2012				
	Less Than Twelve Months		Over Twelve Months		
	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Total Unrealized Losses
States and political subdivisions	$ 1	$ 315	$ 489	$ 2,410	$ 490
Auction rate money market preferred			429	2,771	429
Preferred stocks			496	3,303	496
Mortgage-backed securities					
Collateralized mortgage obligations	104	15,001			104
Total	**$ 105**	**$ 15,316**	**$ 1,414**	**$ 8,484**	**$ 1,519**
Number of securities in an unrealized loss position:		**4**		**6**	**10**

	December 31, 2011				
	Less Than Twelve Months		Over Twelve Months		
	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Total Unrealized Losses
States and political subdivisions	$ 51	$ 1,410	$	$	$ 51
Auction rate money market preferred			1,151	2,049	1,151
Preferred stocks			1,767	5,033	1,767
Mortgage-backed securities	47	24,291			47
Total	**$ 98**	**$ 25,701**	**$ 2,918**	**$ 7,082**	**$ 3,016**
Number of securities in an unrealized loss position:		**6**		**6**	**12**

As of September 30, 2012 and December 31, 2011, we conducted an analysis to determine whether any securities currently in an unrealized loss position should be other-than-temporarily impaired. Such analyses considered, among other factors, the following criteria:

Has the value of the investment declined more than what is deemed to be reasonable based on a risk and maturity adjusted discount rate?

Is the issuer s investment credit rating below investment grade?

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Is it probable that the issuer will be unable to pay the amount when due?

Is it more likely than not that we will have to sell the security before recovery of its cost basis?

Has the duration of the investment been extended?

As of September 30, 2012, we held an auction rate money market preferred security and preferred stocks which continued to be in an unrealized loss position as a result of the securities interest rates, as they are currently lower than the offering rates of securities with similar characteristics. We determined that any declines in the fair value of these securities are the result of changes in interest rates and not risks related to the underlying credit quality of the security. Additionally, none of the issuers of these securities are deemed to be below investment grade, we do not intend to sell the securities in an unrealized loss position, and it is unlikely than that we will have to sell the securities before recovery of their cost basis.

During the three month period ended March 31, 2012, we had one state issued student loan auction rate AFS investment security (which is included in states and political subdivisions) that was downgraded by Moody s from A3 to Caa3. As a result of this downgrade, we engaged the services of an independent investment valuation firm to estimate the amount of credit losses (if any) related to this particular issue as of March 31, 2012. The evaluation calculated a range of estimated credit losses utilizing two different bifurcation methods: 1) Estimated Cash Flow Method and 2) Credit Yield Analysis Method. The two methods were then weighted, with a higher weighting applied to the Estimated Cash Flow Method, to determine the estimated credit related impairment. As a result of this analysis we, recognized an OTTI of $282 in earnings in the first quarter of 2012.

A summary of key valuation assumptions used in the aforementioned analysis as of March 31, 2012, follows:

	Discounted Cash Flow Method
Ratings	
Fitch	Not Rated
Moody s	Caa3
S&P	A
Seniority	Senior
Discount rate	LIBOR + 6.35%
	Credit Yield Analysis Method
Credit discount rate	LIBOR + 4.00%
Average observed discounts based on closed transactions	14.00%

To test for additional impairment of this security during the three months ended September 30, 2012, we obtained another investment valuation (from the same firm engaged to perform the initial valuation as of March 31, 2012) as of September 30, 2012. Based on the results of this valuation, no additional OTTI was indicated as of September 30, 2012.

A rollforward of credit related impairment recognized in earnings on available-for-sale securities in the three and nine months ended September 30, 2012 was as follows:

	Three Months Ended September 30, 2012	Nine Months Ended September 30, 2012
Balance at beginning of period	$ 282	$
Additions to credit losses for which no previous OTTI was recognized		282

September 30, 2012	**$**	**282**	**$**	**282**

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There were no credit losses recognized in earnings on available-for-sale securities during 2011.

Based on our analysis using the above criteria, the fact that we have asserted that we do not have the intent to sell these securities in an unrealized loss position, and it is unlikely that we will have to sell the securities before recovery of their cost basis, we do not believe that the values of any other securities are other-than-temporarily impaired as of September 30, 2012 or December 31, 2011.

NOTE 6 LOANS AND ALLOWANCE FOR LOAN LOSSES

We grant commercial, agricultural, residential real estate, and consumer loans to customers situated primarily in Clare, Gratiot, Isabella, Mecosta, Midland, Montcalm, and Saginaw counties in Michigan. The ability of the borrowers to honor their repayment obligations is often dependent upon the real estate, agricultural, light manufacturing, retail, gaming and tourism, higher education, and general economic conditions of this region. Substantially all of the consumer and residential real estate loans are secured by various items of property, while commercial loans are secured primarily by real estate, business assets, and personal guarantees; a portion of loans are unsecured.

Loans that we have the intent and ability to hold in our portfolio are reported at their outstanding principal balance adjusted for any charge-offs, the ALLL, and any deferred fees or costs. Interest income on loans is accrued over the term of the loan based on the principal amount outstanding. Loan origination fees and certain direct loan origination costs are capitalized and recognized as a component of interest income over the term of the loan using the level yield method.

The accrual of interest on commercial, agricultural, and residential real estate loans is typically discontinued at the time the loan is 90 days or more past due unless the credit is well-secured and in the process of collection. Consumer loans are typically charged off no later than 180 days past due. Past due status is based on contractual terms of the loan. In all cases, loans are placed on nonaccrual or charged off at an earlier date if collection of principal or interest is considered doubtful.

For loans that are placed on nonaccrual status or charged off, all interest accrued in the current calendar year, but not collected, is reversed against interest income while interest accrued in prior calendar years, but not collected, is charged against the allowance for loan losses. The interest on these loans is accounted for on the cash basis, until qualifying for return to accrual status. Loans are typically returned to accrual status after six months of continuous performance. For impaired loans not classified as nonaccrual, interest income continues to be accrued over the term of the loan based on the principal amount outstanding.

Commercial and agricultural loans include loans for commercial real estate, commercial operating loans, farmland and agricultural production, and state and political subdivisions. Repayment of these loans is often dependent upon the successful operation and management of a business; thus, these loans generally involve greater risk than other types of lending. We minimize our risk by limiting the amount of loans to any one borrower to $12,500. Borrowers with credit needs of more than $12,500 are serviced through the use of loan participations with other commercial banks. Commercial and agricultural real estate loans generally require loan-to-value limits of less than 80%. Depending upon the type of loan, past credit history, and current operating results, we may require the borrower to pledge accounts receivable, inventory, and property and equipment. Personal guarantees are generally required from the owners of closely held corporations, partnerships, and sole proprietorships. In addition, we require annual financial statements, prepare cash flow analyses, and review credit reports as deemed necessary.

We offer adjustable rate mortgages, fixed rate balloon mortgages, construction loans, and fixed rate mortgage loans which typically have amortization periods up to a maximum of 30 years. Fixed rate loans with an amortization of greater than 15 years are generally sold upon origination to Freddie Mac. Fixed rate residential real estate loans with an amortization of 15 years or less may be held in our portfolio, held for future sale, or sold upon origination. We consider the direction of interest rates, the sensitivity of our balance sheet to changes in interest rates, and overall loan demand to determine whether or not to sell these loans to Freddie Mac.

