

INDEPENDENT BANK CORP /MI/  
Form 424B3  
November 13, 2012

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Filed Pursuant to Rule 424(b)(3)

File No. 333-169200

PROSPECTUS SUPPLEMENT NO. 4  
TO PROSPECTUS DATED MAY 23, 2012

Common Stock

This Prospectus Supplement No. 4 supplements and amends the prospectus dated May 23, 2012, as amended and supplemented by the Prospectus Supplement No. 1 dated May 30, 2012, the Prospectus Supplement No. 2 dated August 21, 2012, and the Prospectus Supplement No. 3 dated October 31, 2012, which we collectively refer to as the Prospectus, which forms part of our Post-Effective Amendment No. 2 to Registration Statement on Form S-1 (Registration Statement No. 333-169200). The Prospectus relates to the disposition from time to time of up to 1,502,468 shares of our common stock that we may issue to Dutchess Opportunity Fund, II, LP ("Dutchess"), pursuant to an Investment Agreement between us and Dutchess, dated July 7, 2010. We are not selling any common stock under the Prospectus or this Prospectus Supplement No. 4, and will not receive any of the proceeds from the sale of shares by the selling stockholder.

We are filing this Prospectus Supplement No. 4 to update, amend and supplement the information included or incorporated by reference in the Prospectus with the information contained in the quarterly report described below.

This Prospectus Supplement No. 4 includes our Quarterly Report on Form 10-Q, filed with the Securities and Exchange Commission on November 9, 2012.

This Prospectus Supplement No. 4 should be read in conjunction with, and may not be delivered or utilized without, the Prospectus, including any amendments or supplements thereto. This Prospectus Supplement No. 4 is qualified by reference to the Prospectus except to the extent that the information in this Prospectus Supplement No. 4 supersedes the information contained in the Prospectus. All references in the Prospectus to "this prospectus" are hereby amended to read "this prospectus (as supplemented and amended)."

Our common stock is listed on the Nasdaq Global Select Market under the symbol "IBCP." As of November 12, 2012, the closing sale price for our common stock on the Nasdaq Global Select Market was \$3.36 per share.

Investing in our common stock involves risks. These risks are described under the caption "Risk Factors" beginning on page 7 of the Prospectus, as the same may be updated in prospectus supplements.

The shares of common stock offered are not savings accounts, deposits, or other obligations of any of our bank or non-bank subsidiaries and are not insured by the Federal Deposit Insurance Corporation or any other governmental agency.

Neither the Securities and Exchange Commission, any state securities commission, the Federal Deposit Insurance Corporation, the Board of Governors of the Federal Reserve System, nor any other regulatory body has approved or disapproved of these securities or determined if this prospectus is truthful or complete. Any representation to the contrary is a criminal offense.

The date of this prospectus supplement is November 13, 2012.

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SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE QUARTERLY PERIOD ENDED September 30, 2012

Commission file number 0-7818

INDEPENDENT BANK CORPORATION  
(Exact name of registrant as specified in its charter)

Michigan 38-2032782  
State or jurisdiction of Incorporation or Organization (I.R.S. Employer Identification Number)

230 West Main Street, P.O. Box 491, Ionia, Michigan 48846  
(Address of principal executive offices)

(616) 527-5820  
(Registrant's telephone number, including area code)

NONE  
Former name, address and fiscal year, if changed since last report.

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

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

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, non-accelerated filer or smaller reporting company.

Large accelerated filer ☐ Accelerated filer ☐ Non-accelerated filer ☐ Smaller reporting company ☒

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).  
YES ☐ NO ☒

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

date.

Common stock, no par value  
Class

8,907,390  
Outstanding at November 9, 2012

## INDEPENDENT BANK CORPORATION AND SUBSIDIARIES

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Discussions and statements in this report that are not statements of historical fact, including, without limitation, statements that include terms such as “will,” “may,” “should,” “believe,” “expect,” “forecast,” “anticipate,” “estimate,” “project,” “likely,” “optimistic” and “plan,” and statements about future or projected financial and operating results, plans, projections, objectives, expectations, and intentions and other statements that are not historical facts, are forward-looking statements. Forward-looking statements include, but are not limited to, descriptions of plans and objectives for future operations, products or services; projections of our future revenue, earnings or other measures of economic performance; forecasts of credit losses and other asset quality trends; predictions as to our Bank’s ability to maintain certain regulatory capital standards; our expectation that we will have sufficient cash on hand to meet expected obligations during 2012; and descriptions of steps we may take to improve our capital position. These forward-looking statements express our current expectations, forecasts of future events, or long-term goals and, by their nature, are subject to assumptions, risks, and uncertainties. Although we believe that the expectations, forecasts, and goals reflected in these forward-looking statements are reasonable, actual results could differ materially for a variety of reasons, including, among others:

- our ability to successfully raise new equity capital, effect a conversion of our outstanding convertible preferred stock held by the U.S. Treasury into our common stock, and otherwise implement our capital restoration plan;
- the failure of assumptions underlying the establishment of and provisions made to our allowance for loan losses;
- the timing and pace of an economic recovery in Michigan and the United States in general, including regional and local real estate markets;
- the ability of our Bank to remain well-capitalized;
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the failure of assumptions underlying our estimate of probable incurred losses from vehicle service contract payment plan counterparty contingencies, including our assumptions regarding future cancellations of vehicle service contracts, the value to us of collateral that may be available to recover funds due from our counterparties, and our ability to enforce the contractual obligations of our counterparties to pay amounts owing to us;

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- further adverse developments in the vehicle service contract industry;
- potential limitations on our ability to access and rely on wholesale funding sources;
- the risk that sales of our common stock could trigger a reduction in the amount of net operating loss carryforwards that we may be able to utilize for income tax purposes;
- the continued services of our management team, particularly as we work through our asset quality issues and the implementation of our capital restoration plan;
- implementation of the Dodd-Frank Wall Street Reform and Consumer Protection Act or other new legislation, which may have significant effects on us and the financial services industry, the exact nature and extent of which cannot be determined at this time; and
- the risk that our common stock may be delisted from the Nasdaq Global Select Market.

This list provides examples of factors that could affect the results described by forward-looking statements contained in this report, but the list is not intended to be all inclusive. The risk factors disclosed in Part I – Item A of our Annual Report on Form 10-K for the year ended December 31, 2011, as updated by any new or modified risk factors disclosed in Part II – Item 1A of any subsequently filed Quarterly Report on Form 10-Q, include all known risks that our management believes could materially affect the results described by forward-looking statements in this report. However, those risks may not be the only risks we face. Our results of operations, cash flows, financial position, and prospects could also be materially and adversely affected by additional factors that are not presently known to us, that we currently consider to be immaterial, or that develop after the date of this report. We cannot assure you that our future results will meet expectations. While we believe the forward-looking statements in this report are reasonable, you should not place undue reliance on any forward-looking statement. In addition, these statements speak only as of the date made. We do not undertake, and expressly disclaim, any obligation to update or alter any statements, whether as a result of new information, future events, or otherwise, except as required by applicable law.

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## Part I - Item 1.

INDEPENDENT BANK CORPORATION AND SUBSIDIARIES  
Condensed Consolidated Statements of Financial Condition

	September 30, 2012	December 31, 2011
	(unaudited)	
	(In thousands, except share amounts)	
Assets		
Cash and due from banks	\$ 56,911	\$ 62,777
Interest bearing deposits	403,633	278,331
Cash and Cash Equivalents	460,544	341,108
Trading securities	38	77
Securities available for sale	230,186	157,444
Federal Home Loan Bank and Federal Reserve Bank stock, at cost	20,494	20,828
Loans held for sale, carried at fair value	41,969	44,801
Loans held for sale, carried at lower of cost or fair value	52,280	-
Loans		
Commercial	603,538	651,155
Mortgage	537,107	590,876
Installment	197,736	219,559
Payment plan receivables	93,608	115,018
Total Loans	1,431,989	1,576,608
Allowance for loan losses	(48,021)	(58,884 )
Net Loans	1,383,968	1,517,724
Other real estate and repossessed assets	30,347	34,042
Property and equipment, net	47,062	62,548
Bank-owned life insurance	50,493	49,271
Other intangibles	6,793	7,609
Capitalized mortgage loan servicing rights	10,205	11,229
Prepaid FDIC deposit insurance assessment	10,229	12,609
Vehicle service contract counterparty receivables, net	18,773	29,298
Property and equipment held for sale	10,148	-
Accrued income and other assets	27,303	18,818
Total Assets	\$ 2,400,832	\$ 2,307,406
Liabilities and Shareholders' Equity		
Deposits		
Non-interest bearing	\$ 485,109	\$ 497,718
Savings and interest-bearing checking	853,603	1,019,603
Retail time	377,085	526,525
Brokered time	48,859	42,279
Total Deposits	1,764,656	2,086,125
Deposits held for sale relating to branch sale	405,850	-
Other borrowings	17,720	33,387
Subordinated debentures	50,175	50,175
Vehicle service contract counterparty payables	8,414	6,633
Accrued expenses and other liabilities	32,489	28,459
Total Liabilities	2,279,304	2,204,779



## Shareholders' Equity

Convertible preferred stock, no par value, 200,000 shares authorized; 74,426 shares issued and outstanding at September 30, 2012 and December 31, 2011; liquidation preference: \$84,099 at September 30, 2012 and \$81,023 at December 31, 2011	83,097	79,857
Common stock, no par value, 500,000,000 shares authorized; issued and outstanding: 8,804,415 shares at September 30, 2012 and 8,491,526 shares at December 31, 2011	250,080	248,950
Accumulated deficit	(203,217)	(214,259 )
Accumulated other comprehensive loss	(8,432)	(11,921 )
Total Shareholders' Equity	121,528	102,627
Total Liabilities and Shareholders' Equity	\$ 2,400,832	\$ 2,307,406

See notes to interim condensed consolidated financial statements (unaudited)

