

PINNACLE FINANCIAL PARTNERS INC

Form 10-Q

May 07, 2018

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

FORM 10-Q

(mark one)

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

For the quarterly period ended March 31, 2018

or

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

For the transition period from ____ to ____

Commission File Number: 000-31225

, Inc.

(Exact name of registrant as specified in its charter)

Tennessee

62-1812853

(State or other jurisdiction of incorporation or organization) (I.R.S. Employer Identification No.)

150 Third Avenue South, Suite 900, Nashville, Tennessee 37201

(Address of principal executive offices) (Zip Code)

(615) 744-3700

(Registrant's telephone number, including area code)

Not Applicable

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

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for shorter period that the registrant was required to submit and post such files).

Yes No

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

Large Accelerated Filer

Accelerated Filer

Non-accelerated Filer

Smaller reporting company

(do not check if you are a smaller reporting company)

Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

As of May 1, 2018 there were 77,868,340 shares of common stock, \$1.00 par value per share, issued and outstanding.

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Report on Form 10-Q
March 31, 2018

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FORWARD-LOOKING STATEMENTS

All statements, other than statements of historical fact, included in this report, are forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995, Section 27A of the Securities Act and Section 21E of the Exchange Act. The words "expect," "anticipate," "intend," "plan," "believe," "aim", "seek," "estimate" and similar expressions are intended to identify such forward-looking statements, but other statements not based on historical information may also be considered forward-looking statements. These forward-looking statements are subject to known and unknown risks, uncertainties and other factors that could cause the actual results to differ materially from the statements, including, but not limited to: (i) deterioration in the financial condition of borrowers resulting in significant increases in loan losses and provisions for those losses; (ii) continuation of the historically low short-term interest rate environment; (iii) the inability of Pinnacle Financial, or entities in which it has significant investments, like Bankers Healthcare Group, LLC ("BHG"), to maintain the historical growth rate of its, or such entities', loan portfolio; (iv) changes in loan underwriting, credit review or loss reserve policies associated with economic conditions, examination conclusions, or regulatory developments; (v) effectiveness of Pinnacle Financial's asset management activities in improving, resolving or liquidating lower-quality assets; (vi) the impact of competition with other financial institutions, including pricing pressures (including those resulting from the Tax Cuts and Jobs Act) and the resulting impact on Pinnacle Financial's results, including as a result of compression to net interest margin; (vii) greater than anticipated adverse conditions in the national or local economies including in Pinnacle Financial's markets throughout Tennessee, North Carolina, South Carolina and Virginia, particularly in commercial and residential real estate markets; (viii) fluctuations or unanticipated changes in interest rates on loans or deposits or that affect the yield curve; (ix) the results of regulatory examinations; (x) the ability to grow and retain low-cost core deposits and retain large, uninsured deposits; (xi) a merger or acquisition; (xii) risks of expansion into new geographic or product markets; (xiii) any matter that would cause Pinnacle Financial to conclude that there was impairment of any asset, including intangible assets; (xiv) reduced ability to attract additional financial advisors (or failure of such advisors to cause their clients to switch to Pinnacle Bank), to retain financial advisors (including as a result of the competitive environment resulting from the Tax Cuts and Jobs Act) or otherwise to attract customers from other financial institutions; (xv) further deterioration in the valuation of other real estate owned and increased expenses associated therewith; (xvi) inability to comply with regulatory capital requirements, including those resulting from changes to capital calculation methodologies, required capital maintenance levels or regulatory requests or directives, particularly if Pinnacle Financial's level of applicable commercial real estate loans continues to exceed percentage levels of total capital in guidelines recommended by its regulators; (xvii) risks associated with litigation, including the applicability of insurance coverage; (xviii) the risk of successful integration of the businesses Pinnacle Financial has recently acquired with its business; (xix) approval of the declaration of any dividend by Pinnacle Financial's board of directors; (xx) the vulnerability of Pinnacle Bank's network and online banking portals, and the systems of parties with whom Pinnacle Financial contracts, to unauthorized access, computer viruses, phishing schemes, spam attacks, human error, natural disasters, power loss and other security breaches; (xxi) the possibility of increased compliance costs as a result of increased regulatory oversight, including oversight of companies in which Pinnacle Financial or Pinnacle Bank have significant investments, like BHG, and the development of additional banking products for Pinnacle Bank's corporate and consumer clients; (xxii) the risks associated with Pinnacle Financial and Pinnacle Bank being a minority investor in BHG, including the risk that the owners of a majority of the equity interests in BHG decide to sell the company if not prohibited from doing so by the terms of our agreement with them; (xxiii) changes in state and federal legislation, regulations or policies applicable to banks and other financial service providers, like BHG, including regulatory or legislative developments; (xxiv) the risk that the cost savings and any revenue synergies expected from Pinnacle Financial's merger with BNC may not be realized or take longer than anticipated to be realized; (xxv) disruption from Pinnacle Financial's merger with BNC with customers, suppliers, employee or other business partners relationships; (xxvi) the risk of successful integration of Pinnacle Financial's and BNC's businesses; (xxvii) reputational risk and the reaction of the parties' customers, suppliers, employees or other business partners to Pinnacle Financial's merger with BNC; (xxviii) the risk that the integration of Pinnacle Financial's and BNC's operations will be more costly or difficult than expected; (xxix) inability to grow our commercial and industrial loan

portfolio at rates necessary to cause our levels of non-owner occupied commercial real estate and multifamily loans (including construction and land development loans) as a percentage of total capital to fall below levels included in guidelines recommended by our regulators; (xxx) the availability and access to capital; (xxxi) adverse results (including costs, fines, reputational harm and/or other negative effects) from current or future litigation, regulatory examinations or other legal and/or regulatory actions; and (xxxii) general competitive, economic, political and market conditions. Additional factors which could affect the forward looking statements can be found in Pinnacle Financial's Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, and Current Reports on Form 8-K filed with the Securities and Exchange Commission ("SEC") and available on the SEC's website at <http://www.sec.gov>. Pinnacle Financial disclaims any obligation to update or revise any forward-looking statements contained in this report, which speak only as of the date hereof, whether as a result of new information, future events or otherwise.

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Item 1. Part I. Financial Information

PINNACLE FINANCIAL PARTNERS, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

(Unaudited)

(in thousands)

	March 31, 2018	December 31, 2017
ASSETS		
Cash and noninterest-bearing due from banks	\$ 128,855	\$ 176,553
Interest-bearing due from banks	238,029	496,911
Federal funds sold and other	1,879	106,133
Cash and cash equivalents	368,763	779,597
Securities available-for-sale, at fair value	2,960,624	2,515,283
Securities held-to-maturity (fair value of \$20,603 and \$20,830 at March 31, 2018 and December 31, 2017, respectively)	20,677	20,762
Consumer loans held-for-sale	100,231	103,729
Commercial loans held-for-sale	18,625	25,456
Loans	16,326,017	15,633,116
Less allowance for loan losses	(70,204)	(67,240)
Loans, net	16,255,813	15,565,876
Premises and equipment, net	269,439	266,014
Equity method investment	226,704	221,667
Accrued interest receivable	60,918	57,440
Goodwill	1,808,300	1,808,002
Core deposits and other intangible assets	54,012	56,710
Other real estate owned	23,982	27,831
Other assets	767,086	757,333
Total assets	\$22,935,174	\$22,205,700
LIABILITIES AND STOCKHOLDERS' EQUITY		
Deposits:		
Noninterest-bearing	\$4,274,213	\$4,381,386
Interest-bearing	3,040,154	2,987,291
Savings and money market accounts	6,615,562	6,548,964
Time	2,572,980	2,534,061
Total deposits	16,502,909	16,451,702
Securities sold under agreements to repurchase	131,863	135,262
Federal Home Loan Bank advances	1,976,881	1,319,909
Subordinated debt and other borrowings	465,550	465,505
Accrued interest payable	13,592	10,480
Other liabilities	95,076	114,890
Total liabilities	19,185,871	18,497,748
Stockholders' equity:		
Preferred stock, no par value; 10,000 shares authorized; no shares issued and outstanding	—	—
Common stock, par value \$1.00; 90,000 shares authorized; 77,853 and 77,740 shares issued and outstanding at March 31, 2018 and December 31, 2017, respectively	77,853	77,740

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Additional paid-in capital	3,115,990	3,115,304
Retained earnings	591,680	519,144
Accumulated other comprehensive loss, net of taxes	(36,220)	(4,236)
Total stockholders' equity	3,749,303	3,707,952
Total liabilities and stockholders' equity	\$22,935,174	\$22,205,700

See accompanying notes to consolidated financial statements (unaudited).