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Our lending policies generally limit the maximum loan-to-value ratio on residential real estate loans to 95% of the lower of the appraised value of the property or the purchase price, with the condition that private mortgage insurance is required on loans with loan to value ratios in excess of 80%. Substantially all loans upon origination have a loan to value ratio of less than 80%. Underwriting criteria for residential real estate loans include: evaluation of the borrower s ability to make monthly payments, the value of the property securing the loan, ensuring the payment of principal, interest, taxes, and hazard insurance does not exceed 28% of a borrower s gross income, all debt servicing does not exceed 36% of income, acceptable credit reports, verification of employment, income, and financial information. Appraisals are performed by independent appraisers and reviewed internally. All mortgage loan requests are reviewed by our mortgage loan committee or through a secondary market automated underwriting system; loans in excess of $400 require the approval of our Internal Loan Committee, the Board of Directors Loan Committee, or the Board of Directors.

Consumer loans include automobile loans, secured and unsecured personal loans, and overdraft protection related loans. Loans are amortized generally for a period of up to 6 years. The underwriting emphasis is on a borrower s perceived intent and ability to pay rather than collateral value. No consumer loans are sold to the secondary market.

The ALLL is established as losses are estimated to have occurred through a provision for loan losses charged to earnings. Loan losses are charged against the ALLL when we believe the uncollectibility of the loan balance is confirmed. Subsequent recoveries, if any, are credited to the ALLL.

The ALLL is evaluated on a regular basis and is based upon a periodic review of the collectibility of the loans in light of historical experience, the nature and volume of the loan portfolio, adverse situations that may affect the borrower s ability to repay, estimated value of any underlying collateral, and prevailing economic conditions. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available.

The primary factors behind the determination of the level of the ALLL are specific allocations for impaired loans, historical loss percentages, as well as unallocated components. Specific allocations for impaired loans are primarily determined based on the difference between the net realizable value of the loan s underlying collateral or the net present value of the projected payment stream and our recorded investment. Historical loss allocations were calculated at the loan class and segment levels based on a migration analysis of the loan portfolio over the preceding four years. An unallocated component is maintained to cover uncertainties that we believe affect our estimate of probable losses based on qualitative factors. The unallocated component of the allowance reflects the margin of imprecision inherent in the underlying assumptions used in the methodologies for estimating specific and general losses in the portfolio.

A summary of changes in the ALLL and the recorded investment in loans by segments follows:

	Allowance for Loan Losses Three Months Ended September 30, 2012					
	Commercial	Agricultural	Residential Real Estate	Consumer	Unallocated	Total
Allowance for loan losses						
July 1, 2012	$ 6,008	$ 433	$ 3,669	$ 667	$ 1,541	$ 12,318
Loans charged off	(271)		(213)	(127)		(611)
Recoveries	40		34	81		155
Provision for loan losses	1,132	6	(356)	91	(673)	200
September 30, 2012	**$ 6,909**	**$ 439**	**$ 3,134**	**$ 712**	**$ 868**	**$ 12,062**

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	Allowance for Loan Losses Nine Months Ended September 30, 2012					
	Commercial	Agricultural	Residential Real Estate	Consumer	Unallocated	Total
Allowance for loan losses						
January 1, 2012	$ 6,284	$ 1,003	$ 2,980	$ 633	$ 1,475	$ 12,375
Loans charged off	(957)		(566)	(364)		(1,887)
Recoveries	168		95	211		474
Provision for loan losses	1,414	(564)	625	232	(607)	1,100
September 30, 2012	**$ 6,909**	**$ 439**	**$ 3,134**	**$ 712**	**$ 868**	**$ 12,062**

	Allowance for Loan Losses and Recorded Investment in Loans As of September 30, 2012					
	Commercial	Agricultural	Residential Real Estate	Consumer	Unallocated	Total
Allowance for loan losses						
Individually evaluated for impairment	$ 2,915	$	$ 1,354	$	$	$ 4,269
Collectively evaluated for impairment	3,994	439	1,780	712	868	7,793
Total	**$ 6,909**	**$ 439**	**$ 3,134**	**$ 712**	**$ 868**	**$ 12,062**
Loans						
Individually evaluated for impairment	$ 16,593	$ 2,281	$ 8,429	$ 79		$ 27,382
Collectively evaluated for impairment	352,773	81,158	272,002	33,436		739,369
Total	**$ 369,366**	**$ 83,439**	**$ 280,431**	**$ 33,515**		**$ 766,751**

	Allowance for Loan Losses Three Months Ended September 30, 2011					
	Commercial	Agricultural	Residential Real Estate	Consumer	Unallocated	Total
Allowance for loan losses						
July 1, 2011	$ 6,738	$ 764	$ 2,885	$ 660	$ 1,331	$ 12,378
Loans charged off	(215)		(857)	(98)		(1,170)
Recoveries	75	1	39	87		202
Provision for loan losses	116	(331)	1,148	(3)	33	963
September 30, 2011	**$ 6,714**	**$ 434**	**$ 3,215**	**$ 646**	**$ 1,364**	**$ 12,373**

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	Commercial	Agricultural	Residential Real Estate	Consumer	Unallocated	Total
	Allowance for Loan Losses Nine Months Ended September 30, 2011					
Allowance for loan losses						
January 1, 2011	$ 6,048	$ 1,033	$ 3,198	$ 605	$ 1,489	$ 12,373
Loans charged off	(1,084)	(1)	(1,735)	(382)		(3,202)
Recoveries	421	1	142	255		819
Provision for loan losses	1,329	(599)	1,610	168	(125)	2,383
September 30, 2011	**$ 6,714**	**$ 434**	**$ 3,215**	**$ 646**	**$ 1,364**	**$ 12,373**

	Commercial	Agricultural	Residential Real Estate	Consumer	Unallocated	Total
	Allowance for Loan Losses and Recorded Investment in Loans As of December 31, 2011					
Allowance for loan losses						
Individually evaluated for impairment	$ 2,152	$ 822	$ 1,146	$	$	$ 4,120
Collectively evaluated for impairment	4,132	181	1,834	633	1,475	8,255
Total	**$ 6,284**	**$ 1,003**	**$ 2,980**	**$ 633**	**$ 1,475**	**$ 12,375**
Loans						
Individually evaluated for impairment	$ 14,097	$ 3,384	$ 7,664	$ 105		$ 25,250
Collectively evaluated for impairment	351,617	71,261	270,696	31,467		725,041
Total	**$ 365,714**	**$ 74,645**	**$ 278,360**	**$ 31,572**		**$ 750,291**

The following table displays the credit quality indicators for commercial and agricultural credit exposures based on internally assigned credit ratings as of:

	September 30, 2012					
	Commercial			Agricultural		
	Real Estate	Other	Total	Real Estate	Other	Total
Rating						
2 - High quality	$ 25,824	$ 16,871	$ 42,695	$ 2,591	$ 2,196	$ 4,787
3 - High satisfactory	82,108	26,977	109,085	16,293	9,615	25,908
4 - Low satisfactory	126,649	47,965	174,614	25,073	20,704	45,777
5 - Special mention	13,224	2,271	15,495	961	2,751	3,712
6 - Substandard	19,124	2,404	21,528	1,631	1,363	2,994
7 - Vulnerable	2,783	2,358	5,141			
8 - Doubtful	785	23	808		261	261
Total	**$ 270,497**	**$ 98,869**	**$ 369,366**	**$ 46,549**	**$ 36,890**	**$ 83,439**

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	December 31, 2011					
	Commercial			Agricultural		
	Real Estate	Other	Total	Real Estate	Other	Total
Rating						
2 - High quality	$ 11,113	$ 11,013	$ 22,126	$ 3,583	$ 1,390	$ 4,973
3 - High satisfactory	90,064	29,972	120,036	11,154	5,186	16,340
4 - Low satisfactory	118,611	57,572	176,183	24,253	15,750	40,003
5 - Special mention	15,482	4,200	19,682	3,863	2,907	6,770
6 - Substandard	19,017	4,819	23,836	1,640	4,314	5,954
7 - Vulnerable	187		187			
8 - Doubtful	3,621	43	3,664	190	415	605
Total	**$ 258,095**	**$ 107,619**	**$ 365,714**	**$ 44,683**	**$ 29,962**	**$ 74,645**

Internally assigned risk ratings are reviewed, at a minimum, when loans are renewed or when management has knowledge of improvements or deterioration of the credit quality of individual credits. Descriptions of the internally assigned risk ratings for commercial and agricultural loans are as follows:

1. **EXCELLENT Substantially Risk Free**

Credit has strong financial condition and solid earnings history, characterized by:

- High liquidity, strong cash flow, low leverage.
- Unquestioned ability to meet all obligations when due.
- Experienced management, with management succession in place.
- Secured by cash.

