LAKELAND FINANCIAL CORP
Form 10-Q
August 03, 2018

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

FORM 10 Q

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

For the quarterly period ended June 30, 2018

OR

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

For the transition period from ____________ to _____________

LAKELAND FINANCIAL CORPORATION
(Exact name of registrant as specified in its charter)

Indiana	0-11487	35-1559596
(State or Other Jurisdiction of Incorporation or Organization)	(Commission File Number)	(IRS Employer Identification No.)

202 East Center Street, P.O. Box 1387, Warsaw, Indiana 46581 1387
(Address of Principal Executive Offices)(Zip Code)

(574) 267 6144
(Registrant's Telephone Number, Including Area Code)

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

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

Large accelerated filer [X]   Accelerated filer [ ]   Non-accelerated filer [ ] (do not check if a smaller reporting company)
Smaller reporting company [ ]   Emerging growth company [ ]

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

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

Number of shares of common stock outstanding at July 31, 2018: 25,301,732

TABLE OF CONTENTS

ITEM 1. FINANCIAL STATEMENTS

CONSOLIDATED BALANCE SHEETS (in thousands except share data)

	June 30, 2018 (Unaudited)	December 31, 2017
ASSETS		
Cash and due from banks	$147,439	$140,402
Short-term investments	32,786	35,778
Total cash and cash equivalents	180,225	176,180
Securities available for sale (carried at fair value)	563,227	538,493
Real estate mortgage loans held for sale	6,097	3,346
Loans, net of allowance for loan losses of $47,706 and $47,121	3,811,007	3,771,338
Land, premises and equipment, net	57,242	56,466
Bank owned life insurance	76,501	75,879
Federal Reserve and Federal Home Loan Bank stock	13,772	13,772
Accrued interest receivable	15,223	14,093
Goodwill	4,970	4,970
Other assets	32,605	28,439
Total assets	$4,760,869	$4,682,976
LIABILITIES AND STOCKHOLDERS' EQUITY		
LIABILITIES		
Noninterest bearing deposits	$839,784	$885,622
Interest bearing deposits	3,095,169	3,123,033
Total deposits	3,934,953	4,008,655
Borrowings		
Securities sold under agreements to repurchase	106,239	70,652
Federal Home Loan Bank advances	175,000	80,030
Subordinated debentures	30,928	30,928
Total borrowings	312,167	181,610
Accrued interest payable	7,328	6,311
Other liabilities	19,937	17,733
Total liabilities	4,274,385	4,214,309
STOCKHOLDERS' EQUITY		
Common stock: 90,000,000 shares authorized, no par value 25,294,582 shares issued and 25,126,537 outstanding as of June 30, 2018 25,194,903 shares issued and 25,025,933 outstanding as of December 31, 2017	109,223	108,862
Retained earnings	390,404	363,794
Accumulated other comprehensive income/(loss)	(9,710)	(670)
Treasury stock, at cost (2018 - 168,045 shares, 2017 - 168,970 shares)	(3,522)	(3,408)
Total stockholders' equity	486,395	468,578
Noncontrolling interest	89	89

Total equity	486,484	468,667
Total liabilities and equity	$4,760,869	$4,682,976

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

1

CONSOLIDATED STATEMENTS OF INCOME (unaudited - in thousands except share and per share data)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2018	2017	2018	2017
NET INTEREST INCOME				
Interest and fees on loans				
Taxable	$44,439	$36,967	$86,233	$71,414
Tax exempt	202	162	419	312
Interest and dividends on securities				
Taxable	2,492	2,364	4,926	4,684
Tax exempt	1,466	1,274	2,797	2,436
Other interest income	196	54	488	102
Total interest income	48,795	40,821	94,863	78,948
Interest on deposits	10,648	6,243	20,015	11,685
Interest on borrowings				
Short-term	195	431	306	741
Long-term	419	328	786	642
Total interest expense	11,262	7,002	21,107	13,068
NET INTEREST INCOME	37,533	33,819	73,756	65,880
Provision for loan losses	1,700	500	5,000	700
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	35,833	33,319	68,756	65,180
NONINTEREST INCOME				
Wealth advisory fees	1,544	1,284	3,049	2,534
Investment brokerage fees	377	299	667	620
Service charges on deposit accounts	3,800	3,253	7,428	6,396
Loan and service fees	2,421	1,897	4,598	3,790
Merchant card fee income	549	570	1,191	1,108
Bank owned life insurance income	348	402	711	873
Other income	216	659	1,255	1,168
Mortgage banking income	438	378	679	509
Net securities gains/(losses)	0	49	(6)	52
Total noninterest income	9,693	8,791	19,572	17,050
NONINTEREST EXPENSE				
Salaries and employee benefits	11,493	11,014	23,512	22,384
Net occupancy expense	1,237	1,154	2,663	2,274
Equipment costs	1,250	1,156	2,524	2,231
Data processing fees and supplies	2,290	1,974	4,803	3,990
Corporate and business development	1,046	1,196	2,179	2,698
FDIC insurance and other regulatory fees	409	419	870	853
Professional fees	910	801	1,782	1,755
Other expense	1,639	1,638	3,143	3,215
Total noninterest expense	20,274	19,352	41,476	39,400

