ITT CORP
Form DEF 14A
March 27, 2009

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**SCHEDULE 14A**
**(Rule 14a-101)**
**INFORMATION REQUIRED IN PROXY STATEMENT**

**SCHEDULE 14A INFORMATION**

**Proxy Statement Pursuant to Section 14(a) of the Securities Exchange Act of 1934 (Amendment No.1)**

Filed by the Registrant þ

Filed by a Party other than the Registrant o

Check the appropriate box:

o Preliminary Proxy Statement
þ Definitive Proxy Statement
o Definitive Additional Materials
o Soliciting Material Pursuant to Rule 14a-12
o Confidential, for the Use of the Commission Only (as permitted by Rule 14a-6(e)(2))

ITT Corporation
(Name of Registrant as Specified In Its Charter)

(Name of Person(s) Filing Proxy Statement, if other than the Registrant)

Payment of Filing Fee (Check the appropriate box):

þ No fee required.

o Fee computed on table below per Exchange Act Rules 14a-6(i)(1) and 0-11.

(1) Title of each class of securities to which transaction applies:

(2) Aggregate number of securities to which transaction applies:

(3) Per unit price or other underlying value of transaction computed pursuant to Exchange Act Rule 0-11 (Set forth the amount on which the filing fee is calculated and state how it was determined):

(4) Proposed maximum aggregate value of transaction:

(5) Total fee paid:

o Fee paid previously with preliminary materials.

o Check box if any part of the fee is offset as provided by Exchange Act Rule 0-11(a)(2) and identify the filing for which the offsetting fee was paid previously. Identify the previous filing by registration statement number, or the Form or Schedule and the date of its filing.

(1) Amount Previously Paid:

(2) Form, Schedule or Registration Statement No.:

(3) Filing Party:

(4) Date Filed:

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March 27, 2009

Steven R. Loranger
Chairman, President and Chief Executive Officer

*ITT Corporation*

1133 Westchester Avenue
White Plains, NY 10604-3543

Dear Fellow Shareholders:

Enclosed are the Notice of Annual Meeting and Proxy Statement for ITT s 2009 Annual Meeting of Shareholders. This year s meeting is intended to address only the business included on the agenda. Details of the business to be conducted at the Annual Meeting are given in the accompanying Notice of Annual Meeting and Proxy Statement, which provides information as required by applicable laws and regulations.

Your vote is important and we encourage you to vote whether you are a registered owner or a beneficial owner.

This year, in accordance with U.S. Securities and Exchange Commission rules, we are using the Internet as our primary means of furnishing proxy materials to shareholders. Because we are using the Internet, most shareholders will not receive paper copies of our proxy materials. We will instead send these shareholders a notice with instructions for accessing the proxy materials and voting via the Internet. This notice also provides information on how shareholders may obtain paper copies of our proxy materials if they so choose. We believe use of the Internet will make the proxy distribution process more efficient, less costly and help in conserving natural resources.

If you are the registered owner of ITT common stock, you may vote your shares by making a toll-free telephone call or using the Internet. Details of these voting options are explained in the Proxy Statement. If you choose to receive paper copies of our proxy materials, you can vote by completing and returning the enclosed proxy card by mail as soon as possible.

If you are a beneficial owner and someone else, such as your bank or broker, is the owner of record, the owner of record will communicate with you about how to vote your shares.

Whether or not you plan to attend the Annual Meeting, please vote as soon as possible. If you do not vote in person at the Annual Meeting, you may vote via the Internet, by telephone or, if you receive a paper proxy card in the mail, by mailing the completed proxy card. Voting by any of these methods will ensure your representation at the Annual Meeting. Your vote is important.

Sincerely,

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March 27, 2009

**NOTICE OF 2009 Annual Meeting**

| | |
|---|---|
| **Time:** | 10:30 a.m. Eastern Time, on Tuesday, May 12, 2009. |
| **Place:** | 1133 Westchester Avenue, White Plains, NY 10604-3543 |
| **Items of Business:** | 1. Election of ten members of the Board of Directors |
| | 2. Ratification of the appointment of Deloitte & Touche LLP as ITT s Independent Registered Public Accounting Firm for 2009 |
| | 3. Such other business, including a shareholder proposal, if properly presented at the meeting |
| **Who May Vote:** | You can vote if you were a shareholder at the close of business on March 16, 2009, the record date. |
| **Annual Report to Shareholders and Annual Report on Form 10-K:** | Copies of our 2008 Annual Report on Form 10-K and Annual Report to Shareholders are provided to shareholders. |
| **Mailing Date:** | Beginning March 27, 2009, this Notice and the 2009 Proxy Statement are being distributed to shareholders of record on March 16, 2009. |
| **About Proxy Voting:** | Your vote is important. Proxy voting permits shareholders unable to attend the Annual Meeting to vote their shares through a proxy. Most shareholders are unable to attend the Annual Meeting. By appointing a proxy, your shares will be represented and voted in accordance with your instructions. If you do not provide instructions on how to vote, the proxies will vote as recommended by the Board of Directors. You can vote your shares by completing and returning your proxy card. Most shareholders can also vote shares by following the Internet or telephone voting instructions provided on the proxy card. You can change your voting instructions or revoke your proxy at any time prior to the Annual Meeting by following the instructions on pages 1 to 4 of this proxy and on the proxy card. |

**INTERNET AVAILABILITY OF PROXY MATERIALS**

This year, in accordance with U.S. Securities and Exchange Commission rules, we are using the Internet as our primary means of furnishing proxy materials to shareholders. Because we are using the Internet, most shareholders will not receive paper copies of our proxy materials. We will instead send these shareholders a Notice of Internet Availability of Proxy Materials with instructions for accessing the proxy materials, including our proxy statement and annual report,

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and voting via the Internet. The Notice of Internet Availability of Proxy Materials also provides information on how shareholders may obtain paper copies of our proxy materials if they so choose.

**Important Notice Regarding the Availability of Proxy Materials for the Shareholder Meeting to be held on Tuesday, May 12, 2009 at 10:30 a.m. at 1133 Westchester Avenue, White Plains, NY 10604-3543. The Company s 2009 Proxy Statement, 2008 Annual Report on Form 10-K and Annual Report to Shareholders will be available online at https://www.proxydocs.com/itt**

By order of the Board of Directors,

Kathleen S. Stolar
Vice President and Secretary

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## 2009 Proxy Statement

**Why did I receive these proxy materials?** Beginning March 27, 2009, this Proxy Statement is being provided to shareholders who were shareholders as of the March 16, 2009 record date, as part of the Board of Directors solicitation of proxies for ITT s 2009 Annual Meeting and any postponements or adjournments thereof. This Proxy Statement and ITT s 2008 Annual Report to Shareholders and Annual Report on Form 10-K (which have been furnished to shareholders eligible to vote at the 2009 Annual Meeting) contains information that the Board of Directors believes offers an informed view of the Company and meets the regulations of the Securities and Exchange Commission (the SEC ) for proxy solicitations.

**Who is entitled to vote?** You can vote if you owned shares of the Company s common stock as of the March 16, 2009 record date.

**What items of business will I be voting on?** You are voting on the following items of business, which are described on pages 7 to 15:

1. Election of ten members of the Board of Directors

2. Ratification of the appointment of Deloitte & Touche LLP as ITT s Independent Registered Public Accounting Firm for 2009

3. Such other matters, including a shareholder proposal, if properly presented at the meeting

## Information about Voting

**How do I vote?** You can either vote in person at the Annual Meeting or by proxy whether or not you attend the Annual Meeting.

**What are the proxy voting procedures?** If you vote by proxy, you can vote by following the voting procedures on the proxy card. You may vote:

***By the Internet,***

***By Telephone,*** if you call from the United States, or

***By Mail.***

**Why does the Board solicit proxies from shareholders?** Since it is impractical for all shareholders to attend the Annual Meeting and vote in person, the Board of Directors recommends that you appoint the three people named on the accompanying proxy card to act as your proxies at the 2009 Annual Meeting.

**How do the proxies vote?** The proxies vote your shares in accordance with your voting instructions. If you appoint the proxies but do not provide voting instructions, they will vote as recommended by the Board of Directors. If any other matters not described in this Proxy Statement are properly brought before the meeting for a vote, the proxies will use their discretion in deciding how to vote on those matters.

**How many votes do I have?** You have one vote for every share of ITT common stock that you own.

**What if I change my mind?** You can revoke your proxy at any time before it is exercised by mailing a new proxy card with a later date or casting a new vote by the Internet or telephone. You can also send a written revocation to the Secretary at the address listed on the first page of the Proxy Statement. If you come to the Annual Meeting, you can ask that the proxy you submitted earlier not be used.

**What happens if I return my proxy without indicating how I want my shares voted?** If you return the proxy without specifying how you want your shares voted, you are giving discretionary authority to the proxies to vote your shares in accordance with the recommendations of the Board of Directors, which are described on pages 7 to 15. If any other matters are properly presented for consideration at the 2009 Annual Meeting, the persons named as proxies will have discretion to vote on these matters according to their best judgment to the same extent as the person delivering the proxy would be entitled to vote.

There are three formal items scheduled to be voted upon at the Annual Meeting as described on page 1. As of the date of this Proxy Statement, the Board of Directors is not aware of any business other than as described in this Proxy Statement that will be presented for a vote at the 2009 Annual Meeting.

**If I don t return the proxy card for vote at the 2009 Annual Meeting, what happens to my vote?** If your shares are held by a broker, bank or other owner of record, your shares can be voted by the broker for agenda items one and two, election of directors and ratification of Deloitte & Touche LLP as the Company s Independent Registered Public Accounting Firm ( Deloitte ). Your broker does not have discretion to vote your shares held in street name on the other proposed agenda item. If you provide no instructions on how to vote on the remaining agenda item, the vote will be a broker non-vote which means that the broker cannot vote shares with respect to that agenda item. Under Indiana law, the law of the state where the Company is incorporated, broker non-votes and abstentions are counted to determine whether there is a quorum present.

**How many votes are required to elect Directors or approve a proposal? How many votes are required for an agenda item to pass?** The Restated Articles of Incorporation of ITT Corporation authorize the Company s By-laws to provide for majority voting for Directors in uncontested elections, and to further provide in such By-laws that in uncontested elections, any Director nominee who receives less than majority of the votes cast shall not be elected. The Company s By-laws provide for majority voting in uncontested elections. The By-laws provide that in uncontested elections, any Director nominee who fails to be elected by a majority, but who also is a Director at the time, shall promptly provide a written resignation, as a holdover Director, to the Chair of the Nominating and Governance Committee. The Nominating and Governance Committee shall promptly consider the resignation and all relevant facts and circumstances concerning any vote, including whether the cause of the vote may be cured, and the best interests of the Company and its shareholders. The independent Directors of the Board will act on the Nominating and Governance Committee s recommendation at its next regularly scheduled Board Meeting or within 90 days after certification of the shareholder vote, whichever is earlier, and the Board will promptly publicly disclose its decision and the reasons for its decision. This means that in an uncontested election, each of the ten director candidates must receive a majority of votes cast to be elected as a Director of ITT.

Under Indiana law, all other proposed agenda items require that the votes cast in favor of the proposal exceed the votes cast against the proposal. Accordingly, neither abstentions nor broker non-votes have any effect on the votes required under Indiana law.

**How many shares of ITT stock are outstanding?** As of the March 16, 2009 record date, 181,714,471 shares of ITT common stock were outstanding.

**How many holders of ITT outstanding shares must be present to hold the Annual Meeting?** In order to conduct business at the Annual Meeting it is necessary to have a quorum. To have a quorum, a majority of outstanding ITT shares of common stock on the record date must be present in person or by proxy.

**How do I vote?** You may vote for or withhold your vote with respect to any Director standing for reelection. With respect to other agenda items, you may vote for, against or abstain from voting.

**What is the difference between a beneficial owner and a registered owner?** If shares you own are held in an ITT savings plan for salaried or hourly employees, a stock brokerage account, bank or by another holder of record you are considered the beneficial owner because someone

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else holds the shares on your behalf. If the shares you own are held in a Smith Barney account for restricted shares or registered in your name directly with the Bank of New York Mellon our transfer agent, you are the registered owner and the shareholder of record.

**How do I vote if I am a participant in ITT s savings plans for salaried or hourly employees?** If you participate in any of the ITT savings plans for salaried or hourly employees, your plan trustee will vote the ITT shares credited to your savings plan account in accordance with your voting instructions, except as otherwise provided in accordance with the Employee Retirement Income Security Act of 1974 ( ERISA ), as amended. The trustee votes the shares on your behalf because you are the beneficial owner, not the shareholder of record, of the savings plan shares. The trustee votes the savings plan shares for which no voting instructions are received ( Undirected Shares ) in the same proportion as the shares for which the trustee receives voting instructions, except as otherwise provided in accordance with ERISA. Under the savings plans, participants are named fiduciaries to the extent of their authority to direct the voting of ITT shares credited to their savings plan accounts and their proportionate share of Undirected Shares. By submitting voting instructions by telephone, the Internet or by signing and returning the voting instruction card, you direct the trustee of the savings plans to vote these shares, in person or by proxy at the Annual Meeting. ITT Salaried Plan participants should mail their confidential voting instruction card to Broadridge Financial Solutions, Inc. ( Broadridge ), acting as tabulation agent, or vote by telephone or Internet. Instructions must be received by Broadridge no later than 11:59 p.m. Eastern Time the day before the Annual Meeting.

**I participate in the ITT savings plan for salaried employees and am a shareholder of record of shares of ITT common stock. How many proxy cards will I receive?** You will receive only one proxy card. Your savings plan shares and any shares you own as the shareholder of record, including ownership through the ITT Direct Purchase, Sale and Dividend Reinvestment Plan, will be set out separately on the proxy card.

**How many shares are held by participants in the ITT employee savings plans?** As of March 16, 2009, the record date, Wells Fargo Institutional Trust Services, as the trustee for the employee salaried savings plan, held 9,927,867 shares of ITT common stock (approximately 5.46% of the outstanding shares) and The Northern Trust Company, as the trustee for the hourly employees savings plans, held 581,986 shares of ITT common stock (approximately .032% of the outstanding shares).

**Who counts the votes? Is my vote confidential?** Representatives of Broadridge count the votes. Representatives of IVS Associates, Inc. will act as Inspectors of Election for the 2009 Annual Meeting. The Inspectors of Election monitor the voting and certify whether the votes of shareholders are kept in confidence in compliance with ITT s confidential voting policy.

**Who pays for the proxy solicitation cost?** ITT pays the cost of soliciting proxies from registered owners. ITT has appointed Georgeson & Company to help with the solicitation effort. ITT will pay Georgeson & Company a fee of $12,500 to assist with the solicitation and reimburse brokers, nominees, custodians and other fiduciaries for their costs in sending proxy materials to beneficial owners.

**Who solicits proxies?** Directors, officers or other regular employees of ITT may solicit proxies from shareholders in person or by telephone, facsimile transmission or other electronic communication.

**How does a shareholder submit a proposal for the 2010 Annual Meeting?** Rule 14a-8 of the Securities Exchange Act of 1934, or the Exchange Act, establishes the eligibility requirements and the procedures that must be followed for a shareholder proposal to be included in a public company s proxy materials. Under the rule, if a shareholder wants to include a proposal in ITT s proxy materials for its next Annual Meeting, the proposal must be received by ITT at its principal executive offices on or before November 27, 2009 and comply with eligibility requirements and

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procedures. An ITT shareholder who wants to present a matter for action at ITT s next Annual Meeting, but chooses not to do so under Exchange Act Rule 14a-8, must deliver to ITT, at its principal executive offices, on or before November 27, 2009 a written notice to that effect. In either case, as well as for shareholder nominations for Directors, the shareholder must also comply with the requirements in the Company s By-laws with respect to a shareholder properly bringing business before the Annual Meeting. (You can request a copy of the By-laws from the Secretary of ITT.)

**Can a shareholder nominate Director Candidates?** The Company s By-laws permit shareholders to nominate Directors at the Annual Meeting. To make a Director nomination at the 2010 Annual Meeting, you must submit a notice with the name of the candidate on or before November 27, 2009 to the Secretary of ITT. The nomination and notice must meet all other qualifications and requirements of the Company s Governance Principles, By-laws and Regulation 14A of the Exchange Act. The nominee will be evaluated by the Nominating and Governance Committee of the Board using the same standards as it uses for all Director nominees. These standards are discussed in further detail below at pages 19 to 20 under Information about the Board of Directors-Director Selection and Composition. No one may be nominated for election as a Director after he or she has reached 72 years of age. (You can request a copy of the nomination requirements from the Secretary of ITT.)

## Stock Ownership Information

The Board of Directors share ownership guidelines currently provide for share ownership levels at five times the annual retainer amount. Non-Management Directors receive a portion of their retainer in restricted stock or restricted stock units, which are paid in shares when the restricted stock units vest. Non-Management Directors are encouraged to hold such shares until his or her total share ownership meets or exceeds the ownership guidelines.

Share ownership guidelines for corporate officers, first approved by ITT s Board of Directors during 2001, are regularly reviewed. The guidelines specify the desired levels of Company stock ownership and encourage a set of behaviors for each officer to reach the guideline levels. The approved guidelines require share ownership expressed as a multiple of base salary for all corporate officers.

Specifically the guidelines apply as follows: chief executive officer at five times base salary; chief financial officer at three times annual base salary; senior vice presidents and group presidents at two times annual base salary; and all other corporate vice presidents at one times annual base salary. In achieving these ownership levels, shares owned outright, Company restricted stock and restricted stock units, shares held in the Company s dividend reinvestment plan, shares owned in the ITT Salaried Investment and Savings Plan, and phantom shares held in a fund that tracks an index of the Company s stock in the deferred compensation plan are considered.

To attain the ownership levels set forth in the guidelines it is expected that any restricted shares that become unrestricted will be held, and that all shares acquired through exercise of stock options will be held, except, in all cases, to the extent necessary to meet tax obligations.

Compliance with the guidelines is monitored periodically and, as of January 31, 2009, the share ownership levels have been substantially met for most Non-Management Directors and Company officers. Non-Management Directors and Company officers are afforded a reasonable period of time to meet the guidelines. The Company has taken the current world financial crisis, individual tenure, and Non-Management and corporate officer share ownership levels prior to the crisis into account in determining compliance with the guidelines.

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**Share Ownership Guideline Summary**

| | |
|---|---|
| Non-Management Directors | 5 X Annual Retainer Amount |
| CEO | 5 X Annual Base Salary |
| CFO | 3 X Annual Base Salary |
| Senior Vice Presidents | 2 X Annual Base Salary |
| Vice Presidents | 1 X Annual Base Salary |

The following table shows, as of January 31, 2009, the beneficial ownership of ITT common stock and options exercisable within 60 days by each Director, by each of the executive officers named in the Summary Compensation Table at page 55, and by all Directors and executive officers as a group. In addition, with respect to Mr. Loranger and Non-Management Directors, we have provided information about ownership of restricted stock units that provide economic linkage to ITT common stock but do not represent actual beneficial ownership of shares.

**Stock Ownership of Directors and Executive Officers**

| | | Amount and Nature of Beneficial Ownership | | | | |
|---|---|---|---|---|---|---|
| **Name of Beneficial Owner** | **Title of Class ITT Common Stock** | **Total Shares Beneficially Owned** | **ITT Common Stock Shares Owned** | **Options(1)** | **Stock Units** | **Percentage of Class** |
| Steven R. Loranger(2)(3) | Common Stock | 755,915 | 133,464 | 494,400 | 173,051 | 0.416% |
| Curtis J. Crawford | Common Stock | 48,879 | 31,098 | 16,426 | 1,355 | 0.027% |
| Christina A. Gold | Common Stock | 38,938 | 21,157 | 16,426 | 1,355 | 0.021% |
| Ralph F. Hake | Common Stock | 25,898 | 11,677 | 12,866 | 1,355 | 0.014% |
| John J. Hamre | Common Stock | 35,031 | 17,250 | 16,426 | 1,355 | 0.019% |
| Paul J. Kern(4) | Common Stock | 1,016 | | | 1,016 | 0.001% |
| Frank T. MacInnis | Common Stock | 32,450 | 14,669 | 16,426 | 1,355 | 0.018% |
| Surya N. Mohapatra(5) | Common Stock | 4,910 | 2,342 | 1,213 | 1,355 | 0.003% |
| Linda S. Sanford | Common Stock | 39,851 | 22,070 | 16,426 | 1,355 | 0.022% |
| Markos I. Tambakeras | Common Stock | 31,659 | 13,878 | 16,426 | 1,355 | 0.017% |
| Denise L. Ramos | Common Stock | 24,088 | 24,088 | | | 0.013% |

| | | | | | | |
|---|---|---|---|---|---|---|
| Nicholas P. Hill | Common Stock | 67,466 | 14,924 | 52,542 | | 0.037% |
| Vincent A. Maffeo | Common Stock | 91,310 | 44,752 | 46,558 | | 0.050% |
| Gretchen W. McClain | Common Stock | 79,024 | 26,862 | 52,162 | | 0.043% |
| **All Directors and Executive Officers as a Group** | Common Stock | 1,732,730(6) | 478,303 | 1,069,520 | 184,907 | 0.953%(6) |

(1) More detail on outstanding option awards is provided in the 2008 Outstanding Equity Awards at Fiscal Year-End table at page 65. Ms. Ramos outstanding options, reported on page 65, are not exercisable within sixty days. Dr. Mohapatra s and General Kern s outstanding options, reported on page 29, are not exercisable within sixty days.

(2) On June 28, 2004, Mr. Loranger received an award of 250,000 Restricted Stock Units ( RSUs ) under the ITT Corporation 2003 Equity Incentive Plan (the 2003 Plan ), as

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amended and restated, in connection with his employment agreement. One-third of the units vested on June 28, 2007, one-third of the units vested on June 28, 2008 and the remaining one-third will vest on June 28, 2010. One-half of the vesting RSUs settle upon the vesting date and one-half of the vesting RSUs settle within ten days of Mr. Loranger s termination of employment. On June 28, 2007, 85,342 restricted stock units vested and one-half of the vested restricted stock units settled on the vesting date and one-half will settle within ten days of Mr. Loranger s termination of employment. On June 30, 2008, 86,265 vested and one-half of the vested restricted stock units settled on the vesting date and one-half will settle within ten days of Mr. Loranger s termination of employment. During the restriction period, Mr. Loranger may not vote the shares but is credited for RSU dividends.

(3) Mr. Loranger received credit for 2,401 restricted stock units as dividends during 2008.

(4) General Paul J. Kern was elected a Non-Management Director of the Company, effective August 7, 2008 and was awarded 1,016 shares of restricted stock units on that date.

(5) Dr. Mohapatra was elected a Non-Management Director of the Company, effective February 14, 2008. On February 15, 2008, Dr. Mohapatra was awarded 342 shares of restricted stock.

