

SOUTHSIDE BANCSHARES INC
Form 10-Q
May 06, 2010

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2010

OR

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

For the transition period from _____ to _____

Commission file number 0-12247

SOUTHSIDE BANCSHARES, INC.
(Exact name of registrant as specified in its charter)

TEXAS	75-1848732
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

1201 S. Beckham, Tyler, Texas	75701
(Address of principal executive offices)	(Zip Code)

903-531-7111
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was

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required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

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

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

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

The number of shares of the issuer's common stock, par value \$1.25, outstanding as of April 23, 2010 was 15,793,726 shares.

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PART I. FINANCIAL INFORMATION
ITEM 1. FINANCIAL STATEMENTS

SOUTHSIDE BANCSHARES, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

(UNAUDITED)

(in thousands, except share amounts)

	ASSETS	March 31, 2010	December 31, 2009
Cash and due from banks		\$35,805	\$50,350
Interest earning deposits		2,357	1,816
Total cash and cash equivalents		38,162	52,166
Investment securities:			
Available for sale, at estimated fair value		282,199	265,060
Held to maturity, at amortized cost		1,494	1,493
Mortgage-backed and related securities:			
Available for sale, at estimated fair value		1,090,224	1,238,182
Held to maturity, at amortized cost		439,121	242,665
FHLB stock, at cost		36,305	38,629
Other investments, at cost		2,065	2,065
Loans held for sale		2,036	2,857
Loans:			
Loans		1,017,444	1,033,576
Less: allowance for loan loss		(19,468)	(19,896)
Net Loans		997,976	1,013,680
Premises and equipment, net		47,466	46,477
Goodwill		22,034	22,034
Other intangible assets, net		1,010	1,096
Interest receivable		15,348	18,482
Deferred tax asset		4,159	1,611
Other assets		70,142	77,791
TOTAL ASSETS		\$3,049,741	\$3,024,288
	LIABILITIES AND EQUITY		
Deposits:			
Noninterest bearing		\$403,575	\$394,001
Interest bearing		1,524,851	1,476,420
Total Deposits		1,928,426	1,870,421
Short-term obligations:			
Federal funds purchased and repurchase agreements		7,170	13,325
FHLB advances		321,202	322,351
Other obligations		2,776	2,760
Total Short-term obligations		331,148	338,436
Long-term obligations:			
FHLB advances		463,058	532,519
Long-term debt		60,311	60,311
Total Long-term obligations		523,369	592,830
Other liabilities		59,127	20,352

TOTAL LIABILITIES	2,842,070	2,822,039
Off-Balance-Sheet Arrangements, Commitments and Contingencies (Note 12)		
Shareholders' equity:		
Common stock - \$1.25 par, 40,000,000 shares authorized, 17,557,088 shares issued in 2010 (including 753,710 shares declared on March 18, 2010 as a stock dividend) and 16,592,417 shares issued in 2009	21,946	20,928
Paid-in capital	161,460	146,357
Retained earnings	47,401	53,812
Treasury stock (1,763,362 and 1,762,261 shares at cost)	(23,569)	(23,545)
Accumulated other comprehensive (loss) income	(409)	4,229
TOTAL SHAREHOLDERS' EQUITY	206,829	201,781
Noncontrolling interest	842	468
TOTAL EQUITY	207,671	202,249
TOTAL LIABILITIES AND EQUITY	\$3,049,741	\$3,024,288

The accompanying notes are an integral part of these consolidated financial statements.

SOUTHSIDE BANCSHARES, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME
(UNAUDITED)

(in thousands, except per share data)

	Three Months Ended March 31,	
	2010	2009
Interest income		
Loans	\$17,765	\$18,313
Investment securities – taxable	26	319
Investment securities – tax-exempt	2,826	1,494
Mortgage-backed and related securities	14,277	16,404
FHLB stock and other investments	82	104
Other interest earning assets	11	26
Total interest income	34,987	36,660
Interest expense		
Deposits	5,005	6,372
Short-term obligations	1,680	1,165
Long-term obligations	5,226	6,886
Total interest expense	11,911	14,423
Net interest income	23,076	22,237
Provision for loan losses	3,867	3,590
Net interest income after provision for loan losses	19,209	18,647
Noninterest income		
Deposit services	4,064	4,035
Gain on sale of securities available for sale	8,355	13,796
Total other-than-temporary impairment losses	(39)	(5,627)
Portion of loss recognized in other comprehensive income (before taxes)	(36)	4,727
Net impairment losses recognized in earnings	(75)	(900)
Gain on sale of loans	281	335
Trust income	530	563
Bank owned life insurance income	285	301
Other	933	784
Total noninterest income	14,373	18,914
Noninterest expense		
Salaries and employee benefits	10,942	10,484
Occupancy expense	1,643	1,418
Equipment expense	437	375
Advertising, travel & entertainment	537	509
ATM and debit card expense	167	299
Director fees	177	146
Supplies	270	212
Professional fees	406	630
Postage	186	188
Telephone and communications	373	281
FDIC Insurance	679	536
Other	1,635	1,439

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Total noninterest expense	17,452	16,517
Income before income tax expense	16,130	21,044
Provision for income tax expense	3,955	6,146
Net income	12,175	14,898
Less: Net income attributable to the noncontrolling interest	(530)	(753)
Net income attributable to Southside Bancshares, Inc.	\$11,645	\$14,145
Earnings per common share – basic	\$0.74	\$0.91
Earnings per common share – diluted	\$0.74	\$0.90
Dividends paid per common share	\$0.17	\$0.13

The accompanying notes are an integral part of these consolidated financial statements.