2. **HIGH QUALITY Limited Risk**

Credit with sound financial condition and has a positive trend in earnings supplemented by:

- Favorable liquidity and leverage ratios.
- Ability to meet all obligations when due.
- Management with successful track record.
- Steady and satisfactory earnings history.

If loan is secured, collateral is of high quality and readily marketable.

Access to alternative financing.

Well defined primary and secondary source of repayment.

If supported by guaranty, the financial strength and liquidity of the guarantor(s) are clearly evident.

3. **HIGH SATISFACTORY** **Reasonable Risk**
Credit with satisfactory financial condition and further characterized by:

Working capital adequate to support operations.

Cash flow sufficient to pay debts as scheduled.

Management experience and depth appear favorable.

Loan performing according to terms.

If loan is secured, collateral is acceptable and loan is fully protected.

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4. **LOW SATISFACTORY Acceptable Risk**
Credit with bankable risks, although some signs of weaknesses are shown:

- Would include most start-up businesses.
- Occasional instances of trade slowness or repayment delinquency may have been 10-30 days slow within the past year.
- Management s abilities are apparent, yet unproven.
- Weakness in primary source of repayment with adequate secondary source of repayment.
- Loan structure generally in accordance with policy.
- If secured, loan collateral coverage is marginal.
- Adequate cash flow to service debt, but coverage is low.

To be classified as less than satisfactory, only one of the following criteria must be met.

5. **SPECIAL MENTION Criticized**
Credit constitutes an undue and unwarranted credit risk but not to the point of justifying a classification of substandard. The credit risk may be relatively minor yet constitute an unwarranted risk in light of the circumstances surrounding a specific loan:

- Downward trend in sales, profit levels, and margins.
- Impaired working capital position.
- Cash flow is strained in order to meet debt repayment.
- Loan delinquency (30-60 days) and overdrafts may occur.
- Shrinking equity cushion.
- Diminishing primary source of repayment and questionable secondary source.

Management abilities are questionable.

Weak industry conditions.

Litigation pending against the borrower.

Collateral or guaranty offers limited protection.

Negative debt service coverage, however the credit is well collateralized and payments are current.

6. **SUBSTANDARD Classified**
Credit where the borrower s current net worth, paying capacity, and value of the collateral pledged is inadequate. There is a distinct possibility that we will implement collection procedures if the loan deficiencies are not corrected. In addition, the following characteristics may apply:

Sustained losses have severely eroded the equity and cash flow.

Deteriorating liquidity.

Serious management problems or internal fraud.

Original repayment terms liberalized.

Likelihood of bankruptcy.

Inability to access other funding sources.

Reliance on secondary source of repayment.

Litigation filed against borrower.

Collateral provides little or no value.

Requires excessive attention of the loan officer.

Borrower is uncooperative with loan officer.

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7. **VULNERABLE Classified**
Credit is considered Substandard and warrants placing on nonaccrual. Risk of loss is being evaluated and exit strategy options are under review. Other characteristics that may apply:

- Insufficient cash flow to service debt.
- Minimal or no payments being received.
- Limited options available to avoid the collection process.
- Transition status, expect action will take place to collect loan without immediate progress being made.

8. **DOUBTFUL Workout**
Credit has all the weaknesses inherent in a Substandard loan with the added characteristic that collection and/or liquidation is pending. The possibility of a loss is extremely high, but its classification as a loss is deferred until liquidation procedures are completed, or reasonably estimable. Other characteristics that may apply:

- Normal operations are severely diminished or have ceased.
- Seriously impaired cash flow.
- Original repayment terms materially altered.
- Secondary source of repayment is inadequate.
- Survivability as a going concern is impossible.
- Collection process has begun.
- Bankruptcy petition has been filed.
- Judgments have been filed.
- Portion of the loan balance has been charged-off.

9. **LOSS Charge off**

Credits are considered uncollectible and of such little value that their continuance as bankable assets is not warranted. This classification is for charged off loans but does not mean that the asset has absolutely no recovery or salvage value. These loans are further characterized by:

- Liquidation or reorganization under bankruptcy, with poor prospects of collection.
- Fraudulently overstated assets and/or earnings.
- Collateral has marginal or no value.
- Debtor cannot be located.
- Over 120 days delinquent.

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Our primary credit quality indicators for residential real estate and consumer loans is the individual loan s past due aging. The following tables summarize the past due and current loans as of:

	September 30, 2012					
	Accruing Interest and Past Due:			Total Past Due and		
	30-89 Days	90 Days or More	Nonaccrual	Nonaccrual	Current	Total
Commercial						
Commercial real estate	$ 4,100	$ 86	$ 2,939	$ 7,125	$ 263,372	$ 270,497
Commercial other	680	114	2,369	3,163	95,706	98,869
Total commercial	4,780	200	5,308	10,288	359,078	369,366
Agricultural						
Agricultural real estate	36	91		127	46,422	46,549
Agricultural other	328		261	589	36,301	36,890
Total agricultural	364	91	261	716	82,723	83,439
Residential real estate						
Senior liens	2,824	177	1,239	4,240	218,895	223,135
Junior liens	184		32	216	17,233	17,449
Home equity lines of credit	238		185	423	39,424	39,847
Total residential real estate	3,246	177	1,456	4,879	275,552	280,431
Consumer						
Secured	220			220	27,938	28,158
Unsecured	64			64	5,293	5,357
Total consumer	284			284	33,231	33,515
Total	**$ 8,674**	**$ 468**	**$ 7,025**	**$ 16,167**	**$ 750,584**	**$ 766,751**

	December 31, 2011					
	Accruing Interest and Past Due:			Total Past Due and		
	30-89 Days	90 Days or More	Nonaccrual	Nonaccrual	Current	Total
Commercial						
Commercial real estate	$ 1,721	$ 364	$ 4,176	$ 6,261	$ 251,834	$ 258,095
Commercial other	426	3	25	454	107,165	107,619
Total commercial	2,147	367	4,201	6,715	358,999	365,714
Agricultural						
Agricultural real estate		99	189	288	44,395	44,683
Agricultural other	2		415	417	29,545	29,962

Total agricultural	2	99	604	705	73,940	74,645
Residential real estate						
Senior liens	3,004	124	1,292	4,420	213,181	217,601
Junior liens	235	40	94	369	20,877	21,246
Home equity lines of credit	185	125	198	508	39,005	39,513
Total residential real estate	3,424	289	1,584	5,297	273,063	278,360
Consumer						
Secured	158	5		163	26,011	26,174
Unsecured	23			23	5,375	5,398
Total consumer	181	5		186	31,386	31,572
Total	**$ 5,754**	**$ 760**	**$ 6,389**	**$ 12,903**	**$ 737,388**	**$ 750,291**

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Impaired Loans

Loans may be classified as impaired if they meet one or more of the following criteria:

1. There has been a chargeoff of its principal balance (in whole or in part);

2. The loan has been classified as a Troubled Debt Restructuring (TDR); or

3. The loan is in nonaccrual status.

Impairment is measured on a loan by loan basis for commercial, commercial real estate, agricultural, or agricultural real estate loans by either the present value of expected future cash flows discounted at the loan s effective interest rate, the loan s obtainable market price, or the fair value of the collateral, less cost to sell, if the loan is collateral dependent. Large groups of smaller balance homogeneous loans are collectively evaluated for impairment.