(6) Total shares beneficially owned include restricted stock units. Restricted stock units are payable to Mr. Loranger and the Non-Management Directors in shares when the restrictions lapse. Percentage of class includes restricted stock units.

The number of shares beneficially owned by each Non-Management Director or executive officer has been determined under the rules of the SEC, which provide that beneficial ownership includes any shares as to which a person has sole or shared voting or dispositive power, and any shares which the person would have the right to acquire beneficial ownership of within 60 days through the exercise of any stock option or other right. Unless otherwise indicated, each Non-Management Director or executive officer has sole dispositive and voting power, or shares those powers with his or her spouse.

As of January 31, 2009, all Non-Management Directors and executive officers as a group owned 0.953% of the shares deemed to be outstanding. No individual Non-Management Director or executive officer owned in excess of one percent of the shares deemed to be outstanding.

**Schedule 13G Filings**

Set forth below is information reported to the SEC on the most recently filed Schedule 13G by the following persons who owned more than 5% of ITT outstanding common stock. This information does not include holdings by the Trustee with respect to individual participants in the ITT Salaried Investment and Savings Plan.

| Name and address of beneficial owner | Amount and nature of beneficial ownership | Percent of Class |
|---|---|---|
| **Barrow, Hanley, Mewhinney & Strauss, Inc.(1)**<br>2200 Ross Avenue, 31st Floor<br>Dallas, TX 75201-2761 | 13,763,155 | 7.58% |
| **Vanguard Windsor Funds-Vanguard Windsor II Fund(2)** | 10,267,500 | 5.65% |

100 Vanguard Blvd.
Malvern, PA 10355

(1) As reported on Schedule 13G/A dated February 11, 2009, Barrow, Hanley, Mewhinney & Strauss, Inc. has sole voting power with respect to 1,051,155 shares, shared voting power with respect to 12,712,000 shares, and sole dispositive power with respect to 13,763,155 shares.

(2) As reported on Schedule 13G/A dated February 13, 2009, Vanguard Windsor Funds   Vanguard Windsor II Fund, has sole voting power with respect to 10,267,500 shares.

**Section 16(a) Beneficial Ownership Reporting Compliance**

Section 16(a) of the Exchange Act requires that the Company s executive officers and directors, and any persons beneficially owning more than 10% of a registered class of the Company s equity securities, file reports of ownership and changes in ownership with the SEC within specified time periods. To the Company s knowledge, based upon a review of the copies of the reports furnished to the Company and written representations that no other reports were required, all filing requirements were satisfied in a timely manner for the year ended December 31, 2008.

**Proposals to be voted on at the 2009 Annual Meeting**

**1. Election of Directors**

The Board of Directors has nominated ten individuals for election as Directors at the 2009 Annual Meeting. Each of the nominees is currently serving as a Director of ITT and has agreed to continue to serve if elected until his or her retirement, resignation or death. If unforeseen circumstances arise before the 2009 Annual Meeting and a nominee becomes unable to serve, the Board of Directors could reduce the size of the Board or nominate another candidate for election. If the Board nominates another candidate, the proxies could use their discretion to vote for that nominee. Each Director elected at the 2009 Annual Meeting will be elected to serve as a Director until ITT s next Annual Meeting.

**The Board of Directors recommends that you vote FOR the election of each of the following ten nominees:**

**Steven R. Loranger**
Chairman, President and Chief Executive Officer,
ITT Corporation

Mr. Loranger, 57, was appointed President and Chief Executive Officer and elected a Director of ITT on June 28, 2004. He was elected Chairman of the Board of Directors on December 7, 2004. Mr. Loranger previously served as Executive Vice President and Chief Operating Officer of Textron, Inc. from 2002 to 2004, overseeing Textron s manufacturing businesses, including aircraft and defense, automotive, industrial products and components. From 1981 to 2002, Mr. Loranger held executive positions at Honeywell International Inc. and its predecessor company, AlliedSignal, Inc., including serving as President and Chief Executive Officer of its Engines, Systems and Services businesses. Mr. Loranger is a member of the Business Roundtable, serves on the boards of the National Air and Space Museum and the Congressional Medal of Honor Foundation and is on the Executive Committee of the Aerospace Industries Association Board of Governors. Mr. Loranger received bachelors and masters degrees in science from the University of Colorado. Mr. Loranger is also a director of the FedEx Corporation.

Mr. Loranger has been a Director of ITT since 2004.

**Curtis J. Crawford, Ph.D.**
President and Chief Executive Officer, XCEO, Inc., a
leadership and corporate governance consulting firm

Dr. Crawford, 61, is President and Chief Executive Officer of XCEO, Inc. From April 1, 2002 to March 31, 2003 he served as President and Chief Executive Officer of Onix Microsystems, a private photonics technology company. He was Chairman of the Board of Directors of ON Semiconductor Corporation from September 1999 until April 1, 2002. Previously, he was President and Chief Executive Officer of ZiLOG, Inc. from 1998 to 2001 and its Chairman from 1999 to 2001. Dr. Crawford is a Director of E.I. DuPont de Nemours and Company, ON Semiconductor Corporation, and is a member of the Board of Trustees of DePaul University. He received a B.A. degree in business administration and computer science and an M.A. degree from Governors State University, an M.B.A. from DePaul University and a Ph.D. from Capella University. Governors State University awarded him an honorary doctorate in 1996 and he received an honorary doctorate degree from DePaul University in 1999. Dr. Crawford is the author of two books on leadership and corporate governance.

Dr. Crawford has been a Director of ITT since 1996.

**Christina A. Gold**
President, Chief Executive Officer and
Director, The Western Union Company, Inc., a
global leader in money transfer and financial services

Mrs. Gold, 61, has been President and Chief Executive Officer of The Western Union Company, a leading company in global money transfer, since September 2006. From May 2002 to September 2006, Mrs. Gold was President of Western Union Financial Services, Inc. and Senior Executive Vice President of Western Union s parent company, First Data Corporation. From October 1999 to May 2002, she was Chairman, President and Chief Executive Officer of Excel Communications, Inc. Mrs. Gold served as President and Chief Executive Officer of The Beaconsfield Group from March 1998 to October 1999. From 1997 to 1998, Mrs. Gold was Executive Vice President of Global Development of Avon Products, Inc., and from 1993 to 1997, she was President of Avon North America. Mrs. Gold is also a director of The Western Union Company and New York Life Insurance. Mrs. Gold is a graduate of Carleton University, Ottawa, Canada.

Mrs. Gold has been a Director of ITT since 1997.

**Ralph F. Hake**
Former Chairman and Chief Executive,
Maytag Corporation,
a home and commercial appliance company

Mr. Hake, 60, was Chairman and Chief Executive of Maytag Corporation from June of 2001 to March of 2006. Previously, he was Executive Vice President and Chief Financial Officer for Fluor Corporation, an engineering and construction firm. From 1987 to 1999, Mr. Hake served in various executive capacities at Whirlpool Corporation, including Chief Financial Officer and Senior Executive Vice President for global operations. He is also a director of Owens-Corning Corporation. Mr. Hake is a 1971 business and economics graduate of the University of Cincinnati and holds an M.B.A. from the University of Chicago.

Mr. Hake has been a Director of ITT since 2002.

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**John J. Hamre, Ph.D.**
President and Chief Executive Officer, Center for Strategic & International Studies ( CSIS ), a public policy research institution dedicated to strategic, bipartisan global analysis and policy impact

Dr. Hamre, 58, was elected President and Chief Executive Officer of CSIS in April of 2000. Prior to joining CSIS, he served as U.S. Deputy Secretary of Defense from 1997 to 2000 and Under Secretary of Defense (Comptroller) from 1993 to 1997. Dr. Hamre is a Director of MITRE Corporation, and SAIC, Inc. He received a B.A. degree, with highest distinction from Augustana College in Sioux Falls, South Dakota, was a Rockefeller Fellow at Harvard Divinity School and was awarded a Ph.D., with distinction, from the School of Advanced International Studies, Johns Hopkins University, in 1978.

Dr. Hamre has been a Director of ITT since 2000.

**Paul J. Kern**
President and Chief Operating Officer, AM General LLC, a world leader in the design, engineering, production and technical and parts support of military and special purpose vehicles.

General Kern, 63, has served as President and Chief Operating Officer of AM General LLC since August 1, 2008. He is also Senior Counselor to The Cohen Group. In November 2004, General Kern retired from the United States Army as Commanding General, Army Materiel Command (AMC). General Kern graduated from the U.S. Military Academy at West Point. He holds Masters Degrees in both Civil and Mechanical Engineering from the University of Michigan, and he was a Senior Security Fellow at the John F. Kennedy School at Harvard University. General Kern serves on the Board of Directors of iRobot Corporation, CoVant Technologies LLC, and AT Solutions, a subsidiary of CoVant Technologies. General Kern, formerly a Director of the EDO Corporation, was identified as a potential Director in connection with the acquisition of the EDO Corporation by the Company and was also identified by a third-party search firm.

General Kern has been a Director of ITT Corporation since August 2008.

**Frank T. MacInnis**
Chairman and Chief Executive Officer, EMCOR Group, Inc., one of the world s largest providers of electrical and mechanical construction services, energy infrastructure and facilities services.

Mr. MacInnis, 62, has been Chairman of the Board and Chief Executive Officer of EMCOR Group, Inc. since April 1994. He was also President of EMCOR from April 1994 to April 1997. Mr. MacInnis is also a Director of The Williams Companies, Inc., The Greater New York Chapter of the March of Dimes and ComNet Communications, LLC. Mr. MacInnis received an undergraduate degree from The University of Alberta and is a graduate of The University of Alberta Law School, Alberta, Canada.

Mr. MacInnis has been a Director of ITT since 2001.

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**Surya N. Mohapatra, Ph.D.**
Chairman of the Board, President and Chief Executive Officer of Quest Diagnostics Incorporated, the nation s leading provider of diagnostic testing, information and services.

Dr. Mohapatra, 59, was appointed President and Chief Operating Officer of Quest Diagnostics Incorporated in June 1999, a Director in 2002, its Chief Executive Officer in May 2004, and Chairman of the Board in December 2004. Prior to joining Quest Diagnostics Incorporated in February 1999 as Senior Vice President and Chief Operating Officer, Dr. Mohapatra was Senior Vice President of Picker International, a worldwide leader in advanced medical imaging technologies, where he served in various executive positions during his 18-year tenure. Dr. Mohapatra earned a Bachelor of Science degree in electrical engineering from Sambalpur University in India. Additionally, he holds a Master of Science in medical electronics from the University of Salford, England, as well as a doctorate in medical physics from the University of London and The Royal College of Surgeons of England.

Dr. Mohapatra has been a director of ITT since February 2008.

**Linda S. Sanford**
Senior Vice President, Enterprise On Demand Transformation, International Business Machines Corporation ( IBM ), an information technology company

Ms. Sanford, 56, was named Senior Vice President, Enterprise on Demand Transformation, IBM in January 2003. Previously, she was Senior Vice President and Group Executive, IBM Storage Systems Group, responsible for development of IBM s Enterprise Storage Server and other storage-related hardware and software. She also has held positions as General Manager, IBM Global Industries and General Manager of IBM s S/390 Division. Ms. Sanford is a member of the Women in Technology International Hall of Fame and the National Academy of Engineers. She is on the Board of Trustees of St. John s University and Rensselaer Polytechnic Institute, serves on the Board of Directors of Partnership for New York City and is a member of the Board of Directors for the Business Council of New York State, Inc. Ms. Sanford is a graduate of St. John s University and earned an M.S. degree in operations research from Rensselaer Polytechnic Institute.

Ms. Sanford has been a Director of ITT since 1998.

**Markos I. Tambakeras**
Former Chairman, President and Chief Executive Officer, Kennametal, Inc., a premier global tooling solutions, engineered components and advanced materials supplier to the automotive, aerospace, energy, mining, construction and other industries

Mr. Tambakeras, 58, served as Chairman of the Board of Directors, Kennametal, Inc. from July 1, 2002 until December 31, 2006. He was also President and Chief Executive Officer of Kennametal from July 1999 through December 31, 2005. From 1997 to June 1999, Mr. Tambakeras served as President, Industrial Controls Business, for Honeywell Incorporated. Mr. Tambakeras also serves on the Board of Parker Hannifin Corporation and the Newport Group. He is a trustee of Arizona State University. Mr. Tambakeras received a B.Sc. degree from the University of Witwatersrand, Johannesburg, South Africa and an M.B.A. from Loyola Marymount University, Los Angeles, CA.

Mr. Tambakeras has been a Director of ITT since 2001.

## 2. Ratification of Appointment of the Independent Registered Public Accounting Firm

Subject to the shareholders ratification, the Board of Directors has appointed Deloitte & Touche LLP ( Deloitte ) as ITT s independent registered public accounting firm for 2009. Deloitte is registered as a registered public accounting firm by the Public Company Accounting Oversight Board ( PCAOB ). Representatives of Deloitte attended all regularly scheduled meetings of the Audit Committee during 2008. Annually the Audit Committee reviews and considers Deloitte s performance on the Company s Audit. Performance factors reviewed included Deloitte s:

- independence
- experience
- technical capabilities
- client service assessment
- responsiveness
- financial strength
- industry insight
- PCAOB s 2006 report of selected Deloitte audits
- leadership
- the nature of non-audit services provided by Deloitte
- management structure
- peer review program
- commitment to quality report
- appropriateness of fees charged
- compliance and ethics programs

The Audit Committee also reviewed the terms and conditions of Deloitte s engagement letter including an agreement by the Company to submit disputes between Deloitte and the Company to a dispute resolution process and to limit awards based on punitive or exemplary damages under the dispute resolution procedures.

The Audit Committee discussed these considerations, fees and services with Deloitte and Company management. The Audit Committee also determined that any non-audit services (services other than services described in the annual audit services engagement) provided by Deloitte were permitted under the rules and regulations concerning auditor independence promulgated by the SEC to implement the Sarbanes-Oxley Act of 2002, and rules promulgated by the PCAOB in Rule 3526T. Representatives of Deloitte will be present at the 2009 Annual Meeting to answer questions. Representatives of Deloitte also will have the opportunity to make a statement if they desire to do so.

### Independent Registered Public Accounting Firm Fees

Aggregate fees billed to the Company for the fiscal years ended December 31, 2008 and 2007 represent fees billed by the member firms of Deloitte Touche Tohmatsu, and their respective affiliates.

| | Fiscal Year Ended (in thousands) | |
|---|---|---|
| | **2008** | **2007** |
| Audit Fees(1) | $ 10,835 | $ 8,643 |
| Audit-Related Fees(2) | 1,034 | 951 |
| Tax Fees(3) | | |
| Tax Compliance Services | 506 | 428 |

| | | |
|---|---|---|
| Tax Planning Services | 505 | 230 |
| Total Tax Services | 1,011 | 658 |
| Total | $ 12,880 | $ 10,252 |

(1) Fees for audit services billed in 2008 and 2007 consisted of:

Audit of the Company s annual financial statements and internal control over financial reporting;

Reviews of the Company s quarterly financial statements;

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Statutory and regulatory audits, consents and other services related to SEC matters; and

Financial accounting and reporting consultations.

(2) Fees for audit-related services billed in 2008 and 2007 consisted of:

Employee benefit plan audits;

Audits and other attest work related to acquisitions and dispositions;

Internal control advisory services; and

Other miscellaneous attest services.

(3) Fees for tax services billed in 2008 and 2007 consisted of tax compliance and tax planning and advice:

Tax compliance services are services rendered, based upon facts already in existence or transactions that have already occurred, to document, compute, and obtain government approval for amounts to be included in tax filings consisting primarily of:

i. Federal, foreign, state and local income tax return assistance; and

ii. Internal Revenue Code and foreign tax code technical consultations.

Tax planning services are services and advice rendered with respect to proposed transactions or services that alter the structure of a transaction to obtain an anticipated tax result. Such services consisted primarily of:

i. Transfer pricing consultations; and

ii. Tax advice related to intra-group restructuring.

| | 2008 | 2007 |
|---|---|---|
| Ratio of Tax Planning and Advice to Total Fees | 3.9% | 2.2% |

**Pre-Approval of Audit and Non-Audit Services**

The Audit Committee pre-approves audit services provided by Deloitte. The Audit Committee has also adopted a policy on pre-approval of non-audit services provided by Deloitte and certain non-audit services provided by outside internal audit service providers. The purpose of the policy is to identify thresholds for services, project amounts and circumstances where Deloitte and any outside internal audit service providers may perform non-audit services. A second level of review and approval by the Audit Committee is required when such non-audit services, project amounts, or circumstances exceed the specified amounts.

The Audit Committee has determined that, where practical, all non-audit services shall first be placed for competitive bid prior to selection of a service provider. Management may select the party deemed best suited for the particular engagement, which may or may not be Deloitte. Providers other than Deloitte shall be preferred in the selection process for non-audit service related work. The policy and its implementation are reviewed and reaffirmed on a regular basis to assure conformance with applicable rules.

The Audit Committee has approved specific categories of audit, audit-related and tax services incremental to the normal auditing function, which Deloitte may provide without further Audit Committee pre-approval. These categories include among others, the following:

1. Due diligence, closing balance sheet audit services, purchase price dispute support and other services related to mergers, acquisitions and divestitures;

2. Employee benefit advisory services, independent audits and preparation of tax returns for the Company s defined contribution, defined benefit and health and welfare benefit plans, preparation of the associated tax returns or other employee benefit advisory services;

3. Tax compliance and certain tax planning and advice work; and

4. Accounting consultations and support related to generally accepted accounting principles ( GAAP ) or government contract compliance.

The Audit Committee has also approved specific categories of audit-related services, including assessment and review of internal controls and effectiveness of those controls, which outside internal audit service providers may provide without further approval.

If fees for any pre-approved non-audit services provided by either Deloitte or any internal audit service provider exceed a pre-determined threshold during any calendar year, any additional proposed non-audit services provided by that service provider must be submitted for second-level approval by the Audit Committee. Other audit, audit-related and tax services which have not been pre-approved are subject to specific prior approval. The Audit Committee reviews the fees paid or committed to Deloitte on at least a quarterly basis.

The Company may not engage Deloitte to provide the services described below:

1. Bookkeeping or other services related to the accounting records or financial statements of the Company;

2. Financial information systems design and implementation;

3. Appraisal or valuation services, fairness opinions, or contribution-in-kind reports;

4. Actuarial services;

5. Internal auditing services;

6. Management functions or human resources services;

7. Broker-dealer, investment adviser or investment banking services; or

8. Legal services and other expert services unrelated to the audit.

Employees of Deloitte who are senior manager level or above, including lead or concurring partners and who have been involved with the Company in the independent audit, shall not be employed by the Company in any capacity for a period of five years after the termination of their activities on the Company account.

**The Board of Directors recommends you vote FOR ratification of appointment of the Company s Independent Registered Public Accounting Firm.**

## 3. Shareholder Proposal

### Report on Military Sales to Foreign Governments

Several shareholders have advised the Company that they intend to present the following resolution at the Annual Meeting. In accordance with applicable proxy regulations, the proposed resolution and supporting statement, for which the Board of Directors and the Company accept no responsibility, are set forth below. Approval of this proposal would require the affirmative vote of a majority of the outstanding shares of ITT stock present in person or by proxy and entitled to vote at the Annual Meeting. Identical shareholder proposals were received from each of the Mercy Investment Program and the Dominican Sisters of Hope, Corporate Social Responsibility, each located at 205 Avenue C, Apt. 10E New York, NY 10009; the Presbyterian Church (USA), 100 Witherspoon Street Louisville, KY 40202-1396; and the Domestic and Foreign Missionary Society of the Episcopal Church, 815 Second Avenue New York, NY 10017-4503 (collectively, the Proponents ), which shareholders hold 100, 1,800, 54, and 11,500 shares respectively.

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**2009 ITT Industries Resolution on Foreign Military Sales**

WHEREAS the United States exports weapons and related military services through foreign military sales (government-to-government), direct commercial weapons sales (U.S. companies to foreign buyers), equipment leases, transfers of excess defense articles and emergency drawdowns of weaponry.

The United States government has requested $4.54 billion in Foreign Military Financing for Fiscal Year 2008 including $3.9 billion for the Near East region (the recent 10-year agreement to increase military aid to Israel and proposed sales to Saudi Arabia may increase that amount).

In a number of recent United States combat engagements (e.g., the first Gulf War, Somalia, Afghanistan and Iraq), our troops faced adversaries who had previously received U.S. weapons or military technology. In the United States government s Fiscal Year 2007, ITT Industries was ranked the 14th largest Department of Defense contractor with $2.748 billion in contracts. *(Government Executive,* August 15, 2008) On March 27, 2007, our company announced that it would pay a $50 million fine and plead guilty to two violations of the International Traffic in Arms Regulations (ITAR), one for improper handling of sensitive documents, and one for making misleading statements to the State Department s Directorate of Defense Trade Controls (DDTC).

**RESOLVED:** Shareholders request that the Board of Directors provide, within six months of the 2009 annual meeting, a comprehensive report, at reasonable cost and omitting proprietary and classified information, of ITT Industries foreign sales of military and weapons-related products and services.

**SUPPORTING STATEMENT**

We believe with the American Red Cross that the greater the availability of arms, the greater the violations of human rights and international humanitarian law.

Global security is security of all people. Weapons sold to one country at a certain time subsequently can become a threat to our own security, as we have seen several times in our recent history. We also believe that this report will assist shareholders in assessing the effectiveness of newly instituted company procedures to prevent further violations of ITAR. Therefore, we believe it is reasonable that the report include:

1. Processes used to determine and promote foreign sales;

2. Criteria for choosing countries with which to do business;

3. A description of procedures used to negotiate foreign arms sales, government-to government and direct commercial sales and the percentage of sales for each category; and

4. For the past three years, categories of military equipment or components, including dual use items, exported with as much statistical information as possible; categories of contracts for servicing/maintaining equipment; offset agreements for the past three years; and licensing and/or co- production with foreign governments.

We urge you to vote in favor of this reasonable resolution.

**Management s Response**

The proposal requests that the Company provide, within six months of the 2009 annual meeting, a comprehensive report, at reasonable cost and omitting proprietary and classified information, of the foreign sales of military and weapons-related products and services by the Company (identified by its former name). The Company believes that producing the report requested by the Proposal is unnecessary because sufficient information is publicly available. The Company s foreign military sales are a matter of public record through U.S. government-provided information or the news media. The Department of Defense (foreign military sales) and Department of State (direct

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commercial sales) provide notification of such sales to Congress and the media. Furthermore, pursuant to 15 C.F.R. Part 701, Offsets in Military Exports, under the Defense Production Act of 1950, as amended, the Company already provides offset agreement data to the Department of Commerce Bureau of Industry and Security data for its *Offsets in Defense Trade Report* (see, for example, the January 2007, 11th edition), which is publicly available and required pursuant to Section 309 of the Defense Production Act of 1950 (50 U.S.C. § 2099). Sources of publicly available information on the Company s military sales include the website of the Defense Security Cooperation Agency at www.dsca.mil, which lists public notices to Congress of proposed major foreign military sales under Section 36(b) of the Arms Export Control Act, as amended (which are also published in the Federal Register), as well as announcements of foreign military sales contracts, and the website of the Federation of American Scientists at www.fas.org, which also provides information on such public notices and other information regarding foreign military sales and direct commercial sales.