SOUTHSIDE BANCSHARES, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY
(UNAUDITED)

(in thousands, except share amounts)

	Three Months Ended March 31,	
	2010	2009
Common Stock		
Balance, beginning of period	\$20,928	\$19,695
Issuance of common stock (60,543 shares in 2010 and 128,513 shares in 2009)	76	160
Stock dividend declared	942	885
Balance, end of period	21,946	20,740
Paid-in capital		
Balance, beginning of period	146,357	131,112
Issuance of common stock (60,543 shares in 2010 and 128,513 shares in 2009)	396	668
Tax benefit of incentive stock options	145	164
Stock dividend declared	14,562	12,620
Balance, end of period	161,460	144,564
Retained earnings		
Balance, beginning of period	53,812	34,021
Net income attributable to Southside Bancshares, Inc.	11,645	14,145
Dividends paid on common stock (\$0.17 per share in 2010 and \$0.13 per share in 2009)	(2,552)	(1,825)
Stock dividend declared	(15,504)	(13,505)
Balance, end of period	47,401	32,836
Treasury Stock		
Balance, beginning of period	(23,545)	(23,115)
Purchase of common stock (1,101 shares in 2010 and 30,691 shares in 2009)	(24)	(430)
Balance, end of period	(23,569)	(23,545)
Accumulated other comprehensive (loss) income		
Balance, beginning of period	4,229	(1,096)
Net unrealized gains on available for sale securities, net of tax	560	10,496
Reclassification adjustment for gains on sales of available for sale securities included in net income, net of tax	(5,431)	(8,967)
Non-credit portion of other-than-temporary impairment losses on available for sale securities, net of tax	23	408
Other-than-temporary impairment charges on available for sale securities included in net income, net of tax	49	585
Adjustment to net periodic benefit cost, net of tax	161	209
Net change in accumulated other comprehensive (loss) income	(4,638)	2,731
Balance, end of period	(409)	1,635
Total shareholders' equity	206,829	176,230
Noncontrolling interest		
Balance, beginning of period	468	472
Net income attributable to noncontrolling interest shareholders	530	753
Capital distribution to noncontrolling interest shareholders	(156)	(992)
Balance, end of period	842	233
Total equity	\$207,671	\$176,463

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Comprehensive income		
Net income	\$12,175	\$14,898
Net change in accumulated other comprehensive (loss) income	(4,638)	2,731
Comprehensive income	7,537	17,629
Comprehensive income attributable to the noncontrolling interest	(530)	(753)
Comprehensive income attributable to Southside Bancshares, Inc.	\$7,007	\$16,876

The accompanying notes are an integral part of these consolidated financial statements.

SOUTHSIDE BANCSHARES, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(UNAUDITED)
(in thousands)

	Three Months Ended March 31,	
	2010	2009
OPERATING ACTIVITIES:		
Net income	\$12,175	\$14,898
Adjustments to reconcile net income to net cash provided by operations:		
Depreciation	775	601
Amortization of premium	7,120	2,193
Accretion of discount and loan fees	(1,271)	(995)
Provision for loan losses	3,867	3,590
Decrease in interest receivable	3,134	2,666
Decrease in other assets	1,052	670
Net change in deferred taxes	(50)	(455)
Decrease in interest payable	(430)	(498)
Increase in other liabilities	4,380	8,708
Decrease (increase) in loans held for sale	821	(3,371)
Gain on sale of securities available for sale	(8,355)	(13,796)
Net other-than-temporary impairment losses	75	900
Gain on sale of assets	(7)	-
Impairment on other real estate owned	20	-
(Gain) loss on sale of other real estate owned	(15)	1
Net cash provided by operating activities	23,291	15,112
INVESTING ACTIVITIES:		
Proceeds from sales of investment securities available for sale	12,265	124,567
Proceeds from sales of mortgage-backed securities available for sale	388,909	53,170
Proceeds from maturities of investment securities available for sale	2,784	40,800
Proceeds from maturities of mortgage-backed securities available for sale	96,982	48,759
Proceeds from maturities of mortgage-backed securities held to maturity	18,129	9,653
Proceeds from redemption of FHLB stock	2,360	-
Purchases of investment securities available for sale	(15,248)	(30,720)
Purchases of mortgage-backed securities available for sale	(317,794)	(184,673)
Purchases of mortgage-backed securities held to maturity	(215,686)	(41,461)
Purchases of FHLB stock and other investments	(36)	(46)
Net decrease in loans	11,328	4,715
Purchases of premises and equipment	(1,795)	(1,804)
Proceeds from sales of premises and equipment	38	-
Proceeds on bank owned life insurance	-	511
Proceeds from sales of other real estate owned	419	217
Proceeds from sales of repossessed assets	1,199	594
Net cash (used in) provided by investing activities	(16,146)	24,282

The accompanying notes are an integral part of these consolidated financial statements.

SOUTHSIDE BANCSHARES, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS (continued)
(UNAUDITED)
(in thousands)