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## INDEPENDENT BANK CORPORATION AND SUBSIDIARIES

## Condensed Consolidated Statements of Operations

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2012	2011	2012	2011
	(unaudited)			
Interest Income	(In thousands, except per share amounts)			
Interest and fees on loans	\$23,385	\$27,222	\$71,427	\$84,808
Interest on securities				
Taxable	655	297	2,246	1,108
Tax-exempt	261	301	801	931
Other investments	432	367	1,210	1,185
Total Interest Income	24,733	28,187	75,684	88,032
Interest Expense				
Deposits	2,223	3,230	6,952	12,686
Other borrowings	1,059	1,183	3,351	3,738
Total Interest Expense	3,282	4,413	10,303	16,424
Net Interest Income	21,451	23,774	65,381	71,608
Provision for loan losses	251	6,171	6,438	21,029
Net Interest Income After Provision for Loan Losses	21,200	17,603	58,943	50,579
Non-interest Income				
Service charges on deposit accounts	4,739	4,623	13,492	13,689
Interchange income	2,324	2,356	7,053	6,832
Net gains (losses) on assets				
Mortgage loans	4,602	2,025	12,041	5,753
Securities	301	(57)	1,154	271
Other than temporary impairment loss on securities				
Total impairment loss	(70)	(4)	(332)	(146)
Loss recognized in other comprehensive loss	-	-	-	-
Net impairment loss recognized in earnings	(70)	(4)	(332)	(146)
Mortgage loan servicing	(364)	(2,655)	(716)	(1,885)
Title insurance fees	482	299	1,479	1,090
(Increase) decrease in fair value of U.S. Treasury warrant	(32)	29	(211)	1,025
Other	2,560	2,639	8,208	7,793
Total Non-interest Income	14,542	9,255	42,168	34,422
Non-interest Expense				
Compensation and employee benefits	13,610	12,654	39,598	38,032
Loan and collection	2,832	2,658	8,129	10,105
Occupancy, net	2,482	2,651	7,688	8,415
Data processing	2,492	2,502	7,281	7,227
Furniture, fixtures and equipment	1,194	1,308	3,795	4,228
Legal and professional	952	751	3,117	2,330
FDIC deposit insurance	816	885	2,489	2,772
Communications	785	863	2,486	2,700
Net losses on other real estate and repossessed assets	291	1,931	1,911	4,114
Advertising	647	740	1,842	1,964
Credit card and bank service fees	433	869	1,708	2,929
Vehicle service contract counterparty contingencies	281	1,345	1,078	5,002

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Write-down of property and equipment held for sale	860	-	860	-
Provision for loss reimbursement on sold loans	193	251	751	1,020
Costs (recoveries) related to unfunded lending commitments	(538 )	(172 )	(597 )	12
Other	1,966	2,226	4,692	6,385
Total Non-interest Expense	29,296	31,462	86,828	97,235
Income (Loss) Before Income Tax	6,446	(4,604 )	14,283	(12,234 )
Income tax benefit	-	(482 )	-	(748 )
Net Income (Loss)	\$6,446	\$(4,122 )	\$14,283	\$(11,486 )
Preferred stock dividends and discount accretion	1,093	1,043	3,241	3,102
Net Income (Loss) Applicable to Common Stock	\$5,353	\$(5,165 )	\$11,042	\$(14,588 )
Net Income (Loss) Per Common Share				
Basic	\$.61	\$(.61 )	\$1.28	\$(1.78 )
Diluted	.16	(.61 )	.36	(1.78 )
Dividends Per Common Share				
Declared	\$.00	\$.00	\$.00	\$.00
Paid	.00	.00	.00	.00

See notes to interim condensed consolidated financial statements (unaudited)

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## INDEPENDENT BANK CORPORATION AND SUBSIDIARIES

## Condensed Consolidated Statements of Comprehensive Income (Loss)

	Three Months Ended September 30, 2012      2011		Nine Months Ended September 30, 2012      2011	
	(unaudited) (In thousands)		(unaudited) (In thousands)	
Net income (loss)	\$6,446	\$(4,122 )	\$14,283	\$(11,486 )
Other comprehensive income (loss), before tax				
Available for sale securities				
Unrealized gain arising during period	909	357	2,543	930
Change in unrealized losses for which a portion of other than temporary impairment has been recognized in earnings	770	(220 )	1,103	191
Reclassification adjustment for other than temporary impairment included in earnings	70	4	332	146
Reclassification adjustments for (gains) included in earnings	(350 )	-	(1,193 )	(204 )
Unrealized gains recognized in other comprehensive income on available for sale securities	1,399	141	2,785	1,063
Derivative instruments				
Unrealized loss arising during period	(54 )	(215 )	(129 )	(478 )
Reclassification adjustment for expense recognized in earnings	92	200	397	603
Reclassification adjustment for accretion on settled derivatives	145	145	436	514
Unrealized gains recognized in other comprehensive income on derivative instruments	183	130	704	639
Other comprehensive income, before tax	1,582	271	3,489	1,702
Income tax expense related to components of other comprehensive income (loss)	-	95	-	596
Other comprehensive income	1,582	176	3,489	1,106
Comprehensive income (loss)	\$8,028	\$(3,946 )	\$17,772	\$(10,380 )

See notes to interim condensed consolidated financial statements (unaudited)

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INDEPENDENT BANK CORPORATION AND SUBSIDIARIES  
Condensed Consolidated Statements of Cash Flows

	Nine months ended September 30,	
	2012	2011
	(unaudited - In thousands)	
Net Income (Loss)	\$ 14,283	\$ (11,486 )
Adjustments to Reconcile Net Income (Loss) to Net Cash from Operating Activities		
Proceeds from sales of loans held for sale	378,804	270,796
Disbursements for loans held for sale	(363,931)	(243,654 )
Net decrease in loans held for sale relating to branch sale	900	-
Net decrease in deposits held for sale relating to branch sale	(11,671)	-
Provision for loan losses	6,438	21,029
Deferred loan fees	(501)	(428 )
Depreciation, amortization of intangible assets and premiums and accretion of discounts on securities and loans	(3,532)	(9,303 )
Write-down of property and equipment held for sale	860	-
Net gains on mortgage loans	(12,041)	(5,753 )
Net gains on securities	(1,154)	(271 )
Securities impairment recognized in earnings	332	146
Net losses on other real estate and repossessed assets	1,911	4,114
Vehicle service contract counterparty contingencies	1,078	5,002
Share based compensation	572	762
Increase (decrease) in accrued income and other assets	(5,434)	6,714
Increase in accrued expenses and other liabilities	3,957	1,017
Total Adjustments	(3,412)	50,171
Net Cash from Operating Activities	10,871	38,685
Cash Flow from Investing Activities		
Proceeds from the sale of securities available for sale	37,176	70,322
Proceeds from the maturity of securities available for sale	66,868	2,308
Principal payments received on securities available for sale	18,214	5,524
Purchases of securities available for sale	(192,382)	(104,052 )
Redemption of Federal Home Loan Bank stock	-	2,397
Redemption of Federal Reserve Bank stock	334	228
Net decrease in portfolio loans (loans originated, net of principal payments)	75,148	150,436
Proceeds from the collection of vehicle service contract counterparty receivables	7,413	1,438
Proceeds from the sale of other real estate and repossessed assets	14,062	14,241
Capital expenditures	(3,775)	(2,124 )
Net Cash from Investing Activities	23,058	140,718
Cash Flow from (used in) Financing Activities		
Net increase (decrease) in total deposits	98,836	(173,197 )
Net increase (decrease) in other borrowings	3	(3 )
Proceeds from Federal Home Loan Bank advances	12,000	19,000
Payments of Federal Home Loan Bank advances	(27,670)	(54,303 )
Net increase (decrease) in vehicle service contract counterparty payables	1,781	(1,805 )
Proceeds from issuance of common stock	557	1,335
Net Cash from (used in) Financing Activities	85,507	(208,973 )

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Net Increase (Decrease) in Cash and Cash Equivalents	119,436	(29,570 )
Cash and Cash Equivalents at Beginning of Period	341,108	385,374
Cash and Cash Equivalents at End of Period	\$ 460,544	\$ 355,804
Cash paid during the period for		
Interest	\$ 8,647	\$ 15,475
Income taxes	198	26
Transfers to other real estate and repossessed assets	9,110	12,971
Transfer of payment plan receivables to vehicle service contract counterparty receivables	1,225	9,239
Transfers to loans held for sale	54,127	-
Transfers to deposits held for sale	420,261	-
Transfers to fixed assets held for sale	12,611	-

See notes to interim condensed consolidated financial statements (unaudited)

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INDEPENDENT BANK CORPORATION AND SUBSIDIARIES  
Condensed Consolidated Statements of Shareholders' Equity

	Nine months ended September 30, 2012          2011 (unaudited) (In thousands)	
Balance at beginning of period	\$102,627	\$119,085
Net income (loss)	14,283	(11,486 )
Issuance of common stock	557	1,335
Share based compensation	572	762
Net change in accumulated other comprehensive loss, net of related tax effect	3,489	1,106
Balance at end of period	\$121,528	\$110,802

See notes to interim condensed consolidated financial statements (unaudited)

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NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
(unaudited)

1. Preparation of Financial Statements

The interim condensed consolidated financial statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and note disclosures normally included in annual financial statements prepared in accordance with generally accepted accounting principles ("GAAP") have been condensed or omitted pursuant to those rules and regulations, although we believe that the disclosures made are adequate to make the information not misleading. The unaudited condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes for the year ended December 31, 2011 included in our Annual Report on Form 10-K.

In our opinion, the accompanying unaudited condensed consolidated financial statements contain all the adjustments necessary to present fairly our consolidated financial condition as of September 30, 2012 and December 31, 2011, and the results of operations for the three and nine-month periods ended September 30, 2012 and 2011. The results of operations for the three and nine-month periods ended September 30, 2012, are not necessarily indicative of the results to be expected for the full year. Certain reclassifications have been made in the prior period financial statements to conform to the current period presentation. Our critical accounting policies include the assessment for other than temporary impairment ("OTTI") on investment securities, the determination of the allowance for loan losses, the determination of vehicle service contract counterparty contingencies, the valuation of originated mortgage loan servicing rights and the valuation of deferred tax assets. Refer to our 2011 Annual Report on Form 10-K for a disclosure of our accounting policies.

2. New Accounting Standards

In May 2011, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2011-04, "Fair Value Measurement (Topic 820), Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs". This ASU amended guidance that will result in common fair value measurement and disclosure requirements between U.S. GAAP and International Financial Reporting Standards ("IFRS"). Under the amended guidance, entities are required to expand disclosure for fair value instruments categorized within Level 3 of the fair value hierarchy to include (1) the valuation processes used; and (2) a narrative description of the sensitivity of the fair value measurement to changes in unobservable inputs for recurring fair value measurements and the interrelationships between those unobservable inputs, if any. They are also required to disclose the categorization by level of the fair value hierarchy for items that are not measured at fair value in the Consolidated Statement of Financial Condition but for which the fair value is required to be disclosed (e.g. portfolio loans). This amended guidance became effective for us at January 1, 2012. The effect of adopting this standard did not have a material impact on our consolidated operating results or financial condition, but the additional disclosures are included in Notes #12 and #13.



IndexNOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)  
(unaudited)

In June 2011, the FASB issued ASU 2011-05, "Comprehensive Income (Topic 220)". This ASU amended guidance on the presentation requirements for comprehensive income. The amended guidance requires an entity to present total comprehensive income, the components of net income and the components of other comprehensive income on the face of the financial statements, either in a single continuous statement of comprehensive income or in two separate but consecutive statements. The amended guidance did not change the items that must be reported in other comprehensive income or when an item of other comprehensive income must be reclassified to net income. This amended guidance became effective for us at January 1, 2012 and was applied retrospectively. The effect of adopting this standard did not have a material impact on our consolidated operating results or financial condition, but we have included separate Condensed Consolidated Statements of Comprehensive Income (Loss) immediately following our Condensed Consolidated Statements of Operations in our Condensed Consolidated Financial Statements.