INCOME BEFORE INCOME TAX EXPENSE	25,252	22,758	46,852	42,830
Income tax expense	5,110	7,394	8,374	12,952
NET INCOME	$20,142	$15,364	$38,478	$29,878
BASIC WEIGHTED AVERAGE COMMON SHARES	25,293,329	25,183,186	25,275,471	25,167,799
BASIC EARNINGS PER COMMON SHARE	$0.80	$0.61	$1.52	$1.19
DILUTED WEIGHTED AVERAGE COMMON SHARES	25,709,216	25,619,977	25,704,505	25,618,552
DILUTED EARNINGS PER COMMON SHARE	$0.78	$0.60	$1.50	$1.17

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

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (unaudited - in thousands)

	Three months ended June 30,		Six months ended June 30,	
	2018	2017	2018	2017
Net income	$20,142	$15,364	$38,478	$29,878
Other comprehensive income (loss)				
Change in securities available for sale:				
Unrealized holding gain (loss) on securities available for sale arising during the period	(2,242)	3,358	(11,402)	4,070
Reclassification adjustment for gains included in net income	0	(49)	6	(52)
Net securities gain (loss) activity during the period	(2,242)	3,309	(11,396)	4,018
Tax effect	471	(1,079)	2,499	(1,343)
Net of tax amount	(1,771)	2,230	(8,897)	2,675
Defined benefit pension plans:				
Amortization of net actuarial loss	67	67	133	133
Tax effect	(18)	(26)	(35)	(52)
Net of tax amount	49	41	98	81
Total other comprehensive income (loss), net of tax	(1,722)	2,271	(8,799)	2,756
Comprehensive income	$18,420	$17,635	$29,679	$32,634

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

CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY (unaudited - in thousands except share and per share data)

	Common Stock Shares	Stock	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Treasury Stock	Total Stockholders' Equity
Balance at January 1, 2017	24,937,865	$104,405	$327,873	$(2,387)	$(2,913)	$426,978
Comprehensive income:						
Net income			29,878			29,878
Other comprehensive income (loss), net of tax				2,756		2,756
Cash dividends declared, $0.41 per share			(10,324)			(10,324)
Treasury shares purchased under deferred						
directors' plan	(5,638)	256			(256)	0
Stock activity under equity compensation plans	89,532	(1,736)				(1,736)
Stock based compensation expense		2,819				2,819
Balance at June 30, 2017	25,021,759	$105,744	$347,427	$369	$(3,169)	$450,371
Balance at January 1, 2018	25,025,933	$108,862	$363,794	$(670)	$(3,408)	$468,578
Adoption of ASU 2018-02 (See Note 1)			173	(173)		0
Adoption of ASU 2014-09 (See Note 1)			24			24
Adoption of ASU 2016-01 (See Note 1)			68	(68)		0
Comprehensive income:						
Net income			38,478			38,478
Other comprehensive income (loss), net of tax				(8,799)		(8,799)
Cash dividends declared, $0.48 per share			(12,133)			(12,133)
Treasury shares purchased under deferred						
directors' plan	(4,711)	229			(229)	0
Treasury shares sold and distributed under deferred						
directors' plan	5,636	(115)			115	0
Stock activity under equity compensation plans	99,679	(2,435)				(2,435)
Stock based compensation expense		2,682				2,682

Balance at June 30, 2018	25,126,537	$109,223	$390,404	$(9,710)	$(3,522)	$486,395

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

4

CONSOLIDATED STATEMENTS OF CASH FLOWS (unaudited - in thousands)

Six Months Ended June 30	2018	2017
Cash flows from operating activities:		
Net income	$ 38,478	$ 29,878
Adjustments to reconcile net income to net cash from operating activities:		
Depreciation	2,761	2,412
Provision for loan losses	5,000	700
Net loss (gain) on sale and write down of other real estate owned	16	(5)
Amortization of loan servicing rights	254	307
Loans originated for sale	(25,121)	(25,622)
Net gain on sales of loans	(767)	(859)
Proceeds from sale of loans	22,748	27,773
Net loss (gain) on sales of premises and equipment	22	(5)
Net loss (gain) on sales and calls of securities available for sale	6	(52)
Net securities amortization	1,511	1,407
Stock based compensation expense	2,682	2,819
Earnings on life insurance	(711)	(873)
Gain on life insurance	(205)	0
Tax benefit of stock option exercises	(761)	(932)
Net change:		
Interest receivable and other assets	(2,812)	1,784
Interest payable and other liabilities	2,453	(2,804)
Total adjustments	7,076	6,050
Net cash from operating activities	45,554	35,928
Cash flows from investing activities:		
Proceeds from sale of securities available for sale	12,322	35,845
Proceeds from maturities, calls and principal paydowns of securities available for sale	24,809	30,837
Purchases of securities available for sale	(72,740)	(90,140)
Purchase of life insurance	(310)	(490)
Net increase in total loans	(44,669)	(106,011)
Proceeds from sales of land, premises and equipment	28	7
Purchases of land, premises and equipment	(3,587)	(6,814)
Proceeds from sales of other real estate	12	42
Proceeds from life insurance	568	0
Net cash from investing activities	(83,567)	(136,724)
Cash flows from financing activities:		
Net (decrease) increase in total deposits	(73,702)	38,027
Net increase in short-term borrowings	210,587	225,143
Payments on long-term borrowings	(80,030)	(180,002)
Common dividends paid	(12,120)	(10,311)
Preferred dividends paid	(13)	(13)
Payments related to equity incentive plans	(2,435)	(1,736)
Purchase of treasury stock	(229)	(256)
Net cash from financing activities	42,058	70,852
Net change in cash and cash equivalents	4,045	(29,944)
Cash and cash equivalents at beginning of the period	176,180	167,280