	Three Months Ended March 31,	
	2010	2009
FINANCING ACTIVITIES:		
Net increase (decrease) in demand and savings accounts	125,151	(19,520)
Net (decrease) increase in certificates of deposit	(67,420)	143,301
Net (decrease) increase in federal funds purchased and repurchase agreements	(6,155)	224
Proceeds from FHLB advances	1,203,170	1,195,000
Repayment of FHLB advances	(1,273,780)	(1,336,973)
Net capital distributions to non-controlling interest in consolidated entities	(156)	(992)
Tax benefit of incentive stock options	145	164
Purchase of common stock	(24)	(430)
Proceeds from the issuance of common stock	472	828
Dividends paid	(2,552)	(1,825)
Net cash used in financing activities	(21,149)	(20,223)
Net (decrease) increase in cash and cash equivalents	(14,004)	19,171
Cash and cash equivalents at beginning of period	52,166	66,774
Cash and cash equivalents at end of period	\$ 38,162	\$ 85,945
SUPPLEMENTAL DISCLOSURES FOR CASH FLOW INFORMATION:		
Interest paid	\$ 12,341	\$ 14,921
Income taxes paid	-	500
SUPPLEMENTAL DISCLOSURES OF NONCASH INVESTING AND FINANCING ACTIVITIES:		
Acquisition of other repossessed assets and real estate through foreclosure	\$ 1,930	\$ 4,238
Declaration of 5% stock dividend	15,504	13,505
Adjustment to pension liability	(247)	(321)
Unsettled trades to purchase securities	(37,458)	(58,307)
Unsettled trades to sell securities	1,453	-
Unsettled issuances of brokered CDs	19,830	-

The accompanying notes are an integral part of these consolidated financial statements

SOUTHSIDE BANCSHARES, INC. AND SUBSIDIARIES
NOTES TO FINANCIAL STATEMENTS

1. Basis of Presentation

In this report, the words “the Company,” “we,” “us,” and “our” refer to the combined entities of Southside Bancshares, Inc. and its subsidiaries. The words “Southside” and “Southside Bancshares” refer to Southside Bancshares, Inc. The words “Southside Bank” and “the Bank” refer to Southside Bank (which, subsequent to the internal merger of Fort Worth National Bank (“FWNB”) with and into Southside Bank, includes FWNB). “FWBS” refers to Fort Worth Bancshares, Inc., a bank holding company acquired by Southside of which FWNB was a wholly-owned subsidiary. “SFG” refers to Southside Financial Group, LLC, of which Southside owns a 50% interest and consolidates for financial reporting.

The consolidated balance sheet as of March 31, 2010, and the related consolidated statements of income, equity and cash flows and notes to the financial statements for the three month period ended March 31, 2010 and 2009 are unaudited; in the opinion of management, all adjustments necessary for a fair presentation of such financial statements have been included. Such adjustments consisted only of normal recurring items. All significant intercompany accounts and transactions are eliminated in consolidation. The preparation of these consolidated financial statements in conformity with U.S. generally accepted accounting principles (“GAAP”) requires the use of management’s estimates. These estimates are subjective in nature and involve matters of judgment. Actual amounts could differ from these estimates.

Interim results are not necessarily indicative of results for a full year. These financial statements should be read in conjunction with the financial statements and notes thereto in our Annual Report on Form 10-K for the year ended December 31, 2009. All share data has been adjusted to give retroactive recognition to stock splits and stock dividends. For a description of our significant accounting and reporting policies, refer to Note 1 of the Notes to Financial Statements in our Annual Report on Form 10-K for the year ended December 31, 2009.

2. Earnings Per Share

Earnings per share attributable to Southside Bancshares, Inc. on a basic and diluted basis have been adjusted to give retroactive recognition to stock splits and stock dividends and is calculated as follows (in thousands, except per share amounts):

	Three Months Ended March 31,	
	2010	2009
Basic and Diluted Earnings:		
Net Income - Southside Bancshares, Inc.	\$ 11,645	\$ 14,145
Basic weighted-average shares outstanding	15,751	15,490
Add: Stock options	64	221
Diluted weighted-average shares outstanding	15,815	15,711
Basic Earnings Per Share:		
Net Income - Southside Bancshares, Inc.	\$ 0.74	\$ 0.91
Diluted Earnings Per Share:		
Net Income - Southside Bancshares, Inc.	\$ 0.74	\$ 0.90

For the three month period ended March 31, 2010 and 2009, there were no antidilutive options.

3. Comprehensive (Loss) Income

The components of other comprehensive (loss) income are as follows (in thousands):

	Three Months Ended March 31, 2010		
	Before-Tax Amount	Tax (Expense) Benefit	Net-of-Tax Amount
Unrealized losses on securities:			
Unrealized holding gains arising during period	\$861	\$(301)	\$560
Non credit portion of other-than-temporary impairment losses on the AFS securities	36	(13)	23
Less: reclassification adjustment for gains included in net income	8,355	(2,924)	5,431
Less: other-than-temporary impairment charges on AFS securities included in net income	(75)	26	(49)
Net unrealized losses on securities	(7,383)	2,584	(4,799)
Change in pension plans	247	(86)	161
Other comprehensive loss	\$(7,136)	\$2,498	\$(4,638)

	Three Months Ended March 31, 2009		
	Before-Tax Amount	Tax (Expense) Benefit	Net-of-Tax Amount
Unrealized gains on securities:			
Unrealized holding gains arising during period	\$16,149	\$(5,653)	\$10,496
Non credit portion of other-than-temporary impairment losses on the AFS securities	627	(219)	408
Less: reclassification adjustment for gains included in net income	13,796	(4,829)	8,967
Less: other-than-temporary impairment charges on AFS securities included in net income	(900)	315	(585)
Net unrealized gains on securities	3,880	(1,358)	2,522
Change in pension plans	321	(112)	209
Other comprehensive income	\$4,201	\$(1,470)	\$2,731

4. Securities

The amortized cost and estimated market value of investment and mortgage-backed securities as of March 31, 2010 and December 31, 2009, are reflected in the tables below (in thousands):

	March 31, 2010				Estimated Market Value
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses OTTI	Gross Unrealized Losses Other	
AVAILABLE FOR SALE:					
Investment Securities:					
U.S. Treasury	\$4,900	\$-	\$-	\$-	\$4,900
State and Political Subdivisions	265,933	11,001	-	240	276,694
Other Stocks and Bonds	3,308	4	2,694	13	605
Mortgage-backed Securities:					
U.S. Government Agencies	168,331	3,367	-	1,659	170,039
Government-Sponsored Enterprises	911,763	14,369	-	5,947	920,185
Total	\$1,354,235	\$28,741	\$2,694	\$7,859	\$1,372,423