## 3. Securities

Securities available for sale consist of the following:

	Amortized Cost	Unrealized Gains      Losses (In thousands)		Fair Value
September 30, 2012				
U.S. agency	\$45,615	\$77	\$55	\$45,637
U.S. agency residential mortgage-backed	131,427	1,204	11	132,620
Private label residential mortgage-backed	9,503	-	1,201	8,302
Obligations of states and political subdivisions	39,733	699	71	40,361
Trust preferred	4,702	-	1,436	3,266
Total	\$230,980	\$1,980	\$2,774	\$230,186
December 31, 2011				
U.S. agency	\$24,980	\$58	\$21	\$25,017
U.S. agency residential mortgage-backed	93,415	1,007	216	94,206
Private label residential mortgage-backed	11,066	-	2,798	8,268
Obligations of states and political subdivisions	26,865	510	58	27,317
Trust preferred	4,697	-	2,061	2,636
Total	\$161,023	\$1,575	\$5,154	\$157,444

IndexNOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)  
(unaudited)

Our investments' gross unrealized losses and fair values aggregated by investment type and length of time that individual securities have been at a continuous unrealized loss position follows:

	Less Than Twelve Months Unrealized		Twelve Months or More Unrealized		Total Unrealized	
	Fair Value	Losses	Fair Value	Losses	Fair Value	Losses
(In thousands)						
September 30, 2012						
U.S. agency	\$13,065	\$55	\$-	\$-	\$13,065	\$55
U.S. agency residential mortgage-backed	2,653	1	10,264	10	12,917	11
Private label residential mortgage-backed			8,300	1,201	8,300	1,201
Obligations of states and political subdivisions	7,387	71			7,387	71
Trust preferred			3,266	1,436	3,266	1,436
Total	\$23,105	\$127	\$21,830	\$2,647	\$44,935	\$2,774
December 31, 2011						
U.S. agency	\$9,974	\$21	\$-	\$-	\$9,974	\$21
U.S. agency residential mortgage-backed	42,500	216	-	-	42,500	216
Private label residential mortgage-backed	163	90	8,102	2,708	8,265	2,798
Obligations of states and political subdivisions	-	-	1,729	58	1,729	58
Trust preferred	591	1,218	2,045	843	2,636	2,061
Total	\$53,228	\$1,545	\$11,876	\$3,609	\$65,104	\$5,154

Our portfolio of available-for-sale securities is reviewed quarterly for impairment in value. In performing this review management considers (1) the length of time and extent that fair value has been less than cost, (2) the financial condition and near term prospects of the issuer, (3) the impact of changes in market interest rates on the market value of the security and (4) an assessment of whether we intend to sell, or it is more likely than not that we will be required to sell a security in an unrealized loss position before recovery of its amortized cost basis. For securities that do not meet the aforementioned recovery criteria, the amount of impairment recognized in earnings is limited to the amount related to credit losses, while impairment related to other factors is recognized in other comprehensive income or loss.

U.S. agency and U.S. agency residential mortgage-backed securities — at September 30, 2012 we had three U.S. agency and three U.S. agency residential mortgage-backed securities whose fair market value is less than amortized cost. The U.S. Agency securities were purchased on September 28, 2012 and the impairment is primarily attributed to bid-offer spread. As management does not intend to liquidate these securities and it is more likely than not that we will not be required to sell these securities prior to recovery of these unrealized losses, no declines are deemed to be other than temporary.

Private label residential mortgage backed securities — at September 30, 2012 we had eight securities whose fair value is less than amortized cost. Two of the issues are rated by a major rating agency as investment grade while four are below investment grade and two are split rated. Four of these bonds have impairment in excess of 10% and all of these holdings have been impaired for more than 12 months.

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The unrealized losses are largely attributable to credit spread widening on these securities since their acquisition. Prices for these bonds did improve notably during the third quarter of 2012, due in part to the Federal Reserve Bank's recent announcement of a third round of quantitative easing and improving fundamentals in the housing market. The underlying loans within these securities include Jumbo (74%) and Alt A (26%) at September 30, 2012.

	September 30, 2012		December 31, 2011	
	Fair Value	Net Unrealized Gain (Loss)	Fair Value	Net Unrealized Gain (Loss)
	(In thousands)			
Private label residential mortgage-backed				
Jumbo	\$6,128	\$(879)	\$6,454	\$(1,937)
Alt-A	2,174	(322)	1,814	(861)

Seven of the private label residential mortgage-backed transactions have geographic concentrations in California, ranging from 22% to 58% of the collateral pool. Typical exposure levels to California (median exposure is 47%) are consistent with overall market collateral characteristics. Three transactions have modest exposure to Florida, ranging from 5% to 7% and one transaction has modest exposure to Nevada (5%). The underlying collateral pools do not have meaningful exposure to Arizona, Michigan or Ohio. None of the issues involve subprime mortgage collateral. Thus the impact of this market segment is only indirect, in that it has impacted liquidity and pricing in general for private label residential mortgage-backed securities. The majority of transactions are backed by fully amortizing loans. However, six transactions have concentrations in loans that pay interest only for a specified period of time and will fully amortize thereafter ranging from 31% to 94% (at origination date). The structure of the residential mortgage securities portfolio provides protection to credit losses. The portfolio primarily consists of senior securities as demonstrated by the following: super senior (22%), senior (43%), senior support (25%) and mezzanine (10%). The mezzanine class is from a seasoned transaction (97 months) with a significant level of subordination (8.69%). Except for the additional discussion below relating to other than temporary impairment, each private label residential mortgage-backed security has sufficient credit enhancement via subordination to reasonably assure full realization of book value. This assertion is based on a transaction level review of the portfolio.

Individual security reviews include: external credit ratings, forecasted weighted average life, recent prepayment speeds, underwriting characteristics of the underlying collateral, the structure of the securitization and the credit performance of the underlying collateral. The review of underwriting characteristics considers: average loan size, type of loan (fixed or ARM), vintage, rate, FICO, loan-to-value, scheduled amortization, occupancy, purpose, geographic mix and loan documentation. The review of the securitization structure focuses on the priority of cash flows to the bond, the priority of the bond relative to the realization of credit losses and the level of subordination available to absorb credit losses. The review of credit performance includes: current period as well as cumulative realized losses; the level of severe payment problems, which includes other real estate (ORE), foreclosures, bankruptcy and 90 day delinquencies; and the level of less severe payment problems, which consists of 30 and 60 day delinquencies.

All of these securities are receiving some principal and interest payments. Most of these transactions are passthrough structures, receiving pro rata principal and interest payments from a dedicated collateral pool for loans that are performing. The nonreceipt of interest cash flows is not expected and thus not presently considered in our discounted cash flow methodology discussed below.



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In addition to the review discussed above, all private label residential mortgage-backed securities are reviewed for OTTI utilizing a cash flow projection. The cash flow analysis forecasts cash flow from the underlying loans in each transaction and then applies these cash flows to the bonds in the securitization. The cash flows from the underlying loans considers contractual payment terms (scheduled amortization), prepayments, defaults and severity of loss given default. The analysis uses dynamic assumptions for prepayments, defaults and loss severity. Near term prepayment assumptions are based on recently observed prepayment rates. More weight is given to longer term historic performance (12 months). In some cases, recently observed prepayment rates are lower than historic norms due to the absence of new jumbo loan issuances. This loan market is heavily dependent upon securitization for funding, and new securitization transactions have been minimal. Our model projections anticipate that prepayment rates gradually revert to historical levels. For seasoned ARM transactions, normalized prepayment rates range from 12% to 18% CPR which is at the lower end of historically observed speeds for seasoned ARM collateral. For fixed rate collateral (one transaction), the prepayment speeds are projected to rise modestly.

Default assumptions are largely based on the volume of existing real-estate owned, pending foreclosures and severe delinquencies. Other considerations include the quality of loan underwriting, recent default experience, realized loss performance and the volume of less severe delinquencies. Default levels generally are projected to remain elevated or increase for a period of time sufficient to address the level of distressed loans in the transaction. Our projections expect defaults to then decline, generally beginning in year three. Current loss severity assumptions are based on recent observations when meaningful data is available. Loss severity is expected to remain elevated for the next three years. Severity is expected to decline beginning in year four as the back log of foreclosure and distressed sales clear the market. Except for three securities discussed in further detail below (all three are currently below investment grade), our cash flow analysis forecasts complete recovery of our cost basis for each reviewed security.

At September 30, 2012 three below investment grade private label residential mortgage-backed securities with fair values of \$3.6 million, \$1.9 million and \$0.1 million, respectively and unrealized losses of \$0.4 million, \$0.1 million and \$0.03 million, respectively (amortized cost of \$4.0 million, \$2.0 million and \$0.1 million, respectively) had losses that were considered other than temporary.

The underlying loans in the first transaction are 30 year fixed rate jumbos with an average FICO of 744 and an average loan-to-value ratio of 72%. The loans backing this transaction were originated in 2007 and this is our only security backed by 2007 vintage loans. We believe that this vintage is a key differentiating factor between this security and the others in our portfolio that do not have unrealized losses that are considered OTTI. The bond is a senior security that is receiving principal and interest payments similar to principal reductions in the underlying collateral. The cash flow analysis described above calculated \$0.715 million of cumulative credit related OTTI as of September 30, 2012 on this security. \$0.070 million and \$0.004 million of this credit related OTTI was recognized in our Condensed Consolidated Statements of Operations during the three months ended September 30, 2012 and 2011, respectively and \$0.240 million and \$0.056 million of this credit related OTTI was recognized during the nine months ended September 30, 2012 and 2011, respectively, with the balance being recognized in previous periods. The remaining non-credit related unrealized loss was attributed to other factors and is reflected in other comprehensive income (loss) during those same periods.

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The underlying loans in the second transaction are 30 year hybrid ARM Alt-A with an average FICO of 717 and an average loan-to-value ratio of 78%. The loans backing this transaction were originated in 2005. The bond is a super senior security that is receiving principal and interest payments similar to principal reductions in the underlying collateral. The cash flow analysis described above calculated \$0.457 million of cumulative credit related OTTI as of September 30, 2012 on this security. There was no credit related OTTI recognized in our Condensed Consolidated Statements of Operations during the three months ended September 30, 2012 and 2011 while \$0.032 million and zero of this credit related OTTI was recognized during the nine months ended September 30, 2012 and 2011, respectively, with the balance being recognized in previous periods. The remaining non-credit related unrealized loss was attributed to other factors and is reflected in other comprehensive income (loss) during those same periods.