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CONSOLIDATED STATEMENTS OF INCOME

(Unaudited)

(dollars in thousands, except per share data)

	Three months ended	
	March 31,	
	2018	2017
Interest income:		
Loans, including fees	\$ 191,214	\$ 93,218
Securities:		
Taxable	11,222	6,433
Tax-exempt	7,285	1,678
Federal funds sold and other	1,807	814
Total interest income	211,528	102,143
Interest expense:		
Deposits	23,981	8,119
Securities sold under agreements to repurchase	130	50
Federal Home Loan Bank advances and other borrowings	12,946	5,207
Total interest expense	37,057	13,376
Net interest income	174,471	88,767
Provision for loan losses	6,931	3,651
Net interest income after provision for loan losses	167,540	85,116
Noninterest income:		
Service charges on deposit accounts	5,820	3,856
Investment services	5,107	2,822
Insurance sales commissions	3,119	1,859
Gain on mortgage loans sold, net	3,744	4,155
Gain on sale of investment securities, net	30	—
Trust fees	3,117	1,705
Income from equity method investment	9,360	7,823
Other noninterest income	13,886	8,162
Total noninterest income	44,183	30,382
Noninterest expense:		
Salaries and employee benefits	63,719	38,352
Equipment and occupancy	17,743	9,675
Other real estate expense (income)	(794)) 252
Marketing and other business development	2,247	1,879
Postage and supplies	2,039	1,197
Amortization of intangibles	2,698	1,196
Merger related expense	5,353	672
Other noninterest expense	15,575	8,831
Total noninterest expense	108,580	62,054
Income before income taxes	103,143	53,444
Income tax expense	19,633	13,791
Net income	\$ 83,510	\$ 39,653
Per share information:		

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Basic net income per common share	\$1.08	\$ 0.83
Diluted net income per common share	\$1.08	\$ 0.82
Weighted average shares outstanding:		
Basic	77,077,957	48,022,342
Diluted	77,365,664	48,517,920

See accompanying notes to consolidated financial statements (unaudited).

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PINNACLE FINANCIAL PARTNERS, INC. AND SUBSIDIARIES
 CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
 (Unaudited)
 (dollars in thousands)

	Three months ended March 31,	
	2018	2017
Net income	\$83,510	\$39,653
Other comprehensive (loss) income, net of tax:		
Change in fair value on available-for-sale securities, net of tax	(33,541)	(808)
Change in fair value of cash flow hedges, net of tax	1,579	(143)
Net gain on sale of investment securities reclassified from other comprehensive income into net income, net of tax	(22)	—
Total other comprehensive (loss) income, net of tax	(31,984)	(951)
Total comprehensive income	\$51,526	\$38,702

See accompanying notes to consolidated financial statements (unaudited).

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CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

(Unaudited)

(dollars and shares in thousands)

	Common Stock			Retained Earnings	Accumulated Other Comp. Income (Loss), net	Total Stockholder's Equity
	Shares	Amounts	Additional Paid-in Capital			
Balance at December 31, 2016	46,359	\$46,359	\$1,083,491	\$381,073	\$ (14,227)	\$ 1,496,696
Exercise of employee common stock options and related tax benefits	149	149	2,812	—	—	2,961
Common dividends paid	—	—	—	(7,025)	—	(7,025)
Issuance of restricted common shares, net of forfeitures	119	119	(119)	—	—	—
Issuance of common equity, net of costs	3,220	3,220	188,974	—	—	192,194
Restricted shares withheld for taxes and related tax benefit	(57)	(57)	(3,869)	—	—	(3,926)
Compensation expense for restricted shares	—	—	3,474	—	—	3,474
Net income	—	—	—	39,653	—	39,653
Other comprehensive loss	—	—	—	—	(951)	(951)
Balance at March 31, 2017	49,790	\$49,790	\$1,274,763	\$413,701	\$ (15,178)	\$ 1,723,076
Balance at December 31, 2017	77,740	\$77,740	\$3,115,304	\$519,144	\$ (4,236)	\$ 3,707,952
Exercise of employee common stock options	87	87	1,529	—	—	1,616
Common dividends paid	—	—	—	(10,974)	—	(10,974)
Issuance of restricted common shares, net of forfeitures	106	106	(106)	—	—	—
Restricted shares withheld for taxes and related tax benefit	(80)	(80)	(5,185)	—	—	(5,265)
Compensation expense for restricted shares	—	—	4,448	—	—	4,448
Net income	—	—	—	83,510	—	83,510
Other comprehensive loss	—	—	—	—	(31,984)	(31,984)
Balance at March 31, 2018	77,853	\$77,853	\$3,115,990	\$591,680	\$ (36,220)	\$ 3,749,303

See accompanying notes to consolidated financial statements (unaudited).

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CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

(dollars in thousands)

	Three months ended March 31,	
	2018	2017
Operating activities:		
Net income	\$83,510	\$39,653
Adjustments to reconcile net income to net cash provided by operating activities:		
Net amortization/accretion of premium/discount on securities	4,775	1,978
Depreciation, amortization and accretion	(6,181)	(429)
Provision for loan losses	6,931	3,651
Gain on mortgage loans sold, net	(3,744)	(4,155)
Investment gains on sales, net	(30)	—
Stock-based compensation expense	4,448	3,474
Deferred tax expense	8,513	8,699
Losses (gains) on dispositions of other real estate and other investments	(481)	80
Income from equity method investment	(9,360)	(7,823)
Dividends received from equity method investment	4,324	2,450
Excess tax benefit from stock compensation	(2,681)	(3,760)
Gain on other loans sold, net	(936)	(187)
Other loans held for sale:		
Loans originated	(80,193)	(36,888)
Loans sold	87,960	44,308
Consumer loans held for sale:		
Loans originated	(247,025)	(179,473)
Loans sold	254,266	160,740
Increase in other assets	(4,639)	(136)
Decrease in other liabilities	(13,901)	(24,386)
Net cash provided by operating activities	85,556	7,796
Investing activities:		
Activities in securities available-for-sale:		
Purchases	(590,328)	(334,875)
Sales	14,454	—
Maturities, prepayments and calls	81,737	50,445
Activities in securities held-to-maturity:		
Maturities, prepayments and calls	—	145
Increase in loans, net	(683,710)	(193,557)
Purchases of software, premises and equipment	(8,806)	(11,446)
Proceeds from sales of software, premises and equipment	164	—
Purchase of bank owned life insurance policies	—	(25,000)
Increase in other investments	(836)	(640)
Net cash used in investing activities	(1,187,325)	(514,928)
Financing activities:		
Net increase in deposits	52,039	521,563
Net decrease in securities sold under agreements to repurchase	(3,398)	(14,549)
Advances from Federal Home Loan Bank:		
Issuances	762,000	—

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Payments/maturities	(105,014)	(225,020)
Increase (decrease) in other borrowings, net	(30)	50,000
Principal payments of capital lease obligation	(39)	(36)
Proceeds from common stock issuance, net	—	192,194
Exercise of common stock options and stock appreciation rights, net of repurchase of restricted shares	(3,649)	(966)
Common stock dividends paid	(10,974)	(7,025)
Net cash provided by financing activities	690,935	516,161
Net increase (decrease) in cash and cash equivalents	(410,834)	9,029
Cash and cash equivalents, beginning of period	779,597	183,645
Cash and cash equivalents, end of period	\$368,763	\$192,674

See accompanying notes to consolidated financial statements (unaudited).