Cash and cash equivalents at end of the period	$ 180,225	$ 137,336
Cash paid during the period for:		
Interest	$ 20,090	$ 13,936
Income taxes	8,154	11,513
Supplemental non-cash disclosures:		
Loans transferred to other real estate owned	0	79
Securities purchases payable	1,898	0

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

NOTE 1. BASIS OF PRESENTATION

This report is filed for Lakeland Financial Corporation (the "Company") and its wholly owned subsidiaries, Lake City Bank (the "Bank") and LCB Risk Management, a captive insurance company. Also included in this report is the Bank's wholly owned subsidiary, LCB Investments II, Inc. ("LCB Investments"), which manages the Bank's investment portfolio. LCB Investments also owns LCB Funding, Inc. ("LCB Funding"), a real estate investment trust. All significant inter-company balances and transactions have been eliminated in consolidation.

The unaudited consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles ("GAAP") for interim financial information and with the instructions for Form 10-Q. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements and are unaudited. In the opinion of management, all adjustments (all of which are normal and recurring in nature) considered necessary for a fair presentation have been included. Operating results for the three-month and six-month periods ended June 30, 2018 are not necessarily indicative of the results that may be expected for any subsequent reporting periods, including the year ending December 31, 2018. The Company's 2017 Annual Report on Form 10-K should be read in conjunction with these statements.

Adoption of New Accounting Standards
The Company accounts for revenue in accordance with ASU No. 2014-09, "Revenue from Contracts with Customers" and all the subsequent amendments to the ASU (collectively "ASC 606"), which the Company adopted on January 1, 2018, using the modified retrospective approach. Results for reporting periods beginning after January 1, 2018 are presented under ASC 606, while prior period amounts are not adjusted and continue to be reported under the accounting standards in effect for the prior period. We recorded a net increase to opening retained earnings of $24,000 as of January 1, 2018 due to the cumulative impact of adopting ASC 606. Revenue is split between net interest income and noninterest income at a ratio of approximately 80% to 20%, respectively. The scope of the guidance explicitly excludes net interest income as well as many other revenues for financial assets and liabilities including loans, leases, securities, and derivatives. The Company's services that fall within ASC 606 are presented in noninterest income and are recognized as revenue as the Company satisfies its obligation to the customer. The majority of the Company's revenue is from the business of banking and the Company's assigned regions have similar economic characteristics, products, services and customers. Accordingly, all of the Company's operations are considered by management to be aggregated in one reportable operating segment.
The income statement impact of adopting ASC 606 for the three- and six-month periods ended June 30, 2018 is outlined below:

	For the three months ended June 30, 2018			For the six months ended June 30, 2018		
	As reported	Under legacy GAAP	Impact of ASC 606	As reported	Under legacy GAAP	Impact of ASC 606
Noninterest income						
Loan and service fees	$2,421	$2,231	$190	$4,598	$4,214	$384
Other income	216	344	(128)	1,255	1,383	(128)
Total	$2,637	$2,575	$62	$5,853	$5,597	$256
Noninterest expense						
Data processing fees and supplies	2,290	2,228	62	4,803	4,547	256
Total	$2,290	$2,228	$62	$4,803	$4,547	$256
Net Impact	$347	$347	$0	$1,050	$1,050	$0
Net income	$20,142	$20,142	$0	$38,478	$38,478	$0
Comprehensive income	18,420	18,420	0	29,679	29,679	0

Basic earnings per share	$0.80	$0.80	$0	$1.52	$1.52	$0
Diluted earnings per share	0.78	0.78	0	1.50	1.50	0