The underlying loans in the third transaction are 30 year hybrid ARM jumbos with an average FICO of 738 and an average loan-to-value ratio of 57%. The loans backing this transaction were originated in 2005. The bond is a senior support security that is receiving principal and interest payments similar to principal reductions in the underlying collateral. The cash flow analysis described above calculated \$0.380 million of cumulative credit related OTTI as of September 30, 2012 on this security. There was no credit related OTTI recognized in our Condensed Consolidated Statements of Operations during the three months ended September 30, 2012 and 2011, while \$0.060 million and \$0.090 million of this credit related OTTI was recognized during the nine months ended September 30, 2012 and 2011, respectively, with the balance being recognized in previous periods. The remaining non-credit related unrealized loss was attributed to other factors and is reflected in other comprehensive income (loss) during those same periods.

As management does not intend to liquidate these securities and it is more likely than not that we will not be required to sell these securities prior to recovery of these unrealized losses, no other declines discussed above are deemed to be other than temporary.

Obligations of states and political subdivisions — at September 30, 2012 we had seven municipal securities whose fair value is less than amortized cost. The unrealized losses are largely attributed to widening of market spreads. Six of the impaired securities are rated by a major rating agency as investment grade. The non rated security has a periodic internal credit review according to established procedures. As management does not intend to liquidate these securities and it is more likely than not that we will not be required to sell these securities prior to recovery of these unrealized losses, no declines are deemed to be other than temporary.

Trust preferred securities — at September 30, 2012 we had four securities whose fair value is less than amortized cost. All of our trust preferred securities are single issue securities issued by a trust subsidiary of a bank holding company. The pricing of trust preferred securities over the past several years has suffered from credit spread widening fueled by uncertainty regarding potential losses of financial companies and the absence of a liquid functioning secondary market.

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One of the four securities is rated by two major rating agencies as investment grade, while one is rated below investment grade by two major rating agencies and the other two are non-rated. The non-rated issues are relatively small banks and were never rated. The issuers of these non-rated trust preferred securities, which had a total amortized cost of \$2.8 million and total fair value of \$1.8 million as of September 30, 2012, continue to have satisfactory credit metrics and one continues to make interest payments. One non-rated issue began deferring dividend payments in the third quarter of 2011 apparently due to an increase in non-performing assets. Nevertheless, this issuer continues to have satisfactory capital measures and interim profitability.

The following table breaks out our trust preferred securities in further detail as of September 30, 2012 and December 31, 2011:

	September 30, 2012		December 31, 2011	
	Fair Value	Net Unrealized Gain (Loss)	Fair Value	Net Unrealized Gain (Loss)
	(In thousands)			
Trust preferred securities				
Rated issues	\$1,474	\$(421 )	\$1,405	\$(484 )
Unrated issues - no OTTI	1,792	(1,015 )	1,231	(1,577 )

As management does not intend to liquidate these securities and it is more likely than not that we will not be required to sell these securities prior to recovery of these unrealized losses, no declines are deemed to be other than temporary.

We recorded credit related OTTI charges in earnings on securities available for sale of \$0.070 million and \$0.004 during the three month periods ended September 30, 2012 and 2011, respectively and \$0.332 million and \$0.146 million during the nine month periods ended September 30, 2012 and 2011, respectively (see discussion above).

A roll forward of credit losses recognized in earnings on securities available for sale for the three and nine month periods ended September 30, follows:

	Three months ended		Nine months ended	
	September 30, 2012	September 30, 2011	September 30, 2012	September 30, 2011
	(In thousands)			
Balance at beginning of period	\$1,732	\$852	\$1,470	\$710
Additions to credit losses on securities for which no previous OTTI was recognized	-	-	-	-
Increases to credit losses on securities for which OTTI was previously recognized	70	4	332	146
Balance at end of period	\$1,802	\$856	\$1,802	\$856



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The amortized cost and fair value of securities available for sale at September 30, 2012, by contractual maturity, follow. The actual maturity may differ from the contractual maturity because issuers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Amortized Cost (In thousands)	Fair Value
Maturing within one year	\$1,620	\$1,633
Maturing after one year but within five years	6,604	6,818
Maturing after five years but within ten years	25,922	26,106
Maturing after ten years	55,904	54,707
	90,050	89,264
U.S. agency residential mortgage-backed	131,427	132,620
Private label residential mortgage-backed	9,503	8,302
Total	\$230,980	\$230,186

Gains and losses realized on the sale of securities available for sale are determined using the specific identification method and are recognized on a trade-date basis. A summary of proceeds from the sale of securities available for sale and gains and losses for the nine month periods ended September 30, follows:

	Proceeds	Realized Gains (In thousands)	Losses(1)
2012	\$ 37,176	\$ 1,193	\$ -
2011	70,322	279	75

(1) Losses in 2012 and 2011 exclude \$0.332 million and \$0.146 million, respectively of credit related OTTI recognized in earnings.

During 2012 and 2011 our trading securities consisted of various preferred stocks. During the first nine months of 2012 and 2011 we recognized gains (losses) on trading securities of (\$0.039) million and \$0.067 million, respectively, that are included in net gains (losses) on securities in the Condensed Consolidated Statements of Operations. Both of these amounts, relate to gains (losses) recognized on trading securities still held at each respective period end.

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## 4. Loans

Our assessment of the allowance for loan losses is based on an evaluation of the loan portfolio, recent loss experience, current economic conditions and other pertinent factors.

An analysis of the allowance for loan losses by portfolio segment for the three months ended September 30, follows:

	Commercial	Mortgage	Installment	Payment Plan Receivables	Unallocated	Total
	(In thousands)					
2012						
Balance at beginning of period	\$15,476	\$21,271	\$4,981	\$195	\$9,423	\$51,346
Additions (deductions)						
Provision for loan losses	18	1,839	(849 )	(17 )	(740 )	251
Recoveries credited to allowance	782	303	287	-	-	1,372
Loans charged against the allowance	(2,619 )	(1,720 )	(793 )	13	-	(5,119 )
Reclassification to loans held for sale	16	136	133	-	(114 )	171
Balance at end of period	\$13,673	\$21,829	\$3,759	\$191	\$8,569	\$48,021
2011						
Balance at beginning of period	\$17,697	\$23,152	\$6,289	\$346	\$13,035	\$60,519
Additions (deductions)						
Provision for loan losses	3,335	2,642	693	6	(505 )	6,171
Recoveries credited to allowance	229	247	421	1	-	898
Loans charged against the allowance	(4,330 )	(3,254 )	(1,131 )	(53 )	-	(8,768 )
Balance at end of period	\$16,931	\$22,787	\$6,272	\$300	\$12,530	\$58,820

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An analysis of the allowance for loan losses by portfolio segment for the nine months ended September 30, follows:

	Commercial	Mortgage	Installment	Payment Plan Receivables	Unallocated	Total
	(In thousands)					
2012						
Balance at beginning of period	\$18,183	\$22,885	\$6,146	\$197	\$11,473	\$58,884
Additions (deductions)						
Provision for loan losses	2,708	6,644	(331 )	6	(2,589 )	6,438
Recoveries credited to allowance	2,178	1,423	1,002	-	-	4,603
Loans charged against the allowance	(9,242 )	(9,067 )	(2,973 )	(12 )	-	(21,294 )
Reclassification to loans held for sale	(154 )	(56 )	(85 )	-	(315 )	(610 )
Balance at end of period	\$13,673	\$21,829	\$3,759	\$191	\$8,569	\$48,021
2011						
Balance at beginning of period	\$23,836	\$22,642	\$6,769	\$389	\$14,279	\$67,915
Additions (deductions)						
Provision for loan losses	9,378	10,975	2,374	51	(1,749 )	21,029
Recoveries credited to allowance	960	987	1,128	5	-	3,080
Loans charged against the allowance	(17,243 )	(11,817 )	(3,999 )	(145 )	-	(33,204 )
Balance at end of period	\$16,931	\$22,787	\$6,272	\$300	\$12,530	\$58,820

During the third quarter of 2012 we implemented a refinement in the calculation methodology for the historical loss component of our allowance for loan losses relating to homogenous mortgage and installment loan groups. This refinement now uses borrower credit scores and portfolio segment as well as a migration analysis to estimate a probability of default. For homogenous mortgage and installment loans a probability of default for each homogenous pool is calculated by way of credit score migration. Historical loss data for each homogenous pool coupled with the associated probability of default is utilized to calculate an expected loss allocation rate.

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Allowance for loan losses and recorded investment in loans by portfolio segment follows:

	Commercial	Mortgage	Installment	Payment Plan Receivables	Unallocated	Total
	(In thousands)					
September 30, 2012						
Allowance for loan losses:						
Individually evaluated for impairment	\$8,368	\$13,094	\$1,597	\$-	\$-	\$23,059
Collectively evaluated for impairment	5,305	8,735	2,162	191	8,569	24,962
Total ending allowance balance	\$13,673	\$21,829	\$3,759	\$191	\$8,569	\$48,021
Loans						
Individually evaluated for impairment	\$63,711	\$90,580	\$7,505	\$-		\$161,796
Collectively evaluated for impairment	541,588	449,084	191,011	93,608		1,275,291
Total loans recorded investment	605,299	539,664	198,516	93,608		1,437,087
Accrued interest included in recorded investment	1,761	2,557	780	-		5,098
Total loans	\$603,538	\$537,107	\$197,736	\$93,608		\$1,431,989
December 31, 2011						
Allowance for loan losses:						
Individually evaluated for impairment	\$10,252	\$10,285	\$1,762	\$-	\$-	\$22,299
Collectively evaluated for impairment	7,931	12,600	4,384	197	11,473	36,585
Total ending allowance balance	\$18,183	\$22,885	\$6,146	\$197	\$11,473	\$58,884
Loans						
Individually evaluated for impairment	\$58,674	\$93,702	\$7,554	\$-		\$159,930
Collectively evaluated for impairment	594,665	499,919	212,907	115,018		1,422,509
Total loans recorded investment	653,339	593,621	220,461	115,018		1,582,439
Accrued interest included in recorded investment	2,184	2,745	902	-		5,831
Total loans	\$651,155	\$590,876	\$219,559	\$115,018		\$1,576,608

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Loans on non-accrual status and past due more than 90 days ("Non-performing Loans") follow:

	90+ and Still Accruing	Non- Accrual (In thousands)	Total Non- Performing Loans
September 30, 2012			
Commercial			
Income producing - real estate	\$ -	\$ 7,742	\$ 7,742
Land, land development and construction - real estate	-	4,598	4,598
Commercial and industrial	3	7,174	7,177
Mortgage			
1-4 family	59	10,498	10,557
Resort lending	-	4,713	4,713
Home equity line of credit - 1st lien	-	607	607
Home equity line of credit - 2nd lien	-	709	709
Installment			
Home equity installment - 1st lien	-	1,045	1,045
Home equity installment - 2nd lien	-	837	837
Loans not secured by real estate	-	648	648
Other	-	1	1
Payment plan receivables			
Full refund	-	102	102
Partial refund	-	98	98
Other	-	13	13
Total recorded investment	\$ 62	\$ 38,785	\$ 38,847
Accrued interest included in recorded investment	\$ -	\$ -	\$ -
December 31, 2011			
Commercial			
Income producing - real estate	\$ 490	\$ 13,788	\$ 14,278
Land, land development and construction - real estate	43	6,990	7,033
Commercial and industrial	-	7,984	7,984
Mortgage			
1-4 family	54	15,929	15,983
Resort lending	-	8,819	8,819
Home equity line of credit - 1st lien	-	523	523
Home equity line of credit - 2nd lien	-	889	889
Installment			
Home equity installment - 1st lien	-	1,542	1,542
Home equity installment - 2nd lien	-	1,023	1,023
Loans not secured by real estate	-	880	880
Other	-	4	4
Payment plan receivables			
Full refund	-	491	491