	March 31, 2010				Estimated Market Value
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses OTTI	Gross Unrealized Losses Other	
HELD TO MATURITY:					
Investment Securities:					
State and Political Subdivisions	\$1,013	\$111	\$-	\$-	\$1,124
Other Stocks and Bonds	481	18	-	-	499
Mortgage-backed Securities:					
U.S. Government Agencies	27,614	521	-	430	27,705
Government-Sponsored Enterprises	411,507	4,558	-	3,238	412,827
Total	\$440,615	\$5,208	\$-	\$3,668	\$442,155

	December 31, 2009				Estimated Market Value
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses OTTI	Gross Unrealized Losses Other	
AVAILABLE FOR SALE:					
Investment Securities:					
U.S. Treasury	\$4,898	\$1	\$-	\$-	\$4,899
State and Political Subdivisions	250,391	9,431	-	296	259,526
Other Stocks and Bonds	3,383	3	2,730	21	635
Mortgage-backed Securities:					
U.S. Government Agencies	126,264	3,725	-	407	129,582
Government-Sponsored Enterprises	1,092,659	20,787	-	4,846	1,108,600
Total	\$1,477,595	\$33,947	\$2,730	\$5,570	\$1,503,242

	December 31, 2009			Estimated
	Amortized	Gross	Gross Unrealized Losses	

HELD TO MATURITY:	Unrealized				Market Value
	Cost	Gains	OTTI	Other	
Investment Securities:					
State and Political Subdivisions	\$ 1,013	\$ 103	\$-	\$-	\$ 1,116
Other Stocks and Bonds	480	22	-	-	502
Mortgage-backed Securities:					
U.S. Government Agencies	16,677	534	-	36	17,175
Government-Sponsored Enterprises	225,988	5,248	-	766	230,470
Total	\$244,158	\$5,907	\$-	\$802	\$249,263

The following table represents the unrealized loss on securities for the three months ended March 31, 2010 and year ended December 31, 2009 (in thousands):

	Less Than 12 Months		More Than 12 Months		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
As of March 31, 2010:						
Available for Sale						
U.S. Treasury	\$4,900	\$-	\$-	\$-	\$4,900	\$-
State and Political Subdivisions	7,321	61	4,019	179	11,340	240
Other Stocks and Bonds	-	-	409	2,707	409	2,707
Mortgage-Backed Securities	491,022	7,606	63	-	491,085	7,606
Total	\$503,243	\$7,667	\$4,491	\$2,886	\$507,734	\$10,553
Held to Maturity						
Mortgage-Backed Securities	\$229,370	\$3,667	\$196	\$1	\$229,566	\$3,668
Total	\$229,370	\$3,667	\$196	\$1	\$229,566	\$3,668

As of December 31, 2009:

Available for Sale						
State and Political Subdivisions	\$14,520	\$160	\$2,953	\$136	\$17,473	\$296
Other Stocks and Bonds	-	-	441	2,751	441	2,751
Mortgage-Backed Securities	391,889	5,250	1,065	3	392,954	5,253
Total	\$406,409	\$5,410	\$4,459	\$2,890	\$410,868	\$8,300
Held to Maturity						
Mortgage-Backed Securities	\$19,705	\$802	\$-	\$-	\$19,705	\$802
Total	\$19,705	\$802	\$-	\$-	\$19,705	\$802

When it is determined that a decline in fair value of HTM and AFS securities is other-than-temporary, the carrying value of the security is reduced to its estimated fair value, with a corresponding charge to earnings for the credit portion and the non credit portion to other comprehensive income. In estimating other-than-temporary impairment losses, management considers, among other things, the length of time and the extent to which the fair value has been less than cost and the financial condition and near-term prospects of the issuer. Additionally, we do not currently intend to sell the securities and it is not more likely than not that we will be required to sell the securities before the anticipated recovery of its amortized cost basis.

The turmoil in the capital markets had a significant impact on our estimate of fair value for certain of our securities. We believe the market values are reflective of illiquidity and credit impairment. At March 31, 2010, we have in AFS Other Stocks and Bonds, \$2.9 million amortized cost basis in pooled trust preferred securities ("TRUPs"). Those securities are structured products with cash flows dependent upon securities issued by U.S. financial institutions, including banks and insurance companies. Our estimate of fair value at March 31, 2010 for the TRUPs is approximately \$231,000 and reflects the market illiquidity. With the exception of the TRUPs, to the best of management's knowledge and based on our consideration of the qualitative factors associated with each security, there were no securities in our investment and mortgage-backed securities portfolio at March 31, 2010 with an other-than-temporary impairment.