In addition, the Company s Annual Reports to Shareholders, its periodic reports on Forms 10-K and 10-Q, and its corporate website www.itt.com provide extensive information concerning the Company s military products and services. The Company s 2007-2008 Corporate Responsibility Report available through http://www.itt.com/responsibility/ contains detailed information on pages 4 and 5 about the Company s global presence with employees working in more than 55 countries and The Company s Revenue Profile on page 4 indicates that the defense business in its entirety accounts for 46% of the Company s fiscal 2007 revenue. Part I of the Company s Annual Report on Form 10-K for the fiscal year ended December 31, 2008 filed with the Commission on February 25, 2009 (the 2008 Form 10-K ) describes in detail the Company s Defense Electronics & Services segment and its sales and revenues statistics on pages 2 and 3. The defense business represented 54% of the Company 2008 sales and revenue. Note 21 to the Company s consolidated financial statements on pages 77-78 of the 2008 Form 10-K breaks down sales to Western Europe, Asia Pacific and the United States.

The Company also provides extensive information regarding the ITT Defense Electronics & Services business segment on a separate standalone website www.defense.itt.com. The website divides the Defense Electronics & Services segments into quadrants: Communications, Sensing & Surveillance, Space and Advanced Engineering Services. The quadrants have been further divided into various sub-categories covering the entire spectrum of the Defense Electronics & Services products and services. Each sub-category within a quadrant contains detailed information on the specific products sold and services offered in the sub-category. The Company believes this disclosure provides the Company s shareholders with more than adequate information concerning the Company s processes, procedures, criteria and statistics regarding foreign sales of military and weapons-related products and services.

The Company believes that the level of detail required to be compiled by the Proposal does not serve a productive purpose as the information provided would be of a specialized and technical nature. Further, such information could not accurately describe the decision making process of the management and would impinge upon their ability to manage the affairs of the Company, which is ultimately not in the interests of the Company or the shareholders themselves.

**THE BOARD OF DIRECTORS RECOMMENDS YOU VOTE AGAINST THE SHAREHOLDER PROPOSAL REQUIRING THE COMPANY TO PROVIDE A REPORT ON MILITARY SALES TO FOREIGN GOVERNMENTS.**

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## Information about the Board of Directors

**Responsibilities of the Board of Directors.** The Board of Directors sets policy for ITT and advises and counsels the chief executive officer and the executive officers who manage the Company s business and affairs. The Board of Directors is responsible for assuring that:

the Company s businesses are conducted in conformity with applicable laws and regulations;

the Company s systems of financial reporting and internal controls are adequate and properly implemented;

there is continuity in the leadership of the Company;

management develops sound business strategies;

adequate capital and managerial resources are available to implement the business strategies;

the Company s long-term strategies, significant investments in new businesses, joint ventures and partnerships and significant business acquisitions, including assessment of balance sheet impacts and other financial matters are reviewed and approved; and

the Company s operating plans and capital, research and development and engineering budgets are reviewed and approved.

**Governance Principles.** The Board of Directors has adopted principles for governance of the Board (the Corporate Governance Principles ) and charters for each of its standing committees. The Corporate Governance Principles provide, among other things, that an Independent Presiding Director shall be appointed on an annual basis (but no Non-Management Director shall serve more than three consecutive annual terms) to preside at meetings of the Board of Directors at which the Chairman is not present, including regularly scheduled private sessions of the Non-Management Directors.

The Independent Presiding Director, whose position is described more fully at Section 7c of the Board s Corporate Governance Principles, *http://www.itt.com/responsibility/governance/principles/,* is also available to address issues or concerns raised by other Non-Management Directors, senior executives or major shareholders; communicate any issues or concerns to the full Board and the Chairman, President and Chief Executive Officer; assist the Chairman, President and Chief Executive Officer in developing appropriate schedules and agendas for Board and Committee meetings, and act on behalf of the Chairman, President and Chief Executive Officer and the Board as a formal coordinating point for facilitating, canvassing, reconciling and communicating board issues, concerns and recommendations. The Board of Directors has selected Frank T. MacInnis as its Independent Presiding Director, to serve a one-year term, expiring in May 2009.

The Corporate Governance Principles further provide that Directors must be able to devote the requisite time for preparation and attendance at regularly scheduled Board and Board Committee meetings, as well as be able to participate in other matters necessary for good corporate governance. To help assure that Directors are able to fulfill their commitments to the Company, the Corporate Governance Principles provide that Directors who are chief executive officers of publicly traded companies may serve on not more than two public company boards (including the ITT Board) in addition to service on their own board and other Directors may not serve on more than four public company boards (including the ITT Board). The Corporate Governance Principles and Committee Charters are reviewed by the Board at least annually and posted on the Company s website at *http://www.itt.com/responsibility/governance/#principles-charters.* A copy of the Corporate Governance Principles will be provided, free of charge, to any shareholder upon request to the Secretary of ITT.

**Communication with the Board of Directors.** Interested parties may contact the Independent Presiding Director, all outside Directors as a group or an individual Director by submitting a letter to the desired recipient in a sealed envelope labeled Independent Presiding Director, Outside

Directors  or with the name of a specific director. This letter should be placed in a larger envelope and mailed to the Secretary, ITT Corporation, 1133 Westchester Avenue, White Plains, NY 10604, USA. The Secretary will forward the sealed envelope to the designated recipient.

**Policies for Approving Related Person Transactions.** The Company and the Board have adopted formal written policies for evaluation of potential related person transactions, as those terms are defined in the SEC s rules for executive compensation and related person disclosure, which provide for review and pre-approval of transactions which may or are expected to exceed $120,000 involving Non-Management Directors, Executive Officers, members of a Director s Immediate Family and beneficial owners of five percent or more of the Company s common stock or other securities. The Company s Related Person Transaction Policy is posted on the Company s website at: http://www.itt.com/responsibility/governance/related-party-transactions/.

The Company has also adopted the ITT Code of Corporate Conduct which applies to the Company s Chief Executive Officer, Chief Financial Officer and Principal Accounting Officer and, where applicable, to its Non-Management Directors. The Code of Corporate Conduct is also posted on the Company s website at *http://www.itt.com/responsibility/conduct/.* The Company discloses any changes or waivers from its code of ethics on its website for the Company s Chief Executive Officer, Chief Financial Officer, Principal Accounting Officer and other executive officers. A copy of the Code of Corporate Conduct will be provided, free of charge, to any shareholder upon request to the Secretary of ITT.

**Independent Directors.** The Company s By-laws require that a majority of the Directors must be independent directors. Additionally, the Company s Non-Management Directors must meet the New York Stock Exchange ( NYSE ) and the Company s Corporate Governance Principles independence standards. The Company s Corporate Governance Principles define independence. The Charters of the Audit, Compensation and Personnel, Nominating and Governance, and Strategy and Finance Committees as well as the resolution establishing the Special Litigation Committee also require all members to be independent directors.

Based on its review, the Board of Directors affirmatively determined, after considering all relevant facts and circumstances, that no Non-Management Director has a material relationship with the Company and that all Non-Management Directors, including all members of the Audit, Compensation and Personnel, Corporate Responsibility, Nominating and Governance and Strategy and Finance Committees, meet the independence standards of the Company s Corporate Governance Principles and By-laws as well as the independence definition in the current NYSE corporate governance rules for listed companies.

NYSE Independence Requirements:

(a) A Director qualifies as  independent  when the board of directors affirmatively determines that the director has no material relationship with the company, or any subsidiary in a consolidated group (either directly or as a partner, shareholder or officer of an organization that has a relationship with the company). Companies must identify which directors are independent and disclose the basis for that determination.

(b) In addition, a director is not independent if:

(i) The director is, or has been within the last three years, an employee of the listed company, or an immediate family member is, or has been within the last three years, an executive officer, of the listed company.

(ii) The director has received, or has an immediate family member who has received, during any twelve-month period within the last three years, more than $100,000 in direct compensation from the listed company, other than director and committee fees and pension or other forms of deferred compensation for prior service (provided such compensation is not contingent in any way on continued service).

(iii) (A) The director or an immediate family member is a current partner of a firm that is the company s internal or external auditor; (B) the director is a current employee of such a firm; (C) the director has an immediate family member who is a current employee of such a firm and who participates in the firm s audit, assurance or tax compliance (but not tax planning) practice; or (D) the director or an immediate family member was within the last three years (but is no longer) a partner or employee of such a firm and personally worked on the listed company s audit within that time.

(iv) The director or an immediate family member is, or has been within the last three years, employed as an executive officer of another company where any of the listed company s present executive officers at the same time serves or served on that company s compensation committee.

(v) The director is a current employee, or an immediate family member is a current executive officer, of a company that has made payments to, or received payments from, the listed company for property or services in an amount which, in any of the last three fiscal years, exceeds the greater of $1 million, or 2% of such other company s consolidated gross revenues.

In addition to the NYSE standards, and the independence standards in the Company s By-laws, the Board has adopted the following categorical standards for independence described below, which are included in the Board s Corporate Governance Principles.

Under the Corporate Governance Principles, an independent director is someone who is free of any relationship that would interfere with the exercise of independent judgment, and within the past 5 years:

has not been employed by the Company in an executive capacity;

has not been an advisor or consultant to the Company, and has not been affiliated with a company or a firm that is;

has not been affiliated with a significant customer or supplier of the Company;

has not had a personal services contract with the Company;

has not been affiliated with a tax-exempt entity that receives significant contributions from the Company;

has not been related to any of the persons described above; and

has not been part of an interlocking directorate in which an executive officer of the Company is a member of the compensation committee of the company that employs the Director.

Each year, the Company s Directors and executive officers complete annual questionnaires designed to elicit information about potential related person transactions. Additionally, Directors and executive officers must promptly advise the Corporate Secretary if there are any changes to the information previously provided.

The Nominating and Governance Committee reviews and considers all relevant facts and circumstances with respect to independence for each Director standing for election prior to recommending selection as part of the slate of Directors presented to the shareholders for election at the Company s Annual Meeting. The Nominating and Governance Committee reviews its recommendations with the full Board, which separately considers and evaluates the independence of Directors standing for re-election using the categorical standards described above.

In February 2009, the Board considered regular commercial sales and payments in the ordinary course of business as well as charitable contributions with respect to each of the Non-Management Directors standing for re-election at the Company s 2009 Annual Meeting. In particular, the Board evaluated the amount of sales to ITT or purchases by ITT with respect to companies where any of the Directors serve or served as an executive officer or director. In no instances was a Director a current employee, or was an immediate family member of a Director a current executive officer, of a company that has made payments to, or received payments from, the Company for property or services in an amount which, in any of the last three fiscal years, exceeded the greater of $1 million, or 2% for each respective company s consolidated gross revenues. The Board also considered the Company s charitable contributions to non-profit organizations with respect to each of the Non-Management Directors. No contributions exceeded one percent of the consolidated gross revenues of any non-profit organization.

Mr. Loranger is not independent because of his position as Chairman, President and Chief Executive Officer of the Company.

The following are the independent directors standing for election: Drs. Crawford, Hamre, and Mohapatra**;** General Kern; Messrs. Hake, MacInnis, and Tambakeras, Mrs. Gold and Ms. Sanford.

**Compensation Committee Interlocks and Insider Participation**: None of the members of the Compensation and Personnel Committee during fiscal 2008 or as of the date of this proxy statement has been an officer or employee of the Company and no executive officer of the Company served on the compensation committee or board of any company that employed any member of the Company s Compensation and Personnel Committee or Board of Directors.

**Director Selection and Composition**: Directors of the Company must be persons of integrity, with significant accomplishments and recognized business stature. To be considered by the Nominating and Governance Committee as a Director candidate, a nominee must meet the requirements of the Company s By-laws and Corporate Governance Principles. A nominee should also have experience as a board member, chief executive officer or senior officer of a publicly traded or large privately held company, or have achieved recognized prominence in a relevant field as, for example, a distinguished faculty member of a highly regarded educational institution or senior governmental official. In addition to these minimum qualifications, the Nominating and Governance Committee evaluates each nominee s skills to determine if those skills are complementary to the skills demonstrated by current Board members. The Nominating and Governance Committee also evaluates the Board s needs for operational, technical, management, financial, international or other expertise.

Prior to recommending nominees for election as Directors, the Company s Nominating and Governance Committee engages in a deliberative, evaluative process to assure each nominee possesses the skills and attributes that individually and collectively will contribute to an effective Board of Directors. Biographical information for each candidate for election as a Director is evaluated and candidates for election participate in interviews with existing Board members and management, and are subject to thorough background checks. Director nominees must be willing to commit the requisite time for preparation and attendance at regularly scheduled Board and Committee meetings and participation in other matters necessary for good corporate governance.

The Nominating and Governance Committee identifies Director candidates through a variety of sources including personal references and business contacts. On occasion, the Nominating and Governance Committee utilizes a search firm to identify and screen Director candidates and pays a fee to that firm for each such candidate elected to the Board of the Company. In 2008, the Nominating and Governance Committee considered the candidacy of General Paul J. Kern. General Kern was identified as a former director of the EDO Corporation, which was acquired by the Company, as well as by a third-party search firm. The Nominating and Governance Committee will consider shareholder nominees for election to the Company s Board who meet the qualification standards described above. (See Section II.5 of the Nominating and Governance Charter at *http://www.itt.com/responsibility/governance/nominating/.*) The Nominating and Governance Committee also evaluates and makes recommendations to the Board of Directors concerning appointment of Directors to Board Committees, selection of Board Committee Chairs, Committee member qualifications, Committee member appointment and removal, Committee structure and

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operations and proposal of the Board slate for election at the Annual Meeting of Shareholders, consistent with criteria approved by the Board of Directors.

**Committees of the Board of Directors**: The standing Committees of the Board described below perform essential corporate governance functions. In October of 2007 the Board also formed a Special Litigation Committee to oversee an independent investigation involving the Company s Night Vision matter.

***Audit Committee***

2008 Audit Committee Members are:

| | |
|---|---|
| | Ralph F. Hake, Chair<br>Christina A. Gold<br>Surya N. Mohapatra<br>Linda S. Sanford |
| Meetings in 2008: | 9 |
| Responsibilities: | Subject to any action that may be taken by the full Board, the Audit Committee has the ultimate authority and responsibility to determine Deloitte qualifications and independence, and to appoint (or nominate for shareholder ratification), evaluate, and where appropriate, consider rotation or replacement of Deloitte.<br><br>Review and discuss with management and Deloitte, and approve the audited financial statements of the Company and make a recommendation regarding inclusion of those financial statements in any public filing including the Company s Annual Report on Form 10-K (or the Annual Report to Shareholders if distributed prior to the filing of Form 10-K), including discussion of the Company s disclosures under Management s Discussion and Analysis of Financial Condition and Results of Operations.<br><br>Review and consider with Deloitte matters required to be discussed by PCAOB Standards, Statement of Auditing Standards ( SAS ) No. 114 (The Auditor s Communication with Those Charged with Governance) and all other applicable regulatory agencies.<br><br>Review with management and Deloitte the effect of regulatory and accounting initiatives on the Company s financial statements.<br><br>As a whole, or through the Committee chair, review and discuss with Deloitte the Company s interim financial results to be included in the Company s earnings report or quarterly reports to be filed with the SEC, including discussion of the Company s disclosures under Management s Discussion and Analysis of Financial Condition and Results of Operations prior to the filing of its Form 10-Q with the SEC.<br><br>Review and discuss with management the types of information to be disclosed and the types of presentations to be made with respect to the Company s earning releases and rating agency presentations. |

Monitor and discuss with management and Deloitte the quality and adequacy of the Company s internal controls and their

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effectiveness, and meet regularly and privately with the Director of Internal Audit.

Annually request from Deloitte a formal written statement delineating all relationships between Deloitte and the Company, consistent with the Public Company Accounting Oversight Board s Rule 3526T.

With respect to such relationships, the Audit Committee shall:

Discuss with Deloitte any disclosed relationships and the impact of the relationship on Deloitte independence; and

Assess and recommend appropriate action in response to the Deloitte report to satisfy itself of the auditor s independence.

Adopt and monitor implementation and compliance with the Company s Non-Audit Services Policy, which addresses approval requirements and the limited circumstances in which Deloitte or other service providers may be retained for non-audit services.

Confirm the scope of audits to be performed by Deloitte and any internal audit service provider, monitor progress and review results. Review fees and expenses charged by Deloitte and any party retained to provide internal audit services.

On an annual basis, discuss with Deloitte its internal quality control procedures, material issues raised in quality control or peer review and any inquiries by governmental or professional authorities regarding the firm s independent audits of other clients.

Review significant findings or unsatisfactory internal audit reports or audit problems or difficulties encountered by Deloitte, and monitor management s response to such findings.

Provide oversight and discuss with management, internal auditors and Deloitte, the adequacy and effectiveness of the Company s overall risk assessment and risk management process.

Review its performance and Charter at least annually and make recommendations to the Board of Directors for approval and adoption of its Charter.

Review regularly and consider the Company s environmental, safety and health reserves.

Review expense accounts of senior executives.

Update the Board of Directors on a regular basis with respect to matters coming to its attention that may have a significant impact on the Company s financial condition or affairs and the Company s compliance with legal or regulatory requirements and the performance and independence of Deloitte and the internal audit function.

Review major issues regarding accounting principles and financial statement presentations, significant changes to the Company s selection or application of accounting principles and major issues relating to the Company s internal controls including any specifically required steps to correct identified major internal control issues. The Audit Committee also reviews management or Deloitte s analyses regarding significant financial reporting issues and judgments made in preparing financial statements including analyses of alternative GAAP methods as well as the effect of regulatory and accounting initiatives and off-balance sheet structures, if any, on the Company s financial statements.

Review all material related party transactions prior to initiation of the transaction and make recommendations to the Board of Directors for approval or disapproval.

In conjunction with the Board of Directors, evaluate the qualifications of its members and its own performance on an annual basis.

Meet separately, on a regular basis, with Deloitte, internal auditors, and members of management, as well as privately as a Committee.

Establish policies regarding the Company s employment and retention of current or former employees of Deloitte or outsourced internal auditor.

With respect to complaints concerning accounting, internal accounting controls or auditing matters:

Review and approve procedures for receipt, retention and treatment of complaints received by the Company; and

Establish procedures for the confidential, anonymous submission of complaints to the Audit Committee.

Establish levels for payment by the Company of fees to Deloitte and any advisors retained by the Audit Committee.

Receive regular reports from the Chief Executive Officer, Chief Financial Officer and from the Company s disclosure control committee representative on the status of the Company s disclosure controls and related certifications, including disclosure of any material weaknesses or significant deficiencies in the design or operation of internal controls and any fraud that involves management or other employees with a significant role in internal controls.

Prepare the Report of the Audit Committee for the Company s Proxy Statement.

The Board of Directors has identified Ralph F. Hake as the audit committee financial expert.

**Independence**

The Board of Directors has determined that each member of the Audit Committee meets the independence standards set out in the Board s Corporate Governance Principles and its Audit Committee Charter and the requirements of the New York Stock Exchange currently in effect and Rule 10A-3 of the Exchange Act. The Board of Directors has evaluated the performance of the Audit Committee consistent with the regulatory requirements.

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A copy of the Audit Committee Charter is available on the Company s website *http://www.itt.com/responsibility/governance/audit/.* The Company will provide, free of charge, a copy of the Audit Committee Charter to any shareholder, upon request to the Secretary of ITT.

***Compensation and Personnel Committee***

2008 Compensation and Personnel Committee Members are:

| | |
|---|---|
| | Linda S. Sanford, Chair<br>Curtis J. Crawford<br>Ralph F. Hake<br>Frank T. MacInnis |
| Meetings in 2008: | 5 |
| | The Committee s primary objective is to establish a competitive executive compensation program that clearly links executive compensation to business performance and shareholder return, without excessive enterprise risk. |
| Responsibilities: | Approve and oversee administration of the Company s employee compensation program including incentive plans and equity based compensation plans.<br><br>Evaluate senior management and Chief Executive Officer performance, evaluate enterprise risk and other risk factors with respect to compensation objectives, set annual performance objectives for the Chief Executive Officer and approve individual compensation actions for the Chief Executive Officer and officers at the vice president level and above, as well as certain other selected positions.<br><br>Oversee the establishment and administration of the Company s benefit programs.<br><br>Select, retain and determine the terms of engagement for independent compensation and benefits consultants and other outside counsel, as needed, to provide independent advice to the Committee with respect to the Company s current and proposed executive compensation and employee benefit programs. In 2008 and prior years, the Committee obtained such advice.<br><br>Oversee and approve the continuity planning process and review with the full Board of Directors, which provides final approval.<br><br>Regularly report to the Board of Directors on compensation, benefits, continuity and related matters.<br><br>Prepare the Compensation Committee Report for the Company s Proxy Statement.<br><br>Review regularly and consider the Company s Inclusion & Diversity strategy and the effectiveness of related programs and policies.<br><br>Review its performance and Charter at least annually and make recommendations to the Board of Directors for approval and adoption of its Charter. |

More detail regarding the processes and procedures used to determine executive compensation is found in the Compensation Discussion and Analysis starting on page 35.

**Independence**

The Board of Directors has determined that each member of the Compensation and Personnel Committee meets the independence standards set out in the Board s Corporate Governance Principles and its Compensation and Personnel Committee Charter and the requirements of the NYSE currently in effect.

A copy of the Compensation and Personnel Committee Charter is available on the Company s website http://www.itt.com/responsibility/governance/compensation/. The Company will provide, free of charge, a copy of the Compensation and Personnel Committee Charter to any shareholder, upon request to the Secretary of ITT.

***Corporate Responsibility Committee***

2008 Corporate Responsibility Committee Members are:

| | |
|---|---|
| | John J. Hamre, Chair<br>Linda S. Sanford<br>Markos I. Tambakeras |
| Meetings in 2008: | The Corporate Responsibility Committee did not meet in 2008 as the responsibilities of that Committee were addressed by the full Board during its meetings. |
| Responsibilities: | Review and make recommendations concerning the Company s roles and responsibilities as a good corporate citizen.<br><br>Review and consider major claims and litigation involving the Company and its subsidiaries.<br><br>Regularly assess the adequacy and effectiveness of the Company s Code of Corporate Conduct and review any violations of the Code.<br><br>Review its performance and Charter at least annually and make recommendations to the Board of Directors for approval and adoption of its Charter. |

The Board of Directors has determined that each member of the Corporate Responsibility Committee meets the independence standards set out in the Board s Corporate Governance Principles and Company By-laws.