Interest income is recognized on impaired loans in nonaccrual status on the cash basis, but only after all principal has been collected. For impaired loans not in nonaccrual status, interest income is recognized daily as earned according to the terms of the loan agreement.

The following is a summary of information pertaining to impaired loans as of and for the periods ended:

	September 30, 2012			December 31, 2011		
	Outstanding Balance	Unpaid Principal Balance	Valuation Allowance	Outstanding Balance	Unpaid Principal Balance	Valuation Allowance
Impaired loans with a valuation allowance						
Commercial real estate	$ 6,392	$ 6,673	$ 2,259	$ 5,014	$ 5,142	$ 1,881
Commercial other	3,047	3,047	656	734	734	271
Agricultural other				2,689	2,689	822
Residential real estate senior liens	8,089	9,237	1,326	7,271	8,827	1,111
Residential real estate junior liens	152	198	28	195	260	35
Total impaired loans with a valuation allowance	**$ 17,680**	**$ 19,155**	**$ 4,269**	**$ 15,903**	**$ 17,652**	**$ 4,120**
Impaired loans without a valuation allowance						
Commercial real estate	$ 5,356	$ 6,128		$ 7,984	$ 10,570	
Commercial other	1,798	1,908		365	460	
Agricultural real estate				190	190	
Agricultural other	2,281	2,401		505	625	
Residential real estate senior liens	3	65				
Home equity lines of credit	185	485		198	498	
Consumer secured	79	88		105	114	
Total impaired loans without a valuation allowance	**$ 9,702**	**$ 11,075**		**$ 9,347**	**$ 12,457**	
Impaired loans						
Commercial	$ 16,593	$ 17,756	$ 2,915	$ 14,097	$ 16,906	$ 2,152
Agricultural	2,281	2,401		3,384	3,504	822
Residential real estate	8,429	9,985	1,354	7,664	9,585	1,146
Consumer	79	88		105	114	

Total impaired loans	**$ 27,382**	**$ 30,230**	**$ 4,269**	**$ 25,250**	**$ 30,109**	**$ 4,120**

	Three Months Ended September 30, 2012		Nine Months Ended September 30, 2012	
	Average Outstanding Balance	Interest Income Recognized	Average Outstanding Balance	Interest Income Recognized
Impaired loans with a valuation allowance				
Commercial real estate	$ 6,260	$ 106	$ 6,197	$ 287
Commercial other	1,996	67	1,183	95
Agricultural other	1,023		1,878	73
Residential real estate senior liens	7,992	86	7,802	261
Residential real estate junior liens	158	3	174	7
Total impaired loans with a valuation allowance	**$ 17,429**	**$ 262**	**$ 17,234**	**$ 723**
Impaired loans without a valuation allowance				
Commercial real estate	$ 5,651	$ 72	$ 6,749	$ 251
Commercial other	2,026	15	1,860	80
Agricultural real estate	179		214	
Agricultural other	1,417	34	869	41
Residential real estate senior liens	2	2	1	2
Home equity lines of credit	188	6	194	14
Consumer secured	81	2	90	5
Total impaired loans without a valuation allowance	**$ 9,544**	**$ 131**	**$ 9,977**	**$ 393**
Impaired loans				
Commercial	$ 15,933	$ 260	$ 15,989	$ 713
Agricultural	2,619	34	2,961	114
Residential real estate	8,340	97	8,171	284
Consumer	81	2	90	5
Total impaired loans	**$ 26,973**	**$ 393**	**$ 27,211**	**$ 1,116**

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	Three Months Ended September 30, 2011		Nine Months Ended September 30, 2011	
	Average Outstanding Balance	Interest Income Recognized	Average Outstanding Balance	Interest Income Recognized
Impaired loans with a valuation allowance				
Commercial real estate	$ 4,770	$ 130	$ 4,402	$ 250
Commercial other	586	16	577	16
Agricultural real estate	58	3	58	3
Agricultural other	720	(38)	1,140	4
Residential real estate senior liens	6,174	115	5,621	221
Residential real estate junior liens	179	1	165	5
Total impaired loans with a valuation allowance	**$ 12,487**	**$ 227**	**$ 11,963**	**$ 499**
Impaired loans without a valuation allowance				
Commercial real estate	$ 5,743	$ 124	$ 3,878	$ 219
Commercial other	1,941	37	1,076	124
Agricultural real estate	207	2	112	1
Agricultural other	2,411	112	1,770	151
Residential real estate senior liens		1	201	1
Home equity lines of credit	100	10	100	10
Consumer secured	50	2	61	5
Total impaired loans without a valuation allowance	**$ 10,452**	**$ 288**	**$ 7,198**	**$ 511**
Impaired loans				
Commercial	$ 13,040	$ 307	$ 9,933	$ 609
Agricultural	3,396	79	3,080	159
Residential real estate	6,453	127	6,087	237
Consumer	50	2	61	5
Total impaired loans	**$ 22,939**	**$ 515**	**$ 19,161**	**$ 1,010**

Impaired loans, which include TDR s, had $173 and $68 of unfunded commitments under lines of credit as of September 30, 2012 and 2011, respectively.

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Troubled Debt Restructurings

Loan modifications are considered to be TDR s when a concession has been granted to a borrower who is experiencing financial difficulties.

Typical concessions granted include, but are not limited to:

1. Agreeing to interest rates below prevailing market rates for debt with similar risk characteristics.

2. Extending the amortization period beyond typical lending guidelines for debt with similar risk characteristics.

3. Forbearance of principal.

4. Forbearance of accrued interest.

To determine if a borrower is experiencing financial difficulties, we consider if:

1. The borrower is currently in default on any of their debt.

2. The borrower will likely default on any of their debt if the concession is not granted.

3. The borrower s cash flow is insufficient to service all of their debt if the concession is not granted.

4. The borrower has declared, or is in the process of declaring, bankruptcy.

5. The borrower is unlikely to continue as a going concern (if the entity is a business).

The following is a summary of information pertaining to TDR s for the three and nine month periods ended September 30, 2012:

	Loans Restructured in the Three Month Period ended September 30, 2012			Loans Restructured in the Nine Month Period ended September 30, 2012		
	Number of Loans	Pre-Modification Recorded Investment	Post-Modification Recorded Investment	Number of Loans	Pre-Modification Recorded Investment	Post-Modification Recorded Investment
Commercial other	1	$ 178	$ 178	27	$ 5,069	$ 5,069
Agricultural other				6	561	561
Residential real estate senior liens				12	1,405	1,405
Residential real estate junior liens	1	22	22	1	22	22
Total	**2**	**$ 200**	**$ 200**	**46**	**$ 7,057**	**$ 7,057**

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	Loans Restructured in the Three Month Period ended September 30, 2011			Loans Restructured in the Nine Month Period ended September 30, 2011		
	Number of Loans	Pre-Modification Recorded Investment	Post-Modification Recorded Investment	Number of Loans	Pre-Modification Recorded Investment	Post-Modification Recorded Investment
Commercial						
Commercial real estate	1	$ 408	$ 408	1	$ 408	$ 408
Commercial other	21	4,069	3,737	42	12,143	11,700
Total commercial	22	4,477	4,145	43	12,551	12,108
Agricultural other	3	143	143	11	1,481	1,481
Residential real estate senior liens	3	165	165	23	2,454	2,424
Consumer secured	3	34	34	5	50	50
Total	**31**	**$ 4,819**	**$ 4,487**	**82**	**$ 16,536**	**$ 16,063**