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PINNACLE FINANCIAL PARTNERS, INC. AND SUBSIDIARIES
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
 (Unaudited)

Note 1. Summary of Significant Accounting Policies

Nature of Business — Pinnacle Financial Partners, Inc. (Pinnacle Financial) is a bank holding company whose primary business is conducted by its wholly-owned subsidiary, Pinnacle Bank. Pinnacle Bank is a commercial bank headquartered in Nashville, Tennessee. Pinnacle Financial completed its acquisitions of CapitalMark Bank & Trust (CapitalMark), Magna Bank (Magna), Avenue Financial Holdings, Inc. (Avenue) and BNC Bancorp (BNC) on July 31, 2015, September 1, 2015, July 1, 2016 and June 16, 2017, respectively. Pinnacle Financial and Pinnacle Bank also collectively hold a 49% interest in Bankers Healthcare Group, LLC (BHG), a full-service commercial loan provider to healthcare and other professional practices. Pinnacle Bank provides a full range of banking services, including investment, mortgage, insurance, and comprehensive wealth management services, in its 11 primarily urban markets within Tennessee, the Carolinas and Virginia. In addition to the offices in those primary markets, Pinnacle Financial has recently opened loan production offices in Indiana and Texas.

Basis of Presentation — The accompanying unaudited consolidated financial statements have been prepared in accordance with instructions to Form 10-Q and therefore do not include all information and footnotes necessary for a fair presentation of financial position, results of operations, and cash flows in conformity with U.S. generally accepted accounting principles (U.S. GAAP). All adjustments consisting of normally recurring accruals that, in the opinion of management, are necessary for a fair presentation of the financial position and results of operations for the periods covered by the report have been included. The accompanying unaudited consolidated financial statements should be read in conjunction with the Pinnacle Financial consolidated financial statements and related notes appearing in Pinnacle Financial's Annual Report on Form 10-K for the year ended December 31, 2017 (2017 10-K).

These consolidated financial statements include the accounts of Pinnacle Financial and its wholly-owned subsidiaries. Certain statutory trust affiliates of Pinnacle Financial, as noted in Note 12. Subordinated Debt and Other Borrowings are included in these consolidated financial statements pursuant to the equity method of accounting. Significant intercompany transactions and accounts are eliminated in consolidation.

Use of Estimates — The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities as of the balance sheet date and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term include the determination of the allowance for loan losses, determination of any impairment of intangible assets and the valuation of deferred tax assets. There have been no significant changes to Pinnacle Financial's significant accounting policies as disclosed in the 2017 10-K.

Cash Flow Information — Supplemental cash flow information addressing certain cash and noncash transactions for each of the three months ended March 31, 2018 and March 31, 2017 was as follows (in thousands):

	For the three months ended March 31, 2018 2017	
Cash Transactions:		
Interest paid	\$34,909	\$13,667
Income taxes paid, net	425	230
Noncash Transactions:		

Loans charged-off to the allowance for loan losses	8,669	5,162
Loans foreclosed upon and transferred to other real estate owned	232	1,498
Loans foreclosed upon and transferred to other assets	392	3

Income Per Common Share — Basic net income per common share (EPS) is computed by dividing net income by the weighted average common shares outstanding for the period. Diluted EPS reflects the dilution that could occur if securities or other contracts to issue common stock were exercised or converted. The difference between basic and diluted weighted average shares outstanding is attributable to common stock options, common stock appreciation rights, restricted share awards, and restricted share unit awards. The dilutive effect of outstanding options, common stock appreciation rights, restricted share awards, and restricted share unit awards is reflected in diluted EPS by application of the treasury stock method.

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The following is a summary of the basic and diluted net income per share calculations for the three months ended March 31, 2018 and 2017 (in thousands, except per share data):

	Three months ended March 31, 2018 2017	
Basic net income per share calculation:		
Numerator - Net income	\$83,510	\$39,653
Denominator - Weighted average common shares outstanding	77,078	48,022
Basic net income per common share	\$1.08	\$0.83
Diluted net income per share calculation:		
Numerator – Net income	\$83,510	\$39,653
Denominator - Weighted average common shares outstanding	77,078	48,022
Dilutive shares contingently issuable	288	496
Weighted average diluted common shares outstanding	77,366	48,518
Diluted net income per common share	\$1.08	\$0.82

On January 27, 2017, Pinnacle Financial completed the issuance and sale of 3,220,000 shares of common stock (including 420,000 shares issued as a result of the underwriter exercising its over-allotment option) in an underwritten public offering, which shares are included in the share count above. The net proceeds of the offering, after deducting the underwriting discount and estimated offering expenses, were approximately \$192.2 million. Also, Pinnacle Financial issued 27,687,100 shares of common stock in conjunction with the acquisition of BNC on June 16, 2017.

Recently Adopted Accounting Pronouncements — In August 2017, the FASB issued Accounting Standards Update No. 2017-12, Derivatives and Hedging: Targeted Improvements to Accounting for Hedging Activities. The amendments in this ASU make more financial and non-financial hedging strategies eligible for hedge accounting. It also amends the presentation and disclosure requirements and changes how companies assess effectiveness. The amendments will be effective for public companies for interim and annual periods beginning after December 15, 2018. Early adoption is permitted. Pinnacle Financial early adopted this standard in early 2018 and subsequently entered into two derivative contracts under this standard, as noted in Note 9. Derivative Instruments.

In March 2017, the FASB issued Accounting Standards Update No. 2017-08, Receivables - Nonrefundable Fees and Other Costs (Subtopic 310-20): Premium Amortization on Purchased Callable Debt Securities. The amendment in this ASU shortens the amortization period for certain callable debt securities held at a premium to the earliest call date. The amendment does not require an accounting change for securities held at a discount; the discount continues to be amortized to maturity. The amendments are effective for fiscal years beginning after December 15, 2018, including interim periods within those periods. Early adoption is permitted with modified retrospective application. Pinnacle Financial elected to early adopt this standard in the first quarter of 2018 with no material impact to its financial statements.

In August 2016, the FASB issued Accounting Standards Update 2016-15, Statement of Cash Flows (Topic 230) intended to reduce the diversity in practice around how certain transactions are classified within the statement of cash flows. The guidance is effective for public companies for annual periods beginning after December 15, 2017, including interim periods within those fiscal years. Early adoption is permitted with retrospective application. Pinnacle Financial adopted this standard in the first quarter of 2018 with no material impact to its financial statements, with the exception of dividends received from our equity method investments which were reclassified from cash flow

from investments to operating cash flow.