Given the facts and circumstances associated with the TRUPs we performed detailed cash flow modeling for each TRUP using an industry-accepted cash flow model. Prior to loading the required assumptions into the model we reviewed the financial condition of each of the underlying issuing banks within the TRUP collateral pool that had not deferred or defaulted as of March 31, 2010. Management's best estimate of a deferral assumption was assigned to each issuing bank based on the category in which it fell. Our analysis of the underlying cash flows contemplated various default, deferral and recovery scenarios to arrive at our best estimate of cash flows. Based on that detailed analysis, we have concluded that the other-than-temporary impairment, which captures the credit component in compliance with FASB ASC Topic 320, "Investments – Debt and Equity Securities," was estimated at \$3.1 million and \$3.0 million at March 31, 2010 and December 31, 2009, respectively. The non credit charge to other comprehensive income was estimated at \$2.7 million at March 31, 2010 and December 31, 2009. Therefore, the carrying amount of the TRUPs was written down with \$75,000 recognized in earnings for the three months ended March 31, 2010 and \$3.0 million recognized in earnings for the year ended December 31, 2009. The cash flow model assumptions represent management's best estimate and consider a variety of qualitative factors, which include, among others, the credit rating downgrades, the severity and duration of the mark-to-market loss, and the

structural nuances of each TRUP. Management believes that the detailed review of the collateral and cash flow modeling support the conclusion that the TRUPs had an other-than-temporary impairment at March 31, 2010. We will continue to update our assumptions and the resulting analysis each reporting period to reflect changing market conditions. Additionally, we do not currently intend to sell the TRUPs and it is not more likely than not that we will be required to sell the TRUPs before the anticipated recovery of their amortized cost basis.

The table below provides more detail on the TRUPs (dollars in thousands).

TRUP	Par	Credit Loss	Amortized Cost	Fair Value	Tranche	Credit Rating
1	\$ 2,000	\$ 1,075	\$ 925	\$ 168	C1	Ca
2	2,000	550	1,450	36	B1	Ca
3	2,000	1,450	550	27	B2	C
	\$ 6,000	\$ 3,075	\$ 2,925	\$ 231		

The following table presents the impairment activity related to credit loss, which is recognized in earnings, and the impairment activity related to all other factors, which are recognized in other comprehensive income.

	Three Months Ended March 31, 2010		
	Impairment Related to Credit Loss	Impairment Related to All Other Factors	Total Impairment
Balance, beginning of the period	\$3,000	\$2,730	\$5,730
Charges on securities for which other-than-temporary impairment charges were not previously recognized	—	—	—
Additional charges on securities for which other-than-temporary impairment charges were previously recognized	75	(36)	39
Balance, end of the period	\$3,075	\$2,694	\$5,769

Management has the ability and intent to hold the securities classified as HTM until they mature, at which time we will receive full value for the securities. Furthermore, as of March 31, 2010, management also had the ability and intent to hold the securities classified as AFS for a period of time sufficient for a recovery of cost. The unrealized losses are largely due to increases in market interest rates over the yields available at the time the underlying securities were purchased. The fair value is expected to recover as the bonds approach their maturity date or repricing date or if market yields for such investments decline. Management does not believe any of the securities are impaired due to reasons of credit quality.

Interest income recognized on AFS and HTM securities for the period presented:

	Three Months Ended	
	March 31, 2010	March 31, 2009
U.S. Treasury	\$2	\$13

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U.S. Government Agencies	–	140
State and Political Subdivisions	2,836	1,593
Other Stocks and Bonds	14	67
Mortgage-backed Securities	14,277	16,404
Total interest income on securities	\$17,129	\$18,217

There were no securities transferred from AFS to HTM during the three months ended March 31, 2010 and 2009. There were no sales from the HTM portfolio during the three months ended March 31, 2010 or 2009. There were \$440.6 million of securities classified as HTM for the three months ended March 31, 2010 compared to \$244.2 million of securities classified as HTM for the year ended December 31, 2009.

Of the \$8.4 million in net securities gains from the AFS portfolio for the three months ended March 31, 2010, there were \$9.3 million in realized gains and \$0.9 in realized losses. Of the \$13.8 million in net securities gains from the AFS portfolio for the three months ended March 31, 2009, there were \$13.9 million in realized gains and \$0.1 million in realized losses.

The amortized cost and fair value of securities at March 31, 2010, are presented below by contractual maturity. Expected maturities may differ from contractual maturities because issuers may have the right to call or prepay obligations. Mortgage-backed securities are presented in total by category due to the fact that mortgage-backed securities typically are issued with stated principal amounts, and the securities are backed by pools of mortgages that have loans with varying maturities. The characteristics of the underlying pool of mortgages, such as fixed-rate or adjustable-rate, as well as prepayment risk, are passed on to the certificate holder. The term of a mortgage-backed pass-through security thus approximates the term of the underlying mortgages and can vary significantly due to prepayments.

	March 31, 2010	
	Amortized	
	Cost	Fair Value
	(in thousands)	
Available for sale securities:		
Investment Securities		
Due in one year or less	\$7,864	\$7,921
Due after one year through five years	8,713	9,001
Due after five years through ten years	31,360	32,483
Due after ten years	226,204	232,794
	274,141	282,199
Mortgage-backed securities	1,080,094	1,090,224
Total	\$1,354,235	\$1,372,423

	March 31, 2010	
	Amortized	
	Cost	Fair Value
Held to maturity securities:		
Investment Securities		
Due in one year or less	\$-	\$-
Due after one year through five years	-	-
Due after five years through ten years	481	499
Due after ten years	1,013	1,124
	1,494	1,623
Mortgage-backed securities	439,121	440,532
Total	\$440,615	\$442,155

Investment and mortgage-backed securities with book values of \$1.02 billion at March 31, 2010 and \$1.06 billion at December 31, 2009 were pledged to collateralize Federal Home Loan Bank ("FHLB") advances, repurchase agreements, public funds and trust deposits or for other purposes as required by law.

Securities with limited marketability, such as FHLB stock and other investments, are carried at cost, which approximates its fair value and assessed for other-than-temporary impairment. These securities have no maturity date.