A copy of the Corporate Responsibility Committee Charter is available on the Company s website http://www.itt.com/responsibility/governance/corporate-responsibility/. The Company will provide, free of charge, a copy of the Corporate Responsibility Committee Charter to any shareholder, upon request to the Secretary of ITT.

***Nominating and Governance Committee***

2008 Nominating and Governance Committee Members are:

| | |
|---|---|
| | John J. Hamre, Chair<br>Curtis J. Crawford<br>Paul J. Kern<br>Markos I. Tambakeras |
| Meetings in 2008: | 3 |

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Responsibilities:

Develop, annually review, update and recommend to the Board of Directors corporate governance principles for the Company.

In the event it is necessary to select a new chief executive officer, lead the process for candidate evaluation, consideration and screening. The full Board of Directors has the final responsibility to select the Company s chief executive officer.

Evaluate and make recommendations to the Board of Directors concerning the composition, governance and structure of the Board.

Make recommendations to the Board of Directors concerning the qualifications, compensation and retirement age of Directors.

Administer the Board of Directors annual evaluation process.

Review and recommend to the full Board matters and agenda items relating to the Company s Annual Meeting of shareholders.

Review the form of Annual Report to Shareholders, Proxy Statement and related materials.

Review the Company s business continuity and disaster recovery programs and plans.

Review the Company s communication and advertising program and other activities involving community relations, major charitable contributions and promotion of the Company s public image.

Determine desired Board and Director skills and attributes and conduct searches for prospective board members whose skills and attributes reflect those desired for the Board of Directors.

Identify, evaluate and propose nominees for election to the Board of Directors.

Make recommendations to the Board of Directors concerning the appointment of Directors to Board Committees and the selection of Board Committee Chairs.

Evaluate and make recommendations regarding senior management requests for approval to accept membership on outside boards.

Review regularly and consider the Company s programs and policies for effecting compliance with laws and regulations involving the environment, safety and health.

Provide oversight and discuss with management, internal auditors and Deloitte the adequacy and effectiveness of the Company s insurance programs.

Review and consider the Company s policies and efforts with respect to compliance with government contracts, international laws and regulations and export controls.

Review its performance and Charter at least annually and make recommendations to the Board of Directors for approval and adoption of its Charter.

As described on pages 19 to 20 the Nominating and Governance Committee will consider shareholder nominees for election to the Company s Board who meet the qualification standards. (See Section II.5 of the Nominating and Governance Charter at *http://www.itt.com/responsibility/governance/nominating/*).

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### Independence

The Board of Directors has determined that each member of the Nominating and Governance Committee meets the independence standards set out in the Board s Nominating and Governance Committee Charter, its Corporate Governance Principles and the requirements of the New York Stock Exchange currently in effect. A copy of the Nominating and Governance Committee Charter is available on the Company s website *(http://www.itt.com/responsibility/governance/nominating/).* The Company will provide, free of charge, a copy of the Nominating and Governance Committee Charter to any shareholder, upon request to the Secretary of ITT.

***Strategy and Finance Committee***

2008 Strategy and Finance Committee Members are:

| | |
|---|---|
| | Markos I. Tambakeras, Chair<br>Christina A. Gold<br>John J. Hamre<br>Paul J. Kern<br>Surya N. Mohapatra |
| Meetings in 2008: | 4 |
| Responsibilities: | Receive periodic updates on global macroeconomic issues.<br>Review and consider the Company s:<br>Strategic plans<br>Operations excellence performance<br>Operating plan<br>Capital and capital allocation<br>Corporate guarantees<br>Acquisition integration<br>Pension plan performance, category and asset allocation and ERISA compliance<br>Tax compliance, tax planning and related matters<br>Hedge transactions and strategies as needed<br>Investor relations matters as needed<br>Strategic issues<br>Significant business acquisitions and divestitures, and other related matters |

Dividend policies

Review and assess its performance on an annual basis

Review and approve its Charter at least annually

The Strategy and Finance Committee oversees all areas of strategy and corporate finance to assure the Company maintains adequate financial liquidity and appropriate credit ratings and to assure the Company s strategic initiatives are consistent with the Company s financial and strategic plans. The Board retains the ultimate power and authority with respect to strategic direction and major strategic and financial decisions.

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### Independence

The Board of Directors has determined that each member of the Strategy and Finance Committee meets the independence standards set out in the Board s Corporate Governance Principles and the Strategy and Finance Committee Charter.

A copy of the Strategy and Finance Committee Charter is available on the Company s website *(http://www.itt.com/responsibility/governance/strategy-finance/).* The Company will provide, free of charge, a copy of the Strategy and Finance Committee Charter to any shareholder, upon request to the Secretary of ITT.

### Special Litigation Committee

On March 27, 2007, the Company reached a settlement relating to an investigation of its ITT Night Vision Division s compliance with the International Traffic in Arms Regulations ( ITAR ). The settlement included the Company pleading guilty in the United States District Court for the Western District of Virginia to one ITAR violation relating to the improper handling of sensitive documents and one ITAR violation involving making misleading statements. On April 17, 2007, the Company s Board of Directors received a letter on behalf of a shareholder requesting that the Board take appropriate action against the employees responsible for the actions described in the Company s agreements with the United States Attorney s Office for the Western District of Virginia. During the following months, the Board, with the assistance of outside counsel for the Company, engaged in a process of identifying independent counsel to advise it regarding the investigation and the processes required to establish a Special Litigation Committee. In October 2007, the Company created the Special Litigation Committee to oversee the objective, investigative work by independent counsel previously selected to investigate the Night Vision matter and report to the Board with respect to the shareholder letter request. The Special Litigation Committee conducted an investigation with the assistance of independent counsel and concluded in 2008 that no legal actions should be brought by ITT. The members of the Special Litigation Committee are Mr. MacInnis and Dr. Crawford.

The Board of Directors has determined that each member of the Special Litigation Committee meets the independence standards set out in the Board s Corporate Governance Principles.

### Meetings of the Board and Committees

During 2008, there were 5 regularly scheduled Board meetings, one telephonic meeting, and 21 meetings of standing Committees. All Directors attended at least 75% of the aggregate of all meetings of the Board and standing Committees on which they served. It is Company practice that all Directors attend the Company s Annual Meeting. For 2009, the Board has scheduled five regular meetings. In conjunction with the regular meetings, those Directors who are not employees of ITT are scheduled to meet privately (without management) following each Board meeting during the year. The Independent Presiding Director presides over these private meetings.

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### 2008 Non-Management Director Compensation

The following table represents the 2008 Non-Management Director Compensation expense recognized for financial statement reporting purposes and not the value of awards granted in 2008. As discussed in more detail in the narrative following the table, all Non-Management Directors receive the same cash, stock, and options awards for service as a Non-Management Director (except Mr. Hake as the Audit Committee Chair received an additional $10,000 cash payment). Mr. Loranger, as an employee Director, does not receive compensation for his Board service. The grant date fair value of stock awards and option awards granted to Non-Management Directors in 2008 is provided in footnote, (c) and (d) to the table. Stock awards are composed of restricted shares and restricted stock units. Option awards are composed of non-qualified stock options.

| Name (a) | Fees Earned or Paid in Cash (b) ($) | Stock Awards (c) ($) | Option Awards (d) ($) | Non-Equity Incentive Plan Compensation (e) ($) | Change in Pension Value and Nonqualified Deferred Compensation Earnings (f) ($) | All Other Compensation (g) ($) | Total (h) ($) |
|---|---|---|---|---|---|---|---|
| Curtis J. Crawford | 90,000 | 141,308 | 37,378 | | | | 268,686 |
| Christina A. Gold | 90,000 | 117,764 | 37,378 | | | | 245,142 |
| Ralph F. Hake | 100,000 | 117,764 | 37,378 | | | | 255,142 |
| John J. Hamre | 90,000 | 141,308 | 37,378 | | | | 268,686 |
| Paul J. Kern(i) | 67,500 | 35,432 | 4,579 | | | | 107,511 |
| Raymond W. LeBoeuf(j) | | 60,399 | 27,743 | | | | 88,142 |
| Frank T. MacInnis | 90,000 | 125,975 | 37,378 | | | | 253,353 |
| Surya N. Mohapatra(k) | 90,000 | 60,246 | 12,338 | | | | 162,584 |
| Linda S. Sanford | 90,000 | 120,793 | 37,378 | | | | 248,171 |
| Markos I. Tambakeras | 90,000 | 136,125 | 37,378 | | | | 263,503 |

(b) Fees earned may be paid, at the election of the Director, in cash or deferred cash. Non-Management Directors may irrevocably elect deferral into an interest-bearing cash account or an account that tracks an index of the Company s stock. Mr. Hake received an additional $10,000 as the Audit Committee Chair.

(c) and (d) Awards reflect the Company s expense recognized for financial statement reporting purposes for the fiscal year ended December 31, 2008 in accordance with FAS123R. The assumptions used in calculating these values may be found in Note 17 to the Consolidated Financial Statements in the Company s 2008 Form 10-K. Non-Management Directors do not receive differing amounts of compensation. The Company s expense recognized for compensation awards varies due to different tenure. For 2008 grants, the grant date fair value for each Non-Management Director restricted stock award is $90,040 and the grant date fair value for each Director option award is $37,059.

(g) All Other Compensation for Non-Management Directors will be disclosed only if perquisites and other personal benefits exceed $10,000. No Non-Management Directors received perquisites or other personal benefits in excess of $10,000.

(i) General Kern was elected a Non-Management Director of the Company, effective August 7, 2008. General Kern received $67,500 as a pro-rata cash retainer, a pro-rata award of 1,016 of restricted stock units, based on the average of the high and low sales prices per share of ITT common stock on the date of the 2008 Annual Meeting of $66.45, and a pro-rata award of 2,220 non-qualified stock options with an exercise price of $66.74, the closing price of ITT common stock on August 7, 2008.

(j) Mr. LeBoeuf retired from the Board of Directors and did not stand for election at the Company s 2008 Annual Meeting, and was awarded no compensation for the term starting in May 2008. On May 13, 2008, Mr. LeBoeuf s outstanding unvested stock options and restricted stock awards of 2,813 and 6,937 respectively, vested.

(k) Dr. Mohapatra was elected a Non-Management Director of the Company, effective February 14, 2008.

**Non-Management Director Restricted Common Stock and Stock Option Awards Outstanding at 2008 Fiscal Year-End**

| Non-Management Director Name | Outstanding Restricted Common Stock Awards | Outstanding Stock Option Awards |
|---|---|---|
| Curtis J. Crawford | 28,502 | 19,300 |
| Christina A. Gold | 21,152 | 19,300 |
| Ralph F. Hake | 8,952 | 15,740 |
| John J. Hamre | 16,796 | 19,300 |
| Paul J. Kern(1) | 1,016 | 2,200 |
| Raymond W. LeBoeuf(2) | | 16,340 |
| Frank T. MacInnis | 12,452 | 19,300 |
| Surya N. Mohapatra(3) | 1,697 | 3,640 |
| Linda S. Sanford | 9,272 | 19,300 |
| Markos I. Tambakeras | 8,130 | 19,300 |

(1) General Kern was elected a Non-Management Director of the Company effective August 7, 2008.

(2) Mr. LeBoeuf retired as a Non-Management Director of the Company effective with the May 2008 Annual Meeting. Effective with Mr. LeBoeuf s retirement, the restriction on 13,249 restricted shares lapsed.

(3) Dr. Mohapatra was elected as a Non-Management Director of the Company effective February 14, 2008.

On May 13, 2008, the Board of Directors approved compensation for Non-Management Directors consistent with allocation recommendations provided by Towers Perrin. As approved, for 2008, Non-Management Directors received total annual compensation valued at approximately $220,000 when awarded, as follows:

$90,000 payable at the election of each Non-Management Director in cash or deferred cash. Directors choosing deferred cash payment may irrevocably elect to have the deferred cash deposited into an interest-bearing cash account, at an interest rate determined as of the Company s next Annual Meeting, or deposited into an account that tracks an index of the Company s common stock. No deferred compensation selections provide for preferential treatment for Directors;

2/3 of the remainder in restricted stock units (such restricted stock units payable in shares upon following the Non-Management Director s termination of service on the Board of Directors or on a date selected by the Director); and

1/3 of the remainder in non-qualified stock options (vesting over a three-year period in one-third cumulative installments).

Additionally, the Board of Directors approved (with the Audit Committee Chair abstaining) a supplemental retainer of $10,000 in cash to be paid to Mr. Hake, the 2008 Audit Committee chair, effective as of the Company s 2008 Annual

Meeting to reflect the significant responsibilities and time commitments associated with leadership of that Committee.

The number of restricted stock units granted in May 2008 to all Non-Management Directors under the Non-Management Director compensation program, adopted in 2003, was determined by dividing $90,000 by $66.45, the average of the high and low sales prices per share of ITT common stock on the date of the 2008 Annual Meeting. The resulting number of shares, 1,355, was rounded up to the nearest whole share. Directors receive dividend equivalents on the restricted stock units but have no other rights as shareholders with respect to the restricted stock units. Non-Management Director non-qualified stock option grants are priced and awarded on the same day as employee stock options are priced and awarded. The fair value of Non-Management Directors non-qualified stock options granted is calculated using the binomial lattice valuation model. The exercise price of Non-Management Directors non-qualified stock options granted is the closing price on the grant date.

The Compensation and Personnel and Nominating and Governance Committees retained Towers Perrin to review Non-Management Director compensation components and total director compensation paid with director compensation components and total director compensation paid for companies in the S&P® Industrials Index with revenue comparable to ITT. Upon the recommendation of Towers Perrin and after review, the Committees recommended and the full Board approved, an increase in overall Non-Management Director cash compensation to raise Director compensation to a level closer to the median of companies in the S&P® Industrials Index with revenues comparable to ITT. The Board approved Non-Management Director compensation changes to be effective with the Company s 2008 Annual Meeting to increase the cash component of the Non-Management Director compensation to $90,000 and to continue providing the Audit Chair with an additional $10,000 cash payment. The components of Non-Management Director compensation are weighted toward restricted stock or restricted stock units and stock option awards to align the interests of Non-Management Directors with shareholders of the Company. The Board of Directors agreed to review Non-Management Director compensation on a biennial basis.

Restricted shares previously awarded under the ITT 1996 Restricted Stock Plan for Non-Management Directors (the 1996 Plan ), which preceded the 2003 Plan, and under which restricted shares are still outstanding, provided that each Director s restricted shares are held in escrow and may not be transferred in any manner until one of the following events occurs:

| | | | | |
|---|---|---|---|---|
| | 137,856 | | 480 | 470 |
| Due after ten years | 47,812 | 48,962 | 0 | 0 |
| U.S. government sponsored agency mortgage-backed securities | 275,650 | 278,188 | 0 | 0 |
| Total debt securities | 594,241 | 601,215 | 1,661 | 1,653 |
| CRA investment funds | 25,000 | 25,120 | 0 | 0 |
| Total securities | $ 619,241 | $ 626,335 | $ 1,661 | $ 1,653 |

As of March 31, 2015, there was a net gain of $144 thousand realized on sales of AFS securities, consisting of a pre-tax gain of $223 thousand and a pre-tax loss of $79 thousand. As of March 31, 2014, there was a net loss of $60 thousand.

The amortized cost of securities pledged as collateral, to secure public deposits and for other purposes, was $248.2 million at March 31, 2015 and $267.1 million at December 31, 2014.

The amortized cost of securities sold under agreements to repurchase amounted to $277.1 million at March 31, 2015 and $280.9 million at December 31, 2014.

CTBI evaluates its investment portfolio on a quarterly basis for impairment. The analysis performed as of March 31, 2015 indicates that all impairment is considered temporary, market and interest rate driven, and not credit-related.

The percentage of total investments with unrealized losses as of March 31, 2015 was 26.6% compared to 44.1% as of December 31, 2014. The following tables provide the amortized cost, gross unrealized losses, and fair market value, aggregated by investment category and length of time the individual securities have been in a continuous unrealized loss position as of March 31, 2015 that are not deemed to be other-than-temporarily impaired.

Available-for-Sale

| (in thousands) | Amortized Cost | Gross Unrealized Losses | Fair Value |
|---|---|---|---|
| Less Than 12 Months | | | |
| U.S. Treasury and government agencies | $ 9,421 | $ (14 ) | $ 9,407 |
| State and political subdivisions | 7,094 | (50 ) | 7,044 |
| U.S. government sponsored agency mortgage-backed securities | 23,865 | (70 ) | 23,795 |
| Total debt securities | 40,380 | (134 ) | 40,246 |
| CRA investment funds | 0 | 0 | 0 |
| Total <12 months temporarily impaired AFS securities | 40,380 | (134 ) | 40,246 |
| | | | |
| 12 Months or More | | | |
| U.S. Treasury and government agencies | 54,771 | (662 ) | 54,109 |
| State and political subdivisions | 7,828 | (286 ) | 7,542 |
| U.S. government sponsored agency mortgage-backed securities | 65,835 | (1,330 ) | 64,505 |
| Total debt securities | 128,434 | (2,278 ) | 126,156 |
| CRA investment funds | 0 | 0 | 0 |
| Total ≥12 months temporarily impaired AFS securities | 128,434 | (2,278 ) | 126,156 |
| | | | |
| Total | | | |
| U.S. Treasury and government agencies | 64,192 | (676 ) | 63,516 |
| State and political subdivisions | 14,922 | (336 ) | 14,586 |
| U.S. government sponsored agency mortgage-backed securities | 89,700 | (1,400 ) | 88,300 |
| Total debt securities | 168,814 | (2,412 ) | 166,402 |
| CRA investment funds | 0 | 0 | 0 |
| Total temporarily impaired AFS securities | $ 168,814 | $ (2,412 ) | $ 166,402 |

Held-to-Maturity

| (in thousands) | Amortized Cost | Gross Unrealized Losses | Fair Value |
|---|---|---|---|
| 12 Months or More | | | |
| U.S. Treasury and government agencies | $ 480 | $ (10 ) | $ 470 |
| Total temporarily impaired HTM securities | $ 480 | $ (10 ) | $ 470 |

U.S. Treasury and Government Agencies

The unrealized losses in U.S. Treasury and government agencies were caused by interest rate increases. The contractual terms of those investments do not permit the issuer to settle the securities at a price less than amortized cost. CTBI does not consider those investments to be other-than-temporarily impaired at March 31, 2015, because CTBI does not intend to sell the investments and it is not more likely than not that we will be required to sell the investments before recovery of their amortized cost, which may be at maturity.

State and Political Subdivisions

The unrealized losses in securities of state and political subdivisions were caused by interest rate increases. The contractual terms of those investments do not permit the issuer to settle the securities at a price less than amortized cost. CTBI does not consider those investments to be other-than-temporarily impaired at March 31, 2015, because CTBI does not intend to sell the investments before recovery of their amortized cost, which may be at maturity.

U.S. Government Sponsored Agency Mortgage-Backed Securities

The unrealized losses in U.S. government sponsored agency mortgage-backed securities were caused by interest rate increases. CTBI expects to recover the amortized cost basis over the term of the securities. CTBI does not consider those investments to be other-than-temporarily impaired at March 31, 2015, because (i) the decline in market value is attributable to changes in interest rates and not credit quality, (ii) CTBI does not intend to sell the investments, and (iii) it is not more likely than not we will be required to sell the investments before recovery of their amortized cost, which may be at maturity.

The analysis performed as of December 31, 2014 indicated that all impairment was considered temporary, market and interest rate driven, and not credit-related. The following tables provide the amortized cost, gross unrealized losses, and fair market value, aggregated by investment category and length of time the individual securities have been in a continuous unrealized loss position as of December 31, 2014 that are not deemed to be other-than-temporarily impaired.

Available-for-Sale

| (in thousands) | Amortized Cost | Gross Unrealized Losses | Fair Value |
|---|---|---|---|
| Less Than 12 Months | | | |
| U.S. Treasury and government agencies | $31,185 | $ (87) | $31,098 |
| State and political subdivisions | 8,800 | (23) | 8,777 |
| U.S. government sponsored agency mortgage-backed securities | 50,115 | (442) | 49,673 |
| Total debt securities | 90,100 | (552) | 89,548 |
| CRA investment funds | 25,000 | (111) | 24,889 |
| Total <12 months temporarily impaired AFS securities | 115,100 | (663) | 114,437 |
| | | | |
| 12 Months or More | | | |
| U.S. Treasury and government agencies | 65,209 | (2,053) | 63,156 |
| State and political subdivisions | 21,308 | (443) | 20,865 |
| U.S. government sponsored agency mortgage-backed securities | 86,389 | (2,408) | 83,981 |
| Total debt securities | 172,906 | (4,904) | 168,002 |
| CRA investment funds | 0 | 0 | 0 |
| Total ≥12 months temporarily impaired AFS securities | 172,906 | (4,904) | 168,002 |
| | | | |
| Total | | | |
| U.S. Treasury and government agencies | 96,394 | (2,140) | 94,254 |
| State and political subdivisions | 30,108 | (466) | 29,642 |
| U.S. government sponsored agency mortgage-backed securities | 136,504 | (2,850) | 133,654 |
| Total debt securities | 263,006 | (5,456) | 257,550 |
| CRA investment funds | 25,000 | (111) | 24,889 |
| Total temporarily impaired AFS securities | $288,006 | $ (5,567) | $282,439 |

Held-to-Maturity

| (in thousands) | Amortized Cost | Gross Unrealized Losses | Fair Value |
|---|---|---|---|
| 12 Months or More | | | |
| U.S. Treasury and government agencies | $ 480 | $ (19 ) | $ 461 |
| Total temporarily impaired HTM securities | $ 480 | $ (19 ) | $ 461 |

Note 4 – Loans

Major classifications of loans, net of unearned income, deferred loan origination costs, and net premiums on acquired loans, are summarized as follows:

| (in thousands) | March 31 2015 | December 31 2014 |
|---|---|---|
| Commercial construction | $119,222 | $121,942 |
| Commercial secured by real estate | 966,335 | 948,626 |
| Equipment lease financing | 10,908 | 10,344 |
| Commercial other | 341,400 | 352,048 |
| Real estate construction | 60,894 | 62,412 |
| Real estate mortgage | 708,067 | 712,465 |
| Home equity | 87,136 | 88,335 |
| Consumer direct | 120,005 | 122,136 |
| Consumer indirect | 332,515 | 315,516 |
| Total loans | $2,746,482 | $2,733,824 |

CTBI has segregated and evaluates its loan portfolio through nine portfolio segments. CTBI serves customers in small and mid-sized communities in eastern, northeastern, central, and south central Kentucky, southern West Virginia, and northeastern Tennessee. Therefore, CTBI's exposure to credit risk is significantly affected by changes in these communities.