In January 2016, the FASB issued Accounting Standards Update 2016-01 Financial Instruments – Overall (Subtopic 825-10) which, among other things, (i) requires equity investments, excluding those accounted for under the equity method or that result in consolidation, to be measured at fair value with changes in fair value recognized in net income, (ii) simplifies the impairment assessment of equity investments without readily determinable fair values by requiring a qualitative assessment to identify impairment, (iii) eliminates the requirement for public business entities to disclose the methods and significant assumptions used to estimate the fair value that is required to be disclosed for financial instruments measured at amortized cost on the balance sheet, (iv) requires public business entities to use the exit price notion when measuring the fair value of financial instruments for disclosure purposes, (v) requires an entity to present separately in other comprehensive income the portion of the total change in the fair value of a liability resulting from a change in the instrument-specific credit risk when the entity has elected to measure the liability at fair value in accordance with the fair value option for financial instruments, (vi) requires separate presentation of financial assets and financial liabilities by measurement category and form of financial asset on the balance sheet or the accompanying notes to the financial

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statements and (viii) clarifies that an entity should evaluate the need for a valuation allowance on a deferred tax asset related to available-for-sale securities in combination with the entity's other deferred tax assets. ASU 2016-01 became effective for Pinnacle Financial in the first quarter of 2018 and did not have a material impact on our financial statements. See Note 10. Fair Value of Financial Instruments for disclosure of the fair value of financial instruments based on an exit price notion as required by ASU 2016-01.

In May 2014, the FASB issued Accounting Standards Update 2014-09, Revenue from Contracts with Customers (Topic 606) developed as a joint project with the International Accounting Standards Board to remove inconsistencies in revenue requirements and provide a more robust framework for addressing revenue issues. The ASU's core principle is that an entity should recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which an entity expects to be entitled in exchange for those goods or services. In August 2015, the FASB issued Accounting Standards Update 2015-14, which deferred the effective date by one year (i.e., interim and annual reporting periods beginning after December 15, 2017). Early adoption is permitted, but not before the original effective date (i.e., interim and annual reporting periods beginning after December 15, 2016). The ASU may be adopted using either a modified retrospective method or a full retrospective method. Pinnacle Financial adopted the ASU during the first quarter of 2018, as required, using a modified retrospective approach. The majority of Pinnacle Financial's revenue stream is generated from interest income on loans and deposits, which are outside the scope of Topic 606. Pinnacle Financial's sources of income that fall within the scope of Topic 606 include service charges on deposits, investment services, insurance sales commissions, trust fees, interchange fees and gains and losses on sales of other real estate, all of which are presented within noninterest income. Pinnacle Financial has evaluated the effect of Topic 606 on these fee-based income streams and concluded that adoption of the standard did not materially impact its financial statements. The following is a summary of the implementation considerations for the revenue streams that fall within the scope of Topic 606:

Service charges on deposits, investment services, trust fees and interchange fees — Fees from these services are either transaction based, for which the performance obligations are satisfied when the individual transaction is processed, or set periodic service charges, for which the performance obligations are satisfied over the period the service is provided. Transaction based fees are recognized at the time the transaction is processed, and periodic service charges are recognized over the service period. The adoption of Topic 606 had no impact on Pinnacle Financial's revenue recognition practice for these services.

Insurance sales commissions — Insurance commissions are received from insurance companies in return for the placement of policies with customers. While additional services, such as claims assistance, may be provided over the term of the policy, the revenues are substantially earned at the time of policy placement. The only contingency in earning the revenue relates to the potential for subsequent cancellation of policies. Accordingly, revenue is recognized at the time of policy placement, net of an allowance for estimated policy cancellations. The adoption of Topic 606 had no impact on Pinnacle Financial's revenue recognition related to insurance sales commissions.

Gains on sales of other real estate — ASU 2014-09 creates Topic 610-20, under which a gain on sale should be recognized when a contract for sale exists and control of the asset has been transferred to the buyer. Topic 606 lists several criteria which must exist to conclude that a contract for sale exists, including a determination that the institution will collect substantially all of the consideration to which it is entitled. This presents a key difference between the current and new guidance related to the recognition of the gain when the institution finances the sale of the property. Rather than basing recognition on the amount of the buyer's initial investment, which was the primary consideration under prior guidance, the analysis is now based on various factors including not only the loan to value, but also the credit quality of the borrower, the structure of the loan, and any other factors that may affect collectability. While these differences may affect the decision to recognize or defer gains on sales of other real estate in circumstances where Pinnacle Financial has financed the sale, the effects would not be material to its financial statements.

Subsequent Events — Accounting Standards Codification (ASC) Topic 855, Subsequent Events, establishes general standards of accounting for and disclosure of events that occur after the balance sheet date but before financial statements are issued. Pinnacle Financial evaluated all events or transactions that occurred after March 31, 2018 through the date of the issued financial statements. Following early adoption of ASU 2017-12 as noted above, Pinnacle Financial entered into a derivative transaction on April 10, 2018 that has been more fully disclosed in Note 9. Derivative Instruments. Other than the above-noted transaction, no other subsequent events were noted.

On April 17, 2018, Pinnacle Financial's shareholders approved an amendment to Pinnacle Financial's Charter to increase the number of authorized shares of capital stock from 100,000,000 to 190,000,000 shares, in both instances 10,000,000 of which are reserved for issuance as preferred stock.

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Note 2. Acquisitions

BNC Bancorp. On June 16, 2017, Pinnacle Financial consummated its merger with BNC. Pursuant to the terms of the Agreement and Plan of Merger, dated as of January 22, 2017, by and between Pinnacle Financial and BNC, BNC merged with and into Pinnacle Financial, with Pinnacle Financial continuing as the surviving corporation (the BNC Merger). On that same day, Pinnacle Bank and Bank of North Carolina, BNC's wholly-owned bank subsidiary, merged, with Pinnacle Bank continuing as the surviving entity.

The following summarizes the consideration paid and presents a preliminary allocation of purchase price to net assets acquired (in thousands):

	Number of Shares	Amount
Equity consideration:		
Common stock issued	27,687,100	\$ 1,858,133
Total equity consideration		\$ 1,858,133
Non-equity consideration:		
Cash paid to redeem common stock		\$ 129
Total consideration paid		\$ 1,858,262
Allocation of total consideration paid:		
Fair value of net assets assumed including estimated identifiable intangible assets		\$ 601,509
Goodwill		1,256,753
		\$ 1,858,262

Pinnacle Financial recorded costs incurred in connection with the issuance of Pinnacle Financial common stock resulting from the BNC Merger of \$7.2 million, net of related tax benefits, as a reduction to additional paid in capital. Certain merger-related charges resulting from cultural and systems integrations, as well as stock-based compensation expense incurred as a result of change-in-control provisions applicable to assumed equity-based awards were recorded as merger-related expense.

Goodwill originating from the BNC Merger resulted primarily from anticipated synergies arising from the combination of certain operational areas of the businesses of BNC and Pinnacle Financial as well as the purchase premium inherent in buying a complete and successful banking operation. Goodwill associated with the BNC Merger is not amortizable for book or tax purposes. Adjustments totaling \$83.2 million were recorded to goodwill to appropriately reflect the valuation of the loan portfolio, OREO acquired, and certain liabilities assumed and have been included in the table below.

Pinnacle Financial accounted for the BNC Merger under the acquisition method in accordance with ASC Topic 805. Accordingly, the purchase price is allocated to the fair value of the assets acquired and liabilities assumed as of the date of merger.