5. Loans and Allowance for Probable Loan Losses

The following table sets forth loan totals by category for the periods presented (in thousands):

	At March 31, 2010	At December 31, 2009
Real Estate Loans:		
Construction	\$86,372	\$88,566
1-4 Family Residential	233,879	234,379
Other	209,412	212,731
Commercial Loans	153,670	159,529
Municipal Loans	155,304	150,111
Loans to Individuals	178,807	188,260
Total Loans	\$1,017,444	\$1,033,576

The summaries of the Allowance for Loan Losses and Reserve for Unfunded Loan Commitments are as follows (in thousands):

	Three Months Ended March 31, 2010	
	2010	2009
Allowance for Loan Losses:		
Balance at beginning of period	\$ 19,896	\$ 16,112
Provision for loan losses	3,867	3,590
Loans charged off	(4,926)	(2,704)
Recoveries of loans charged off	631	434
Balance at end of period	\$ 19,468	\$ 17,432
Reserve for Unfunded Loan Commitments:		
Balance at beginning of period	\$ 5	\$ 7
Provision for losses on unfunded loan commitments	15	-
Balance at end of period	\$ 20	\$ 7

6. Goodwill and Core Deposit Intangible Assets

Goodwill. Goodwill totaled \$22.0 million at both March 31, 2010 and December 31, 2009.

We measured our goodwill for impairment at December 31, 2009. We have identified Southside Bank as the sole operating segment and reporting unit for our impairment assessment.

Step one of the impairment test involves comparing the fair value of the reporting unit which, in our case, is the entire entity, to the carrying value of the reporting unit. If the fair value of the reporting unit is greater than the carrying value of the reporting unit, no additional testing is required. If the fair value of the reporting unit is less than the carrying value of the reporting unit, step two of the impairment test must be performed. At December 31, 2009, the fair value of the reporting unit was greater than the carrying value of the reporting unit. As a result, we did not record any goodwill impairment for the year ended December 31, 2009. As of March 31, 2010, there were no trigger events to warrant an updated impairment analysis.

During the fourth quarter of 2007, we recorded core deposit intangibles totaling \$2.0 million in connection with the acquisition of FWBS. Core deposit intangibles are amortized on an accelerated basis over their estimated lives, which range from four to ten years.

Core Deposit Intangibles. Core deposit intangible assets were as follows (in thousands):

	Gross Intangible Assets	Accumulated Amortization	Net Intangible Assets
March 31, 2010			
Core deposits	\$ 2,047	\$ (1,037)	\$ 1,010
	\$ 2,047	\$ (1,037)	\$ 1,010
December 31, 2009			
Core deposits	\$ 2,047	\$ (951)	\$ 1,096
	\$ 2,047	\$ (951)	\$ 1,096

For the three months ended March 31, 2010 and 2009, amortization expense related to intangible assets totaled \$86,000 and \$102,000, respectively. The estimated aggregate future amortization expense for intangible assets remaining as of March 31, 2010 is as follows (in thousands):

Remainder of 2010	\$ 233
2011	255
2012	198
2013	146
2014	99
Thereafter	79
	\$ 1,010

7. Long-term Obligations

Long-term obligations are summarized as follows (in thousands):

	March 31, 2010	December 31, 2009
FHLB Advances (1)		
Varying maturities to 2028	\$463,058	\$532,519
Long-term Debt (2)		
Southside Statutory Trust III Due 2033 (3)	20,619	20,619
Southside Statutory Trust IV Due 2037 (4)	23,196	23,196
Southside Statutory Trust V Due 2037 (5)	12,887	12,887
Magnolia Trust Company I Due 2035 (6)	3,609	3,609
Total Long-term Debt	60,311	60,311
Total Long-term Obligations	\$523,369	\$592,830

(1) At March 31, 2010, the weighted average cost of these advances was 3.66%.

(2) This long-term debt consists of trust preferred securities that qualify under the risk-based capital guidelines as Tier 1 capital, subject to certain limitations.

(3) This debt carries an adjustable rate of 3.23013% through June 29, 2010 and adjusts quarterly at a rate equal to three-month LIBOR plus 294 basis points.

(4) This debt carries a fixed rate of 6.518% through October 30, 2012 and thereafter, adjusts quarterly at a rate equal to three-month LIBOR plus 130 basis points.

(5) This debt carries a fixed rate of 7.48% through December 15, 2012 and thereafter, adjusts quarterly at a rate equal to three-month LIBOR plus 225 basis points.

(6) This debt carries an adjustable rate of 2.05194% through May 23, 2010 and thereafter, adjusts quarterly at a rate equal to three-month LIBOR plus 180 basis points.

8. Employee Benefit Plans

The components of net periodic benefit cost are as follows (in thousands):

	Three Months Ended March 31,			
	Defined Benefit		Restoration Plan	
	Pension Plan		Restoration Plan	
	2010	2009	2010	2009
Service cost	\$ 339	\$ 339	\$ 29	\$ 23
Interest cost	678	641	72	60
Expected return on assets	(879)	(678)	-	-
Net loss recognition	213	293	45	39
Prior service credit amortization	(10)	(10)	(1)	(1)
Net periodic benefit cost	\$ 341	\$ 585	\$ 145	\$ 121

Employer Contributions. We previously disclosed in our financial statements for the year ended December 31, 2009, that we expected to contribute \$3.0 million to our defined benefit pension plan and \$80,000 to our post retirement benefit plan in 2010. As of March 31, 2010, no contributions had been made to our defined benefit plan, and

contributions of \$20,000 had been made to our post retirement benefit plan.

9. Incentive Stock Options

In April 1993, we adopted the Southside Bancshares, Inc. 1993 Incentive Stock Option Plan ("the ISO Plan"), a stock-based incentive compensation plan. The ISO Plan expired March 31, 2003.

As of March 31, 2010 and 2009, there were no nonvested shares. For the three months ended March 31, 2010 and 2009, there was no stock-based compensation expense.

As of March 31, 2010 and 2009, there was no unrecognized compensation cost related to the ISO Plan for nonvested options granted in March 2003.