Commercial construction loans are for the purpose of erecting or rehabilitating buildings or other structures for commercial purposes, including any infrastructure necessary for development. Included in this category are improved property, land development, and tract development loans. The terms of these loans are generally short-term with permanent financing upon completion.

Commercial real estate loans include loans secured by nonfarm, nonresidential properties, 1-4 family/multi-family properties, farmland, and other commercial real estate. These loans are originated based on the borrower's ability to service the debt and secondarily based on the fair value of the underlying collateral.

Equipment lease financing loans are fixed, variable, and tax exempt leases for commercial purposes.

Commercial other loans consist of commercial check loans, agricultural loans, receivable financing, floorplans, loans to financial institutions, loans for purchasing or carrying securities, and other commercial purpose loans. Commercial loans are underwritten based on the borrower's ability to service debt from the business's underlying cash flows. As a general practice, we obtain collateral such as real estate, equipment, or other assets, although such loans may be uncollateralized but guaranteed.

Real estate construction loans are typically for owner-occupied properties. The terms of these loans are generally short-term with permanent financing upon completion.

Residential real estate loans are a mixture of fixed rate and adjustable rate first and second lien residential mortgage loans. As a policy, CTBI holds adjustable rate loans and sells the majority of its fixed rate first lien mortgage loans into the secondary market. Changes in interest rates or market conditions may impact a borrower's ability to meet contractual principal and interest payments. Residential real estate loans are secured by real property.

Home equity lines are revolving adjustable rate credit lines secured by real property.

Consumer direct loans are fixed rate products comprised of unsecured loans, consumer revolving credit lines, deposit secured loans, and all other consumer purpose loans.

Consumer indirect loans are fixed rate loans secured by automobiles, trucks, vans, and recreational vehicles originated at the selling dealership underwritten and purchased by CTBI's indirect lending department. Both new and used products are financed. Only dealers who have executed dealer agreements with CTBI participate in the indirect lending program.

Not included in the loan balances above were loans held for sale in the amount of $1.5 million at March 31, 2015 and $2.3 million at December 31, 2014, respectively.

Refer to note 1 to the condensed consolidated financial statements for further information regarding our nonaccrual policy. Nonaccrual loans segregated by class of loans were as follows:

| (in thousands) | March 31 2015 | December 31 2014 |
|---|---|---|
| Commercial: | | |
| Commercial construction | $4,063 | $ 4,339 |
| Commercial secured by real estate | 4,709 | 6,725 |
| Commercial other | 2,269 | 2,423 |
| | | |
| Residential: | | |
| Real estate construction | 596 | 602 |
| Real estate mortgage | 5,381 | 6,513 |
| Home equity | 246 | 369 |
| Total nonaccrual loans | $17,264 | $ 20,971 |

The following tables present CTBI's loan portfolio aging analysis, segregated by class, as of March 31, 2015 and December 31, 2014:

| | March 31, 2015 | | | | | | |
|---|---|---|---|---|---|---|---|
| (in thousands) | 30-59 Days Past Due | 60-89 Days Past Due | 90+ Days Past Due | Total Past Due | Current | Total Loans | 90+ and Accruing* |
| Commercial: | | | | | | | |
| Commercial construction | $298 | $190 | $5,764 | $6,252 | $112,970 | $119,222 | $ 1,701 |
| Commercial secured by real estate | 4,434 | 3,120 | 8,119 | 15,673 | 950,662 | 966,335 | 5,685 |
| Equipment lease financing | 0 | 0 | 0 | 0 | 10,908 | 10,908 | 0 |
| Commercial other | 667 | 1,586 | 4,054 | 6,307 | 335,093 | 341,400 | 2,320 |

| | | | | | | | |
|---|---|---|---|---|---|---|---|
| Residential: | | | | | | | |
| Real estate construction | 437 | 76 | 778 | 1,291 | 59,603 | 60,894 | 196 |
| Real estate mortgage | 1,618 | 3,898 | 11,626 | 17,142 | 690,925 | 708,067 | 7,284 |
| Home equity | 784 | 641 | 431 | 1,856 | 85,280 | 87,136 | 280 |
| Consumer: | | | | | | | |
| Consumer direct | 841 | 160 | 163 | 1,164 | 118,841 | 120,005 | 163 |
| Consumer indirect | 1,823 | 368 | 169 | 2,360 | 330,155 | 332,515 | 169 |
| Total | $10,902 | $10,039 | $31,104 | $52,045 | $2,694,437 | $2,746,482 | $ 17,798 |

| | December 31, 2014 | | | | | | |
|---|---|---|---|---|---|---|---|
| (in thousands) | 30-59 Days Past Due | 60-89 Days Past Due | 90+ Days Past Due | Total Past Due | Current | Total Loans | 90+ and Accruing* |
| Commercial: | | | | | | | |
| Commercial construction | $40 | $31 | $6,171 | $6,242 | $115,700 | $121,942 | $ 1,863 |
| Commercial secured by real estate | 2,471 | 1,595 | 10,763 | 14,829 | 933,797 | 948,626 | 4,682 |
| Equipment lease financing | 0 | 0 | 0 | 0 | 10,344 | 10,344 | 0 |
| Commercial other | 826 | 55 | 4,205 | 5,086 | 346,962 | 352,048 | 2,367 |
| Residential: | | | | | | | |
| Real estate construction | 92 | 144 | 985 | 1,221 | 61,191 | 62,412 | 383 |
| Real estate mortgage | 1,005 | 5,171 | 13,049 | 19,225 | 693,240 | 712,465 | 7,742 |
| Home equity | 779 | 197 | 703 | 1,679 | 86,656 | 88,335 | 422 |
| Consumer: | | | | | | | |
| Consumer direct | 1,307 | 295 | 141 | 1,743 | 120,393 | 122,136 | 141 |
| Consumer indirect | 2,304 | 586 | 385 | 3,275 | 312,241 | 315,516 | 385 |
| Total | $8,824 | $8,074 | $36,402 | $53,300 | $2,680,524 | $2,733,824 | $ 17,985 |

*90+ and Accruing are also included in 90+ Days Past Due column.

The risk characteristics of CTBI's material portfolio segments are as follows:

Commercial construction loans generally are made to customers for the purpose of building income-producing properties. Personal guarantees of the principals are generally required. Such loans are made on a projected cash flow basis and are secured by the project being constructed. Construction loan draw procedures are included in each specific loan agreement, including required documentation items and inspection requirements. Construction loans may convert to term loans at the end of the construction period, or may be repaid by the take-out commitment from another financing source. If the loan is to convert to a term loan, the repayment ability is based on the borrower's projected cash flow. Risk is mitigated during the construction phase by requiring proper documentation and inspections whenever a draw is requested. Loans in amounts greater than $500,000 generally require a performance bond to be posted by the general contractor to assure completion of the project.

Commercial real estate loans are viewed primarily as cash flow loans and secondarily as loans secured by real estate. Commercial real estate lending typically involves higher loan principal amounts and the repayment of these loans is generally dependent on the successful operation of the property securing the loan or the business conducted on the property securing the loan. Commercial real estate loans may be more adversely affected by conditions in the real estate markets or in the general economy. Management monitors and evaluates commercial real estate loans based on collateral and risk grade criteria.

Equipment lease financing is underwritten by our commercial lenders using the same underwriting standards as would be applied to a secured commercial loan requesting 100% financing. The pricing for equipment lease financing is comparable to that of borrowers with similar quality commercial credits with similar collateral. Maximum terms of equipment leasing are determined by the type and expected life of the equipment to be leased. Residual values are determined by appraisals or opinion letters from industry experts. Leases must be in conformity with our consolidated annual tax plan. As we underwrite our equipment lease financing in a manner similar to our commercial loan portfolio described below, the risk characteristics for this portfolio mirror that of the commercial loan portfolio.

Commercial loans are primarily based on the identified cash flows of the borrower and secondarily on the underlying collateral provided by the borrower. The cash flows of borrowers, however, may not be as expected and the collateral securing these loans may fluctuate in value. Most commercial loans are secured by the assets being financed or other business assets such as accounts receivable or inventory and may incorporate a personal guarantee; however, some short-term loans may be made on an unsecured basis. In the case of loans secured by accounts receivable, the availability of funds for the repayment of these loans may be substantially dependent on the ability of the borrower to collect amounts due from its customers.

With respect to residential loans that are secured by 1-4 family residences and are generally owner occupied, CTBI generally establishes a maximum loan-to-value ratio and requires private mortgage insurance if that ratio is exceeded. Home equity loans are typically secured by a subordinate interest in 1-4 family residences. Residential construction loans are handled through the home mortgage area of the bank. The repayment ability of the borrower and the maximum loan-to-value ratio are calculated using the normal mortgage lending criteria. Draws are processed based on percentage of completion stages including normal inspection procedures. Such loans generally convert to term loans after the completion of construction.

Consumer loans are secured by consumer assets such as automobiles or recreational vehicles. Some consumer loans are unsecured such as small installment loans and certain lines of credit. Our determination of a borrower's ability to repay these loans is primarily dependent on the personal income and credit rating of the borrowers, which can be impacted by economic conditions in their market areas such as unemployment levels. Repayment can also be impacted by changes in property values on residential properties. Risk is mitigated by the fact that the loans are of smaller individual amounts and spread over a large number of borrowers.

The indirect lending area of the bank generally deals with purchasing/funding consumer contracts with new and used automobile dealers. The dealers generate consumer loan applications which are forwarded to the indirect loan processing area for approval or denial. Loan approvals or denials are based on the creditworthiness and repayment ability of the borrower, and on the collateral value. The dealers may have recourse agreements with the Bank.

Credit Quality Indicators:

CTBI categorizes loans into risk categories based on relevant information about the ability of borrowers to service their debt such as: current financial information, historical payment experience, credit documentation, public information, and current economic trends, among other factors. CTBI also considers the fair value of the underlying collateral and the strength and willingness of the guarantor(s). CTBI analyzes commercial loans individually by classifying the loans as to credit risk. Loans classified as loss, doubtful, substandard, or special mention are reviewed quarterly by CTBI for further deterioration or improvement to determine if appropriately classified and valued if deemed impaired. All other commercial loan reviews are completed every 12 to 18 months. In addition, during the renewal process of any loan, as well as if a loan becomes past due or if other information becomes available, CTBI will evaluate the loan grade. CTBI uses the following definitions for risk ratings:

Ø Pass grades include investment grade, low risk, moderate risk, and acceptable risk loans. The loans range from loans that have no chance of resulting in a loss to loans that have a limited chance of resulting in a loss. Customers in this grade have excellent to fair credit ratings. The cash flows are adequate to meet required debt repayments.

Ø

Ø Watch graded loans are loans that warrant extra management attention but are not currently criticized. Loans on the watch list may be potential troubled credits or may warrant "watch" status for a reason not directly related to the asset quality of the credit. The watch grade is a management tool to identify credits which may be candidates for future classification or may temporarily warrant extra management monitoring.

Ø Other assets especially mentioned (OAEM) reflects loans that are currently protected but are potentially weak. These loans constitute an undue and unwarranted credit risk but not to the point of justifying a classification of substandard. The credit risk may be relatively minor yet constitute an unwarranted risk in light of circumstances surrounding a specific asset. Loans in this grade display potential weaknesses which may, if unchecked or uncorrected, inadequately protect CTBI's credit position at some future date. The loans may be adversely affected by economic or market conditions.

Ø Substandard grading indicates that the loan is inadequately protected by the current sound worth and paying capacity of the obligor or of the collateral pledged. These loans have a well-defined weakness or weaknesses that jeopardize the orderly liquidation of the debt with the distinct possibility that CTBI will sustain some loss if the deficiencies are not corrected.

Ø Doubtful graded loans have the weaknesses inherent in the substandard grading 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. The probability of loss is extremely high, but because of certain important and reasonably specific pending factors which may work to CTBI's advantage or strengthen the asset(s), its classification as an estimated loss is deferred until its more exact status may be determined. Pending factors include proposed merger, acquisition, or liquidation procedures, capital injection, perfecting liens on additional collateral, and refinancing plans.

The following table presents the credit risk profile of CTBI's commercial loan portfolio based on rating category and payment activity, segregated by class of loans, as of March 31, 2015 and December 31, 2014:

| (in thousands) | Commercial Construction | Commercial Secured by Real Estate | Equipment Leases | Commercial Other | Total |
|---|---|---|---|---|---|
| March 31, 2015 | | | | | |
| Pass | $ 98,846 | $ 853,434 | $ 10,908 | $ 296,424 | $1,259,612 |
| Watch | 9,473 | 73,254 | 0 | 36,668 | 119,395 |
| OAEM | 1,153 | 6,642 | 0 | 828 | 8,623 |
| Substandard | 5,688 | 29,074 | 0 | 5,618 | 40,380 |
| Doubtful | 4,062 | 3,931 | 0 | 1,862 | 9,855 |
| Total | $ 119,222 | $ 966,335 | $ 10,908 | $ 341,400 | $1,437,865 |
| | | | | | |
| December 31, 2014 | | | | | |
| Pass | $ 101,314 | $ 834,751 | $ 10,344 | $ 307,270 | $1,253,679 |
| Watch | 9,857 | 69,123 | 0 | 36,114 | 115,094 |
| OAEM | 934 | 10,973 | 0 | 881 | 12,788 |
| Substandard | 5,647 | 27,901 | 0 | 5,772 | 39,320 |
| Doubtful | 4,190 | 5,878 | 0 | 2,011 | 12,079 |
| Total | $ 121,942 | $ 948,626 | $ 10,344 | $ 352,048 | $1,432,960 |

The following table presents the credit risk profile of the CTBI's residential real estate and consumer loan portfolios based on performing or nonperforming status, segregated by class, as of March 31, 2015 and December 31, 2014:

| (in thousands) | Consumer | Total |
|---|---|---|

| | Real Estate Construction | Real Estate Mortgage | Home Equity | Consumer Direct | Indirect | |
|---|---|---|---|---|---|---|
| March 31, 2015 | | | | | | |
| Performing | $ 60,102 | $ 695,402 | $ 86,610 | $ 119,842 | $ 332,346 | $ 1,294,302 |
| Nonperforming (1) | 792 | 12,665 | 526 | 163 | 169 | 14,315 |
| Total | $ 60,894 | $ 708,067 | $ 87,136 | $ 120,005 | $ 332,515 | $ 1,308,617 |
| | | | | | | |
| December 31, 2014 | | | | | | |
| Performing | $ 61,427 | $ 698,210 | $ 87,544 | $ 121,995 | $ 315,131 | $ 1,284,307 |
| Nonperforming (1) | 985 | 14,255 | 791 | 141 | 385 | 16,557 |
| Total | $ 62,412 | $ 712,465 | $ 88,335 | $ 122,136 | $ 315,516 | $ 1,300,864 |

(1) A loan is considered nonperforming if it is 90 days or more past due and/or on nonaccrual.

In accordance with ASC 310-10-50-35, the total of consumer mortgage loans secured by real estate properties for which formal foreclosure proceedings are in process totaled $4.6 million at March 31, 2015 compared to $5.9 million at December 31, 2014.

A loan is considered impaired, in accordance with the impairment accounting guidance, when based on current information and events, it is probable CTBI will be unable to collect all amounts due from the borrower in accordance with the contractual terms of the loan. Impaired loans include nonperforming commercial loans but also include loans modified in troubled debt restructurings where concessions have been granted to borrowers experiencing financial difficulties. These concessions could include a reduction in the interest rate on the loan, payment extensions, forgiveness of principal, forbearance, or other actions intended to maximize collection.

The following tables present impaired loans, the average investment in impaired loans, and interest income recognized on impaired loans for the periods ended March 31, 2015, December 31, 2014, and March 31, 2014:

| | March 31, 2015 | | | | |
|---|---|---|---|---|---|
| (in thousands) | Recorded Balance | Unpaid Contractual Principal Balance | Specific Allowance | Average Investment in Impaired Loans | *Interest Income Recognized |
| Loans without a specific valuation allowance: | | | | | |
| Commercial construction | $ 5,280 | $ 5,280 | $ 0 | $ 5,297 | $ 51 |
| Commercial secured by real estate | 29,606 | 30,431 | 0 | 29,991 | 310 |
| Commercial other | 12,747 | 14,337 | 0 | 12,868 | 61 |
| Real estate mortgage | 900 | 900 | 0 | 902 | 12 |
| | | | | | |
| Loans with a specific valuation allowance: | | | | | |
| Commercial construction | 3,863 | 3,863 | 734 | 3,895 | 0 |
| Commercial secured by real estate | 3,222 | 3,650 | 869 | 3,440 | 1 |
| Commercial other | 846 | 970 | 184 | 859 | 0 |
| | | | | | |
| Totals: | | | | | |
| Commercial construction | 9,143 | 9,143 | 734 | 9,192 | 51 |
| Commercial secured by real estate | 32,828 | 34,081 | 869 | 33,431 | 311 |
| Commercial other | 13,593 | 15,307 | 184 | 13,727 | 61 |
| Real estate mortgage | 900 | 900 | 0 | 902 | 12 |
| Total | $ 56,464 | $ 59,431 | $ 1,787 | $ 57,252 | $ 435 |

| (in thousands) | December 31, 2014 Recorded Balance | Unpaid Contractual Principal Balance | Specific Allowance | Average Investment in Impaired Loans | *Interest Income Recognized |
|---|---|---|---|---|---|
| Loans without a specific valuation allowance: | | | | | |
| Commercial construction | $5,653 | $ 5,654 | $ 0 | $ 5,415 | $ 205 |
| Commercial secured by real estate | 31,639 | 33,268 | 0 | 34,650 | 1,180 |
| Commercial other | 13,069 | 14,597 | 0 | 15,663 | 783 |
| Real estate mortgage | 1,277 | 1,277 | 0 | 1,507 | 53 |
| Loans with a specific valuation allowance: | | | | | |
| Commercial construction | 3,974 | 3,974 | 734 | 4,216 | 0 |
| Commercial secured by real estate | 2,718 | 2,876 | 827 | 4,376 | 11 |
| Commercial other | 738 | 862 | 181 | 531 | 1 |
| Totals: | | | | | |
| Commercial construction | 9,627 | 9,628 | 734 | 9,631 | 205 |
| Commercial secured by real estate | 34,357 | 36,144 | 827 | 39,026 | 1,191 |
| Commercial other | 13,807 | 15,459 | 181 | 16,194 | 784 |
| Real estate mortgage | 1,277 | 1,277 | 0 | 1,507 | 53 |
| Total | $59,068 | $ 62,508 | $ 1,742 | $ 66,358 | $ 2,233 |

| (in thousands) | March 31, 2014 Recorded Balance | Unpaid Contractual Principal Balance | Specific Allowance | Average Investment in Impaired Loans | *Interest Income Recognized |
|---|---|---|---|---|---|
| Loans without a specific valuation allowance: | | | | | |
| Commercial construction | $5,430 | $ 5,431 | $ 0 | $ 5,441 | $ 50 |
| Commercial secured by real estate | 35,719 | 36,618 | 0 | 36,416 | 265 |
| Commercial other | 14,191 | 15,726 | 0 | 14,324 | 114 |
| Real estate mortgage | 1,021 | 1,021 | 0 | 1,022 | 10 |
| Loans with a specific valuation allowance: | | | | | |
| Commercial construction | 4,278 | 4,284 | 939 | 4,312 | 0 |
| Commercial secured by real estate | 4,234 | 4,611 | 1,084 | 4,686 | 4 |
| Commercial other | 413 | 536 | 112 | 439 | 0 |
| Totals: | | | | | |
| Commercial construction | 9,708 | 9,715 | 939 | 9,753 | 50 |
| Commercial secured by real estate | 39,953 | 41,229 | 1,084 | 41,102 | 269 |
| Commercial other | 14,604 | 16,262 | 112 | 14,763 | 114 |
| Real estate mortgage | 1,021 | 1,021 | 0 | 1,022 | 10 |
| Total | $65,286 | $ 68,227 | $ 2,135 | $ 66,640 | $ 443 |

*Cash basis interest is substantially the same as interest income recognized.

Included in certain loan categories of impaired loans are certain loans and leases that have been modified in a troubled debt restructuring, where economic concessions have been granted to borrowers who have experienced financial difficulties. These concessions typically result from our loss mitigation activities and could include reductions in the interest rate, payment extensions, forgiveness of principal, forbearance or other actions. Modifications of terms for our loans and their inclusion as troubled debt restructurings are based on individual facts and circumstances. Loan modifications that are included as troubled debt restructurings may involve either an increase or reduction of the interest rate, extension of the term of the loan, or deferral of principal and/or interest payments, regardless of the period of the modification. All of the loans identified as troubled debt restructuring were modified due to financial stress of the borrower. In order to determine if a borrower is experiencing financial difficulty, an evaluation is performed to determine the probability that the borrower will be in payment default on any of its debt in the foreseeable future without the modification. This evaluation is performed under CTBI's internal underwriting policy.

When we modify loans and leases in a troubled debt restructuring, we evaluate any possible impairment similar to other impaired loans based on the present value of expected future cash flows, discounted at the contractual interest rate of the original loan or lease agreement, or use the current fair value of the collateral, less selling costs for collateral dependent loans. If we determined that the value of the modified loan is less than the recorded investment in the loan (net of previous charge-offs, deferred loan fees or costs and unamortized premium or discount), impairment is recognized through an allowance estimate or a charge-off to the allowance. In periods subsequent to modification, we evaluate all troubled debt restructuring, including those that have payment defaults, for possible impairment and recognize impairment through the allowance.

During 2015, certain loans were modified in troubled debt restructurings, where economic concessions were granted to borrowers consisting of reductions in the interest rates, payment extensions, forgiveness of principal, and forbearances. Presented below, segregated by class of loans, are troubled debt restructurings that occurred during the three months ended March 31, 2015 and 2014 and the year ended December 31, 2014:

| | Three Months Ended March 31, 2015 | | | | |
|---|---|---|---|---|---|
| (in thousands) | Number of Loans | Term Modification | Rate Modification | Combination | Post-Modification Outstanding Balance |
| Commercial: | | | | | |
| Commercial secured by real estate | 4 | $ 290 | $ 0 | $ 0 | $ 290 |
| Commercial other | 2 | 36 | 0 | 0 | 36 |
| Total troubled debt restructurings | 6 | $ 326 | $ 0 | $ 0 | $ 326 |

| | Year Ended December 31, 2014 | | | | |
|---|---|---|---|---|---|
| (in thousands) | Number of Loans | Term Modification | Rate Modification | Combination | Post-Modification Outstanding Balance |
| Commercial: | | | | | |
| Commercial construction | 1 | $ 7 | $ 0 | $ 0 | $ 7 |
| Commercial secured by real estate | 11 | 5,707 | 0 | 68 | 5,775 |
| Commercial other | 8 | 1,268 | 0 | 0 | 1,268 |
| Residential: | | | | | |
| Real estate mortgage | 2 | 0 | 0 | 848 | 848 |
| Total troubled debt restructurings | 22 | $ 6,982 | $ 0 | $ 916 | $ 7,898 |

| | Three Months Ended March 31, 2014 | | | | |
|---|---|---|---|---|---|
| (in thousands) | Number of | Term Modification | Rate Modification | Combination | Post-Modification Outstanding |

| | Loans | | | | Balance |
|---|---|---|---|---|---|
| Commercial: | | | | | |
| Commercial secured by real estate | 2 | $ 126 | $ 0 | $ 0 | $ 126 |
| Commercial other | 2 | 41 | 0 | 0 | 41 |
| Total troubled debt restructurings | 4 | $ 167 | $ 0 | $ 0 | $ 167 |

No charge-offs have resulted from modifications for any of the presented periods.