In January 2016, the Financial Accounting Standards Board (the "FASB") amended existing accounting guidance related to the recognition and measurement of financial assets and financial liabilities. These amendments make targeted improvements to U.S. GAAP as follows: (1) Require equity investments (except those accounted for under the equity method of accounting or those that result in consolidation of the investee) to be measured at fair value with changes in fair value recognized in net income. However, an entity may choose to measure equity investments that do not have readily determinable fair values at cost minus impairment, if any, plus or minus changes resulting from observable price changes in orderly transactions for the identical or a similar investment of the same issuer. (2) Simplify the impairment assessment of equity investments without readily determinable fair values by requiring a qualitative assessment to identify impairment. When a qualitative assessment indicates that impairment exists, an entity is required to measure the investment at fair value. (3) Eliminate the requirement to disclose the fair value of financial instruments measured at amortized cost for entities that are not public business entities. (4) Eliminate the requirement for public business entities to disclose the method(s) and significant assumptions used to estimate the fair value that is required to be disclosed for financial instruments measured at amortized cost on the balance sheet. (5) Require public business entities to use the exit price notion when measuring the fair value of financial instruments for disclosure purposes. (6) Require an entity to present separately in other comprehensive income the portion of the total change in the fair value of a liability resulting from a change in the instrument-specific credit risk when the entity has elected to measure the liability at fair value in accordance with the fair value option for financial instruments. (7) Require separate presentation of financial assets and financial liabilities by measurement category and form of financial asset (that is, securities or loans and receivable) on the balance sheet or the accompanying notes to the financial statements. (8) Clarify that an entity should evaluate the need for a valuation allowance on a deferred tax asset related to available-for-sale securities in combination with the entity's other deferred tax assets. This guidance was effective beginning January 1, 2018. Adopting this standard resulted in a credit to retained earnings for the reclassification in the amount of $68,000.

In August 2016, the FASB issued guidance related to the classification of certain cash receipts and cash payments in the statement of cash flow. This standard provides cash flow statement classification guidance for certain transactions including how the predominance principle should be applied when cash receipts and cash payments have aspects of more than one class of cash flows. This guidance was effective beginning January 1, 2018. Adopting this standard did not have a significant impact on the Company's financial condition or results of operations.

In March 2017, the FASB issued ASU No. 2017-07, "Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost." Under the new guidance, employers will present the service cost component of the net periodic benefit cost in the same income statement line item as other employee compensation costs arising from services rendered during the period. In addition, only the service cost component will be eligible for capitalization in assets. Employers will present the other components separately from the line item that includes the service cost. The guidance was effective beginning January 1, 2018. As a result of the applicable plans being frozen April 1, 2000, there was no service cost recognized for the six-month periods ending June 30, 2018 and 2017. All other components of cost were recorded in other expense under noninterest expenses on the Consolidated Statements of Income for all periods presented. Adopting this standard did not have a significant impact on the Company's financial condition or results of operations.

In February 2018, the FASB issued ASU No. 2018-02, "Income Statement – Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income." The ASU required a reclassification from accumulated other comprehensive income to retained earnings for stranded tax effects resulting from the newly enacted federal corporate income tax rate as a result of the Tax Cuts and Jobs Act of 2017. The amount reclassified was the difference between the historical corporate income tax rate and the newly 21% federal corporate income tax rate. The new guidance is effective for fiscal years beginning after December 15, 2018, and early adoption is permitted. The Company elected to early adopt the guidance during the first quarter of 2018, and recorded a credit to retained earnings for the reclassification in the amount of $173,000 during the first quarter.

Newly Issued But Not Yet Effective Accounting Standards

In February 2016, the FASB issued new accounting guidance related to leases. This update, effective for the Company beginning January 1, 2019, will replace existing lease guidance in GAAP and will require lessees to recognize lease assets and lease liabilities on the balance sheet for all leases and disclose key information about leasing arrangements. When implemented, lessees and lessors will be required to recognize and measure leases at the beginning of the earliest period presented using a modified retrospective approach. The Company currently has approximately $5.2 million of lease obligations that would come on balance sheet as both assets and liabilities upon adoption of this accounting standard.

In June 2016, the FASB issued guidance related to credit losses on financial instruments. This update will change the accounting for credit losses on loans and debt securities. The measurement of expected credit losses is to be based on information about past events, including historical experience, current conditions, and reasonable and supportable forecasts that affect the collectability of the reported amount. For loans, this measurement will take place at the time the financial asset is first added to the balance sheet and periodically thereafter. This differs significantly from the "incurred loss" model required under current GAAP, which delays recognition until it is probable a loss has been incurred. In addition, the guidance will modify the other-than-temporary impairment model for available-for-sale debt securities to require an allowance for credit impairment instead of a direct write-down, which will allow for reversal of credit impairments in future periods. This guidance is effective for public business entities that meet the definition of an SEC filer for fiscal years beginning after December 15, 2019, including interim periods in those fiscal years. The Company has formed a cross-functional committee that has evaluated existing technology and other solutions for calculating losses under this new standard, selected a vendor to validate data currently loaded in the technology solution selected, and reviewed the validation assessment report. The committee is currently evaluating the various methods available for calculating the credit losses, including but not limited to discounted cash flows, migration, and vintage. Management expects to recognize credit losses earlier upon adoption of this accounting standard and the expected credit loss model than it has historically done under the current incurred credit loss model and is evaluating the impact of adopting this new accounting standard on our financial statements.

In January 2017, the FASB issued ASU No. 2017-04 "Intangibles - Goodwill and Other - Simplifying the Test for Goodwill Impairment." These amendments eliminate Step 2 from the goodwill impairment test. The amendments also eliminate the requirements for any reporting unit with a zero or negative carrying amount to perform a qualitative assessment and, if it fails that qualitative test, to perform Step 2 of the goodwill impairment test. An entity still has the option to perform the qualitative assessment for a reporting unit to determine if the quantitative impairment test is necessary. The guidance is effective for annual or any interim goodwill impairment tests in fiscal years beginning after December 15, 2019. Early adoption is permitted for interim or annual goodwill impairment tests performed on testing dates after January 1, 2017. ASU 2017-04 should be adopted on a prospective basis. Management does not expect the adoption of this new accounting standard to have a material impact on our financial statements.