	Loans Restructured in the Three Month Period Ended September 30, 2012				Loans Restructured in the Nine Month Period Ended September 30, 2012			
	Below Market Interest Rate		Below Market Interest Rate and Extension of Amortization Period		Below Market Interest Rate		Below Market Interest Rate and Extension of Amortization Period	
	Number of Loans	Pre-Modification Recorded Investment	Number of Loans	Pre-Modification Recorded Investment	Number of Loans	Pre-Modification Recorded Investment	Number of Loans	Pre-Modification Recorded Investment
Commercial other	1	$ 178		$	25	$ 4,924	2	$ 145
Agricultural other					6	561		
Residential real estate senior liens					4	324	8	1,081
Residential real estate junior liens			1	22			1	22
Total	**1**	**$ 178**	**1**	**$ 22**	**35**	**$ 5,809**	**11**	**$ 1,248**

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	Loans Restructured in the Three Month Period Ended September 30, 2011								
	Below Market Interest Rate			Extension of Amortization Period			Below Market Interest Rate and Extension of Amortization Period		
	Number of Loans	Pre-Modification Recorded Investment		Number of Loans	Pre-Modification Recorded Investment		Number of Loans	Pre-Modification Recorded Investment	
Commercial									
Commercial real estate	1	$	408		$			$	
Commercial other	21		4,069						
Total commercial	22		4,477						
Agricultural other	3		143						
Residential real estate senior liens	1		85	1		7	1		73
Consumer secured	3		34						
Total	**29**	**$**	**4,739**	**1**	**$**	**7**	**1**	**$**	**73**

	Loans Restructured in the Nine Month Period Ended September 30, 2012								
	Below Market Interest Rate			Extension of Amortization Period			Below Market Interest Rate and Extension of Amortization Period		
	Number of Loans	Pre-Modification Recorded Investment		Number of Loans	Pre-Modification Recorded Investment		Number of Loans	Pre-Modification Recorded Investment	
Commercial									
Commercial real estate	1	$	408		$			$	
Commercial other	38		9,500	3		913	1		1,730
Total commercial	39		9,908	3		913	1		1,730
Agricultural other	11		1,481						
Residential real estate senior liens	18		2,083	2		57	3		314
Consumer secured	5		50						
Total	**73**	**$**	**13,522**	**5**	**$**	**970**	**4**	**$**	**2,044**

We did not restructure any loans through the forbearance of principal or accrued interest in the three or nine month periods ended September 30, 2012 or 2011.

Based on our historical loss experience, losses associated with TDR s are not significantly different than other impaired loans within the same loan segment. As such, TDR s, including TDR s that have been modified in the past 12 months that subsequently defaulted, are analyzed in the same manner as other impaired loans within their respective loan segment.

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Following is a summary of loans that defaulted in the three and nine month periods ended September 30, 2012, which were modified within 12 months prior to the default date:

	Three Months Ended September 30, 2012				Nine Months Ended September 30, 2012			
	Number of Loans	Pre-Default Recorded Investment	Charge Off Recorded Upon Default	Post-Default Recorded Investment	Number of Loans	Pre-Default Recorded Investment	Charge Off Recorded Upon Default	Post-Default Recorded Investment
Commercial other	2	$ 50	$ 25	$ 25	3	$ 132	$ 66	$ 66
Residential real estate senior liens					1	47	43	4
Consumer secured	1	8	8		1	8	8	
Total	**3**	**$ 58**	**$ 33**	**$ 25**	**5**	**$ 187**	**$ 117**	**$ 70**

Total Depreciation and Other Amortization
$
29,238

$
29,484

$
(246
)

(0.8
)%
Depreciation and other amortization for same store properties remained relatively unchanged. Depreciation and other amortization from acquired properties increased $0.1 million due to properties acquired subsequent to December 31, 2011. Depreciation and other amortization from sold properties decreased $0.9 million due to properties sold subsequent to December 31, 2011. Depreciation and other amortization for (re)developments and land increased $0.3 million primarily due to an increase in substantial completion of developments. Corporate furniture, fixtures and equipment depreciation expense decreased $0.1 million due to assets becoming fully depreciated.
Interest income decreased $0.1 million, or 11.5%, primarily due to a decrease in the weighted average note receivable balance outstanding for the three months ended June 30, 2013 as compared to the three months ended June 30, 2012.
Interest expense for the three months ended June 30, 2013 and 2012, respectively, decreased $2.7 million, or 12.9%, primarily due to a decrease in the weighted average debt balance outstanding for the three months ended June 30, 2013 ($1,313.5 million) as compared to the three months ended June 30, 2012 ($1,468.1 million), and an increase in capitalized interest of $1.0 million for the three months ended June 30, 2013 as compared to the three months ended June 30, 2012 due to an increase in development activities, partially offset by an increase in the weighted average interest rate for the three months ended June 30, 2013 (5.95%), as compared to the three months ended June 30, 2012 (5.82%).
Amortization of deferred financing costs remained relatively unchanged.
We recorded $0.06 million in mark-to-market gain, inclusive of $0.3 million in swap payments, for the three months ended June 30, 2013, as compared to $0.4 million in mark-to-market loss, inclusive of $0.2 million in swap payments, for the three months ended June 30, 2012.

For the three months ended June 30, 2013, we recognized a net loss from retirement of debt of $4.4 million due to the partial repurchase of certain series of our senior unsecured notes and the early payoff of certain mortgage loans. For the three months ended June 30, 2012, we recognized a net loss from retirement of debt of $6.2 million due to the partial repurchase of certain series of our senior unsecured notes.
Equity in income of joint ventures remained relatively unchanged.

The income tax provision decreased $5.4 million or 99.9% during the three months ended June 30, 2013 compared to the three months ended June 30, 2012 primarily due to a one-time IRS audit adjustment related to the 2009 liquidation of a former taxable REIT subsidiary that was recorded during the three months ended June 30, 2012.

The following table summarizes certain information regarding the industrial properties included in discontinued operations for the three months ended June 30, 2013 and 2012.

	Three Months Ended June 30,	
	2013	2012
	($ in 000's)	
Total Revenues	$595	$3,474
Property Expenses	(282)	(1,511)
Impairment of Real Estate	(176)	—
Depreciation and Amortization	(81)	(950)
Gain on Sale of Real Estate	13,481	1,386
Income from Discontinued Operations	$13,537	$2,399

Income from discontinued operations for the three months ended June 30, 2013 reflects the results of operations and gain on sale of real estate relating to eight industrial properties that were sold during the three months ended June 30, 2013 and the results of operations of two industrial properties that were identified as held for sale at June 30, 2013. The impairment loss for the three months ended June 30, 2013 of $0.2 million primarily relates to an impairment charge recorded due to the carrying values of certain properties exceeding the estimated fair value, less costs to sell, based upon a third party purchase contract for properties held for sale during 2013.

Income from discontinued operations for the three months ended June 30, 2012 reflects the gain on sale of real estate relating to four industrial properties that were sold during the three months ended June 30, 2012, the results of operations of 28 industrial properties that were sold during the year ended December 31, 2012, the results of operations of 12 industrial properties that were sold during the six months ended June 30, 2013 and the results of operations of the two industrial properties identified as held for sale at June 30, 2013.

LEASING ACTIVITY

The following table provides a summary of our leasing activity for the three and six months ended June 30, 2013. The table does not include month to month leases or leases with terms less than twelve months. New leases where there were no prior comparable leases, due to extended downtime or materially different lease structures, are also excluded.