Loans retain their accrual status at the time of their modification. As a result, if a loan is on nonaccrual at the time it is modified, it stays as nonaccrual, and if a loan is on accrual at the time of the modification, it generally stays on accrual. Commercial and consumer loans modified in a troubled debt restructuring are closely monitored for delinquency as an early indicator of possible future default. If loans modified in a troubled debt restructuring subsequently default, CTBI evaluates the loan for possible further impairment. The allowance for loan losses may be increased, adjustments may be made in the allocation of the allowance, or partial charge-offs may be taken to further write-down the carrying value of the loan. Presented below, segregated by class of loans, are loans that were modified as troubled debt restructurings within the past twelve months which have subsequently defaulted. CTBI generally considers a loan in default when it is 90 days or more past due or transferred to nonaccrual.

| (in thousands) | Three Months Ended March 31, 2015 | |
|---|---|---|
| | Number of Loans | Recorded Balance |
| Commercial: | | |
| Commercial construction | 0 | $ 0 |
| Commercial secured by real estate | 1 | 261 |
| Commercial other | 0 | 0 |
| Total defaulted restructured loans | 1 | $ 261 |

| (in thousands) | Three Months Ended March 31, 2014 | |
|---|---|---|
| | Number of Loans | Recorded Balance |
| Commercial: | | |
| Commercial construction | 0 | $ 0 |
| Commercial secured by real estate | 0 | 0 |
| Commercial other | 2 | 34 |
| Total defaulted restructured loans | 2 | $ 34 |

Note 5 – Allowance for Loan and Lease Losses

The following tables present the balance in the allowance for loan and lease losses ("ALLL") and the recorded investment in loans based on portfolio segment and impairment method as of March 31, 2015, December 31, 2014, and March 31, 2014:

| (in thousands) | March 31, 2015 Commercial Construction | Commercial Secured by Real Estate | Equipment Lease Financing | Commercial Other | Real Estate Construction | Real Estate Mortgage | Home Equity | Consumer Direct | Consumer Indirect | Total |
|---|---|---|---|---|---|---|---|---|---|---|
| Allowance for loan losses | | | | | | | | | | |
| Beginning balance | $2,896 | $13,618 | $119 | $4,263 | $534 | $6,094 | $756 | $1,574 | $4,593 | $34,447 |
| Provision charged to expense | (34) | 630 | 6 | 55 | 75 | 364 | 17 | 200 | 588 | 1,901 |
| Losses charged off | 1 | 433 | 0 | 441 | 90 | 438 | 42 | 357 | 834 | 2,636 |
| Recoveries | 3 | 45 | 0 | 248 | 0 | 10 | 11 | 104 | 473 | 894 |
| Ending balance | $2,864 | $13,860 | $125 | $4,125 | $519 | $6,030 | $742 | $1,521 | $4,820 | $34,606 |
| Ending balance: Individually evaluated for impairment | $734 | $869 | $0 | $184 | $0 | $0 | $0 | $0 | $0 | $1,787 |
| Collectively evaluated for impairment | $2,130 | $12,991 | $125 | $3,941 | $519 | $6,030 | $742 | $1,521 | $4,820 | $32,819 |
| Loans Ending balance: Individually evaluated for impairment | $9,143 | $32,828 | $0 | $13,593 | $0 | $900 | $0 | $0 | $0 | $56,464 |
| Collectively evaluated for impairment | $110,079 | $933,507 | $10,908 | $327,807 | $60,894 | $707,167 | $87,136 | $120,005 | $332,515 | $2,690,018 |

| (in thousands) | December 31, 2014 Commercial Construction | Commercial Secured by Real Estate | Equipment Lease Financing | Commercial Other | Real Estate Construction | Real Estate Mortgage | Home Equity | Consumer Direct | Consumer Indirect | Total |
|---|---|---|---|---|---|---|---|---|---|---|
| Allowance for loan | | | | | | | | | | |

| | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| losses | | | | | | | | | | |
| Beginning balance | $3,396 | $14,535 | $121 | $5,238 | $397 | $4,939 | $601 | $1,127 | $3,654 | $34,008 |
| Provision charged to expense | (513 ) | 941 | (2 ) | 1,545 | 258 | 2,173 | 265 | 1,207 | 2,881 | 8,755 |
| Losses charged off | 15 | 2,163 | 0 | 3,141 | 123 | 1,058 | 115 | 1,326 | 3,495 | 11,436 |
| Recoveries | 28 | 305 | 0 | 621 | 2 | 40 | 5 | 566 | 1,553 | 3,120 |
| Ending balance | $2,896 | $13,618 | $119 | $4,263 | $534 | $6,094 | $756 | $1,574 | $4,593 | $34,447 |
| Ending balance: Individually evaluated for impairment | $734 | $827 | $0 | $181 | $0 | $0 | $0 | $0 | $0 | $1,742 |
| Collectively evaluated for impairment | $2,162 | $12,791 | $119 | $4,082 | $534 | $6,094 | $756 | $1,574 | $4,593 | $32,705 |
| Loans Ending balance: Individually evaluated for impairment | $9,627 | $34,357 | $0 | $13,807 | $0 | $1,277 | $0 | $0 | $0 | $59,068 |
| Collectively evaluated for impairment | $112,315 | $914,269 | $10,344 | $338,241 | $62,412 | $711,188 | $88,335 | $122,136 | $315,516 | $2,674,756 |

| | March 31, 2014 | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| (in thousands) | Commercial Construction | Commercial Secured by Real Estate | Equipment Lease Financing | Commercial Other | Real Estate Construction | Real Estate Mortgage | Home Equity | Consumer Direct | Consumer Indirect | Total |
| Allowance for loan losses | | | | | | | | | | |
| Beginning balance | $3,396 | $14,535 | $121 | $5,238 | $397 | $4,939 | $601 | $1,127 | $3,654 | $34,008 |
| Provision charged to expense | (296 ) | (106 ) | (14 ) | (13 ) | 44 | 356 | 51 | 753 | 570 | 1,345 |
| Losses charged off | 0 | 322 | 0 | 633 | 0 | 164 | 27 | 453 | 946 | 2,545 |
| Recoveries | 7 | 76 | 0 | 162 | 1 | 12 | 1 | 146 | 402 | 807 |

| | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| Ending balance | $3,107 | $14,183 | $107 | $4,754 | $442 | $5,143 | $626 | $1,573 | $3,680 | $33,615 |
| Ending balance: Individually evaluated for impairment | $939 | $1,084 | $0 | $112 | $0 | $0 | $0 | $0 | $0 | $2,135 |
| Collectively evaluated for impairment | $2,168 | $13,099 | $107 | $4,642 | $442 | $5,143 | $626 | $1,573 | $3,680 | $31,480 |
| Loans Ending balance: Individually evaluated for impairment | $9,708 | $39,953 | $0 | $14,604 | $0 | $1,021 | $0 | $0 | $0 | $65,286 |
| Collectively evaluated for impairment | $101,564 | $834,484 | $8,122 | $337,044 | $59,730 | $694,493 | $84,694 | $117,497 | $282,594 | $2,520,222 |

Note 6 – Other Real Estate Owned

Activity for other real estate owned was as follows:

| (in thousands) | March 31, 2015 | March 31, 2014 |
|---|---|---|
| Beginning balance of other real estate owned | $36,776 | $39,188 |
| New assets acquired | 5,570 | 1,268 |
| Capitalized costs | 85 | 0 |
| Fair value adjustments | (64 ) | (874 ) |
| Sale of assets | (3,632 ) | (3,283 ) |
| Ending balance of other real estate owned | $38,735 | $36,299 |

Carrying costs and fair value adjustments associated with foreclosed properties for the three months ended March 31, 2015 and 2014 were $0.5 million and $1.5 million, respectively.

Note 7 – Earnings Per Share

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

| | Three Months Ended March 31 | |
|---|---|---|
| (in thousands except per share data) | 2015 | 2014 |

| | | |
|---|---|---|
| Numerator: | | |
| Net income | $10,938 | $10,140 |
| | | |
| Denominator: | | |
| Basic earnings per share: | | |
| Weighted average shares | 17,400 | 17,308 |
| Diluted earnings per share: | | |
| Effect of dilutive stock options and restricted stock grants | 51 | 95 |
| Adjusted weighted average shares | 17,451 | 17,403 |
| | | |
| Earnings per share: | | |
| Basic earnings per share | $0.63 | $0.59 |
| Diluted earnings per share | 0.63 | 0.58 |

Options to purchase 68,063 common shares at a weighted average price of $35.409 were excluded from the diluted calculations above for the three months ended March 31, 2015, because the exercise prices on the options were greater than the average market price for the period. In addition to in-the-money stock options, unvested restricted stock grants were also used in the calculation of diluted earnings per share based on the treasury method. There were no options to purchase common shares that were excluded from the diluted calculations above for the three months ended March 31, 2014.

Note 8 – Fair Market Value of Financial Assets and Liabilities

Fair Value Measurements

ASC 820, Fair Value Measurements, defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles and expands disclosures about fair value measurements. ASC 820 applies whenever other standards require (or permit) assets or liabilities to be measured at fair value but does not expand the use of fair value in any new circumstances. Fair value measurements must maximize the use of observable inputs and minimize the use of unobservable inputs. In this standard, the FASB clarifies the principle that fair value should be based on the assumptions market participants would use when pricing the asset or liability. In support of this principle, ASC 820 establishes a fair value hierarchy that prioritizes the information used to develop those assumptions. The fair value hierarchy is as follows:

Level 1 Inputs – Quoted prices in active markets for identical assets or liabilities.

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 and liabilities in active markets, and inputs other than quoted prices that are observable for the asset or liability, such as interest rates and yield curves that are observable at commonly quoted intervals.

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.

Recurring Measurements

The following tables present the fair value measurements of assets recognized in the accompanying balance sheets measured at fair value on a recurring basis as of March 31, 2015 and December 31, 2014 and indicate the level within the fair value hierarchy of the valuation techniques.

Fair Value Measurements at

| (in thousands) | Fair Value | March 31, 2015 Using Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
|---|---|---|---|---|
| Assets measured – recurring basis | | | | |
| Available-for-sale securities: | | | | |
| U.S. Treasury and government agencies | $ 186,714 | $ 498 | $ 186,216 | $ 0 |
| State and political subdivisions | 136,313 | 0 | 136,313 | 0 |
| U.S. government sponsored agency mortgage-backed securities | 278,188 | 0 | 278,188 | 0 |
| CRA investment funds | 25,120 | 25,120 | 0 | 0 |
| Mortgage servicing rights | 2,797 | 0 | 0 | 2,797 |

| (in thousands) | Fair Value | Fair Value Measurements at December 31, 2014 Using Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
|---|---|---|---|---|
| Assets measured – recurring basis | | | | |
| Available-for-sale securities: | | | | |
| U.S. Treasury and government agencies | $ 188,932 | $ 492 | $ 188,440 | $ 0 |
| State and political subdivisions | 137,458 | 0 | 137,458 | 0 |
| U.S. government sponsored agency mortgage-backed securities | 288,907 | 0 | 288,907 | 0 |
| CRA investment funds | 24,889 | 24,889 | 0 | 0 |
| Mortgage servicing rights | 2,968 | 0 | 0 | 2,968 |

Following is a description of the valuation methodologies and inputs used for assets measured at fair value on a recurring basis and recognized in the accompanying balance sheets, as well as the general classification of such assets pursuant to the valuation hierarchy. These valuation methodologies were applied to all of CTBI's financial assets carried at fair value. CTBI had no liabilities measured at fair value as of March 31, 2015 and December 31, 2014. There have been no significant changes in the valuation techniques during the quarter ended March 31, 2015. For assets classified within Level 3 of the fair value hierarchy, the process used to develop the reported fair value is described below.

Available-for-Sale Securities

Securities classified as available-for-sale are reported at fair value on a recurring basis. U.S. Treasury and government agencies and CTBI's CRA investment funds are classified as Level 1 of the valuation hierarchy where quoted market prices are available in the active market on which the individual securities are traded.

If quoted market prices are not available, CTBI obtains fair value measurements from an independent pricing service, such as Interactive Data, which utilizes pricing models to determine fair value measurement. CTBI reviews the pricing quarterly to verify the reasonableness of the pricing. The fair value measurements consider observable data that may include dealer quotes, market spreads, cash flows, the U.S. Treasury yield curve, live trading levels, trade execution data, market consensus prepayment speeds, credit information and the bond's terms and conditions, among other factors. U.S. Treasury and government agencies, state and political subdivisions, and U.S. government sponsored agency mortgage-backed securities are classified as Level 2 inputs.

In certain cases where Level 1 or Level 2 inputs are not available, securities are classified within Level 3 of the hierarchy. Fair value determinations for Level 3 measurements are estimated on a quarterly basis where assumptions used are reviewed to ensure the estimated fair value complies with accounting standards generally accepted in the United States. As of March 31, 2015, CTBI does not own any securities classified as Level 3 inputs.

Mortgage Servicing Rights

Mortgage servicing rights do not trade in an active, open market with readily observable prices. CTBI reports mortgage servicing rights at fair value on a recurring basis with subsequent remeasurement of MSRs based on change in fair value.

In determining fair value, CTBI utilizes the expertise of an independent third party. Accordingly, fair value is determined by the independent third party by utilizing assumptions about factors such as mortgage interest rates, discount rates, mortgage loan prepayment speeds, market trends and industry demand. Due to the nature of the valuation inputs, mortgage servicing rights are classified within Level 3 of the hierarchy. Fair value determinations for Level 3 measurements of mortgage servicing rights are tested for impairment on a quarterly basis where assumptions used are reviewed to ensure the estimated fair value complies with accounting standards generally accepted in the United States. See the table below for inputs and valuation techniques used for Level 3 mortgage servicing rights.

Transfers between Levels

There were no transfers between Levels 1, 2, and 3 as of March 31, 2015.

Level 3 Reconciliation

Following is a reconciliation of the beginning and ending balances of recurring fair value measurements recognized in the accompanying balance sheet using significant unobservable (Level 3) inputs for the three months ended March 31, 2015 and 2014:

| (in thousands) | Three Months Ended March 31, 2015 Mortgage Servicing Rights |
|---|---|
| Beginning balance | $ 2,968 |
| Total recognized losses | |
| Included in net income | (161 ) |

| | |
|---|---|
| Issues | 84 |
| Settlements | (94 ) |
| Ending balance | $ 2,797 |
| Total losses for the period included in net income attributable to the change in unrealized gains or losses related to assets still held at the reporting date | $ (161 ) |

| (in thousands) | Three Months Ended March 31, 2014 Mortgage Servicing Rights |
|---|---|
| Beginning balance | $ 3,424 |
| Total recognized losses | |
| Included in net income | (126 ) |
| Issues | 63 |
| Settlements | (103 ) |
| Ending balance | $ 3,258 |
| Total losses for the period included in net income attributable to the change in unrealized gains or losses related to assets still held at the reporting date | $ (126 ) |

Realized and unrealized gains and losses for items reflected in the tables above are included in net income in the consolidated statements of income as follows:

| (in thousands) | Three Months Ended March 31, 2015 | |
|---|---|---|
| | Noninterest Income | Noninterest Expense |
| Total losses | $ (255 ) | $ 0 |

| (in thousands) | Three Months Ended March 31, 2014 | |
|---|---|---|
| | Noninterest Income | Noninterest Expense |
| Total losses | $ (229 ) | $ 0 |

Nonrecurring Measurements

The following tables present the fair value measurements of assets recognized in the accompanying balance sheets measured at fair value on a nonrecurring basis as of March 31, 2015 and December 31, 2014 and indicate the level within the fair value hierarchy of the valuation techniques.

| (in thousands) | Fair Value Measurements at March 31, 2015 Using |
|---|---|

| | Fair Value | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
|---|---|---|---|---|
| Assets measured – nonrecurring basis | | | | |
| Impaired loans (collateral dependent) | $2,760 | $0 | $ 0 | $ 2,760 |
| Other real estate/assets owned | 265 | 0 | 0 | 265 |

| | | Fair Value Measurements at December 31, 2014 Using | | |
|---|---|---|---|---|
| (in thousands) | Fair Value | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
| Assets measured – nonrecurring basis | | | | |
| Impaired loans (collateral dependent) | $4,665 | $0 | $ 0 | $ 4,665 |
| Other real estate/assets owned | 6,472 | 0 | 0 | 6,472 |

Following is a description of the valuation methodologies and inputs used for assets measured at fair value on a nonrecurring basis and recognized in the accompanying balance sheet, as well as the general classification of such assets pursuant to the valuation hierarchy.  For assets classified within Level 3 of the fair value hierarchy, the process used to develop the reported fair value is described below.

Impaired Loans (Collateral Dependent)

The estimated fair value of collateral-dependent impaired loans is based on the appraised fair value of the collateral, less estimated cost to sell.  Collateral-dependent impaired loans are classified within Level 3 of the fair value hierarchy.

CTBI considers the appraisal or evaluation as the starting point for determining fair value and then considers other factors and events in the environment that may affect the fair value.  Appraisals of the collateral underlying collateral-dependent loans are obtained when the loan is determined to be collateral-dependent and subsequently as deemed necessary by the Chief Credit Officer.  Appraisals are reviewed for accuracy and consistency by the Chief Credit Officer.  Appraisers are selected from the list of approved appraisers maintained by management.  The appraised values are reduced by discounts to consider lack of marketability and estimated cost to sell if repayment or satisfaction of the loan is dependent on the sale of the collateral.  These discounts and estimates are developed by the Chief Credit Officer by comparison to historical results.

Loans considered impaired under ASC 310-35, Impairment of a Loan, are loans for which, based on current information and events, it is probable that the creditor will be unable to collect all amounts due according to the contractual terms of the loan agreement. Impaired loans are subject to nonrecurring fair value adjustments to reflect subsequent (i) partial write-downs that are based on the observable market price or current appraised value of the collateral or (ii) the full charge-off of the loan carrying value. Quarter-to-date fair value adjustments on impaired loans disclosed above were $0.5 million, $0.3 million, and $0.2 million for the quarters ended March 31, 2015, December 31, 2014, and March 31, 2014, respectively.

Other Real Estate Owned

In accordance with the provisions of ASC 360, Property, Plant, and Equipment, other real estate owned (OREO) is carried at the lower of fair value at acquisition date or current estimated fair value, less estimated cost to sell when the real estate is acquired. Estimated fair value of OREO is based on appraisals or evaluations. OREO is classified within Level 3 of the fair value hierarchy. Long-lived assets are subject to nonrecurring fair value adjustments to reflect subsequent partial write-downs that are based on the observable market price or current appraised value of the collateral. Quarter-to-date fair value adjustments on other real estate/assets owned were $0.05 million, $1.5 million, and $0.8 million for the quarters ended March 31, 2015, December 31, 2014, and March 31, 2014, respectively.

Our policy for determining the frequency of periodic reviews is based upon consideration of the specific properties and the known or perceived market fluctuations in a particular market and is typically between 12 and 18 months but generally not more than 24 months. Appraisers are selected from the list of approved appraisers maintained by management.

Unobservable (Level 3) Inputs

The following tables present quantitative information about unobservable inputs used in recurring and nonrecurring Level 3 fair value measurements at March 31, 2015 and December 31, 2014.

| (in thousands) | Quantitative Information about Level 3 Fair Value Measurements | | | |
|---|---|---|---|---|
| | Fair Value at March 31, 2015 | Valuation Technique(s) | Unobservable Input | Range (Weighted Average) |
| Mortgage servicing rights | $2,797 | Discount cash flows, computer pricing model | Constant prepayment rate | 4.7% - 25.4% (12.10%) |
| | | | Probability of default | 0.0% - 100.0% (3.50%) |
| | | | Discount rate | Not applicable, (10.13%) |
| Impaired loans (collateral-dependent) | $2,760 | Market comparable properties | Marketability discount | 5.0% - 10.0% (7.0%) |
| Other real estate/assets owned | $265 | Market comparable properties | Comparability adjustments | 5.0% - 93.0% (29.57%) |

| (in thousands) | Quantitative Information about Level 3 Fair Value Measurements |
|---|---|

| | Fair Value at December 31, 2014 | Valuation Technique(s) | Unobservable Input | Range (Weighted Average) |
|---|---|---|---|---|
| Mortgage servicing rights | $2,968 | Discount cash flows, computer pricing model | Constant prepayment rate | 4.6% - 25.1% (11.3%) |
| | | | Probability of default | 0.0% - 100.0% (3.61%) |
| | | | Discount rate | 10.0% - 11.5% (10.1%) |
| Impaired loans (collateral-dependent) | $4,665 | Market comparable properties | Marketability discount | 5.0% - 10.0% (7.0%) |
| Other real estate/assets owned | $6,472 | Market comparable properties | Comparability adjustments | 3.0% - 67.0% (18.0%) |

Sensitivity of Significant Unobservable Inputs

The following is a discussion of the sensitivity of significant unobservable inputs, the interrelationships between those inputs and other unobservable inputs used in recurring fair value measurement and of how those inputs might magnify or mitigate the effect of changes in the unobservable inputs on the fair value measurement.

Mortgage Servicing Rights

Market value for mortgage servicing rights is derived based on unobservable inputs, such as prepayment speeds of the underlying loans generated using the Andrew Davidson Prepayment Model, FHLMC/FNMA guidelines, the weighted-average life of the loan, the discount rate, the weighted average coupon, and the weighted average default rate.  Significant increases (decreases) in either of those inputs in isolation would result in a significantly lower (higher) fair value measurement.  Generally, a change in the assumption used for prepayment speeds is accompanied by a directionally opposite change in the assumption for interest rates.