The fair value of each stock option granted is estimated on the date of grant using the Black-Scholes method of option pricing with the following weighted-average assumptions for grants in 2003: dividend yield of 1.93%; risk-free interest rate of 4.93%; expected life of six years; and expected volatility of 28.90%.

Under the ISO Plan, we were authorized to issue shares of common stock pursuant to "Awards" granted in the form of incentive stock options (intended to qualify under Section 422 of the Internal Revenue Code of 1986, as amended). Before the ISO Plan expired, awards were granted to selected employees and directors. No stock options have been available for grant under the ISO Plan since its expiration in March 2003.

The ISO Plan provided that the exercise price of any stock option not be less than the fair market value of the common stock on the date of grant. The outstanding stock options have contractual terms of 10 years. All options vest on a graded schedule, 20% per year for five years, beginning on the first anniversary date of the grant date.

A summary of the status of our outstanding stock options as of March 31, 2010 and the changes during the three months ended March 31, 2010 is presented below:

	Number of Options	Weighted Average Exercise Prices	Weighted Average Remaining Contract Life (Years)	Aggregate Intrinsic Value (in thousands)
Outstanding at December 31, 2009	108,115	\$ 5.14	–	–
Exercised	(51,933)	\$ 4.53	–	–
Cancelled	–	\$ –	–	–
Outstanding at March 31, 2010	56,182	\$ 5.70	0.89	\$ 834
Exercisable at March 31, 2010	56,182	\$ 5.70	0.89	\$ 834

The total intrinsic value (i.e., the amount by which the fair value of the underlying common stock exceeds the exercise price of a stock option on exercise date) of stock options exercised during the three months ended March 31, 2010 and 2009 were \$775,000 and \$1.2 million, respectively.

Cash received from stock option exercises for the three months ended March 31, 2010 and 2009 was \$212,000 and \$178,000, respectively. The tax benefit realized for the deductions related to the stock option exercises were \$145,000 and \$164,000 for the three months ended March 31, 2010 and 2009, respectively.

On April 16, 2009, our shareholders approved the Southside Bancshares, Inc. 2009 Incentive Plan (the "2009 Incentive Plan"), which is a stock-based incentive compensation plan. A total of 1,050,000 shares of our common stock are reserved and available for issuance pursuant to awards granted under the 2009 Incentive Plan. As of March 31, 2010, no awards had been granted under this plan.

10. Fair Value Measurement

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. A fair value measurement assumes that the transaction to sell the asset or transfer the liability occurs in the principal market for the asset or liability or, in the absence of a principal market, the most advantageous market for the asset or liability. The price in the principal (or most advantageous) market used to measure the fair value of the asset or liability shall not be adjusted for transaction costs. An orderly transaction is a transaction that assumes exposure to the market for a period prior to the measurement date to allow for marketing activities that are usual and customary for transactions involving such assets and liabilities; it is not a forced transaction. Market participants are buyers and sellers in the principal market that are (i) independent, (ii) knowledgeable, (iii) able to transact and (iv) willing to transact.

Valuation techniques including the market approach, the income approach and/or the cost approach are utilized to determine fair value. Inputs to valuation techniques refer to the assumptions that market participants would use in pricing the asset or liability. An entity must consider all aspects of nonperforming risk, including the entity's own credit standing when measuring fair value of a liability. Inputs may be observable, meaning those that reflect the assumptions market participants would use in pricing the asset or liability developed based on market data obtained from independent sources, or unobservable, meaning those that reflect the reporting entity's own assumptions about the assumptions market participants would use in pricing the asset or liability developed based on the best information available in the circumstances. A fair value hierarchy for valuation inputs gives the highest priority to quoted prices in active markets for identical assets or liabilities and the lowest priority to unobservable inputs. The fair value hierarchy is as follows:

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

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

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

A description of the valuation methodologies used for assets and liabilities measured at fair value, as well as the general classification of such instruments pursuant to the valuation hierarchy, is set forth below.

Securities Available for Sale - Securities classified as available for sale primarily consist of U. S. Treasuries, government-sponsored enterprise debentures, mortgage-backed securities, municipal bonds, and, to a lesser extent, TRUPs and equity securities. We use quoted market prices of identical assets on active exchanges, or Level 1 measurements, where possible. Where such quoted market prices are not available, we typically employ quoted market prices of similar instruments (including matrix pricing) and/or discounted cash flows using observable inputs to estimate a value of these securities, or Level 2 measurements. Discounted cash flow analyses are typically based on market interest rates, prepayment speeds and/or option adjusted spreads. Level 3 measurements include a range of fair value estimates in the marketplace as a result of the illiquid market specific to the type of security or discounted cash flow analyses based on assumptions that are not readily observable in the market place. Such assumptions include projections of future cash flows, including loss assumptions and discount rates.

Certain financial assets are measured at fair value in accordance with GAAP. Adjustments to the fair value of these assets usually result from the application of fair value accounting or write-downs of individual assets. Transfers between levels of the fair value hierarchy are recognized on the actual date of the event or circumstances that caused the transfer, which generally coincides with our monthly and/or quarterly valuation process. There were no transfers between Level 1 and Level 2 during the three months ended March 31, 2010.

Loans Held for Sale - These loans are reported at the lower of cost or fair value. Fair value is determined based on expected proceeds, which are based on sales contracts and commitments and are considered Level 2 inputs. At March 31, 2010, based on our estimates of fair value, no valuation allowance was recognized.