	Number of Leases Signed	Square Feet Signed (in 000's)	Net Effective Rent Per Square Foot (1)	GAAP Basis Rent Growth (2)	Weighted Average Lease Term (3)	Turnover Costs Per Square Foot (4)	Weighted Average Retention (5)
New Leases - Second Quarter 2013	58	1,036	$ 5.16	(6.5)%	6.0	$ 10.17	N/A
Renewal Leases - Second Quarter 2013	117	2,116	$ 4.75	5.7%	3.1	$ 1.30	74.5%
Second Quarter 2013	175	3,152	$ 4.88	1.1%	4.1	$ 4.21	74.5%
New Leases - Year to Date 2013	109	1,600	$ 4.80	(6.0)%	5.9	$ 9.08	N/A
Renewal Leases - Year to Date 2013	228	4,965	$ 4.35	7.6%	3.2	$ 1.09	77.4%
Year to Date 2013	337	6,565	$ 4.46	3.7%	3.9	$ 3.04	77.4%

(1) Net effective rent is the average net rent calculated in accordance with GAAP, over the term of the lease.
(2) GAAP basis rent growth is a ratio of the change in net effective rent (on a GAAP basis, including straight-line rent adjustments as required by GAAP) compared to the net effective rent (on a GAAP basis) of the comparable lease.
(3) The lease term is expressed in years. Assumes no exercise of lease renewal option, if any.
(4)

Turnover costs are comprised of the costs incurred or capitalized for improvements of vacant and renewal spaces, as well as the commissions paid and costs capitalized for leasing transactions. Turnover costs per square foot represent the total turnover costs expected to be incurred on the leases signed during the period and do not reflect actual expenditures for the period.

(5) Represents the weighted average square feet of tenants renewing their respective leases.

During the three and six months ended June 30, 2013, we signed 44 and 73 new leases, respectively, with free rent periods during the lease term on 0.9 million and 1.2 million square feet of GLA, respectively. Total concessions are $2.0 million and $2.3 million, respectively, associated with these new leases. Additionally, during the three and six months ended June 30, 2013, we signed 25 and 43 renewal leases, respectively, with free rent periods during the lease term on 0.6 million and 1.0 million square feet of GLA, respectively. Total concessions are $0.4 million and $0.7 million, respectively, associated with these renewal leases.

LIQUIDITY AND CAPITAL RESOURCES

At June 30, 2013, our cash and cash equivalents were approximately $4.7 million. We also had $342.0 million available for additional borrowings under our Unsecured Credit Facility, subject to certain restrictions.

We considered our short-term (through June 30, 2014) liquidity needs and the adequacy of our estimated cash flow from operations and other expected liquidity sources to meet these needs. Our 2014 Notes, in the aggregate principal amount of $81.8 million, are due June 1, 2014. Additionally, we have $22.3 million in mortgage loans payable outstanding at June 30, 2013 that have maturities prior to June 30, 2014. We expect to satisfy the payment obligations on the 2014 Notes and the mortgage loans payable due prior to June 30, 2014 with borrowings on our Unsecured Credit Facility. With the exception of the 2014 Notes and the $22.3 million of mortgage loans payable, we believe that our principal short-term liquidity needs are to fund normal recurring expenses, property acquisitions, developments, renovations, expansions and other nonrecurring capital improvements, debt service requirements, preferred dividends, the minimum distributions required to maintain our REIT qualification under the Code and distributions approved by our Board of Directors. We anticipate that these needs will be met with cash flows provided by operating activities as well as the disposition of select assets. These needs may also be met by the issuance of additional equity securities, subject to market conditions.

We expect to meet long-term (after June 30, 2014) liquidity requirements such as property acquisitions, developments, scheduled debt maturities, major renovations, expansions and other nonrecurring capital improvements through the disposition of select assets, long-term unsecured and secured indebtedness and the issuance of additional equity securities, subject to market conditions.

We also financed the development or acquisition of additional properties through borrowings under our Unsecured Credit Facility and may finance the development or acquisition of additional properties through such borrowings, to the extent capacity is available, in the future. At June 30, 2013, borrowings under our Unsecured Credit Facility bore interest at a weighted average interest rate of 1.893%. As of August 2, 2013, we had approximately $422.0 million available for additional borrowings under our New Credit Facility, subject to certain restrictions. Our New Credit Facility contains certain financial covenants including limitations on incurrence of debt and debt service coverage. Our access to borrowings may be limited if we fail to meet any of these covenants. We believe that we were in compliance with our financial covenants as of June 30, 2013, and we anticipate that we will be able to operate in compliance with our financial covenants for the remainder of 2013.

Our senior unsecured notes have been assigned credit ratings from Standard & Poor’s, Moody’s and Fitch Ratings of BB+/Ba2/BB, respectively. In the event of a downgrade, we believe we would continue to have access to sufficient capital; however, our cost of borrowing would increase and our ability to access certain financial markets may be limited.

Six Months Ended June 30, 2013

Net cash provided by operating activities of approximately $45.7 million for the six months ended June 30, 2013, was comprised primarily of the non-cash adjustments of approximately $57.8 million and net income of approximately $10.2 million, offset by the net change in operating assets and liabilities of approximately $18.2 million and payments of premiums, discounts and prepayment penalties associated with retirement of debt of approximately $4.1 million. The adjustments for the non-cash items of approximately $57.8 million are primarily comprised of depreciation and amortization of approximately $63.2 million, the loss from retirement of debt of approximately $5.6 million, the impairment of real estate of approximately $1.6 million and the provision for bad debt of approximately $0.5 million, offset by the gain on sale of real estate of approximately $10.7 million and the effect of the straight-lining of rental income of approximately $2.4 million.

Net cash used in investing activities of approximately $48.5 million for the six months ended June 30, 2013, was comprised primarily of the acquisition of one industrial property and several land parcels, the development of real estate, capital expenditures related to the improvement of existing real estate and payments related to leasing activities, offset by the net proceeds from the sale of real estate, a decrease in escrows and the repayments on our notes receivable.

During the six months ended June 30, 2013, we acquired one industrial property comprising approximately 0.5 million square feet of GLA and several land parcels. The purchase price of these acquisitions totaled approximately $46.5 million, excluding costs incurred in conjunction with the acquisition of the industrial property and land parcels.

During the six months ended June 30, 2013, we sold 12 industrial properties comprising approximately 1.3 million square feet of GLA and two land parcels. Proceeds from the sales of the 12 industrial properties and two land parcels, net of closing costs, were approximately $50.4 million. We are in various stages of discussions with third parties for the sale of additional properties and plan to continue to selectively market other properties for sale for the remainder of 2013.

Net cash provided by financing activities of approximately $2.6 million for the six months ended June 30, 2013, was comprised primarily of net proceeds from the issuance of common stock and net proceeds from our Unsecured Credit Facility, offset by the redemption of our 7.25% Series J Cumulative Redeemable Preferred Stock (the "Series J Preferred Stock"), repayments on our senior unsecured notes and mortgage loans payable, common stock and preferred stock dividends and advanced preferred stock dividends, the repurchase and retirement of restricted stock, payments on the interest rate swap agreement and payments of equity issuance costs.

During the six months ended June 30, 2013, we paid off and retired prior to maturity mortgage loans in the amount of $26.2 million and we repurchased $29.0 million of our unsecured notes at an aggregate purchase price of $32.6 million. We may from time to time repay additional amounts of our outstanding debt. Any repayments would depend upon prevailing market conditions, our liquidity requirements, contractual restrictions and other factors we consider important. Future repayments may materially impact our liquidity, taxable income and results of operations.

During the six months ended June 30, 2013, we redeemed the remaining 4,000,000 Depositary Shares of the Series J Preferred Stock for $25.00 per Depositary Share, or $100.0 million in the aggregate, and paid a prorated second quarter dividend of $0.055382 per Depositary Share, totaling approximately $0.2 million.