The following purchase price allocations on the BNC Merger are preliminary and will be finalized upon the receipt of final valuations on certain assets and liabilities. Upon receipt of final fair value estimates, which must be received within one year of the BNC Merger date, Pinnacle Financial will make any final adjustments to the purchase price allocation and prospectively adjust any goodwill recorded. Information regarding Pinnacle Financial's loan discount and related deferred tax asset, core deposit intangible asset and related deferred tax liability, as well as income taxes payable and the related deferred tax balances recorded in the BNC Merger, may be adjusted as Pinnacle Financial refines its estimates. Determining the fair value of assets and liabilities, particularly illiquid assets and liabilities, is a complicated process involving significant judgment regarding estimates and assumptions used to calculate estimated

fair value. Fair value adjustments based on updated estimates could materially affect the goodwill recorded on the BNC Merger. Pinnacle Financial may incur losses on the acquired loans that are materially different from losses Pinnacle Financial originally projected.

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(in thousands)	As of June 16, 2017		
	BNC Historical Cost Basis	Fair Value Adjustments ⁽¹⁾	As Recorded by Pinnacle Financial
Assets			
Cash and cash equivalents	\$ 155,271	\$ —	\$ 155,271
Investment securities	643,875	1,667	645,542
Loans ⁽²⁾	5,782,720	(181,430) 5,601,290
Mortgage loans held for sale	27,026	—	27,026
Other real estate owned ⁽³⁾	20,143	645	20,788
Core deposit and other intangible ⁽⁴⁾	—	50,422	50,422
Property, plant and equipment ⁽⁵⁾	156,805	(3,341) 153,464
Other assets ⁽⁶⁾	320,988	53,614	374,602
Total Assets	\$ 7,106,828	\$ (78,423) \$ 7,028,405
Liabilities			
Interest-bearing deposits ⁽⁷⁾	\$ 5,003,653	\$ 4,355	\$ 5,008,008
Non-interest bearing deposits	1,199,342	—	1,199,342
Borrowings ⁽⁸⁾	183,389	(6,412) 176,977
Other liabilities ⁽⁹⁾	35,729	6,840	42,569
Total Liabilities	\$ 6,422,113	\$ 4,783	\$ 6,426,896
Net Assets Acquired	\$ 684,715	\$ (83,206) \$ 601,509

Explanation of certain fair value adjustments:

The amount represents the adjustment of the book value of BNC's assets and liabilities to their estimated fair value (1) on the date of acquisition. Fair value adjustments are updated subsequent to the merger date based on the results of finalized valuation assessments.

The amount represents the adjustment of the net book value of BNC's loans to their estimated fair value based on (2) interest rates and expected cash flows as of the date of acquisition, which includes estimates of expected credit losses inherent in the portfolio of approximately 2.6% of the 3.1% mark on the acquired loan portfolio.

(3) Although not complete, this adjustment reflects the Day 1 value of OREO properties subsequently sold.

The amount represents the fair value of the core deposit intangible asset representing the intangible value of the (4) deposit base acquired and the fair value of the customer relationship intangible assets representing the intangible value of customer relationships acquired.

(5) The amount represents the adjustment of the net book value of BNC's property, plant and equipment to estimated fair value based on market values of similar assets.

(6) The amount represents the deferred tax asset recognized on the fair value adjustment of BNC's acquired assets and assumed liabilities.

The amount represents the adjustment necessary because the weighted average interest rate of BNC's deposits (7) exceeded the cost of similar funding at the time of acquisition. The fair value adjustment will be amortized to reduce future interest expense over the life of the portfolio.

The amount represents the combined adjustment necessary because the weighted average interest rate of BNC's subordinated debt issuance exceeded the cost of similar funding at the time of acquisition and because the weighted (8) average interest rate of BNC's trust preferred securities issuances was lower than the cost of similar funding at the time of acquisition. The combined fair value adjustments will be amortized to increase future interest expense over the lives of the instruments.

(9)

The amount represents the adjustment to accrue obligations that existed but had not been recorded as of the acquisition date and the fair value of BNC lease obligations.

Supplemental Pro Forma Combined Results of Operations

The supplemental proforma information below for the three months ended March 31, 2017 gives effect to the BNC acquisition as if it had occurred on January 1, 2017. These results combine the historical results of BNC into Pinnacle Financial's consolidated statement of income and, while certain adjustments were made for the estimated impact of certain fair value adjustments, they are not indicative of what would have occurred had the BNC Merger taken place on the indicated date nor are they intended to represent or be indicative of future results of operations. In particular, no adjustments have been made to eliminate the amount of BNC's provision for credit losses for the first three months of 2017 that may not have been necessary had the acquired loans been recorded at fair value as of the beginning of 2017. Additionally, these financial statements were not adjusted for non-recurring expenses, such as merger-related charges incurred by either Pinnacle Financial or BNC. Pinnacle Financial expects to achieve operating cost savings and other business synergies as a result of the acquisition which are also not reflected in the proforma amounts.

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	Three Months Ended March 31, 2017
(dollars in thousands)	
Revenue ⁽¹⁾	\$219,665
Income before income taxes	\$74,999

⁽¹⁾ Net interest income plus noninterest income.

Note 3. Equity method investment

A summary of BHG's financial position as of March 31, 2018 and December 31, 2017 and results of operations as of and for the three months ended March 31, 2018 and 2017, were as follows (in thousands):

	As of	
	March 31, December 31,	
	2018	2017
Assets	\$340,760	\$ 330,030
Liabilities	232,978	224,837
Membership interests	107,782	105,193
Total liabilities and membership interests	\$340,760	\$ 330,030

	For the three months ended March 31,	
	2018	2017
Revenues	\$43,750	\$34,235
Net income	\$19,003	\$16,012

At March 31, 2018, technology, trade name and customer relationship intangibles, net of related amortization, totaled \$12.7 million compared to \$13.4 million as of December 31, 2017. Amortization expense of \$693,000 was included for the three months ended March 31, 2018 compared to \$832,000 for the same period in the prior year. Accretion income of \$742,000 was included in the three months ended March 31, 2018 compared to \$806,000 for the same period in the prior year.

During the three months ended March 31, 2018, Pinnacle Financial and Pinnacle Bank received dividends from BHG of \$4.3 million in the aggregate compared to \$2.5 million for the same period in the prior year. Earnings from BHG are included in Pinnacle Financial's consolidated tax return. Profits from intercompany transactions are eliminated. No loans were purchased from BHG by Pinnacle Bank for the three month periods ended March 31, 2018 or 2017, respectively.