In March 2017, the FASB issued ASU No. 2017-08, "Receivables—Nonrefundable Fees and Other Costs: Premium Amortization on Purchased Callable Debt Securities." This update amends the amortization period for certain purchased callable debt securities held at a premium. FASB is shortening the amortization period for the premium to the earliest call date. Under current GAAP, entities generally amortize the premium as an adjustment of yield over the contractual life of the instrument. Concerns were raised that current GAAP excludes certain callable debt securities from consideration of early repayment of principal even if the holder is certain that the call will be exercised. As a result, upon the exercise of a call on a callable debt security held at a premium, the unamortized premium is recorded as a loss in earnings. There is diversity in practice (1) in the amortization period for premiums of callable debt securities and (2) in how the potential for exercise of a call is factored into current impairment assessments. The amendments in this update become effective for annual periods and interim periods within those annual periods beginning after December 15, 2018. Management is evaluating the impact of adopting the new guidance on our consolidated financial statements on a quarterly basis, and plans to adopt on January 1, 2019. The Company estimates the impact of this standard as of June 30, 2018, would be a reduction to retained earnings of approximately $840,000, net of tax, to reflect the acceleration of amortization of premiums on debt securities.

In August 2017, the FASB issued ASU 2017-12, "Derivatives and Hedging: Targeted Improvements to Accounting for Hedging Activities". The purpose of this updated guidance is to better align a company's financial reporting for hedging activities with the economic objectives of those activities. ASU 2017-12 is effective for public business entities for fiscal years beginning after December 15, 2018, with early adoption, including adoption in an interim period, permitted. The Company plans to adopt ASU 2017-12 on January 1, 2019. ASU 2017-12 requires a modified retrospective transition method in which the Company will recognize the cumulative effect of the change on the opening balance of each affected component of equity in the statement of financial position as of the date of adoption. While the Company continues to assess all potential impacts of the standard, we currently expect adoption to have an immaterial impact on our consolidated financial statements.

Reclassifications

Certain amounts appearing in the financial statements and notes thereto for prior periods have been reclassified to conform with the current presentation. The reclassifications had no effect on net income or stockholders' equity as previously reported.

NOTE 2. SECURITIES

Information related to the fair value and amortized cost of securities available for sale and the related gross unrealized gains and losses recognized in accumulated other comprehensive income is provided in the tables below.

(dollars in thousands)	Amortized Cost	Gross Unrealized Gain	Gross Unrealized Losses	Fair Value
June 30, 2018				
U.S. Treasury securities	$992	$0	$(13)	$979
U.S. government sponsored agencies	4,894	0	(131)	4,763
Mortgage-backed securities: residential	338,057	1,071	(8,347)	330,781
Mortgage-backed securities: commercial	34,890	0	(756)	34,134
State and municipal securities	194,573	1,119	(3,122)	192,570
Total	$573,406	$2,190	$(12,369)	$563,227
December 31, 2017				
U.S. Treasury securities	$992	$5	$0	$997
U.S. government sponsored agencies	5,191	0	(69)	5,122
Mortgage-backed securities: residential	314,650	2,099	(2,975)	313,774
Mortgage-backed securities: commercial	44,208	75	(72)	44,211
State and municipal securities	172,375	2,990	(976)	174,389
Total	$537,416	$5,169	$(4,092)	$538,493

Information regarding the fair value and amortized cost of available for sale debt securities by maturity as of June 30, 2018 is presented below. Maturity information is based on contractual maturity for all securities other than mortgage-backed securities. Actual maturities of securities may differ from contractual maturities because borrowers may have the right to prepay the obligation without a prepayment penalty.

(dollars in thousands)	Amortized Cost	Fair Value
Due in one year or less	$2,303	$2,324
Due after one year through five years	23,944	24,077
Due after five years through ten years	35,390	35,273
Due after ten years	138,822	136,638
	200,459	198,312
Mortgage-backed securities	372,947	364,915
Total debt securities	$573,406	$563,227

Securities proceeds, gross gains and gross losses are presented below.

(dollars in thousands)	Three months ended June 30, 2018	2017	Six months ended June 30, 2018	2017
Sales of securities available for sale				
Proceeds	$0	$19,034	$12,322	$35,845
Gross gains	0	59	21	256
Gross losses	0	(10)	(27)	(204)

The Company sold 22 securities with a total book value and a total fair value of $12.3 million during the first six months of 2018. The Company sold eight securities with a total book value and a total fair value of $19.0 million during the second quarter of 2017. The Company sold 35 securities with a total book value and a total fair value of $35.8 million during the first six months of 2017. No sales occurred during the second quarter of 2018.