Impaired Loans – Certain impaired loans may be reported at the fair value of the underlying collateral if repayment is expected solely from the collateral. Collateral values are estimated using Level 3 inputs based on customized discounting criteria or appraisals. During the three months ended March 31, 2010, certain impaired loans were remeasured and reported at fair value through a specific valuation allowance allocation of the allowance for possible loan losses based upon the fair value of the underlying collateral. Impaired loans with a carrying value of \$20.4 million were reduced by specific valuation allowance allocations totaling \$4.3 million to a total reported fair value of \$16.1 million based on collateral valuations utilizing Level 3 valuation inputs. During the three months ended March 31, 2009, certain impaired loans were remeasured and reported at fair value through a specific valuation allowance allocation of the allowance for possible loan losses based upon the fair value of the underlying collateral. Impaired loans with a carrying value of \$12.1 million were reduced by specific valuation allowance allocations totaling \$3.5 million to a total reported fair value of \$8.6 million based on collateral valuations utilizing Level 3 valuation inputs.

Certain non-financial assets and non-financial liabilities measured at fair value on a recurring basis include reporting units measured at fair value in the first step of a goodwill impairment test. Certain non-financial assets measured at fair value on a non-recurring basis include non-financial assets and non-financial liabilities measured at fair value in the second step of a goodwill impairment test, as well as intangible assets and other non-financial long-lived assets (such as real estate owned) that are measured at fair value in the event of an impairment. The framework became applicable to these fair value measurements beginning January 1, 2009.

The following tables summarize financial assets and financial liabilities measured at fair value on a recurring basis as of March 31, 2010 and December 31, 2009, segregated by the level of the valuation inputs within the fair value hierarchy utilized to measure fair value (in thousands):

Securities Available For Sale	As of March 31, 2010			Total Fair Value
	Level 1 Input	Level 2 Input	Level 3 Input	
Investment Securities:				
U.S. Treasury	\$4,900	\$–	\$–	\$4,900
State and Political Subdivisions	–	276,694	–	276,694
Other Stocks and Bonds	374	–	231	605
Mortgage-backed Securities:				
U.S. Government Agencies	–	170,039	–	170,039
Government-Sponsored Enterprise	–	920,185	–	920,185
Total	\$5,274	\$1,366,918	\$231	\$1,372,423

Securities Available For Sale	As of December 31, 2009			Total Fair Value
	Level 1 Input	Level 2 Input	Level 3 Input	
Investment Securities:				
U.S. Treasury	\$4,899	\$–	\$–	\$4,899
State and Political Subdivisions	–	259,526	–	259,526
Other Stocks and Bonds	365	–	270	635

Mortgage-backed Securities:

U.S. Government Agencies	–	129,582	–	129,582
Government-Sponsored Enterprise	–	1,108,600	–	1,108,600
Total	\$5,264	\$1,497,708	\$270	\$1,503,242

The following tables present additional information about financial assets and liabilities measured at fair value on a recurring basis and for which we have utilized Level 3 inputs to determine fair value (in thousands):

	Three Months Ended March 31,	
	2010	2009
Other Stocks and Bonds		
Balance at Beginning of Period	\$270	\$646
Total gains or losses (realized/unrealized):		
Included in earnings (or changes in net assets)	(75)	(900)
Included in other comprehensive income (loss)	36	627
Purchases, issuances and settlements	-	-
Transfers in and/or out of Level 3	-	-
Balance at End of Period	\$231	\$373
The amount of total gains or losses for the periods included in earnings (or changes in net assets) attributable to the change in unrealized gains or losses relating to assets still held at reporting date		
	\$(75)	\$(900)

Disclosure of fair value information about financial instruments, whether or not recognized in the balance sheet is required, for which it is practicable to estimate that value. In cases where quoted market prices are not available, fair values are based on estimates using present value or other estimation techniques. Those techniques are significantly affected by the assumptions used, including the discount rate and estimates of future cash flows. Such techniques and assumptions, as they apply to individual categories of our financial instruments, are as follows:

Cash and cash equivalents - The carrying amounts for cash and cash equivalents is a reasonable estimate of those assets' fair value.

Investment and mortgage-backed and related securities - Fair values for these securities are based on quoted market prices, where available. If quoted market prices are not available, fair values are based on quoted market prices for similar securities or estimates from independent pricing services.

FHLB stock and other investments - The carrying amount of FHLB stock is a reasonable estimate of those assets' fair value.

Loans receivable - For adjustable rate loans that reprice frequently and with no significant change in credit risk, the carrying amounts are a reasonable estimate of those assets' fair value. The fair value of fixed rate loans is estimated by discounting the future cash flows using the current rates at which similar loans would be made to borrowers with similar credit ratings and for the same remaining maturities. Nonperforming loans are estimated using discounted cash flow analyses or the underlying value of the collateral where applicable.

Deposit liabilities - The fair value of demand deposits, savings accounts, and certain money market deposits is the amount on demand at the reporting date, that is, the carrying value. Fair values for fixed rate certificates of deposits are estimated using a discounted cash flow calculation that applies interest rates currently being offered for deposits of similar remaining maturities.

Federal funds purchased and repurchase agreements - Federal funds purchased and repurchase agreements generally have an original term to maturity of one day and thus are considered short-term borrowings. Consequently, their carrying value is a reasonable estimate of fair value.

FHLB advances - The fair value of these advances is estimated by discounting the future cash flows using rates at which advances would be made to borrowers with similar credit ratings and for the same remaining maturities.

Long-term debt - The carrying amount for the long-term debt is estimated by discounting future cash flows using rates at which long-term debt would be made to borrowers with similar credit ratings and for the remaining maturities.

The following table presents our assets, liabilities, and unrecognized financial instruments at both their respective carrying amounts and fair value:

	At March 31, 2010		At December 31, 2009	
Carrying Amount	Fair Value	Carrying Amount	Fair Value	
		(in thousands)		