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Note 4. Securities

The amortized cost and fair value of securities available-for-sale and held-to-maturity at March 31, 2018 and December 31, 2017 are summarized as follows (in thousands):

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
March 31, 2018:				
Securities available-for-sale:				
U.S. Treasury securities	\$31,002	\$ —	\$ 56	\$30,946
U.S. government agency securities	176,305	43	2,905	173,443
Mortgage-backed securities	1,302,274	4,393	29,394	1,277,273
State and municipal securities	1,206,777	3,890	18,202	1,192,465
Asset-backed securities	204,800	377	505	204,672
Corporate notes and other	81,860	868	903	81,825
	\$3,003,018	\$ 9,571	\$ 51,965	\$ 2,960,624
Securities held-to-maturity:				
State and municipal securities	\$20,677	\$ 46	\$ 120	\$20,603
	\$20,677	\$ 46	\$ 120	\$20,603
December 31, 2017:				
Securities available-for-sale:				
U.S. Treasury securities	\$30,505	\$—	\$ 60	\$30,445
U.S. government agency securities	182,500	67	1,766	180,801
Mortgage-backed securities	1,270,625	5,318	12,124	1,263,819
State and municipal securities	774,949	12,251	2,588	784,612
Asset-backed securities	173,346	262	316	173,292
Corporate notes and other	81,615	1,346	647	82,314
	\$2,513,540	\$19,244	17,501	\$2,515,283
Securities held-to-maturity:				
State and municipal securities	\$20,762	\$114	\$ 46	\$20,830
	\$20,762	\$114	\$ 46	\$20,830

At March 31, 2018, approximately \$1.4 billion of securities within Pinnacle Financial's investment portfolio were pledged to secure either public funds and other deposits or securities sold under agreements to repurchase. At March 31, 2018, repurchase agreements comprised of secured borrowings totaled \$131.9 million and were secured by \$131.9 million of pledged U.S. government agency securities, municipal securities, asset backed securities, and corporate debentures. As the fair value of securities pledged to secure repurchase agreements may decline, Pinnacle Financial regularly evaluates its need to pledge additional securities to remain adequately secured.

The amortized cost and fair value of debt securities as of March 31, 2018 by contractual maturity are shown below. Actual maturities may differ from contractual maturities of mortgage- and asset-backed securities since the mortgages and assets underlying the securities may be called or prepaid with or without penalty. Therefore, these securities are not included in the maturity categories in the following summary (in thousands):

March 31, 2018:	Available-for-sale		Held-to-maturity	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Due in one year or less	\$—	\$—	\$—	\$—
Due in one year to five years	96,941	97,087	7,496	7,489
Due in five years to ten years	177,898	177,231	10,385	10,316

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Due after ten years	1,221,105	1,204,361	2,796	2,798
Mortgage-backed securities	1,302,274	1,277,273	—	—
Asset-backed securities	204,800	204,672	—	—
	\$3,003,018	\$2,960,624	\$20,677	\$20,603

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At March 31, 2018 and December 31, 2017, the following investments had unrealized losses. The table below classifies these investments according to the term of the unrealized losses of less than twelve months or twelve months or longer (in thousands):

	Investments with an Unrealized Loss of less than 12 months		Investments with an Unrealized Loss of 12 months or longer		Total Investments with an Unrealized Loss	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
At March 31, 2018						
U.S. Treasury securities	\$30,697	\$ 56	\$—	\$ —	\$30,697	\$ 56
U.S. government agency securities	145,967	2,904	248	1	146,215	2,905
Mortgage-backed securities	779,194	17,392	297,735	12,002	1,076,929	29,394
State and municipal securities	863,010	15,987	47,894	2,335	910,904	18,322
Asset-backed securities	79,428	449	9,482	56	88,910	505
Corporate notes	31,880	754	11,697	149	43,577	903
Total temporarily-impaired securities	\$1,930,176	\$ 37,542	\$367,056	\$ 14,543	\$2,297,232	\$ 52,085

At December 31, 2017

U.S. Treasury securities	\$29,948	\$ 60	\$—	\$ —	\$29,948	\$ 60
U.S. government agency securities	173,677	1,766	—	—	173,677	1,766
Mortgage-backed securities	607,408	5,042	285,561	7,082	892,969	12,124
State and municipal securities	115,403	1,408	50,083	1,226	165,486	2,634
Asset-backed securities	68,742	198	14,136	118	82,878	316
Corporate notes	22,168	547	11,944	100	34,112	647
Total temporarily-impaired securities	\$1,017,346	\$ 9,021	\$361,724	\$ 8,526	\$1,379,070	\$ 17,547

The applicable dates for determining when securities were in an unrealized loss position were March 31, 2018 and December 31, 2017. As such, it is possible that a security had a market value that exceeded its amortized cost on other days during the past twelve-month periods ended March 31, 2018 and December 31, 2017, but is not in the "Investments with an Unrealized Loss of less than 12 months" category above.

As shown in the tables above, including both available-for-sale and held-to-maturity investment securities, at March 31, 2018, Pinnacle Financial had approximately \$52.1 million in unrealized losses on \$2.30 billion of securities. The unrealized losses associated with these investment securities are driven by changes in interest rates and are not due to the credit quality of the securities. These securities will continue to be monitored as a part of Pinnacle Financial's ongoing impairment analysis. Management evaluates the financial performance of the issuers on a quarterly basis to determine if it is probable that the issuers can make all contractual principal and interest payments. Because Pinnacle Financial currently does not intend to sell those securities that have an unrealized loss at March 31, 2018, and it is not more-likely-than-not that Pinnacle Financial will be required to sell the securities before recovery of their amortized cost bases, which may be maturity, Pinnacle Financial does not consider these securities to be other-than-temporarily impaired at March 31, 2018.

Periodically, available-for-sale securities may be sold or the composition of the portfolio realigned to improve yields, quality or marketability, or to implement changes in investment or asset/liability strategy, including maintaining collateral requirements and raising funds for liquidity purposes. Additionally, if an available-for-sale security loses its investment grade or tax-exempt status, the underlying credit support is terminated or collection otherwise becomes uncertain based on factors known to management, Pinnacle Financial will consider selling the security, but will

review each security on a case-by-case basis as these factors become known. Consistent with the investment policy, during the first quarter of 2018 available-for-sale securities of approximately \$14.5 million were sold and net unrealized gains, net of tax, of \$22,000 were reclassified from accumulated other comprehensive income into net income.

The carrying values of Pinnacle Financial's investment securities could decline in the future if the financial condition of issuers deteriorates and management determines it is probable that Pinnacle Financial will not recover the entire amortized cost bases of the securities. As a result, there is a risk that other-than-temporary impairment charges may occur in the future. Additionally, there is a risk that other-than-temporary impairment charges may occur in the future if management's intention to hold these securities to maturity and/or recovery changes.

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Note 5. Loans and Allowance for Loan Losses

For financial reporting purposes, Pinnacle Financial classifies its loan portfolio based on the underlying collateral utilized to secure each loan. This classification is consistent with those utilized in the Quarterly Report of Condition and Income filed by Pinnacle Bank with the Federal Deposit Insurance Corporation (FDIC).

Pinnacle Financial uses five loan categories: commercial real estate mortgage, consumer real estate mortgage, construction and land development, commercial and industrial, and consumer and other.

Commercial real estate mortgage loans. Commercial real estate mortgage loans are categorized as such based on investor exposures where repayment is largely dependent upon the operation, refinance, or sale of the underlying real estate. Commercial real estate mortgage also includes owner occupied commercial real estate which shares a similar risk profile to Pinnacle Financial's commercial and industrial products.

Consumer real estate mortgage loans. Consumer real estate mortgage consists primarily of loans secured by 1-4 residential properties, including home equity lines of credit.

Construction and land development loans. Construction and land development loans include loans where the repayment is dependent on the successful operation of the related real estate project. Construction and land development loans include 1-4 family construction projects and commercial construction endeavors such as warehouses, apartments, office and retail space and land acquisition and development.

Commercial and industrial loans. Commercial and industrial loans include loans to business enterprises issued for commercial, industrial and/or other professional purposes.

Consumer and other loans. Consumer and other loans include all loans issued to individuals not included in the consumer real estate mortgage classification. Examples of consumer and other loans are automobile loans, credit cards and loans to finance education, among others.