Purchase premiums or discounts are recognized in interest income using the interest method over the terms of the securities or over the estimated lives of mortgage-backed securities. Gains and losses on sales are based on the amortized cost of the security sold and recorded on the trade date.

Securities with carrying values of $189.3 million and $171.1 million were pledged as of June 30, 2018 and December 31, 2017, respectively, as collateral for securities sold under agreements to repurchase, borrowings from the Federal Home Loan Bank and for other purposes as permitted or required by law.

Information regarding securities with unrealized losses as of June 30, 2018 and December 31, 2017 is presented below. The tables divide the securities between those with unrealized losses for less than twelve months and those with unrealized losses for twelve months or more.

	Less than 12 months		12 months or more		Total	
(dollars in thousands)	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
June 30, 2018						
US Treasury	$979	$13	$0	$0	$979	$13
U.S. government sponsored agencies	2,210	51	2,553	80	4,763	131
Mortgage-backed securities: residential	231,456	5,493	56,429	2,854	287,885	8,347
Mortgage-backed securities: commercial	34,134	756	0	0	34,134	756
State and municipal securities	63,633	914	48,071	2,208	111,704	3,122
Total temporarily impaired	$332,412	$7,227	$107,053	$5,142	$439,465	$12,369
December 31, 2017						
U.S. government sponsored agencies	$2,353	$6	$2,769	$63	$5,122	$69
Mortgage-backed securities: residential	142,834	1,412	59,024	1,563	201,858	2,975
Mortgage-backed securities: commercial	23,505	72	0	0	23,505	72
State and municipal securities	8,585	47	49,552	929	58,137	976
Total temporarily impaired	$177,277	$1,537	$111,345	$2,555	$288,622	$4,092

The total number of securities with unrealized losses as of June 30, 2018 and December 31, 2017 is presented below.

	Less than 12 months	12 months or more	Total
June 30, 2018			
US Treasury	1	0	1
U.S. government sponsored agencies	1	1	2
Mortgage-backed securities: residential	79	22	101
Mortgage-backed securities: commercial	8	0	8
State and municipal securities	82	62	144
Total temporarily impaired	171	85	256
December 31, 2017			
U.S. government sponsored agencies	1	1	2
Mortgage-backed securities: residential	46	21	67
Mortgage-backed securities: commercial	5	0	5
State and municipal securities	17	62	79
Total temporarily impaired	69	84	153

The following factors are considered in determining whether or not the impairment of these securities is other-than-temporary. In making this determination, management considers the extent and duration of the unrealized loss, and the financial condition and near-term prospects of the issuer, as well as the underlying fundamentals of the relevant market and the outlook for such market in the near future. Management also assesses whether it intends to sell, or it is more likely than not that it will be required to sell, a security in an unrealized loss position before recovery of its amortized cost basis. If either of the criteria regarding intent or requirement to sell is met, the entire difference between amortized cost and fair value is recognized as impairment through earnings. For debt securities that do not meet the aforementioned criteria, the amount of impairment is split into two components as follows: 1) OTTI related to credit loss, which must be recognized in the income statement and 2) OTTI related to other factors, which is recognized in other comprehensive income. Credit loss is defined as the difference between the present value of the cash flows expected to be collected and the amortized cost basis. As of June 30, 2018 and December 31, 2017, all of the securities in the Company's portfolio were backed by the U.S. government, government agencies, government sponsored entities or were A-rated or better, except for certain non-local or local municipal securities, which are not rated. For the government, government agency, government-sponsored entity and municipal securities, management did not believe that there would be credit losses or that full principal would not be received. Management considers the unrealized losses on these securities to be primarily interest rate driven and does not expect material losses given current market conditions unless the securities are sold. However, at this time management does not have the intent to sell, and it is more likely than not that the Company will not be required to sell these securities before the recovery of their amortized cost basis.

NOTE 3. LOANS

(dollars in thousands)	June 30, 2018		December 31, 2017	
Commercial and industrial loans:				
Working capital lines of credit loans	$780,910	20.2 %	$743,609	19.4 %
Non-working capital loans	691,118	17.9	675,072	17.7
Total commercial and industrial loans	1,472,028	38.1	1,418,681	37.1
Commercial real estate and multi-family residential loans:				
Construction and land development loans	200,438	5.2	224,474	5.9
Owner occupied loans	569,453	14.8	538,603	14.1
Nonowner occupied loans	518,840	13.4	508,121	13.3
Multifamily loans	221,579	5.7	173,715	4.5
Total commercial real estate and multi-family residential loans	1,510,310	39.1	1,444,913	37.8
Agri-business and agricultural loans:				
Loans secured by farmland	148,396	3.9	186,437	4.9
Loans for agricultural production	155,826	4.0	196,404	5.1
Total agri-business and agricultural loans	304,222	7.9	382,841	10.0
Other commercial loans	120,541	3.1	124,076	3.3
Total commercial loans	3,407,101	88.2	3,370,511	88.2
Consumer 1-4 family mortgage loans:				
Closed end first mortgage loans	180,099	4.7	179,302	4.7
Open end and junior lien loans	179,622	4.7	181,865	4.8
Residential construction and land development loans	13,226	0.3	13,478	0.3
Total consumer 1-4 family mortgage loans	372,947	9.7	374,645	9.8
Other consumer loans	80,097	2.1	74,369	2.0
Total consumer loans	453,044	11.8	449,014	11.8
Subtotal	3,860,145	100.0 %	3,819,525	100.0 %
Less: Allowance for loan losses	(47,706)		(47,121)	
Net deferred loan fees	(1,432)		(1,066)	
Loans, net	$3,811,007		$3,771,338	

The recorded investment in loans does not include accrued interest.