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Partial refund	-	424	424
Other	-	23	23
Total recorded investment	\$ 587	\$ 59,309	\$ 59,896
Accrued interest included in recorded investment	\$ 13	\$ -	\$ 13

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An aging analysis of loans by class follows:

		Loans Past Due			Loans not	Total
	30-59 days	60-89 days	90+ days	Total	Past Due	Loans
	(In thousands)					
September 30, 2012						
Commercial						
Income producing - real estate	\$3,543	\$441	\$4,606	\$8,590	\$205,666	\$214,256
Land, land development and construction - real estate	301	1,871	1,090	3,262	40,310	43,572
Commercial and industrial	1,292	495	3,451	5,238	342,233	347,471
Mortgage						
1-4 family	3,532	1,343	10,557	15,432	282,731	298,163
Resort lending	206	154	4,713	5,073	169,633	174,706
Home equity line of credit - 1st lien	271	-	607	878	18,811	19,689
Home equity line of credit - 2nd lien	602	90	709	1,401	45,705	47,106
Installment						
Home equity installment - 1st lien	767	235	1,045	2,047	31,545	33,592
Home equity installment - 2nd lien	239	139	837	1,215	40,739	41,954
Loans not secured by real estate	862	204	648	1,714	118,514	120,228
Other	18	8	1	27	2,715	2,742
Payment plan receivables						
Full refund	2,272	620	102	2,994	82,868	85,862
Partial refund	178	94	98	370	7,089	7,459
Other	12	7	13	32	255	287
Total recorded investment	\$14,095	\$5,701	\$28,477	\$48,273	\$1,388,814	\$1,437,087
Accrued interest included in recorded investment	\$117	\$48	\$-	\$165	\$4,933	\$5,098
December 31, 2011						
Commercial						
Income producing - real estate	\$1,701	\$937	\$6,408	\$9,046	\$264,620	\$273,666
Land, land development and construction - real estate	487	66	2,720	3,273	51,453	54,726
Commercial and industrial	1,861	1,132	3,516	6,509	318,438	324,947
Mortgage						
1-4 family	3,507	1,418	15,983	20,908	294,771	315,679
Resort lending	2,129	932	8,819	11,880	184,943	196,823
Home equity line of credit - 1st lien	96	196	523	815	24,705	25,520
Home equity line of credit - 2nd lien	506	159	889	1,554	54,045	55,599

Installment						
Home equity installment - 1st lien	757	264	1,542	2,563	41,239	43,802
Home equity installment - 2nd lien	676	365	1,023	2,064	51,224	53,288
Loans not secured by real estate	1,173	463	880	2,516	117,661	120,177
Other	36	10	4	50	3,144	3,194
Payment plan receivables						
Full refund	2,943	951	491	4,385	99,284	103,669
Partial refund	380	200	424	1,004	9,918	10,922
Other	23	24	23	70	357	427
Total recorded investment	\$ 16,275	\$ 7,117	\$ 43,245	\$ 66,637	\$ 1,515,802	\$ 1,582,439
Accrued interest included in recorded investment	\$ 160	\$ 105	\$ 13	\$ 278	\$ 5,553	\$ 5,831



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Impaired loans are as follows :

	September 30, 2012	December 31, 2011
	(In thousands)	
Impaired loans with no allocated allowance		
TDR	\$26,094	\$26,945
Non - TDR	417	423
Impaired loans with an allocated allowance		
TDR - allowance based on collateral	18,071	20,142
TDR - allowance based on present value cash flow	108,312	98,130
Non - TDR - allowance based on collateral	8,361	13,773
Non - TDR - allowance based on present value cash flow	-	-
Total impaired loans	\$161,255	\$159,413
Amount of allowance for loan losses allocated		
TDR - allowance based on collateral	\$5,370	\$6,004
TDR - allowance based on present value cash flow	15,246	12,048
Non - TDR - allowance based on collateral	2,443	4,247
Non - TDR - allowance based on present value cash flow	-	-
Total amount of allowance for loan losses allocated	\$23,059	\$22,299

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Impaired loans by class are as follows (1):

	September 30, 2012			December 31, 2011		
	Recorded Investment	Unpaid Principal Balance	Related Allowance	Recorded Investment	Unpaid Principal Balance	Related Allowance
With no related allowance recorded:						
	(In thousands)					
Commercial						
Income producing - real estate	\$1,806	\$2,672	\$-	\$4,626	\$6,386	\$-
Land, land development & construction-real estate	3,468	3,456	-	219	243	-
Commercial and industrial	3,634	4,144	-	3,593	3,677	-
Mortgage						
1-4 family	6,891	9,079	-	6,975	9,242	-
Resort lending	5,933	6,386	-	7,156	7,680	-
Home equity line of credit - 1st lien	15	32	-	-	-	-
Home equity line of credit - 2nd lien	44	118	-	134	211	-
Installment						
Home equity installment - 1st lien	2,026	2,201	-	2,100	2,196	-
Home equity installment - 2nd lien	2,226	2,225	-	1,987	1,987	-
Loans not secured by real estate	550	622	-	637	688	-
Other	22	21	-	24	24	-
	26,615	30,956	-	27,451	32,334	-
With an allowance recorded:						
Commercial						
Income producing - real estate	25,530	28,980	2,813	22,781	29,400	3,642
Land, land development & construction-real estate	9,367	11,847	2,279	12,362	14,055	3,633
Commercial and industrial	19,906	23,882	3,276	15,093	18,357	2,977
Mortgage						
1-4 family	59,389	61,071	8,868	61,214	63,464	7,716
Resort lending	18,261	18,500	4,195	18,159	19,351	2,534
Home equity line of credit - 1st lien	47	46	31	64	73	35
Home equity line of credit - 2nd lien	-	-	-	-	-	-
Installment						
Home equity installment - 1st lien	1,298	1,348	639	1,232	1,293	660
Home equity installment - 2nd lien	1,108	1,119	877	1,421	1,458	1,062

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Loans not secured by real estate	275	284	81	153	156	40
Other	-	-	-	-	-	-
	135,181	147,077	23,059	132,479	147,607	22,299
<b>Total</b>						
<b>Commercial</b>						
Income producing - real estate	27,336	31,652	2,813	27,407	35,786	3,642
Land, land development & construction-real estate	12,835	15,303	2,279	12,581	14,298	3,633
Commercial and industrial	23,540	28,026	3,276	18,686	22,034	2,977
<b>Mortgage</b>						
1-4 family	66,280	70,150	8,868	68,189	72,706	7,716
Resort lending	24,194	24,886	4,195	25,315	27,031	2,534
Home equity line of credit - 1st lien	62	78	31	64	73	35
Home equity line of credit - 2nd lien	44	118	-	134	211	-
<b>Installment</b>						
Home equity installment - 1st lien	3,324	3,549	639	3,332	3,489	660
Home equity installment - 2nd lien	3,334	3,344	877	3,408	3,445	1,062
Loans not secured by real estate	825	906	81	790	844	40
Other	22	21	-	24	24	-
Total	\$ 161,796	\$ 178,033	\$ 23,059	\$ 159,930	\$ 179,941	\$ 22,299
<b>Accrued interest included in recorded investment</b>						
	\$ 541			\$ 517		

(1) There were no impaired payment plan receivables at September 30, 2012 or December 31, 2011.

IndexNOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)  
(unaudited)

Average recorded investment in and interest income earned on impaired loans by class for the three month periods ended September 30, follows:

	2012		2011	
	Average Recorded Investment	Interest Income Recognized	Average Recorded Investment	Interest Income Recognized
	(In thousands)			
With no related allowance recorded:				
Commercial				
Income producing - real estate	\$1,827	\$15	\$2,214	\$65
Land, land development & construction-real estate	3,131	61	188	13
Commercial and industrial	3,483	58	1,711	83
Mortgage				
1-4 family	7,271	80	9,042	82
Resort lending	5,923	52	8,877	99
Home equity line of credit - 1st lien	19	-	-	-
Home equity line of credit - 2nd lien	45	-	124	-
Installment				
Home equity installment - 1st lien	2,063	20	2,053	24
Home equity installment - 2nd lien	2,233	29	2,133	24
Loans not secured by real estate	540	8	737	11
Other	22	1	26	-
	26,557	324	27,105	401
With an allowance recorded:				
Commercial				
Income producing - real estate	26,233	207	19,789	30
Land, land development & construction-real estate	9,785	31	7,356	(9)
Commercial and industrial	20,749	136	10,445	(49)
Mortgage				
1-4 family	59,322	626	61,934	668
Resort lending	18,411	212	18,522	109
Home equity line of credit - 1st lien	47	1	47	-
Home equity line of credit - 2nd lien	-	-	10	-
Installment				
Home equity installment - 1st lien	1,348	11	1,421	14
Home equity installment - 2nd lien	1,130	13	1,421	16
Loans not secured by real estate	277	2	131	2
Other	-	-	-	-
	137,302	1,239	121,076	781
Total				
Commercial				
Income producing - real estate	28,060	222	22,003	95
Land, land development & construction-real estate	12,916	92	7,544	4
Commercial and industrial	24,232	194	12,156	34
Mortgage				
1-4 family	66,593	706	70,976	750

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Resort lending	24,334	264	27,399	208
Home equity line of credit - 1st lien	66	1	47	-
Home equity line of credit - 2nd lien	45	-	134	-
<b>Installment</b>				
Home equity installment - 1st lien	3,411	31	3,474	38
Home equity installment - 2nd lien	3,363	42	3,554	40
Loans not secured by real estate	817	10	868	13
Other	22	1	26	-
Total	\$163,859	\$1,563	\$148,181	\$1,182

(1) There were no impaired payment plan receivables during the three month periods ended September 30, 2012 and 2011.

IndexNOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)  
(unaudited)

Average recorded investment in and interest income earned on impaired loans by class for the nine month periods ended September 30, follows:

	2012		2011	
	Average Recorded Investment	Interest Income Recognized	Average Recorded Investment	Interest Income Recognized
	(In thousands)			
With no related allowance recorded:				
Commercial				
Income producing - real estate	\$2,713	\$45	\$2,806	\$95
Land, land development & construction-real estate	2,360	97	712	40
Commercial and industrial	3,755	104	2,694	100
Mortgage				
1-4 family	7,274	229	8,964	296
Resort lending	6,339	178	7,900	322
Home equity line of credit - 1st lien	9	-	-	-
Home equity line of credit - 2nd lien	67	2	115	2
Installment				
Home equity installment - 1st lien	1,945	72	1,919	72
Home equity installment - 2nd lien	2,047	80	2,021	73
Loans not secured by real estate	533	21	588	27
Other	23	2	13	1
	27,065	830	27,732	1,028
With an allowance recorded:				
Commercial				
Income producing - real estate	24,228	474	17,820	152
Land, land development & construction-real estate	10,680	136	9,195	60
Commercial and industrial	18,227	406	10,603	92
Mortgage				
1-4 family	59,793	1,926	63,210	2,019
Resort lending	18,355	582	22,648	505
Home equity line of credit - 1st lien	57	2	24	1
Home equity line of credit - 2nd lien	24	-	11	-
Installment				
Home equity installment - 1st lien	1,487	41	1,453	42
Home equity installment - 2nd lien	1,367	38	1,478	46
Loans not secured by real estate	227	7	172	3
Other	-	-	-	-
	134,445	3,612	126,614	2,920
Total				
Commercial				
Income producing - real estate	26,941	519	20,626	247
Land, land development & construction-real estate	13,040	233	9,907	100
Commercial and industrial	21,982	510	13,297	192
Mortgage				
1-4 family	67,067	2,155	72,174	2,315

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Resort lending	24,694	760	30,548	827
Home equity line of credit - 1st lien	66	2	24	1
Home equity line of credit - 2nd lien	91	2	126	2
<b>Installment</b>				
Home equity installment - 1st lien	3,432	113	3,372	114
Home equity installment - 2nd lien	3,414	118	3,499	119
Loans not secured by real estate	760	28	760	30
Other	23	2	13	1
Total	\$161,510	\$4,442	\$154,346	\$3,948

(1) There were no impaired payment plan receivables during the nine month periods ended September 30, 2012 and 2011.

IndexNOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)  
(unaudited)

Our average investment in impaired loans was approximately \$163.9 million and \$148.2 million for the three-month periods ended September 30, 2012 and 2011, respectively and \$161.5 million and \$154.3 million for the nine-month periods ended September 30, 2012 and 2011, respectively. Cash receipts on impaired loans on non-accrual status are generally applied to the principal balance. Interest income recognized on impaired loans during the three months ended September 30, 2012 and 2011 was approximately \$1.6 million and \$1.2 million, respectively and was approximately \$4.4 million and \$3.9 million during the nine months ended September 30, 2012 and 2011, respectively.

Troubled debt restructurings follow:

	September 30, 2012		
	Commercial	Retail	Total
	(In thousands)		
Performing TDR's	\$ 44,061	\$ 88,441	\$ 132,502
Non-performing TDR's(1)	10,738	9,237 (2)	19,975
Total	\$ 54,799	\$ 97,678	\$ 152,477

	December 31, 2011		
	Commercial	Retail	Total
	(In thousands)		
Performing TDR's	\$ 29,799	\$ 86,770	\$ 116,569
Non-performing TDR's(1)	14,567	14,081 (2)	28,648
Total	\$ 44,366	\$ 100,851	\$ 145,217

(1) Included in non-performing loans table shown previously.

(2) Also includes loans on non-accrual at the time of modification until six payments are received on a timely basis.

The Company has allocated \$20.6 million and \$18.1 million of specific reserves to customers whose loan terms have been modified in troubled debt restructurings as of September 30, 2012 and December 31, 2011, respectively.

During the three and nine months ended September 30, 2012 and 2011, the terms of certain loans were modified as troubled debt restructurings. The modification of the terms of such loans generally included one or a combination of the following: a reduction of the stated interest rate of the loan; an extension of the maturity date at a stated rate of interest lower than the current market rate for new debt with similar risk; or a permanent reduction of the recorded investment in the loan.

Modifications involving a reduction of the stated interest rate of the loan have generally been for periods ranging from 9 months to 60 months but have extended to as much as 480 months in certain circumstances. Modifications involving an extension of the maturity date have generally been for periods ranging from 1 month to 60 months but have extended to as much as 472 months in certain circumstances.



IndexNOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)  
(unaudited)

Loans that have been classified as troubled debt restructurings during the three-month periods ended September 30 follow:

	Number of Contracts	Pre-modification Recorded Balance (Dollars in thousands)	Post-modification Recorded Balance
2012			
Commercial			
Income producing - real estate	4	\$ 626	\$ 545
Land, land development & construction-real estate	2	460	523
Commercial and industrial	10	631	558
Mortgage			
1-4 family	10	1,870	1,656
Resort lending	7	1,575	1,562
Home equity line of credit - 1st lien	-	-	-
Home equity line of credit - 2nd lien	-	-	-
Installment			
Home equity installment - 1st lien	4	137	98
Home equity installment - 2nd lien	2	59	56
Loans not secured by real estate	2	22	21
Other	-	-	-
Total	41	\$ 5,380	\$ 5,019
2011			
Commercial			
Income producing - real estate	5	\$ 6,579	\$ 6,370
Land, land development & construction-real estate	1	1,900	1,804
Commercial and industrial	-	-	-
Mortgage			
1-4 family	6	1,603	1,629
Resort lending	4	1,515	1,501
Home equity line of credit - 1st lien	-	-	-
Home equity line of credit - 2nd lien	-	-	-
Installment			
Home equity installment - 1st lien	4	98	99
Home equity installment - 2nd lien	-	-	-
Loans not secured by real estate	5	67	68
Other	-	-	-
Total	25	\$ 11,762	\$ 11,471

IndexNOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)  
(unaudited)

Loans that have been classified as troubled debt restructurings during the nine-month periods ended September 30 follow:

	Number of Contracts	Pre-modification Recorded Balance (Dollars in thousands)	Post-modification Recorded Balance
2012			
Commercial			
Income producing - real estate	18	\$ 8,894	\$ 8,736
Land, land development & construction-real estate	5	3,347	3,436
Commercial and industrial	43	8,827	8,453
Mortgage			
1-4 family	58	7,738	7,330
Resort lending	29	7,529	7,356
Home equity line of credit - 1st lien	1	15	-
Home equity line of credit - 2nd lien	-	-	-
Installment			
Home equity installment - 1st lien	14	561	521
Home equity installment - 2nd lien	16	604	590
Loans not secured by real estate	12	299	278
Other	-	-	-
Total	196	\$ 37,814	\$ 36,700
2011			
Commercial			
Income producing - real estate	16	\$ 14,793	\$ 13,928
Land, land development & construction-real estate	3	5,111	1,893
Commercial and industrial	10	1,129	1,111
Mortgage			
1-4 family	59	7,663	7,540
Resort lending	27	7,474	7,393
Home equity line of credit - 1st lien	1	45	47
Home equity line of credit - 2nd lien	1	23	19
Installment			
Home equity installment - 1st lien	18	475	470
Home equity installment - 2nd lien	14	464	450
Loans not secured by real estate	23	411	404
Other	-	-	-
Total	172	\$ 37,588	\$ 33,255

The troubled debt restructurings described above for 2012 increased the allowance for loan losses by \$0.4 million and resulted in zero charge offs during the three months ended September 30, 2012, respectively and increased the allowance by \$1.5 million and resulted in \$0.4 million charge offs during the nine months ended September 30, 2012, respectively.

The troubled debt restructurings described above for 2011 increased the allowance for loan losses by \$0.1 million and resulted in charge offs of \$0.3 million during the three months ended September 30, 2011, respectively and increased the allowance by \$0.7 million and resulted in charge offs of \$3.8 million during the nine months ended September 30, 2011, respectively.

IndexNOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)  
(unaudited)

Loans that have been classified as troubled debt restructurings during the past twelve months and that have subsequently defaulted during the three-month periods ended September 30 follow:

	Number of Contracts	Recorded Balance (Dollars in thousands)
2012		
Commercial		
Income producing - real estate	2	\$827
Land, land development & construction-real estate	-	-
Commercial and industrial	-	-
Mortgage		
1-4 family	-	-
Resort lending	2	468
Home equity line of credit - 1st lien	-	-
Home equity line of credit - 2nd lien	-	-
Installment		
Home equity installment - 1st lien	-	-
Home equity installment - 2nd lien	-	-
Loans not secured by real estate	-	-
Other	-	-
	4	\$1,295
2011		
Commercial		
Income producing - real estate	1	\$136
Land, land development & construction-real estate	-	-
Commercial and industrial	-	-
Mortgage		
1-4 family	4	607
Resort lending	1	340
Home equity line of credit - 1st lien	-	-
Home equity line of credit - 2nd lien	-	-
Installment		
Home equity installment - 1st lien	-	-
Home equity installment - 2nd lien	1	46
Loans not secured by real estate	-	-
Other	-	-
	7	\$1,129

IndexNOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)  
(unaudited)

Loans that have been classified as troubled debt restructurings during the past twelve months and that have subsequently defaulted during the nine-month periods ended September 30 follows:

	Number of Contracts	Recorded Balance (Dollars in thousands)
2012		
Commercial		
Income producing - real estate	2	\$827
Land, land development & construction-real estate	1	136
Commercial and industrial	7	520
Mortgage		
1-4 family	2	148
Resort lending	3	584
Home equity line of credit - 1st lien	-	-
Home equity line of credit - 2nd lien	-	-
Installment		
Home equity installment - 1st lien	1	26
Home equity installment - 2nd lien	1	20
Loans not secured by real estate	-	-
Other	-	-
	17	\$2,261
2011		
Commercial		
Income producing - real estate	3	\$1,042
Land, land development & construction-real estate	1	1,222
Commercial and industrial	-	-
Mortgage		
1-4 family	8	1,024
Resort lending	5	1,128
Home equity line of credit - 1st lien	-	-
Home equity line of credit - 2nd lien	-	-
Installment		
Home equity installment - 1st lien	1	19
Home equity installment - 2nd lien	4	264
Loans not secured by real estate	-	-
Other	-	-
	22	\$4,699

A loan is considered to be in payment default generally once it is 90 days contractually past due under the modified terms.

The troubled debt restructurings that subsequently defaulted described above for 2012 increased the allowance for loan losses by \$0.7 million and resulted in zero charge offs during the three months ended September 30, 2012, respectively and increased the allowance for loan losses by \$0.7 million and resulted in charge offs of \$0.4 million during the nine months ended September 30, 2012, respectively.

The troubled debt restructurings that subsequently defaulted described above for 2011 increased the allowance for loan losses by \$0.2 million and resulted in charge offs of \$0.1 million during the three months ended September 30, 2011, respectively and decreased the allowance for loan losses by \$0.4 million and resulted in charge offs of \$1.5 million during the nine months ended September 30, 2011, respectively.

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NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)  
(unaudited)

The terms of certain other loans were modified during the three and nine months ended September 30, 2012 and 2011 that did not meet the definition of a troubled debt restructuring. The modification of these loans could have included modification of the terms of a loan to borrowers who were not experiencing financial difficulties or a delay in a payment that was considered to be insignificant.