Commercial loans receive risk ratings assigned by a financial advisor and approved by a senior credit officer subject to validation by Pinnacle Financial's independent loan review department. Risk ratings are categorized as pass, special mention, substandard, substandard-nonaccrual or doubtful-nonaccrual. Pinnacle Financial believes that its categories follow those used by Pinnacle Bank's primary regulators. At March 31, 2018, approximately 81.1% of Pinnacle Financial's loan portfolio was analyzed as a commercial loan type with a specifically assigned risk rating. Consumer loans and small business loans are generally not assigned an individual risk rating but are evaluated as either accrual or nonaccrual based on the performance of the individual loans. However, certain consumer real-estate mortgage loans and certain consumer and other loans receive a specific risk rating due to the loan proceeds being used for commercial purposes even though the collateral may be of a consumer loan nature.

Risk ratings are subject to continual review by a financial advisor and a senior credit officer. At least annually, Pinnacle Financial's credit procedures require that every risk rated loan of \$1.0 million or more be subject to a formal credit risk review process by the assigned financial advisor. Each loan's risk rating is also subject to review by Pinnacle Financial's independent loan review department, which reviews a substantial portion of Pinnacle Financial's risk rated portfolio annually. Included in the coverage are independent loan reviews of loans in targeted higher-risk portfolio segments such as certain commercial and industrial loans, land loans and/or loan types in certain geographies.

The following table presents Pinnacle Financial's loan balances by primary loan classification and the amount within each risk rating category. Pass rated loans include all credits other than those included in special mention, substandard, substandard-nonaccrual and doubtful-nonaccrual which are defined as follows:

Special mention loans have potential weaknesses that deserve management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the asset or in Pinnacle Financial's credit position at some future date.

Substandard loans are inadequately protected by the current sound worth and paying capacity of the obligor or of the collateral pledged, if any. Assets so classified must have a well-defined weakness or weaknesses that jeopardize collection of the debt. Substandard loans are characterized by the distinct possibility that Pinnacle Financial could sustain some loss if the deficiencies are not corrected.

Substandard-nonaccrual loans are substandard loans that have been placed on nonaccrual status.

Doubtful-nonaccrual loans have all the characteristics of substandard-nonaccrual loans with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions and values, highly questionable and improbable.

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The following table outlines the amount of each loan classification categorized into each risk rating category as of March 31, 2018 and December 31, 2017 (in thousands):

	Commercial real estate - mortgage	Consumer real estate - mortgage	Construction and land development	Commercial and industrial	Consumer and other	Total
March 31, 2018						
Pass	\$6,628,989	\$2,533,268	\$2,081,071	\$4,360,699	\$362,599	\$15,966,626
Special Mention	76,856	11,661	4,149	33,524	746	126,936
Substandard ⁽¹⁾	63,343	17,307	7,037	74,491	75	162,253
Substandard-nonaccrual	25,100	18,530	3,618	22,172	782	70,202
Doubtful-nonaccrual	—	—	—	—	—	—
Total loans	\$6,794,288	\$2,580,766	\$2,095,875	\$4,490,886	\$364,202	\$16,326,017
December 31, 2017						
Pass	\$6,487,368	\$2,503,688	\$1,880,704	\$4,014,656	\$351,359	\$15,237,775
Special Mention	94,134	18,356	8,148	46,898	1,177	168,713
Substandard ⁽¹⁾	72,044	21,053	13,468	62,529	79	169,173
Substandard-nonaccrual	16,064	18,117	5,968	17,258	48	57,455
Doubtful-nonaccrual	—	—	—	—	—	—
Total loans	\$6,669,610	\$2,561,214	\$1,908,288	\$4,141,341	\$352,663	\$15,633,116

Potential problem loans represent those loans with a well-defined weakness and where information about possible credit problems of borrowers has caused management to have doubts about the borrower's ability to comply with present repayment terms. This definition is believed to be substantially consistent with the standards established by (1) Pinnacle Bank's primary regulators for loans classified as substandard, excluding the impact of nonaccrual loans and troubled debt restructurings. Potential problem loans, which are not included in nonaccrual loans, amounted to approximately \$158.1 million at March 31, 2018, compared to \$164.0 million at December 31, 2017.

Loans acquired with deteriorated credit quality are recorded pursuant to the provisions of ASC 310-30, and are referred to as purchase credit impaired loans. The following table provides a rollforward of purchase credit impaired loans from December 31, 2017 through March 31, 2018 (in thousands):

	Gross Carrying Value	Accretable Yield	Nonaccretable Yield	Net Carrying Value
December 31, 2017	\$74,324	\$ (132)	\$ (31,537)	\$42,655
Acquisition	—	—	—	—
Year-to-date settlements	(5,298)	23	1,491	(3,784)
March 31, 2018	\$69,026	\$ (109)	\$ (30,046)	\$38,871

Certain of these loans have been deemed to be collateral dependent and as such, no accretable yield has been recorded for these loans. The carrying value is adjusted for additional draws, pursuant to contractual arrangements, offset by loan paydowns. Year-to-date settlements include both loans that were charged-off as well as loans that were paid off, typically as a result of refinancings at other institutions.

For the three months ended March 31, 2018, the average balance of impaired loans was \$105.0 million compared to \$41.1 million for the same period in 2017. Pinnacle Financial's policy is that the accrual of interest income will be discontinued when (1) there is a significant deterioration in the financial condition of the borrower and full repayment of principal and interest is not expected or (2) the principal or interest is more than 90 days past due, unless the loan is both well secured and in the process of collection. As such, at the date the above mentioned loans were placed on nonaccrual status, Pinnacle Financial reversed all previously accrued interest income against current year earnings.

Pinnacle Financial's policy is that once a loan is placed on nonaccrual status each subsequent payment is reviewed on a case-by-case basis to determine if the payment should be applied to interest or principal pursuant to regulatory guidelines. Pinnacle Financial recognized no interest income from cash payments received on nonaccrual loans during the three months ended March 31, 2018 compared to approximately \$49,000 during the three months ended March 31, 2017. Had these nonaccruing loans been on accruing status, interest income would have been higher by \$1.4 million for the three months ended March 31, 2018 compared to \$640,000 higher for the three months ended March 31, 2017.

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The following table details the recorded investment, unpaid principal balance and related allowance of Pinnacle Financial's impaired loans at March 31, 2018 and December 31, 2017 by loan classification (in thousands):

	At March 31, 2018			At December 31, 2017		
	Recorded investment	Unpaid principal balances	Related allowance	Recorded investment	Unpaid principal balances	Related allowance
Collateral dependent impaired loans:						
Commercial real estate – mortgage	\$36,258	\$43,809	\$ 778	\$33,073	\$40,771	\$ 38
Consumer real estate – mortgage	5,166	7,233	—	6,314	8,560	115
Construction and land development	5,939	11,537	—	8,513	14,115	6
Commercial and industrial	8,716	14,374	1,262	2,812	8,435	362
Consumer and other	—	—	—	—	—	—
Total	\$56,079	\$76,953	\$ 2,040	\$50,712	\$71,881	\$ 521
Cash flow dependent impaired loans:						
Commercial real estate – mortgage	\$6,808	\$9,106	\$ 93	\$5,944	\$8,237	\$ 95
Consumer real estate – mortgage	20,200	23,370	296	19,904	23,387	411
Construction and land development	1,017	1,883	13	3,222	4,184	12
Commercial and industrial	23,451	26,595	152	21,852	26,058	1,278
Consumer and other	782	810	210	—	—	—
Total	\$52,258	\$61,764	\$ 764	\$50,922	\$61,866	\$ 1,796
Total impaired loans	\$108,337	\$138,717	\$ 2,804	\$101,634	\$133,747	\$ 2,317