The Company had $258,000 in residential real estate loans in the process of foreclosure as of June 30, 2018, compared to $47,000 as of December 31, 2017.

NOTE 4. ALLOWANCE FOR LOAN LOSSES AND CREDIT QUALITY

The following tables present the activity in the allowance for loan losses by portfolio segment for the three-month periods ended June 30, 2018 and 2017:

(dollars in thousands)	Commercial and Industrial	Commercial Real Estate and Multifamily Residential	Agri-business and Agricultural	Other Commercial	Consumer 1-4 Family Mortgage	Other Consumer	Unallocated	Total
Three Months Ended June 30, 2018								
Beginning balance, April 1	$20,725	$14,438	$4,848	$510	$2,018	$245	$2,843	$45,627
Provision for loan losses	1,392	508	(268)	(46)	(68)	65	117	1,700
Loans charged-off	(57)	0	0	0	0	(71)	0	(128)
Recoveries	464	8	5	0	3	27	0	507
Net loans charged-off	407	8	5	0	3	(44)	0	379
Ending balance	$22,524	$14,954	$4,585	$464	$1,953	$266	$2,960	$47,706

(dollars in thousands)	Commercial and Industrial	Commercial Real Estate and Multifamily Residential	Agri-business and Agricultural	Other Commercial	Consumer 1-4 Family Mortgage	Other Consumer	Unallocated	Total
Three Months Ended June 30, 2017								
Beginning balance, April 1	$19,781	$13,718	$3,459	$545	$2,790	$379	$3,102	$43,774
Provision for loan losses	160	61	405	23	(123)	23	(49)	500
Loans charged-off	(11)	(211)	0	0	(6)	(33)	0	(261)
Recoveries	289	207	6	0	28	20	0	550
Net loans charged-off	278	(4)	6	0	22	(13)	0	289
Ending balance	$20,219	$13,775	$3,870	$568	$2,689	$389	$3,053	$44,563

The following tables present the activity in the allowance for loan losses by portfolio segment for the six-month periods ended June 30, 2018 and 2017:

(dollars in thousands)	Commercial and Industrial	Commercial Real Estate and Multifamily Residential	Agri-business and Agricultural	Other Commercial	Consumer 1-4 Family Mortgage	Other Consumer	Unallocated	Total
Six Months Ended June 30, 2018								
Beginning balance, January 1	$21,097	$14,714	$4,920	$577	$2,768	$379	$2,666	$47,121
Provision for loan losses	5,294	715	(344)	(113)	(862)	16	294	5,000
Loans charged-off	(4,417)	(491)	0	0	(7)	(190)	0	(5,105)
Recoveries	550	16	9	0	54	61	0	690
Net loans charged-off	(3,867)	(475)	9	0	47	(129)	0	(4,415)
Ending balance	$22,524	$14,954	$4,585	$464	$1,953	$266	$2,960	$47,706

(dollars in thousands)	Commercial and Industrial	Commercial Real Estate and Multifamily Residential	Agri-business and Agricultural	Other Commercial	Consumer 1-4 Family Mortgage	Other Consumer	Unallocated	Total
Six Months Ended June 30, 2017								
Beginning balance, January 1	$20,272	$13,452	$3,532	$461	$2,827	$387	$2,787	$43,718
Provision for loan losses	(179)	318	328	107	(200)	60	266	700
Loans charged-off	(386)	(259)	0	0	(13)	(106)	0	(764)
Recoveries	512	264	10	0	75	48	0	909
Net loans charged-off	126	5	10	0	62	(58)	0	145
Ending balance	$20,219	$13,775	$3,870	$568	$2,689	$389	$3,053	$44,563

12

The following tables present the balance in the allowance for loan losses and the recorded investment in loans by portfolio segment and based on impairment method as of June 30, 2018 and December 31, 2017:

(dollars in thousands)	Commercial and Industrial	Commercial Real Estate and Multifamily Residential	Agri-business and Agricultural	Other Commercial	Consumer 1-4 Family Mortgage	Other Consumer	Unallocated	Total
June 30, 2018								
Allowance for loan losses:								
Ending allowance balance attributable to loans:								
Individually evaluated for impairment	$2,046	$536	$0	$0	$205	$26	$0	$2,813
Collectively evaluated for impairment	20,478	14,418	4,585	464	1,748	240	2,960	44,893
Total ending allowance balance	$22,524	$14,954	$4,585	$464	$1,953	$266	$2,960	$47,706
Loans:								
Loans individually evaluated for impairment	$10,603	$4,291	$283	$0	$1,712	$47	$0	$16,936
Loans collectively evaluated for impairment	1,461,326	1,503,794	304,033	120,395	372,394	79,835	0	3,841,777
Total ending loans balance	$1,471,929	$1,508,085	$304,316	$120,395	$374,106	$79,882	$0	$3,858,713