During the six months ended June 30, 2013, we issued 8,400,000 shares of the Company's common stock through a public offering, resulting in proceeds, net of the underwriter's discount, of approximately $132.3 million. Additionally, during the six months ended June 30, 2013, we issued 2,315,704 shares of the Company's common stock through the Company's "at-the-market" equity offering program, resulting in net proceeds of approximately $41.8 million. We may access the equity markets again, subject to contractual restrictions and market conditions. To the extent additional equity offerings occur, we expect to use at least a portion of the proceeds received to reduce our indebtedness or fund property acquisitions and developments.

Market Risk

The following discussion about our risk-management activities includes “forward-looking statements” that involve risk and uncertainties. Actual results could differ materially from those projected in the forward-looking statements. Our business subjects us to market risk from interest rates, and to a much lesser extent, foreign currency fluctuations.

Interest Rate Risk

This analysis presents the hypothetical gain or loss in earnings, cash flows or fair value of the financial instruments and derivative instruments which are held by us at June 30, 2013 that are sensitive to changes in interest rates. While this analysis may have some use as a benchmark, it should not be viewed as a forecast.

In the normal course of business, we also face risks that are either non-financial or non-quantifiable. Such risks principally include credit risk and legal risk and are not represented in the following analysis.

At June 30, 2013, $1,176.3 million (91.6% of total debt at June 30, 2013) of our debt was fixed rate debt and $108.0 million (8.4% of total debt at June 30, 2013) of our debt was variable rate debt. Currently, we do not enter into financial instruments for trading or other speculative purposes.

For fixed rate debt, changes in interest rates generally affect the fair value of the debt, but not our earnings or cash flows. Conversely, for variable rate debt, changes in the base interest rate used to calculate the all-in interest rate generally do not impact the fair value of the debt, but would affect our future earnings and cash flows. The interest rate risk and changes in fair market value of fixed rate debt generally do not have a significant impact on us until we are required to refinance such debt. See Note 5 to the Consolidated Financial Statements for a discussion of the maturity dates of our various fixed rate debt.

Based upon the amount of variable rate debt outstanding at June 30, 2013, a 10% increase or decrease in the interest rate on our variable rate debt would decrease or increase, respectively, future net income and cash flows by approximately $0.2 million per year. The foregoing calculation assumes an instantaneous increase or decrease in the rates applicable to the amount of borrowings outstanding under our Unsecured Credit Facility at June 30, 2013. Changes in LIBOR could result in a greater than 10% increase to such rates. In addition, the calculation does not account for other possible actions, such as prepayment, that we might take in response to any rate increase. A 10% increase in interest rates would decrease the fair value

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of the fixed rate debt at June 30, 2013 by approximately $22.7 million to $1,209.1 million. A 10% decrease in interest rates would increase the fair value of the fixed rate debt at June 30, 2013 by approximately $23.5 million to $1,255.4 million.

The use of derivative financial instruments allows us to manage risks of increases in interest rates with respect to the effect these fluctuations would have on our earnings and cash flows. As of June 30, 2013, we had one outstanding derivative with a notional amount of $50.0 million which mitigates our exposure to floating interest rates related to the coupon rate reset of our Series F Preferred Stock.

Foreign Currency Exchange Rate Risk

Owning industrial property outside of the United States exposes us to the possibility of volatile movements in foreign exchange rates. Changes in foreign currencies can affect the operating results of international operations reported in U.S. dollars and the value of the foreign assets reported in U.S. dollars. The economic impact of foreign exchange rate movements is complex because such changes are often linked to variability in real growth, inflation, interest rates, governmental actions and other factors. At June 30, 2013, we owned one land parcel for which the U.S. dollar was not the functional currency. The land parcel is located in Ontario, Canada and uses the Canadian dollar as its functional currency.

IRS Tax Refund

On August 24, 2009, we received a private letter ruling from the IRS granting favorable loss treatment under Sections 331 and 336 of the Code on the tax liquidation of one of our former taxable REIT subsidiaries. On November 6, 2009, legislation was signed that allowed businesses with net operating losses for 2008 or 2009 to carry back those losses for up to five years. As a result, we received a refund from the IRS of $40.4 million in the fourth quarter of 2009 (the “Refund”) in connection with this tax liquidation. The IRS examination team, which is required by statute to review all refund claims in excess of $2.0 million on behalf of the Joint Committee on Taxation, indicated to us that it disagreed with certain of the property valuations we obtained from an independent valuation expert in support of our fair value of the liquidated taxable REIT subsidiary and our claim for the Refund. During the year ended December 31, 2012, we reached an agreement with the regional office of the IRS on a proposed adjustment to the Refund. The total agreed-upon adjustment to taxable income was $13.7 million, which equates to $4.8 million of taxes owed. We were also required to pay accrued interest of $0.5 million. During the year ended December 31, 2012, the Company recorded the charge for the agreed-upon adjustment and the related estimated accrued interest which was reflected as a component of income tax expense. During 2013, the settlement amount was approved by the Joint Committee on Taxation.

As a result of the Joint Committee on Taxation's approval, during 2013 we entered into closing agreements with the IRS that determined the timing of the settlement on the tax characterization of the limited partners of the Operating Partnership and the stockholders of the Company. Pursuant to these closing agreements, $8.2 million of the preferred stock distributions for the year ended December 31, 2012 are taxable as capital gain. During the three months ended June 30, 2013, we paid the agreed upon taxes and related accrued interest.

Supplemental Earnings Measure

Investors in and industry analysts following the real estate industry utilize funds from operations (“FFO”) and net operating income ("NOI") as supplemental operating performance measures of an equity REIT. Historical cost accounting for real estate assets in accordance with accounting principles generally accepted in the United States of America (“GAAP”) implicitly assumes that the value of real estate assets diminishes predictably over time through depreciation. Since real estate values instead have historically risen or fallen with market conditions, many industry analysts and investors prefer to supplement operating results that use historical cost accounting with measures such as FFO and NOI, among others. We provide information related to FFO and same store NOI (“SS NOI”) both because such industry analysts are interested in such information, and because our management believes FFO and SS NOI are important performance measures. Management uses FFO and SS NOI as measures of our performance, including for purposes of determining the compensation of our executive officers under our 2013 incentive compensation plan.

Neither FFO nor SS NOI should be considered as a substitute for net income (loss), or any other measures derived in accordance with GAAP. Neither FFO nor SS NOI represents cash generated from operating activities in accordance with GAAP and neither should be considered as an alternative to cash flow from operating activities as a measure of our liquidity, nor is either indicative of funds available for our cash needs, including our ability to make cash distributions.

Funds From Operations

The National Association of Real Estate Investment Trusts ("NAREIT") created FFO as a supplemental measure of REIT operating performance that excludes historical cost depreciation, among other items, from net income (loss) determined in accordance with GAAP. FFO is a non-GAAP financial measure. FFO is calculated by us in accordance with the definition adopted by the Board of Governors of NAREIT and therefore may not be comparable to other similarly titled measures of other companies.

Management believes that the use of FFO available to common stockholders and participating securities, combined with net income (loss) (which remains the primary measure of performance), improves the understanding of operating results of REITs among the investing public and makes comparisons of REIT operating results more meaningful. Management believes that, by excluding gains or losses related to sales of previously depreciated real estate assets, real estate asset depreciation and amortization and impairment charges (reversals) recorded on depreciable real estate, investors and analysts are able to identify the operating results of the long-term assets that form the core of a REIT's activity and use these operating results for assistance in comparing these operating results between periods or to those of different companies.

The following table shows a reconciliation of net income (loss) available to common stockholders and participating securities to the calculation of FFO available to common stockholders and participating securities for the three and six months ended June 30, 2013 and 2012.