The following table details the average recorded investment and the amount of interest income recognized on a cash basis for the three months ended March 31, 2018 and 2017, respectively, on Pinnacle Financial's impaired loans that remain on the balance sheets as of such date (in thousands):

	For the three months ended			
	March 31, 2018		2017	
	Average recorded investment	Interest recognized	Average recorded investment	Interest recognized
Collateral dependent impaired loans:				
Commercial real estate – mortgage	\$34,666	\$ —	—\$2,100	\$ —
Consumer real estate – mortgage	5,740	—	2,216	—
Construction and land development	7,226	—	2,078	49
Commercial and industrial	5,764	—	6,312	—
Consumer and other	—	—	—	—
Total	\$53,396	\$ —	—\$12,706	\$ 49
Cash flow dependent impaired loans:				
Commercial real estate – mortgage	\$6,376	\$ —	—\$2,597	\$ —
Consumer real estate – mortgage	19,941	—	9,393	—
Construction and land development	2,120	—	3,288	—
Commercial and industrial	22,669	—	12,440	—
Consumer and other	487	—	689	—
Total	\$51,593	\$ —	—\$28,407	\$ —

Total impaired loans	\$ 104,989\$	—\$41,113\$	49
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At March 31, 2018 and December 31, 2017, there were \$6.1 million and \$6.6 million, respectively, of troubled debt restructurings that were performing as of their restructure date and which were accruing interest. Troubled commercial loans are restructured by specialists within Pinnacle Bank's Special Assets Group, and all restructurings are approved by committees and credit officers separate and apart from the normal loan approval process. These specialists are charged with reducing Pinnacle Financial's overall risk and exposure to loss in the event of a restructuring by obtaining some or all of the following: improved documentation, additional guaranties, increase in curtailments, reduction in collateral release terms, additional collateral or other similar strategies.

The following table outlines the amount of each loan category where troubled debt restructurings were made during the three months ended March 31, 2018 and 2017 (dollars in thousands):

	Three months ended March 31,	
	Pre Modification Number of Outstanding Contracts Investment	Post Modification Outstanding Recorded Investment, net of related allowance
2018		
Commercial real estate – mortgage	—\$ —	\$ —
Consumer real estate – mortgage	—	—
Construction and land development	—	—
Commercial and industrial	—	—
Consumer and other	—	—
	—\$ —	\$ —
2017		
Commercial real estate – mortgage	—\$ —	\$ —
Consumer real estate – mortgage	—	—
Construction and land development	—	—
Commercial and industrial	1 3,457	3,457
Consumer and other	—	—
	1 \$ 3,457	\$ 3,457

During the three months ended March 31, 2018 and 2017, Pinnacle Financial did not have any troubled debt restructurings that subsequently defaulted within twelve months of the restructuring.

At March 31, 2018 and 2017, the allowance for loan losses included no allowance and \$44,000, respectively, specifically related to accruing troubled debt restructurings, which are classified as impaired loans pursuant to U.S. GAAP, but which loans continued to accrue interest at contractual rates at those dates.

In addition to the loan metrics above, Pinnacle Financial analyzes its commercial loan portfolio to determine if a concentration of credit risk exists to any industries. Pinnacle Financial utilizes broadly accepted industry classification systems in order to classify borrowers into various industry classifications. Pinnacle Financial has a credit exposure (loans outstanding plus unfunded lines of credit) exceeding 25% of Pinnacle Bank's total risk-based capital to borrowers in the following industries at March 31, 2018 with the comparative exposures for December 31, 2017 (in thousands):

March 31, 2018

	Outstanding Principal Balances	Unfunded Commitments	Total exposure	Total Exposure at December 31, 2017
Lessors of nonresidential buildings	\$2,879,195	\$ 691,591	\$3,570,786	\$ 2,810,951
Lessors of residential buildings	929,097	275,564	1,204,661	884,244
Hotels (except Casino Hotels) and Motels	678,619	195,623	874,242	628,991

Additionally, Pinnacle Financial monitors two ratios regarding construction and commercial real estate lending as part of its concentration management processes. Both ratios are calculated by dividing certain types of loan balances for each of the two categories by Pinnacle Bank's total risk-based capital. At March 31, 2018 and December 31, 2017, Pinnacle Bank's construction and land development loans as a percentage of total risk-based capital were 96.1% and 89.4%, respectively. Non-owner occupied commercial real estate and multifamily loans (including construction and land development loans) as a percentage of total risk-based capital were 306.2% and 297.1% as of March 31, 2018 and December 31, 2017, respectively. Banking regulations have established guidelines for the construction ratio of less than 100% of total risk-based capital and for the non-owner occupied ratio of less than 300% of total risk-based capital. When a bank's ratios are in excess of one or both of these guidelines, banking regulations generally

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require an increased level of monitoring in these lending areas by bank management. At March 31, 2018 Pinnacle Bank slightly exceeded the 300% guideline and has established what it believes to be appropriate controls to monitor Pinnacle Bank's lending in this area.

The table below presents past due balances by loan classification and segment at March 31, 2018 and December 31, 2017, allocated between accruing and nonaccrual status (in thousands):

March 31, 2018	Accruing		Total past due and accruing	Current and accruing	Purchase credit impaired	Nonaccruing		Total loans
	30-89 days past due and accruing	90 days or more past due and accruing				Nonaccrual	Nonaccruing purchase credit impaired	
Commercial real estate:								
Owner-occupied	\$3,805	\$5	\$3,810	\$2,398,599	\$4,430	\$19,935	\$1,172	\$2,427,946
All other	6,678	132	6,810	4,343,636	11,903	1,206	2,787	4,366,342
Consumer real estate – mortgage	13,367	19	13,386	2,544,825	4,024	11,336	7,195	2,580,766
Construction and land development	606	3	609	2,088,310	3,339	381	3,236	2,095,875
Commercial and industrial	9,262	589	9,851	4,458,161	702	22,090	82	4,490,886
Consumer and other	4,816	383	5,199	358,221	—	781	1	364,202
Total	\$38,534	\$1,131	\$39,665	\$16,191,752	\$24,398	\$55,729	\$14,473	\$16,326,017
December 31, 2017								
Commercial real estate:								
Owner-occupied	\$6,772	\$104	\$6,876	\$2,435,819	\$4,820	\$11,395	\$1,105	\$2,460,015
All other	16,559	—	16,559	4,177,454	12,018	704	2,860	4,209,595
Consumer real estate – mortgage	14,835	1,265	16,100	2,521,748	5,249	9,320	8,797	2,561,214
Construction and land development	4,136	146	4,282	1,894,560	3,478	2,878	3,090	1,908,288
Commercial and industrial	7,406	1,348	8,754	4,114,127	1,154	17,222	84	4,141,341
Consumer and other	6,311	1,276	7,587	345,076	—	—	—	352,663
Total	\$56,019	\$4,139	\$60,158	\$15,488,784	\$26,719	\$41,519	\$15,936	\$15,633,116

(1) Approximately \$56.3 million and \$45.8 million of nonaccrual loans as of March 31, 2018 and December 31, 2017, respectively, were performing pursuant to their contractual terms at those dates.

The following table details the changes in the allowance for loan losses for the three months ended March 31, 2018 and 2017, respectively, by loan classification (in thousands):

Three months ended March 31, 2018:	Commercial real estate - mortgage	Consumer real estate - mortgage	Construction and land development	Commercial and industrial	Consumer and other	Unallocated	Total
Balance at December 31, 2017	\$ 21,188	\$ 5,031	\$ 8,962	\$ 24,863	\$ 5,874		