In order to determine whether a borrower is experiencing financial difficulty, we perform an evaluation of 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 our internal underwriting policy.

Credit Quality Indicators – As part of our on on-going monitoring of the credit quality of our loan portfolios, we track certain credit quality indicators including (a) weighted-average risk grade of commercial loans, (b) the level of classified commercial loans (c) credit scores of mortgage and installment loan borrowers (d) investment grade of certain counterparties for payment plan receivables and (e) delinquency history and non-performing loans.

For commercial loans we use a loan rating system that is similar to those employed by state and federal banking regulators. Loans are graded on a scale of 1 to 12. A description of the general characteristics of the ratings follows:

Rating 1 through 6: These loans are generally referred to as our “non-watch” commercial credits that include very high or exceptional credit fundamentals through acceptable credit fundamentals.

Rating 7 and 8: These loans are generally referred to as our “watch” commercial credits. This rating includes loans to borrowers that exhibit potential credit weakness or downward trends. If not checked or cured these trends could weaken our asset or credit position. While potentially weak, no loss of principal or interest is envisioned with these ratings.

Rating 9: These loans are generally referred to as our “substandard accruing” commercial credits. This rating includes loans to borrowers that exhibit a well-defined weakness where payment default is probable and loss is possible if deficiencies are not corrected. Generally, loans with this rating are considered collectible as to both principal and interest primarily due to collateral coverage.

Rating 10 and 11: These loans are generally referred to as our “substandard - non-accrual” and “doubtful” commercial credits. This rating includes loans to borrowers with weaknesses that make collection of debt in full, on the basis of current facts, conditions and values at best questionable and at worst improbable. All of these loans are placed in non-accrual.

Rating 12: These loans are generally referred to as our “loss” commercial credits. This rating includes loans to borrowers that are deemed incapable of repayment and are charged-off.

IndexNOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)  
(unaudited)

The following table summarizes loan ratings by loan class for our commercial loan segment:

	Non-watch 1-6	Watch 7-8	Commercial Substandard Accrual 9 (In thousands)	Non- Accrual 10-11	Total
September 30, 2012					
Income producing - real estate	\$ 166,740	\$ 37,261	\$ 2,513	\$ 7,742	\$ 214,256
Land, land development and construction - real estate	31,129	5,172	2,673	4,598	43,572
Commercial and industrial	294,232	30,032	16,033	7,174	347,471
Total	\$ 492,101	\$ 72,465	\$ 21,219	\$ 19,514	\$ 605,299
Accrued interest included in total	\$ 1,430	\$ 240	\$ 91	\$ -	\$ 1,761
December 31, 2011					
Income producing - real estate	\$ 201,655	\$ 52,438	\$ 5,785	\$ 13,788	\$ 273,666
Land, land development and construction - real estate	33,515	9,421	4,800	6,990	54,726
Commercial and industrial	275,245	27,783	13,935	7,984	324,947
Total	\$ 510,415	\$ 89,642	\$ 24,520	\$ 28,762	\$ 653,339
Accrued interest included in total	\$ 1,677	\$ 381	\$ 126	\$ -	\$ 2,184



IndexNOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)  
(unaudited)

For each of our mortgage and consumer segment classes we generally monitor credit quality based on the credit scores of the borrowers. These credit scores are generally updated at least annually.

The following table summarizes credit scores by loan class for our mortgage and installment loan segments:

	1-4 Family	Resort Lending	Mortgage (1) Home Equity 1st Lien (In thousands)	Home Equity 2nd Lien	Total
September 30, 2012					
800 and above	\$ 23,203	\$ 19,052	\$ 2,586	\$ 5,282	\$ 50,123
750-799	58,758	64,803	5,871	13,757	143,189
700-749	57,904	46,530	3,476	9,033	116,943
650-699	59,330	23,087	2,347	8,432	93,196
600-649	34,130	10,136	2,578	4,507	51,351
550-599	27,993	6,786	1,326	2,941	39,046
500-549	22,506	2,888	885	2,308	28,587
Under 500	8,961	847	468	668	10,944
Unknown	5,378	577	152	178	6,285
Total	\$ 298,163	\$ 174,706	\$ 19,689	\$ 47,106	\$ 539,664
Accrued interest included in total	\$ 1,392	\$ 808	\$ 101	\$ 256	\$ 2,557
December 31, 2011					
800 and above	\$ 26,509	\$ 17,345	\$ 4,062	\$ 6,317	\$ 54,233
750-799	63,746	76,381	8,058	16,892	165,077
700-749	55,047	53,210	4,280	12,131	124,668
650-699	54,579	21,579	2,854	7,909	86,921
600-649	40,977	12,750	2,485	5,066	61,278
550-599	29,732	10,698	1,547	3,466	45,443
500-549	28,573	3,716	1,615	2,758	36,662
Under 500	12,434	565	539	886	14,424
Unknown	4,082	579	80	174	4,915
Total	\$ 315,679	\$ 196,823	\$ 25,520	\$ 55,599	\$ 593,621
Accrued interest included in total	\$ 1,404	\$ 928	\$ 123	\$ 290	\$ 2,745

IndexNOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)  
(unaudited)

	Home Equity 1st Lien	Home Equity 2nd Lien	Installment(1) Loans not Secured by Real Estate (In thousands)	Other	Total
September 30, 2012					
800 and above	\$ 3,900	\$ 3,741	\$ 19,738	\$ 46	\$ 27,425
750-799	8,350	11,554	46,222	551	66,677
700-749	5,507	9,231	23,674	711	39,123
650-699	5,813	7,541	14,369	592	28,315
600-649	3,791	4,666	6,685	497	15,639
550-599	3,309	2,489	3,269	170	9,237
500-549	2,164	1,786	2,802	125	6,877
Under 500	710	939	793	24	2,466
Unknown	48	7	2,676	26	2,757
Total	\$ 33,592	\$ 41,954	\$ 120,228	\$ 2,742	\$ 198,516
Accrued interest included in total	\$ 144	\$ 160	\$ 453	\$ 23	\$ 780
December 31, 2011					
800 and above	\$ 5,466	\$ 5,047	\$ 18,245	\$ 70	\$ 28,828
750-799	11,651	16,475	41,501	572	70,199
700-749	6,899	10,693	23,174	883	41,649
650-699	7,144	8,407	15,646	673	31,870
600-649	4,943	5,412	7,599	434	18,388
550-599	3,435	3,221	4,573	270	11,499
500-549	3,021	3,145	3,011	183	9,360
Under 500	1,160	854	1,391	50	3,455
Unknown	83	34	5,037	59	5,213
Total	\$ 43,802	\$ 53,288	\$ 120,177	\$ 3,194	\$ 220,461
Accrued interest included in total	\$ 176	\$ 208	\$ 489	\$ 29	\$ 902

(1) Credit scores have been updated within the last twelve months.

Mepco Finance Corporation (“Mepco”) is a wholly-owned subsidiary of our Bank that operates a vehicle service contract payment plan business throughout the United States. See Note #14 for more information about Mepco’s business. As of September 30, 2012, approximately 91.7% of Mepco’s outstanding payment plan receivables relate to programs in which a third party insurer or risk retention group is obligated to pay Mepco the full refund owing upon cancellation of the related service contract (including with respect to both the portion funded to the service contract seller and the portion funded to the administrator). These receivables are shown as “Full Refund” in the table below. Another approximately 8.0% of Mepco’s outstanding payment plan receivables as of September 30, 2012, relate to programs in which a third party insurer or risk retention group is obligated to pay Mepco the refund owing upon cancellation only with respect to the unearned portion previously funded by Mepco to the administrator (but not to the service contract seller). These receivables are shown as “Partial Refund” in the table below. The balance of Mepco’s outstanding payment plan receivables relate to programs in which there is no insurer or risk retention group that has

any contractual liability to Mepco for any portion of the refund amount. These receivables are shown as “Other” in the table below. For each class of our payment plan receivables we monitor credit ratings of the counterparties as we evaluate the credit quality of this portfolio.

IndexNOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)  
(unaudited)

The following table summarizes credit ratings of insurer or risk retention group counterparties by class of payment plan receivable:

	Full Refund	Payment Plan Receivables Partial Refund		Other	Total
		(In thousands)			
September 30, 2012					
AM Best rating					
A +	\$ -	\$ -	\$ 149	\$ 149	
A	29,211	4,657	-		33,868
A-	18,001	2,802	-		20,803
B +	162	-	-		162
B	-	-	-		-
Not rated	38,488	-	138		38,626
Total	\$ 85,862	\$ 7,459	\$ 287	\$ 93,608	
December 31, 2011					
AM Best rating					
A +	\$ -	\$ 118	\$ 7	\$ 125	
A	32,461	165	269		32,895
A-	27,056	10,639	-		37,695
B +	1,390	-	-		1,390
B	-	-	-		-
Not rated	42,762	-	151		42,913
Total	\$ 103,669	\$ 10,922	\$ 427	\$ 115,018	

Although Mepco has contractual recourse against various counterparties for refunds owing upon cancellation of vehicle service contracts, please see Note #14 below regarding certain risks and difficulties associated with collecting these refunds.

## 5. Segments

Our reportable segments are based upon legal entities. We currently have two reportable segments: Independent Bank (“IB” or “Bank”) and Mepco. These business segments are also differentiated based on the products and services provided. We evaluate performance based principally on net income (loss) of the respective reportable segments.

In the normal course of business, our IB segment provides funding to our Mepco segment through an intercompany line of credit priced at the prime rate of interest as published in the Wall Street Journal. Our IB segment also provides certain administrative services to our Mepco segment which reimburses at an agreed upon rate. These intercompany transactions are eliminated upon consolidation. The only other material intersegment balances and transactions are investments in subsidiaries at the parent entities and cash balances on deposit at our IB segment.

IndexNOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)  
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A summary of selected financial information for our reportable segments as of or for the three-month and nine-month periods ended September 30 follows:

As of or for the three months ended September 30,

	IB	Mepco	Other(1) (In thousands)	Elimination(2)	Total
2012					
Total assets	\$ 2,252,476	\$ 145,690	\$ 178,098	\$ (175,432 )	\$ 2,400,832
Interest income	21,057	3,676	-	-	24,733
Net interest income	19,380	2,806	(735 )	-	21,451
Provision for loan losses	270	(19 )	-	-	251
Income (loss) before income tax	6,988	405	(923 )	(24 )	6,446
Net income (loss)	7,125	268	(923 )	(24 )	6,446

2011					
Total assets	\$ 2,116,134	\$ 202,034	\$ 168,422	\$ (169,217 )	\$ 2,317,373
Interest income	22,913	5,274	-	-	28,187
Net interest income	20,474	3,982	(682 )	-	23,774
Provision for loan losses	6,165	6	-	-	6,171
Loss before income tax	(3,594 )	(150 )	(836 )	(24 )	(4,604 )
Net loss	(3,164 )	(96 )	(838 )	(24 )	(4,122 )

(1) Includes amounts relating to our parent company and certain insignificant operations.