	Three Months Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
	(In thousands)			
Net Income (Loss) Available to First Industrial Realty Trust, Inc.'s Common Stockholders and Participating Securities	$5,294	$(14,326)	$554	$(17,826)
Adjustments:				
Depreciation and Other Amortization of Real Estate	29,074	29,206	56,044	60,597
Depreciation and Other Amortization of Real Estate Included in Discontinued Operations	81	950	528	2,328
Equity in Depreciation and Other Amortization of Joint Ventures	55	82	110	172
Impairment of Depreciated Real Estate	1,429	—	1,429	(153)
Impairment of Depreciated Real Estate Included in Discontinued Operations	176	—	176	1,399
Non-NAREIT Compliant Gain	(13,481)	(1,386)	(10,407)	(7,585)
Non-NAREIT Compliant Gain from Joint Ventures	—	(1)	—	(57)
Gain on Change in Control of Interests	—	—	—	(776)
Noncontrolling Interest Share of Adjustments	(702)	(1,585)	(2,049)	(3,105)
Funds from Operations Available to First Industrial Realty Trust, Inc.'s Common Stockholders and Participating Securities	$21,926	$12,940	$46,385	$34,994

Same Store Net Operating Income

SS NOI is a non-GAAP financial measure that provides a measure of rental operations, and does not factor in depreciation and amortization, general and administrative expense, interest expense, impairment charges, interest income, equity in income from joint ventures, income tax expense and gains and losses on retirement of debt, sale of real estate and mark-to-market of interest rate protection agreements. We define SS NOI as revenues minus property expenses such as real estate taxes, repairs and maintenance, property management, utilities, insurance and other expenses, minus the NOI of properties that are not same store properties and minus the impact of straight-line rent, the amortization of lease inducements, the amortization of above/below market rent and lease termination fees. As so defined, SS NOI may not be comparable to same store net operating income or similar measures reported by other REITs that define same store properties or NOI differently. The major factors influencing SS NOI are occupancy levels, rental rate increases or decreases and tenant recoveries increases or decreases. Our success depends largely upon our ability to lease space and to recover the operating costs associated with those leases from our tenants.

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The following table shows a reconciliation of the same store revenues and property expenses disclosed in the results of operations (and reconciled to revenues and expenses reflected on the statements of operations) to SS NOI for the three and six months ended June 30, 2013 and 2012.

	Three Months Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
	(In thousands)			
Same Store Properties - Revenues	$82,146	$80,460	$163,188	$159,471
Same Store Properties - Property Expenses	24,941	23,342	50,353	47,421
Same Store Net Operating Income Before Adjustments	$57,205	$57,118	$112,835	$112,050
Adjustments:				
Lease Inducement Amortization	282	351	570	614
Straight-line Rent	(117)	(463)	(532)	(1,503)
Above / Below Market Rent Amortization	(141)	(219)	(266)	(457)
Lease Termination Fees	(93)	(735)	(172)	(832)
Same Store Net Operating Income	$57,136	$56,052	$112,435	$109,872

Recent Accounting Pronouncements

Refer to Note 2 to the Consolidated Financial Statements.

Subsequent Events

On July 1, 2013 and July 5, 2013, we paid off prior to maturity mortgage loans payable in the aggregate amount of $14.0 million.

Effective July 1, 2013, certain officers and employees were granted performance units under the 2013 Long-Term Incentive Program, newly adopted by the Board of Directors. The performance units vest based upon the relative total shareholder return (“TSR”) of our stock compared to the weighted average TSR of the MSCI US REIT Index and the NAREIT Industrial Index. The TSR for half of the granted units is calculated based upon the performance from July 1, 2013 through June 30, 2014 and the other half is calculated based upon the performance from July 1, 2013 through December 31, 2015. At the end of the performance periods, each participant will be issued shares of our common stock equal to the participant's share of the aggregate unit value. The participants will also be entitled to dividend equivalents representing any common dividends that have accrued with respect to such shares after the issuance of the performance units and prior to the date of vesting.

On July 18, 2013, we redeemed the 2,000,000 Depositary Shares, each representing 1/10,000th of a share, of our 7.25% Series K Cumulative Redeemable Preferred Stock, $0.01 par value, at a redemption price of $25.00 per Depositary Share, totaling $50.0 million plus pro-rated accrued dividends.

On July 19, 2013, we entered into an amendment and restatement of our Unsecured Credit Agreement (as amended and restated, the "New Credit Facility") which increased the borrowing capacity thereunder to $625.0 million. We may request that the borrowing capacity under the New Credit Facility be increased to $825.0 million, subject to certain restrictions. The New Credit Facility provides for interest only payments initially at LIBOR plus 145 basis points, that varies based on our leverage ratio. In the event we achieve an investment grade rating from one of certain rating agencies, the rate may be decreased at our election, based on the investment grade rating. The New Credit Facility matures on September 29, 2017, unless extended an additional one year at our election, subject to certain restrictions.

From July 1, 2013 to August 2, 2013, we sold three industrial properties and one land parcel for approximately $6.1 million. There were no industrial properties acquired during the period.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Response to this item is included in Item 2, “Management’s Discussion and Analysis of Financial Condition and Results of Operations” above.

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Item 4. Controls and Procedures

Our principal executive officer and principal financial officer, in evaluating 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 on the evaluation of these controls and procedures required by Exchange Act Rules 13a-15(b) or 15d-15(b), have concluded that as of the end of such period our disclosure controls and procedures were effective.

There has been no change in our internal control over financial reporting that occurred during the fiscal quarter covered by this report 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
None.
Item 1A. Risk Factors
None.
Item 2. Unregistered Sales of Equity Securities and Use of Proceeds
None.
Item 3. Defaults Upon Senior Securities
None.
Item 4. Mine Safety Disclosures
None.
Item 5. Other Information
None.
Item 6. Exhibits

Exhibit Number	Description
3.1*	Conformed Articles of Incorporation of Amendment and Restatement of First Industrial Realty Trust, Inc.
3.2	Second Amended and Restated Bylaws of First Industrial Realty Trust, Inc. (incorporated by reference to Exhibit 3.2 of the Form 8-K of the Company filed May 10, 2013).
10.1	First Industrial Realty Trust, Inc. 2013 Long-Term Incentive Program (incorporated by reference to Exhibit 10.1 of the Form 8-K of the Company filed June 25, 2013).
10.2	Form of Performance Unit Award Agreement (incorporated by reference to Exhibit 10.2 of the Form 8-K of the Company filed June 25, 2013).
10.3	Amended and Restated Unsecured Revolving Credit Agreement dated as of July 19, 2013 among First Industrial, L.P., First Industrial Realty Trust, Inc., Wells Fargo Bank, N.A and the other lenders thereunder (incorporated by reference to Exhibit 10.1 of the Form 8-K of the Company filed July 22, 2013).
31.1*	Certification of the Principal Executive Officer pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934, as amended.
31.2*	Certification of the Principal Financial Officer pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934, as amended.
32.1**	Certification of the Principal Executive Officer and the Principal Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.1*	The following financial statements from First Industrial Realty Trust, Inc.'s Quarterly Report on Form 10-Q for the quarter ended June 30, 2013, formatted in XBRL: (i) Consolidated Balance Sheets (unaudited), (ii) Consolidated Statements of Operations (unaudited), (iii) Consolidated Statements of Comprehensive Income (unaudited), (iv) Consolidated Statement of Changes in Stockholders' Equity (unaudited), (v) Consolidated Statements of Cash Flows (unaudited) and (vi) Notes to Consolidated Financial Statements (unaudited).

* Filed herewith.

** Furnished herewith.

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SIGNATURE

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.

FIRST INDUSTRIAL REALTY TRUST, INC.

By: /S/ SCOTT A. MUSIL
Scott A. Musil
Chief Financial Officer
(Principal Financial Officer)

Date: August 2, 2013

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