Fair Value of Financial Instruments

The following table presents estimated fair value of CTBI's financial instruments as of March 31, 2015 and indicates the level within the fair value hierarchy of the valuation techniques.

| | | Fair Value Measurements at March 31, 2015 Using | | |
|---|---|---|---|---|
| (in thousands) | Carrying Amount | Quoted Prices in Active Markets for | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |

| | | | | |
|---|---|---|---|---|
| | | Identical Assets (Level 1) | | |
| Financial assets: | | | | |
| Cash and cash equivalents | $141,049 | $141,049 | $0 | $ 0 |
| Certificates of deposit in other banks | 6,665 | 0 | 6,680 | 0 |
| Securities available-for-sale | 626,335 | 25,618 | 600,717 | 0 |
| Securities held-to-maturity | 1,661 | 0 | 1,653 | 0 |
| Loans held for sale | 1,505 | 1,535 | 0 | 0 |
| Loans, net | 2,711,876 | 0 | 0 | 2,710,825 |
| Federal Home Loan Bank stock | 17,927 | 0 | 17,927 | 0 |
| Federal Reserve Bank stock | 4,887 | 0 | 4,887 | 0 |
| Accrued interest receivable | 13,543 | 0 | 13,543 | 0 |
| Mortgage servicing rights | 2,797 | 0 | 0 | 2,797 |
| | | | | |
| Financial liabilities: | | | | |
| Deposits | $2,939,540 | $704,150 | $2,231,379 | $ 0 |
| Repurchase agreements | 244,570 | 0 | 0 | 244,855 |
| Federal funds purchased | 12,041 | 0 | 12,041 | 0 |
| Advances from Federal Home Loan Bank | 1,141 | 0 | 1,318 | 0 |
| Long-term debt | 61,341 | 0 | 0 | 35,674 |
| Accrued interest payable | 1,021 | 0 | 1,021 | 0 |
| | | | | |
| Unrecognized financial instruments: | | | | |
| Letters of credit | $0 | $0 | $0 | $ 0 |
| Commitments to extend credit | 0 | 0 | 0 | 0 |
| Forward sale commitments | 0 | 0 | 0 | 0 |

The following table presents estimated fair value of CTBI's financial instruments as of December 31, 2014 and indicates the level within the fair value hierarchy of the valuation techniques.

| (in thousands) | | Fair Value Measurements at December 31, 2014 Using | | |
|---|---|---|---|---|
| | Carrying Amount | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
| Financial assets: | | | | |
| Cash and cash equivalents | $105,517 | $105,517 | $0 | $ 0 |
| Certificates of deposit in other banks | 8,197 | 0 | 8,213 | 0 |
| Securities available-for-sale | 640,186 | 25,381 | 614,805 | 0 |
| Securities held-to-maturity | 1,662 | 0 | 1,644 | 0 |
| Loans held for sale | 2,264 | 2,321 | 0 | 0 |
| Loans, net | 2,699,377 | 0 | 0 | 2,691,906 |
| Federal Home Loan Bank stock | 17,927 | 0 | 17,927 | 0 |
| Federal Reserve Bank stock | 4,869 | 0 | 4,869 | 0 |
| Accrued interest receivable | 13,548 | 0 | 13,548 | 0 |

| | | | | |
|---|---|---|---|---|
| Mortgage servicing rights | 2,968 | 0 | 0 | 2,968 |
| | | | | |
| Financial liabilities: | | | | |
| Deposits | $2,874,257 | $677,626 | $2,192,848 | $ 0 |
| Repurchase agreements | 235,186 | 0 | 0 | 235,193 |
| Federal funds purchased | 11,041 | 0 | 11,041 | 0 |
| Advances from Federal Home Loan Bank | 61,170 | 0 | 61,106 | 0 |
| Long-term debt | 61,341 | 0 | 0 | 35,615 |
| Accrued interest payable | 908 | 0 | 908 | 0 |
| | | | | |
| Unrecognized financial instruments: | | | | |
| Letters of credit | $0 | $0 | $0 | $ 0 |
| Commitments to extend credit | 0 | 0 | 0 | 0 |
| Forward sale commitments | 0 | 0 | 0 | 0 |

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

Cash and cash equivalents – The carrying amount approximates fair value.

Certificates of deposit in other banks – Fair values are based on quoted market prices or dealer quotes for similar instruments.

Securities held-to-maturity – Fair values are based on quoted market prices, if available. If a quoted price is not available, fair value is estimated using quoted prices for similar securities. The fair value estimate is provided to management from a third party using modeling assumptions specific to each type of security that are reviewed and approved by management. Quarterly sampling of fair values provided by additional third parties supplement the fair value review process.

Loans held for sale – The fair value is predetermined at origination based on sale price.

Loans (net of the allowance for loan and lease losses) – The fair value of fixed rate loans and variable rate mortgage loans is estimated by discounting the future cash flows using current rates at which similar loans would be made to borrowers with similar credit ratings and for the same remaining maturities. For other variable rate loans, the carrying amount approximates fair value.

Federal Home Loan Bank stock – The carrying value of Federal Home Loan Bank stock approximates fair value based on the redemption provisions of the Federal Home Loan Bank.

Federal Reserve Bank stock – The carrying value of Federal Reserve Bank stock approximates fair value based on the redemption provisions of the Federal Reserve Bank.

Accrued interest receivable – The carrying amount approximates fair value.

Deposits – The fair value of fixed maturity time deposits is estimated by discounting the future cash flows using the rates currently offered for deposits of similar remaining maturities. For deposits including demand deposits, savings accounts, NOW accounts, and certain money market accounts, the carrying value approximates fair value.

Repurchase agreements – The fair value is estimated by discounting future cash flows using current rates.

Federal funds purchased – The carrying amount approximates fair value.

Advances from Federal Home Loan Bank – The fair value of these fixed-maturity advances is estimated by discounting future cash flows using rates currently offered for advances of similar remaining maturities.

Long-term debt – The fair value is estimated by discounting future cash flows using current rates.

Accrued interest payable – The carrying amount approximates fair value.

Commitments to originate loans, forward sale commitments, letters of credit, and lines of credit – The fair value of commitments to originate loans is estimated using the fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the present creditworthiness of the counterparties. For fixed-rate loan commitments, fair value also considers the difference between current levels of interest rates and the committed rates. The fair value of forward sale commitments is estimated based on current market prices for loans of similar terms and credit quality. The fair values of letters of credit and lines of credit are based on fees currently charged for similar agreements or on the estimated cost to terminate or otherwise settle the obligations with the counterparties at the reporting date. The fair values of these commitments are not material.

Note 9 – Accumulated Other Comprehensive Income

Unrealized gains (losses) on AFS securities

Amounts reclassified from accumulated other comprehensive income (AOCI) and the affected line items in the statements of income during the three months ended March 31, 2015 and 2014 were:

| (in thousands) | Amounts Reclassified from AOCI Three Months Ended March 31 | |
|---|---|---|
| | 2015 | 2014 |
| Affected line item in the statements of income | | |
| Securities gains (losses) | $ 144 | $ (60 ) |
| Tax expense (benefit) | 50 | (21 ) |
| Total reclassifications out of AOCI | $ 94 | $ (39 ) |

Item 2. Management's Discussion and Analysis of Financial Condition
and Results of Operations

Overview

The following Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD&A") is intended to help the reader understand Community Trust Bancorp, Inc., our operations, and our present business environment. The MD&A is provided as a supplement to – and should be read in conjunction with – our condensed consolidated financial statements and the accompanying notes contained in this quarterly report. The MD&A includes the following sections:

v Our Business

v Results of Operations and Financial Condition

v Dividends

v Liquidity and Market Risk

v Interest Rate Risk

v Capital Resources

v Impact of Inflation, Changing Prices, and Economic Conditions

v Stock Repurchase Program

v Critical Accounting Policies and Estimates

Our Business

Community Trust Bancorp, Inc. ("CTBI") is a bank holding company headquartered in Pikeville, Kentucky. Currently, we own one commercial bank and one trust company. Through our subsidiaries, we have eighty-one banking locations in eastern, northeastern, central, and south central Kentucky, southern West Virginia, and northeastern Tennessee, four trust offices across Kentucky, and one trust office in northeastern Tennessee. At March 31, 2015, we had total consolidated assets of $3.8 billion and total consolidated deposits, including repurchase agreements, of $3.2 billion. Total shareholders' equity at March 31, 2015 was $457.4 million. Trust assets under management at March 31, 2015 were $2.0 billion.

Through its subsidiaries, CTBI engages in a wide range of commercial and personal banking and trust and wealth management activities, which include accepting time and demand deposits; making secured and unsecured loans to corporations, individuals and others; providing cash management services to corporate and individual customers; issuing letters of credit; renting safe deposit boxes; and providing funds transfer services. The lending activities of CTB include making commercial, construction, mortgage, and personal loans. Lease-financing, lines of credit, revolving lines of credit, term loans, and other specialized loans, including asset-based financing, are also available. Our corporate subsidiaries act as trustees of personal trusts, as executors of estates, as trustees for employee benefit trusts, as registrars, transfer agents, and paying agents for bond and stock issues, as investment agent, as depositories for securities, and as providers of full service brokerage and insurance services. For further information, see Item 1 of our annual report on Form 10-K for the year ended December 31, 2014.

Results of Operations and Financial Condition

For the quarter ended March 31, 2015, we reported earnings of $10.9 million, or $0.63 per basic share, compared to $10.1 million, or $0.59 per basic share, earned during the first quarter 2014 and $10.0 million, or $0.58 per basic share, earned during the fourth quarter 2014.

Income Statement Review

| (dollars in thousands) | | | Change 2015 vs. 2014 | |
|---|---|---|---|---|
| Three Months Ended March 31 | 2015 | 2014 | Amount | Percent |
| Net interest income | $32,905 | $32,750 | $155 | 0.5 % |
| Provision for loan losses | 1,901 | 1,345 | 556 | 41.3 |
| Noninterest income | 10,736 | 10,065 | 671 | 6.7 |
| Noninterest expense | 25,818 | 26,861 | (1,043 ) | (3.9 ) |
| Income taxes | 4,984 | 4,469 | 515 | 11.5 |
| Net income | $10,938 | $10,140 | $798 | 7.9 % |
| | | | | |
| Average earning assets | $3,480,600 | $3,389,490 | $91,110 | 2.7 % |
| | | | | |
| Yield on average earnings assets | 4.22 % | 4.32 % | (0.10 )% | (2.4 )% |
| Cost of interest bearing funds | 0.45 % | 0.47 % | (0.02 )% | (4.7 )% |
| | | | | |
| Net interest margin | 3.89 % | 3.97 % | (0.08 )% | (2.0 )% |

Net Interest Income

Net interest income for the quarter increased $0.2 million, or 0.5%, from prior year first quarter but decreased $0.6 million, or 1.8%, from prior quarter, while our net interest margin decreased 8 basis points and 1 basis point during the respective time periods. Average earning assets increased $91.1 million, or 2.7%, from first quarter 2014 and $20.9 million, or 0.6%, from prior quarter, while our yield on average earning assets decreased 10 basis points and 1 basis point, respectively, during these time periods. The cost of interest bearing funds decreased 2 basis points from prior year same quarter but remained flat to prior quarter. Our average loans to deposits, including repurchase agreements, for the quarter ended March 31, 2015 were 86.6% compared to 83.4% for the quarter ended March 31, 2014 and 86.1% for the quarter ended December 31, 2014.

Provision for Loan Losses

The provision for loan losses that was added to the allowance for the first quarter 2015 was $1.9 million compared to $1.3 million in the first quarter 2014 and $3.4 million for the quarter ended December 31, 2014. This provision represented a charge against current earnings in order to maintain the allowance at an appropriate level determined using the accounting estimates described in the Critical Accounting Policies and Estimates section. Our provision decreased from prior quarter as net charge-offs decreased and loan growth slowed in comparison to the fourth quarter 2014. Our reserve coverage (allowance for loan and lease loss reserve to nonperforming loans) at March 31, 2015 was 98.7% compared to 79.2% at March 31, 2014 and 88.4% at December 31, 2014. Our loan loss reserve as a percentage of total loans outstanding remained at 1.26% from December 31, 2014, a decrease from the 1.30% at March 31, 2014.

Noninterest Income

Noninterest income for the quarter ended March 31, 2015 increased $0.7 million, or 6.7%, from prior year same quarter but decreased $1.3 million, or 10.8%, from prior quarter. Year over year, we experienced increases in gains on sales of loans of $0.1 million, deposit service charges of $0.2 million, trust revenue of $0.1 million, and loan related fees of $0.2 million. However, all of these areas experienced declines quarter over quarter. Gains on sales of loans decreased $0.4 million, deposit service charges decreased $0.6 million, trust revenue decreased $0.1 million, and loan related fees decreased $0.1 million. The decrease in deposit service charges quarter over quarter was primarily seasonal as we had a fewer number of days along with substantial inclement weather in the first quarter 2015. The decline in brokerage revenue for the quarter was primarily a result of reclassifying life insurance commissions earned through our trust subsidiary from brokerage revenue in the first quarter 2015 and going forward. Insurance commissions received during the first quarter 2015 from our trust subsidiary totaled $0.2 million. We had securities gains for the quarter ended March 31, 2015 of $0.1 million in comparison to losses of $0.1 million in both the first and fourth quarters of 2014.

Noninterest Expense

Noninterest expense for the quarter ended March 31, 2015 decreased $1.0 million, or 3.9%, from prior year first quarter and $2.2 million, or 7.9%, from prior quarter. The quarterly decrease was primarily the result of a $0.7 million decrease in personnel expense, a $0.5 million decrease in net other real estate owned expense, and a $0.3 million decrease in repossession expense, along with a decrease in other direct expenses due to a $0.5 million accrual booked in the fourth quarter 2014 for anticipated customer refunds. The decrease in personnel expense consisted of a $0.7 million decrease in our group medical and life insurance. The year over year decrease was primarily due to a $1.0 million decrease in net other real estate owned expense.

Balance Sheet Review

CTBI's total assets at $3.8 billion increased $35.6 million, or an annualized 3.9%, from December 31, 2014 and $90.8 million, or 2.5%, from March 31, 2014. Loans outstanding at March 31, 2015 were $2.7 billion, increasing $12.7 million, or an annualized 1.9%, from December 31, 2014 and $161.0 million, or 6.2%, from March 31, 2014. We experienced growth during the quarter of $4.9 million in the commercial loan portfolio and $17.0 million in the indirect loan portfolio, partially offset by decreases of $7.1 million in the residential loan portfolio and $2.1 million in the consumer direct loan portfolio. CTBI's investment portfolio decreased $13.9 million, or an annualized 8.8%, from December 31, 2014 and $23.8 million, or 3.7%, from March 31, 2014. The decline in the investment portfolio was primarily from scheduled cash flows retained to provide additional liquidity. Deposits, including repurchase agreements, at $3.2 billion increased $74.7 million, or an annualized 9.7%, from December 31, 2014 and $42.3 million, or 1.3%, from March 31, 2014. Our deposits in other banks increased $30.7 million during the quarter as deposit growth outpaced loan growth.

Shareholders' equity at March 31, 2015 was $457.4 million compared to $447.9 million at December 31, 2014 and $422.0 million at March 31, 2014. Our tangible common equity/tangible assets ratio increased to 10.60%.

Loans

| (in thousands) | March 31, 2015 | | | | |
|---|---|---|---|---|---|
| Loan Category | Balance | Variance from Prior Year-End | Net Charge-Offs | Nonperforming | ALLL |
| Commercial: | | | | | |
| Construction | $119,222 | (2.2)% | $ (2) | $ 5,764 | $2,864 |
| Secured by real estate | 966,335 | 1.9 | 388 | 10,394 | 13,860 |
| Equipment lease financing | 10,908 | 5.5 | 0 | 0 | 125 |
| Commercial other | 341,400 | (3.0) | 193 | 4,589 | 4,125 |

| | | | | | |
|---|---|---|---|---|---|
| Total commercial | 1,437,865 | 0.3 | 579 | 20,747 | 20,974 |
| | | | | | |
| Residential: | | | | | |
| Real estate construction | 60,894 | (2.4 ) | 90 | 792 | 519 |
| Real estate mortgage | 708,067 | (0.6 ) | 428 | 12,665 | 6,030 |
| Home equity | 87,136 | (1.4 ) | 31 | 526 | 742 |
| Total residential | 856,097 | (0.8 ) | 549 | 13,983 | 7,291 |
| | | | | | |
| Consumer: | | | | | |
| Consumer direct | 120,005 | (1.7 ) | 253 | 163 | 1,521 |
| Consumer indirect | 332,515 | 5.4 | 361 | 169 | 4,820 |
| Total consumer | 452,520 | 3.4 | 614 | 332 | 6,341 |
| | | | | | |
| Total loans | $2,746,482 | 0.5 % | $ 1,742 | $ 35,062 | $34,606 |

Asset Quality

CTBI's total nonperforming loans were $35.1 million at March 31, 2015, a 10.0% decrease from the $39.0 million at December 31, 2014 and a 17.4% decrease from the $42.4 million at March 31, 2014. Nonaccrual loans decreased $3.7 million for the quarter and loans 90+ days past due decreased $0.2 million. Loans 30-89 days past due at $17.8 million was an increase of $2.7 million from December 31, 2014. The increase in 30-89 days past due was primarily in the commercial loan portfolio; however, it was not isolated to any one market or industry. Our loan portfolio management processes focus on the immediate identification, management, and resolution of problem loans to maximize recovery and minimize loss. Our loan risk management processes include weekly delinquent loan review meetings at the market levels and monthly delinquent loan review meetings involving senior corporate management to review all nonaccrual loans and loans 30 days or more past due. Any activity regarding a criticized/classified loan (i.e. problem loan) must be approved by CTB's Watch List Asset Committee (i.e. Problem Loan Committee). CTB's Watch List Asset Committee also meets on a quarterly basis and reviews every criticized/classified loan of $100,000 or greater. We also have a Loan Review Department that reviews every market within CTB annually and performs extensive testing of the loan portfolio to assure the accuracy of loan grades and classifications for delinquency, troubled debt restructuring, impaired status, impairment, nonaccrual status, and adequate loan loss reserves.

Impaired loans, loans not expected to meet contractual principal and interest payments other than insignificant delays, at March 31, 2015 totaled $56.5 million, a $2.6 million decline from the $59.1 million at December 31, 2014 and an $8.8 million decline from the $65.3 million at March 31, 2014. Included in certain loan categories of impaired loans are troubled debt restructurings that were classified as impaired. At March 31, 2015, CTBI had $23.6 million in commercial loans secured by real estate, $7.0 million in commercial real estate construction loans, $9.2 million in commercial other loans, and $0.9 million in real estate mortgage loans that were modified in troubled debt restructurings and impaired. Management evaluates all impaired loans for impairment and records a direct charge-off or provides specific reserves when necessary.

For further information regarding nonperforming and impaired loans, see note 4 to the condensed consolidated financial statements.

CTBI generally does not offer high risk loans such as option ARM products, high loan to value ratio mortgages, interest-only loans, loans with initial teaser rates, or loans with negative amortizations, and therefore, CTBI would have no significant exposure to these products.

Net loan charge-offs for the quarter ended March 31, 2015 were $1.7 million, or 0.26% of average loans annualized, compared to $3.0 million, or 0.44%, for the fourth quarter 2014 and $1.7 million, or 0.27%, experienced for the first quarter 2014. Of the net charge-offs for the quarter, $0.6 million were in commercial loans, $0.4 million were in indirect auto loans, and $0.5 million were in residential real estate mortgage loans.

Our level of foreclosed properties at $38.7 million at March 31, 2015 was an increase from $36.8 million at December 31, 2014 and $36.3 million at March 31, 2014. The $1.9 million increase for the quarter included an additional $2.2 million in income producing commercial real estate which was put on nonaccrual in the first quarter 2014. Sales of foreclosed properties for the quarter ended March 31, 2015 totaled $3.6 million while new foreclosed properties totaled $5.6 million. At March 31, 2015, the book value of properties under contracts to sell was $4.5 million; however, the closings had not occurred at quarter-end.

When foreclosed properties are acquired, appraisals are obtained and the properties are booked at the current market value less expected sales costs. Additionally, periodic updated appraisals are obtained on unsold foreclosed properties. When an updated appraisal reflects a market value below the current book value, a charge is booked to current earnings to reduce the property to its new market value less expected sales costs. Charges to earnings in the first quarter 2015 to reflect the decrease in current market values of foreclosed properties totaled $64 thousand. There were seven properties appraised during the first quarter 2015. Of these, one property was written down by a total of $6 thousand. Charges during the quarters ended March 31, 2014 and December 31, 2014 were $0.9 million and $0.3 million, respectively. Our policy for determining the frequency of periodic reviews is based upon consideration of the specific properties and the known or perceived market fluctuations in a particular market and is typically between 12 and 18 months but generally not more than 24 months. Approximately sixty-eight percent of our OREO properties have been reappraised within the past 12 months. Management anticipates that our foreclosed properties will remain elevated as we work through current market conditions.

The major classifications of foreclosed properties are shown in the following table:

| (in thousands) | March 31, 2015 | December 31, 2014 |
|---|---|---|
| 1-4 family | $9,642 | $ 10,337 |
| Agricultural/farmland | 116 | 116 |
| Construction/land development/other | 18,702 | 18,735 |
| Multifamily | 1,289 | 1,289 |
| Non-farm/non-residential | 8,986 | 6,299 |
| Total foreclosed properties | $38,735 | $ 36,776 |

The appraisal aging analysis of foreclosed properties, as well as the holding period, at March 31, 2015 is shown below:

(in thousands)

| Appraisal Aging Analysis | | Holding Period Analysis | |
|---|---|---|---|
| Days Since Last Appraisal | Current Book Value | Holding Period | Current Book Value |
| Up to 3 months | $2,739 | Less than one year | $12,264 |
| 3 to 6 months | 6,395 | 1 to 2 years | 3,112 |
| 6 to 9 months | 3,823 | 2 to 3 years | 2,368 |
| 9 to 12 months | 13,468 | 3 to 4 years | 11,454 |
| 12 to 24 months | 12,001 | 4 to 5 years | 3,258 |
| Over 24 months | 309 | Over 5 years* | 6,279 |
| Total | $38,735 | Total | $38,735 |

*Regulatory approval is required and has been obtained to hold these properties beyond the initial period of 5 years. Additional approval may be required to continue to hold these properties should they not be liquidated during the extension period.

Dividends

The following schedule shows the quarterly cash dividends paid for the past six quarters:

| Pay Date | Record Date | Amount Per Share |
|---|---|---|
| April 1, 2015 | March 15, 2015 | $ 0.300 |
| January 1, 2015 | December 15, 2014 | $ 0.300 |
| October 1, 2014 | September 15, 2014 | $ 0.300 |
| July 1, 2014 | June 15, 2014 | $ 0.290 |
| April 1, 2014 | March 15, 2014 | $ 0.291 |
| January 1, 2014 | December 15, 2013 | $ 0.291 |

The Board of Directors of CTBI declared a quarterly cash dividend of $0.30 per share to be paid on July 1, 2015 to shareholders of record on June 15, 2015.