(2)Includes parent company's investment in subsidiaries and cash balances maintained at subsidiary.

As of or for the nine months ended September 30,

	IB	Mepco	Other(1) (In thousands)	Elimination(2)	Total
2012					
Total assets	\$ 2,252,476	\$ 145,690	\$ 178,098	\$ (175,432 )	\$ 2,400,832
Interest income	64,452	11,232	-	-	75,684
Net interest income	59,085	8,487	(2,191 )	-	65,381
Provision for loan losses	6,436	2	-	-	6,438
Income (loss) before income tax	14,945	2,298	(2,889 )	(71 )	14,283
Net income (loss)	15,726	1,517	(2,889 )	(71 )	14,283

2011					
Total assets	\$ 2,116,134	\$ 202,034	\$ 168,422	\$ (169,217 )	\$ 2,317,373
Interest income	71,226	16,806	-	-	88,032
Net interest income	61,078	12,556	(2,026 )	-	71,608

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Provision for loan losses	20,986	43	-	-	21,029
Loss before income tax	(9,463 )	(1,062 )	(1,638 )	(71 )	(12,234 )
Net loss	(9,097 )	(678 )	(1,640 )	(71 )	(11,486 )

(1)Includes amounts relating to our parent company and certain insignificant operations.

(2)Includes parent company's investment in subsidiaries and cash balances maintained at subsidiary.

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## 6. Earnings Per Common Share

	Three months ended September 30,		Nine months ended September 30,	
	2012	2011	2012	2011
(In thousands, except per share amounts)				
Net income (loss) applicable to common stock	\$5,353	\$ (5,165 )	\$ 11,042	\$ (14,588 )
Convertible preferred stock dividends	1,093	-	3,241	-
Net income (loss) applicable to common stock for calculation of diluted earnings per share(1) (2)	\$6,446	\$ (5,165 )	\$ 14,283	\$ (14,588 )
Weighted average shares outstanding	8,779	8,401	8,637	8,209
Effect of convertible preferred stock	30,523	42,452	30,523	42,452
Restricted stock units	221	140	167	116
Stock units for deferred compensation plan for non-employee directors	81	7	54	7
Effect of stock options	9	-	-	-
Weighted average shares outstanding for calculation of diluted earnings per share(1)	39,613	51,000	39,381	50,784
Net income (loss) per common share				
Basic	\$.61	\$ (.61 )	\$ 1.28	\$ (1.78 )
Diluted(2)	.16	(.61 )	.36	(1.78 )

(1) For any period in which a loss is recorded, dividends on convertible preferred stock are not added back in the diluted per share calculation. For any period in which a loss is recorded, the assumed conversion of convertible preferred stock, assumed exercise of common stock warrants, assumed exercise of stock options, restricted stock units and stock units for a deferred compensation plan for non-employee directors would have an anti-dilutive impact on the loss per share and thus are ignored in the diluted per share calculation.

(2) Basic income (loss) per share includes weighted average common shares outstanding during the period and participating share awards.

Weighted average stock options outstanding that were not included in weighted average shares outstanding for calculation of diluted earnings per share because they were anti-dilutive totaled 0.1 million and 0.2 million for the three-month periods ended September 30, 2012 and 2011, respectively and totaled 0.2 million and 0.1 million for the nine-month periods ended September 30, 2012 and 2011, respectively. The warrant to purchase 346,154 shares of our common stock (see Note #15) was not included in weighted average shares outstanding for calculation of diluted earnings per share in all periods in 2012 and 2011 as it was anti-dilutive.

## 7. Derivative Financial Instruments

We are required to record derivatives on our Condensed Consolidated Statements of Financial Condition as assets and liabilities measured at their fair value. The accounting for increases and decreases in the value of derivatives depends upon the use of derivatives and whether the derivatives qualify for hedge accounting.



IndexNOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)  
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Our derivative financial instruments according to the type of hedge in which they are designated follows:

	September 30, 2012		
	Notional	Average	Fair
	Amount	Maturity	Value
		(years)	
	(Dollars in thousands)		
Cash Flow Hedges - Pay fixed interest-rate swap agreements	\$ 10,000	2.3	\$(835 )
No hedge designation			
Mandatory commitments to sell mortgage loans	\$ 62,883	0.1	\$ 2,787
Rate-lock mortgage loan commitments	101,482	0.1	(1,475 )
Amended Warrant	2,504	6.2	(385 )
Total	\$ 166,869	0.2	\$ 927

We have established management objectives and strategies that include interest-rate risk parameters for maximum fluctuations in net interest income and market value of portfolio equity. We monitor our interest rate risk position via simulation modeling reports. The goal of our asset/liability management efforts is to maintain profitable financial leverage within established risk parameters.

We use variable-rate and short-term fixed-rate (less than 12 months) debt obligations to fund a portion of our balance sheet, which exposes us to variability in interest rates. To meet our objectives, we may periodically enter into derivative financial instruments to mitigate exposure to fluctuations in cash flows resulting from changes in interest rates ("Cash Flow Hedges"). Cash Flow Hedges currently include certain pay-fixed interest-rate swaps. Pay-fixed interest-rate swaps convert the variable-rate cash flows on debt obligations to fixed-rates.

We record the fair value of Cash Flow Hedges in accrued income and other assets and accrued expenses and other liabilities. On an ongoing basis, we adjust our Condensed Consolidated Statements of Financial Condition to reflect the then current fair value of Cash Flow Hedges. The related gains or losses are reported in other comprehensive income or loss and are subsequently reclassified into earnings, as a yield adjustment in the same period in which the related interest on the hedged items (primarily variable-rate debt obligations) affect earnings. It is anticipated that approximately \$0.4 million, of unrealized losses on Cash Flow Hedges at September 30, 2012 will be reclassified to earnings over the next twelve months. To the extent that the Cash Flow Hedges are not effective, the ineffective portion of the Cash Flow Hedges is immediately recognized as interest expense. The maximum term of any Cash Flow Hedge at September 30, 2012 is 2.3 years.

Certain financial derivative instruments have not been designated as hedges. The fair value of these derivative financial instruments has been recorded on our Condensed Consolidated Statements of Financial Condition and are adjusted on an ongoing basis to reflect their then current fair value. The changes in fair value of derivative financial instruments not designated as hedges are recognized in earnings.

IndexNOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)  
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In the ordinary course of business, we enter into rate-lock mortgage loan commitments with customers (“Rate Lock Commitments”). These commitments expose us to interest rate risk. We also enter into mandatory commitments to sell mortgage loans (“Mandatory Commitments”) to reduce the impact of price fluctuations of mortgage loans held for sale and Rate Lock Commitments. Mandatory Commitments help protect our loan sale profit margin from fluctuations in interest rates. The changes in the fair value of Rate Lock Commitments and Mandatory Commitments are recognized currently as part of net gains on mortgage loans. We obtain market prices on Mandatory Commitments and Rate Lock Commitments. Net gains on mortgage loans, as well as net income (loss) may be more volatile as a result of these derivative instruments, which are not designated as hedges.

During 2010, we entered into an amended and restated warrant with the U.S. Department of the Treasury (“UST”) that would allow them to purchase our common stock at a fixed price (see Note #15). Because of certain anti-dilution features included in the Amended Warrant (as defined in Note #15), it is not considered to be indexed to our common stock and is therefore accounted for as a derivative instrument and recorded as a liability. Any change in value of the Amended Warrant is recorded in other income in our Condensed Consolidated Statements of Operations.

The following tables illustrate the impact that the derivative financial instruments discussed above have on individual line items in the Condensed Consolidated Statements of Financial Condition for the periods presented:

## Fair Values of Derivative Instruments

Asset Derivatives					Liability Derivatives			
September 30, 2012		December 31, 2011			September 30, 2012		December 31, 2011	
Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value		Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value
(In thousands)								
Derivatives designated as hedging instruments								
Pay-fixed interest rate swap agreements					Other liabilities	\$835	Other liabilities	\$1,103
Total						835		1,103
Derivatives not designated as hedging instruments								
Rate-lock mortgage loan commitments								
Other assets	\$2,787	Other assets	\$857					
Mandatory commitments to sell mortgage	-		-		1,475		Other liabilities	606

loans

Amended Warrant	-	-	Other liabilities	385	Other liabilities	174
Total	2,787	857		1,860		780
Total derivatives	\$2,787	\$857		\$ 2,695		\$1,883

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The effect of derivative financial instruments on the Condensed Consolidated Statements of Operations follows:

		Three Month Periods Ended September 30,									
		Gain (Loss) Recognized in Other Comprehensive Income (Loss) (Effective Portion)		Location of Gain (Loss) Reclassified from Accumulated Other Comprehensive Income into Income (Effective Portion)		Gain (Loss) Reclassified from Accumulated Other Comprehensive Loss into Income (Effective Portion)		Location of Gain (Loss) Recognized in Income (1)		Gain (Loss) Recognized in Income	
		2012	2011			2012	2011		2012	2011	
(In thousands)											
Cash Flow											
Hedges											
Pay-fixed interest rate swap agreements											
	\$ (54 )	\$ (215 )	Interest expense	\$ (237 )	\$ (345 )				\$ -	\$ 3	
Interest-rate cap agreements											
	-	-	Interest expense	-	-				-	-	
Total	\$ (54 )	\$ (215 )		\$ (237 )	\$ (345 )				\$ -	\$ 3	
No hedge designation											
Rate-lock mortgage loan commitments											
								Net mortgage loan gains	\$ 804	\$ 369	
Mandatory commitments to sell mortgage loans											
								Net mortgage loan gains (Increase) decrease in fair value of U.S. Treasury warrant	(779 )	(339 )	
Amended warrant									(32 )	29	
Total									\$ (7 )	\$ 59	

(1)For cash flow hedges, this location and amount refers to the ineffective portion.

IndexNOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)  
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		Nine Month Periods Ended September 30,					
		Location of Gain (Loss) Reclassified from		Gain (Loss) Reclassified from Accumulated Other		Location of Gain (Loss) Recognized	
Gain (Loss) Recognized in Other Comprehensive Income (Loss) (Effective Portion)		Accumulated Other Comprehensive Income into Income (Effective Portion)		Gain (Loss) Reclassified from Accumulated Other Comprehensive Loss into Income (Effective Portion)		Gain (Loss) Recognized in Income	
2012	2011			2012	2011	in Income (1)	2012 2011
(In thousands)							
Cash Flow							
Hedges							
Pay-fixed							
interest rate							
swap							
agreements	\$ (129 )	\$ (508 )	Interest expense	\$ (833 )	\$ (1,102 )		\$ - \$ -
Interest-rate							
cap							
agreements	-	30	Interest expense	-	(15 )		- -
Total	\$ (129 )	\$ (478 )		\$ (833 )	\$ (1,117 )		\$ - \$ -
No hedge							
designation							