Liquidity and Market Risk

The objective of CTBI's Asset/Liability management function is to maintain consistent growth in net interest income within our policy limits. This objective is accomplished through management of our consolidated balance sheet composition, liquidity, and interest rate risk exposures arising from changing economic conditions, interest rates, and customer preferences. The goal of liquidity management is to provide adequate funds to meet changes in loan and lease demand or deposit withdrawals. This is accomplished by maintaining liquid assets in the form of cash and cash equivalents and investment securities, sufficient unused borrowing capacity, and growth in core deposits. As of March 31, 2015, we had approximately $141.0 million in cash and cash equivalents and approximately $626.3 million in securities valued at estimated fair value designated as available-for-sale and available to meet liquidity needs on a continuing basis compared to $105.5 million and $640.2 million at December 31, 2014. Additional asset-driven liquidity is provided by the remainder of the securities portfolio and the repayment of loans. In addition to core deposit funding, we also have a variety of other short-term and long-term funding sources available. We also rely on Federal Home Loan Bank advances for both liquidity and management of our asset/liability position. Federal Home Loan Bank advances were $1.1 million at March 31, 2015 compared to $61.2 million at December 31, 2014. As of March 31, 2015, we had a $375 million available borrowing position with the Federal Home Loan Bank compared to $312.3 million at December 31, 2014. We generally rely upon net inflows of cash from financing activities, supplemented by net inflows of cash from operating activities, to provide cash for our investing activities. As is typical of many financial institutions, significant financing activities include deposit gathering, use of short-term borrowing facilities such as repurchase agreements and federal funds purchased, and issuance of long-term debt. At March 31, 2015 and December 31, 2014, we had $44 million in lines of credit with various correspondent banks available to meet any future cash needs. Our primary investing activities include purchases of securities and loan originations. We do not rely on any one source of liquidity and manage availability in response to changing consolidated balance sheet needs. At March 31, 2015, federal funds sold were $3.2 million compared to $4.9 million at December 31, 2014, and deposits with the Federal Reserve were $73.0 million compared to $40.9 million at December 31, 2014. Additionally, we project cash flows from our investment portfolio to generate additional liquidity over the next 90 days.

The investment portfolio consists of investment grade short-term issues suitable for bank investments. The majority of the investment portfolio is in U.S. government and government sponsored agency issuances. The average life of the portfolio is 3.51 years. At March 31, 2015, available-for-sale ("AFS") securities comprised approximately 99.7% of the total investment portfolio, and the AFS portfolio was approximately 137% of equity capital. Ninety percent of the pledge eligible portfolio was pledged.

Interest Rate Risk

We consider interest rate risk one of our most significant market risks. Interest rate risk is the exposure to adverse changes in net interest income due to changes in interest rates. Consistency of our net interest revenue is largely dependent upon the effective management of interest rate risk. We employ a variety of measurement techniques to identify and manage our interest rate risk including the use of an earnings simulation model to analyze net interest income sensitivity to changing interest rates. The model is based on actual cash flows and repricing characteristics for on and off-balance sheet instruments and incorporates market-based assumptions regarding the effect of changing interest rates on the prepayment rates of certain assets and liabilities. Assumptions based on the historical behavior of deposit rates and balances in relation to changes in interest rates are also incorporated into the model. These assumptions are inherently uncertain, and as a result, the model cannot precisely measure net interest income or precisely predict the impact of fluctuations in interest rates on net interest income. Actual results will differ from simulated results due to timing, magnitude, and frequency of interest rate changes as well as changes in market conditions and management strategies.

CTBI's Asset/Liability Management Committee (ALCO), which includes executive and senior management representatives and reports to the Board of Directors, monitors and manages interest rate risk within Board-approved policy limits. Our current exposure to interest rate risks is determined by measuring the anticipated change in net interest income spread evenly over the twelve-month period.

Capital Resources

Shareholders' equity was $457.4 million at March 31, 2015 and $447.9 million at December 31, 2014. CTBI's annualized dividend yield to shareholders as of March 31, 2015 was 3.62%. Our primary source of capital growth is the retention of earnings. Cash dividends were $0.300 per share and $0.291 per share for the three months ended March 31, 2015 and 2014, respectively. We retained 52.4% of our earnings for the first three months of 2015 compared to 50.7% for the first three months of 2014.

On July 2, 2013, the Federal Reserve approved final rules that substantially amend the regulatory risk-based capital rules applicable to CTBI and CTB. The FDIC subsequently approved these rules. The final rules implement the "Basel III" regulatory capital reforms and changes required by the Dodd-Frank Act.

The rules include new risk-based capital and leverage ratios, which are being phased in from 2015 to 2019, and refine the definition of what constitutes "capital" for purposes of calculating those ratios. The new minimum capital level requirements applicable to CTBI and CTB under the final rules would be: (i) a new common equity Tier 1 capital ratio of 4.5%; (ii) a Tier 1 capital ratio of 6% (increased from 4%); (iii) a total capital ratio of 8% (unchanged from current rules); and (iv) a Tier 1 leverage ratio of 4% for all institutions. The final rules also establish a "capital conservation buffer" above the new regulatory minimum capital requirements, which must consist entirely of common equity Tier 1 capital. The capital conservation buffer will be phased-in over four years beginning on January 1, 2016.

The final rules also implement revisions and clarifications consistent with Basel III regarding the various components of Tier 1 capital, including common equity, unrealized gains and losses, as well as certain instruments that will no longer qualify as Tier 1 capital, some of which will be phased out over time. However, the final rules provide that small depository institution holding companies with less than $15 billion in total assets as of December 31, 2009 (which includes CTBI) will be able to permanently include non-qualifying instruments that were issued and included in Tier 1 or Tier 2 capital prior to May 19, 2010 in additional Tier 1 or Tier 2 capital until they redeem such instruments or until the instruments mature.

The final rules also contain revisions to the prompt corrective action framework, which is designed to place restrictions on insured depository institutions, including the Bank, if their capital levels begin to show signs of weakness. These revisions took effect January 1, 2015. Under the prompt corrective action requirements, which are designed to complement the capital conservation buffer, insured depository institutions are required to meet the following increased capital level requirements in order to qualify as "well capitalized:" (i) a new common equity Tier 1 capital ratio of 6.5%; (ii) a Tier 1 capital ratio of 8% (increased from 6%); (iii) a total capital ratio of 10% (unchanged from current rules); and (iv) a Tier 1 leverage ratio of 5% (unchanged from current rules).

The final rules set forth certain changes for the calculation of risk-weighted assets, which we were required to utilize beginning January 1, 2015. The standardized approach final rule utilizes an increased number of credit risk exposure categories and risk weights, and also addresses: (i) an alternative standard of creditworthiness consistent with Section 939A of the Dodd-Frank Act; (ii) revisions to recognition of credit risk mitigation; (iii) rules for risk weighting of equity exposures and past due loans; (iv) revised capital treatment for derivatives and repo-style transactions; and (v) disclosure requirements for top-tier banking organizations with $50 billion or more in total assets that are not subject to the "advance approach rules" that apply to banks with greater than $250 billion in consolidated assets. For more information regarding Basel III, please refer to the Supervision and Regulation section of Item 1. Business in our annual report on Form 10-K for the year ended December 31, 2014.

As of March 31, 2015, following implementation of the new rules, CTBI had a common equity Tier 1 capital ratio of 14.01%, a Tier 1 capital ratio of 16.17%, a total capital ratio of 17.41%, and a Tier 1 leverage ratio of 12.16%, all above the required levels to be considered "well-capitalized."

As of March 31, 2015, we are not aware of any other current recommendations by banking regulatory authorities which, if they were to be implemented, would have, or are reasonably likely to have, a material adverse impact on our liquidity, capital resources, or operations, except as provided for in Basel III and the Dodd-Frank Act, which is discussed in the Supervision and Regulation section of Item 1. Business in our annual report on Form 10-K for the year ended December 31, 2014.

Impact of Inflation, Changing Prices, and Economic Conditions

The majority of our assets and liabilities are monetary in nature. Therefore, CTBI differs greatly from most commercial and industrial companies that have significant investment in nonmonetary assets, such as fixed assets and inventories. However, inflation does have an important impact on the growth of assets in the banking industry and on the resulting need to increase equity capital at higher than normal rates in order to maintain an appropriate equity to assets ratio. Inflation also affects other expenses, which tend to rise during periods of general inflation.

We believe one of the most significant impacts on financial and operating results is our ability to react to changes in interest rates. We seek to maintain an essentially balanced position between interest rate sensitive assets and liabilities in order to protect against the effects of wide interest rate fluctuations.

Since 2008 the U.S. economy has faced a severe economic crisis including a major recession from which it is slowly recovering. Commerce and business growth across a wide range of industries and regions in the U.S. remains reduced and local governments and many businesses continue to experience financial difficulty. While reflecting some improvement in many parts of the country and in parts of our own service area, unemployment levels remain elevated. There can be no assurance that these conditions will continue to improve and these conditions could worsen. Regionally, recent economic conditions in the coal industry could result in increased unemployment in the markets we serve where coal is a major contributor to the economy. In addition, ongoing federal budget negotiations, the implementation of the Patient Protection and Affordable Care Act, the Federal Open Market Committee's plan for economic easing, and the level of U.S. debt may have a destabilizing effect on financial markets.

Our financial performance generally, and in particular the ability of borrowers to pay interest on and repay principal of outstanding loans and the value of collateral securing those loans, as well as demand for loans and other products and services we offer, is highly dependent upon the business environment in the markets where we operate, in the states of Kentucky, West Virginia, and Tennessee and in the United States as a whole.  A favorable business environment is generally characterized by, among other factors, economic growth, efficient capital markets, low inflation, low unemployment, high business and investor confidence, and strong business earnings.  Unfavorable or uncertain economic and market conditions can be caused by declines in economic growth, business activity, or investor or business confidence; limitations on the availability or increases in the cost of credit and capital; increases in inflation or interest rates; high unemployment; natural disasters; or a combination of these or other factors.

Overall, during recent years, the business environment has been adverse for many households and businesses in the United States and worldwide.  While economic conditions in the United States and worldwide have improved since the recession, there can be no assurance that this improvement will continue.  Economic pressure on consumers and uncertainty regarding continuing economic improvement may result in changes in consumer and business spending, borrowing, and savings habits.  Such conditions could adversely affect the credit quality of our loans and our business, financial condition, and results of operations.

Stock Repurchase Program

CTBI has not acquired any shares of common stock through the stock repurchase program since February 2008.  There are 67,371 shares remaining under CTBI's current repurchase authorization.

Critical Accounting Policies and Estimates

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires the appropriate application of certain accounting policies, many of which require us to make estimates and assumptions about future events and their impact on amounts reported in our consolidated financial statements and related notes.  Since future events and their impact cannot be determined with certainty, the actual results will inevitably differ from our estimates.  Such differences could be material to the consolidated financial statements.

We believe the application of accounting policies and the estimates required therein are reasonable.  These accounting policies and estimates are constantly reevaluated, and adjustments are made when facts and circumstances dictate a change.  Historically, we have found our application of accounting policies to be appropriate, and actual results have not differed materially from those determined using necessary estimates.

We have identified the following critical accounting policies:

Investments – Management determines the classification of securities at purchase.  We classify securities into held-to-maturity, trading, or available-for-sale categories.  Held-to-maturity securities are those which we have the positive intent and ability to hold to maturity and are reported at amortized cost.  In accordance with Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 320, Investment Securities, investments in debt securities that are not classified as held-to-maturity and equity securities that have readily determinable fair values shall be classified in one of the following categories and measured at fair value in the statement of financial position:
a. Trading securities. Securities that are bought and held principally for the purpose of selling them in the near term (thus held for only a short period of time) shall be classified as trading securities. Trading generally reflects active and frequent buying and selling, and trading securities are generally used with the objective of generating profits on short-term differences in price.
b. Available-for-sale securities. Investments not classified as trading securities (nor as held-to-maturity securities) shall be classified as available-for-sale securities.

We do not have any securities that are classified as trading securities. Available-for-sale securities are reported at fair value, with unrealized gains and losses included as a separate component of shareholders' equity, net of tax. If declines in fair value are other than temporary, the carrying value of the securities is written down to fair value as a realized loss with a charge to income for the portion attributable to credit losses and a charge to other comprehensive income for the portion that is not credit related.

Gains or losses on disposition of securities are computed by specific identification for all securities except for shares in mutual funds, which are computed by average cost. Interest and dividend income, adjusted by amortization of purchase premium or discount, is included in earnings.

When the fair value of a security is below its amortized cost, and depending on the length of time the condition exists and the extent the fair market value is below amortized cost, additional analysis is performed to determine whether an other than temporary impairment condition exists. Available-for-sale and held-to-maturity securities are analyzed quarterly for possible other than temporary impairment. The analysis considers (i) whether we have the intent to sell our securities prior to recovery and/or maturity and (ii) whether it is more likely than not that we will not have to sell our securities prior to recovery and/or maturity. Often, the information available to conduct these assessments is limited and rapidly changing, making estimates of fair value subject to judgment. If actual information or conditions are different than estimated, the extent of the impairment of the security may be different than previously estimated, which could have a material effect on the CTBI's results of operations and financial condition.

Loans – Loans with the ability and the intent to be held until maturity and/or payoff are reported at the carrying value of unpaid principal reduced by unearned interest, an allowance for loan and lease losses, and unamortized deferred fees or costs. Income is recorded on the level yield basis. Interest accrual is discontinued when management believes, after considering economic and business conditions, collateral value, and collection efforts, that the borrower's financial condition is such that collection of interest is doubtful. Any loan greater than 90 days past due must be well secured and in the process of collection to continue accruing interest. Cash payments received on nonaccrual loans generally are applied against principal, and interest income is only recorded once principal recovery is reasonably assured. Loans are not reclassified as accruing until principal and interest payments remain current for a period of time, generally six months, and future payments appear reasonably certain. Included in certain loan categories of impaired loans are troubled debt restructurings that were classified as impaired. A restructuring of a debt constitutes a troubled debt restructuring if the creditor for economic or legal reasons related to the debtor's financial difficulties grants a concession to the debtor that it would not otherwise consider.

Loan origination and commitment fees and certain direct loan origination costs are deferred and the net amount amortized over the estimated life of the related loans, leases, or commitments as a yield adjustment.

Allowance for Loan and Lease Losses – We maintain an allowance for loan and lease losses ("ALLL") at a level that is appropriate to cover estimated credit losses on individually evaluated loans determined to be impaired, as well as estimated credit losses inherent in the remainder of the loan and lease portfolio. Since arriving at an appropriate ALLL involves a high degree of management judgment, we use an ongoing quarterly analysis to develop a range of estimated losses. In accordance with accounting principles generally accepted in the United States, we use our best estimate within the range of potential credit loss to determine the appropriate ALLL. Credit losses are charged and recoveries are credited to the ALLL.

We utilize an internal risk grading system for commercial credits. Those larger commercial credits that exhibit probable or observed credit weaknesses are subject to individual review. The borrower's cash flow, adequacy of collateral coverage, and other options available to CTBI, including legal remedies, are evaluated. The review of individual loans includes those loans that are impaired as defined by ASC 310-35, Impairment of a Loan. We evaluate the collectability of both principal and interest when assessing the need for loss provision. Historical loss rates are analyzed and applied to other commercial loans not subject to specific allocations. The ALLL allocation for this pool of commercial loans is established based on the historical average, maximum, minimum, and median loss ratios.

A loan is considered impaired when, based on current information and events, it is probable that CTBI will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed. Impairment is measured on a loan-by-loan basis for commercial and construction loans by either the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's obtainable market price, or the fair value of the collateral if the loan is collateral dependent.

Homogenous loans, such as consumer installment, residential mortgages, and home equity lines are not individually risk graded. The associated ALLL for these loans is measured under ASC 450, Contingencies.

When any secured commercial loan is considered uncollectable, whether past due or not, a current assessment of the value of the underlying collateral is made. If the balance of the loan exceeds the fair value of the collateral, the loan is placed on non-accrual and the loan is charged down to the value of the collateral less estimated cost to sell or a specific reserve equal to the difference between book value of the loan and the fair value assigned to the collateral is created until such time as the loan is foreclosed. When the foreclosed collateral has been legally assigned to CTBI, a charge off is taken, if necessary, in order that the remaining balance reflects the fair value estimated less costs to sell of the collateral then transferred to other real estate owned or other repossessed assets. When any unsecured commercial loan is considered uncollectable the loan is charged off no later than at 90 days past due.

All closed-end consumer loans (excluding conventional 1-4 family residential loans and installment and revolving loans secured by real estate) are charged off no later than 120 days (5 monthly payments) delinquent. If a loan is considered uncollectable, it is charged off earlier than 120 days delinquent. For conventional 1-4 family residential loans and installment and revolving loans secured by real estate, when a loan is 90 days past due, a current assessment of the value of the real estate is made. If the balance of the loan exceeds the fair value of the property, the loan is placed on nonaccrual. Foreclosure proceedings are normally initiated after 120 days. When the foreclosed property has been legally assigned to CTBI, the fair value less estimated costs to sell is transferred to other real estate owned and the remaining balance is taken as a charge-off.

Historical loss rates for loans are adjusted for significant factors that, in management's judgment, reflect the impact of any current conditions on loss recognition. We use twelve rolling quarters for our historical loss rate analysis. Factors that we consider include delinquency trends, current economic conditions and trends, strength of supervision and administration of the loan portfolio, levels of underperforming loans, level of recoveries to prior year's charge-offs, trends in loan losses, industry concentrations and their relative strengths, amount of unsecured loans, and underwriting exceptions. Based upon management's judgment, "best case," "worst case," and "most likely" scenarios are determined. The total of each of these weighted factors is then applied against the applicable portion of the portfolio and the ALLL is adjusted accordingly to approximate the most likely scenario. Management continually reevaluates the other subjective factors included in its ALLL analysis.

Other Real Estate Owned – When foreclosed properties are acquired, appraisals are obtained and the properties are booked at the current market value less expected sales costs. Additionally, periodic updated appraisals are obtained on unsold foreclosed properties. When an updated appraisal reflects a market value below the current book value, a charge is booked to current earnings to reduce the property to its new market value less expected sales costs. Our policy for determining the frequency of periodic reviews is based upon consideration of the specific properties and the known or perceived market fluctuations in a particular market and is typically between 12 and 18 months but generally not more than 24 months. All revenues and expenses related to the carrying of other real estate owned are recognized by a charge to income.

Income Taxes – Income tax expense is based on the taxes due on the consolidated tax return plus deferred taxes based on the expected future tax benefits and consequences of temporary differences between carrying amounts and tax bases of assets and liabilities, using enacted tax rates. Any interest and penalties incurred in connection with income taxes are recorded as a component of income tax expense in the consolidated financial statements. During the quarters ended March 31, 2015 and 2014, CTBI did not recognize a significant amount of interest expense or penalties in connection with income taxes.

CTBI is currently under IRS examination of its 2013 corporate income tax return. Management does not expect that the results of the examination will have a material effect on our financial condition. While management believes our tax positions are appropriate, the IRS could challenge our positions as a part of this examination.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Interest rate risk management focuses on maintaining consistent growth in net interest income within Board-approved policy limits. CTBI uses an earnings simulation model to analyze net interest income sensitivity to movements in interest rates. Given a 200 basis point increase to the yield curve used in the simulation model, it is estimated net interest income for CTBI would increase by 0.91 percent over one year and decrease by 0.20 percent over two years. A 25 basis point decrease in the yield curve would decrease net interest income by an estimated 0.09 percent over one year and increase by 0.02 percent over two years. For further discussion of CTBI's market risk, see the Management's Discussion and Analysis of Financial Condition and Results of Operations—Liquidity and Market Risk included in the annual report on Form 10-K for the year ended December 31, 2014.

Item 4. Controls and Procedures

EVALUATION OF DISCLOSURE CONTROLS AND PROCEDURES

CTBI's management is responsible for establishing and maintaining effective disclosure controls and procedures, as defined under Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934. As of the end of the period covered by this report, an evaluation was carried out by CTBI's management, with the participation of our Chief Executive Officer and the Executive Vice President, Chief Financial Officer, and Treasurer, of the effectiveness of the design and operation of our disclosure controls and procedures. Based on this evaluation, management concluded that disclosure controls and procedures as of March 31, 2015 were effective in ensuring material information required to be disclosed in this quarterly report on Form 10-Q was recorded, processed, summarized, and reported on a timely basis.

CHANGES IN INTERNAL CONTROL OVER FINANCIAL REPORTING

There were no changes in CTBI's internal control over financial reporting that occurred during the quarter ended March 31, 2015 that have materially affected, or are reasonably likely to materially affect, CTBI's internal control over financial reporting.

PART II - OTHER INFORMATION

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| Item 1. Legal Proceedings | None |

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| Item 1A. | Risk Factors | None |

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

(c) Upon the vesting of restricted stock in January 2015, the Compensation Committee of the Board of Directors, in accordance with provisions of the 2006 Stock Ownership Incentive Plan, allowed employees to elect to use the share withholding process to satisfy their tax withholding obligations. As a result, CTBI withheld and canceled 5,724 shares of stock at an average price of $33.03 per share.

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| Item 3. | Defaults Upon Senior Securities | None |
| Item 4. | Mine Safety Disclosure | Not applicable |
| Item 5. | Other Information: | |
| | CTBI's Principal Executive Officer and Principal Financial Officer have furnished to the SEC the certifications with respect to this Form 10-Q that are required by Sections 302 and 906 of the Sarbanes-Oxley Act of 2002 | |
| Item 6. | a. Exhibits: | |
| | (1) Certifications Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 | Exhibit 31.1<br>Exhibit 31.2 |
| | (2) Certifications Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 | Exhibit 32.1<br>Exhibit 32.2 |
| | (3) XBRL Instance Document | Exhibit 101.INS |
| | (4) XBRL Taxonomy Extension Schema | Exhibit 101.SCH |
| | (5) XBRL Taxonomy Extension Calculation Linkbase | Exhibit 101.CAL |
| | (6) XBRL Taxonomy Extension Definition Linkbase | Exhibit 101.DEF |
| | (7) XBRL Taxonomy Extension Label Linkbase | Exhibit 101.LAB |
| | (8) XBRL Taxonomy Extension Presentation Linkbase | Exhibit 101.PRE |

SIGNATURES

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

**COMMUNITY TRUST BANCORP, INC.**

Date: May 8, 2015 By: /s/ Jean R. Hale
Jean R. Hale
Chairman, President and Chief Executive Officer

/s/ Kevin J. Stumbo
Kevin J. Stumbo
Executive Vice President, Chief Financial Officer and Treasurer