	Commercial and	Commercial Real Estate and Multifamily	Agri-business and	Other	Consumer 1-4 Family	Other

(dollars in thousands)	Industrial	Residential	Agricultural	Commercial	Mortgage	Consumer	Unallocated	Total
December 31, 2017								
Allowance for loan losses:								
Ending allowance balance attributable to loans:								
Individually evaluated for impairment	$2,067	$795	$0	$0	$310	$44	$0	$3,216
Collectively evaluated for impairment	19,030	13,919	4,920	577	2,458	335	2,666	43,905
Total ending allowance balance	$21,097	$14,714	$4,920	$577	$2,768	$379	$2,666	$47,121
Loans:								
Loans individually evaluated for impairment	$6,979	$4,802	$283	$0	$1,756	$50	$0	$13,870
Loans collectively evaluated for impairment	1,411,648	1,438,219	382,643	123,922	374,013	74,144	0	3,804,589
Total ending loans balance	$1,418,627	$1,443,021	$382,926	$123,922	$375,769	$74,194	$0	$3,818,459

The following table presents loans individually evaluated for impairment by class of loans as of June 30, 2018:

(dollars in thousands)	Unpaid Principal Balance	Recorded Investment	Allowance for Loan Losses Allocated
With no related allowance recorded:			
Commercial and industrial loans:			
Working capital lines of credit loans	$491	$491	$0
Non-working capital loans	3,006	1,611	0
Commercial real estate and multi-family residential loans:			
Construction and land development loans	88	88	0
Owner occupied loans	2,928	2,548	0
Agri-business and agricultural loans:			
Loans secured by farmland	603	283	0
Consumer 1-4 family loans:			
Closed end first mortgage loans	579	500	0
Open end and junior lien loans	243	244	0
With an allowance recorded:			
Commercial and industrial loans:			
Working capital lines of credit loans	7,282	4,594	707
Non-working capital loans	4,857	3,907	1,339
Commercial real estate and multi-family residential loans:			
Construction and land development loans	325	324	124
Owner occupied loans	1,689	1,331	412
Consumer 1-4 family mortgage loans:			
Closed end first mortgage loans	967	968	205
Other consumer loans	47	47	26
Total	$23,105	$16,936	$2,813

14

The following table presents loans individually evaluated for impairment by class of loans as of December 31, 2017:

(dollars in thousands)	Unpaid Principal Balance	Recorded Investment	Allowance for Loan Losses Allocated
With no related allowance recorded:			
Commercial and industrial loans:			
Working capital lines of credit loans	$ 491	$ 491	$ 0
Non-working capital loans	2,973	1,579	0
Commercial real estate and multi-family residential loans:			
Construction and land development loans	88	88	0
Owner occupied loans	2,558	2,310	0
Agri-business and agricultural loans:			
Loans secured by farmland	603	283	0
Consumer 1-4 family loans:			
Closed end first mortgage loans	636	570	0
With an allowance recorded:			
Commercial and industrial loans:			
Working capital lines of credit loans	1,617	1,617	667
Non-working capital loans	3,292	3,292	1,400
Commercial real estate and multi-family residential loans:			
Construction and land development loans	827	827	350
Owner occupied loans	1,577	1,577	445
Consumer 1-4 family mortgage loans:			
Closed end first mortgage loans	950	950	269
Open end and junior lien loans	235	236	41
Other consumer loans	50	50	44
Total	$ 15,897	$ 13,870	$ 3,216

15

The following table presents loans individually evaluated for impairment by class of loans as of and for the three-month period ended June 30, 2018:

(dollars in thousands)	Average Recorded Investment	Interest Income Recognized	Cash Basis Interest Income Recognized
With no related allowance recorded:			
Commercial and industrial loans:			
Working capital lines of credit loans	$1,011	$6	$14
Non-working capital loans	1,738	16	26
Commercial real estate and multi-family residential loans:			
Construction and land development loans	88	2	3
Owner occupied loans	2,868	9	12
Agri-business and agricultural loans:			
Loans secured by farmland	283	0	0
Consumer 1-4 family loans:			
Closed end first mortgage loans	533	2	3
Open end and junior lien loans	247	0	0
With an allowance recorded:			
Commercial and industrial loans:			
Working capital lines of credit loans	3,005	2	2
Non-working capital loans	3,513	3	6
Commercial real estate and multi-family residential loans:			
Construction and land development loans	491	6	13
Owner occupied loans	1,041	1	1
Consumer 1-4 family mortgage loans:			
Closed end first mortgage loans	993	8	10
Other consumer loans	48	0	2
Total	$15,859	$55	$92

The following table presents loans individually evaluated for impairment by class of loans as of and for the three-month period ended June 30, 2017:

(dollars in thousands)	Average Recorded Investment	Interest Income Recognized	Cash Basis Interest Income Recognized
With no related allowance recorded:			
Commercial and industrial loans:			
Working capital lines of credit loans	$562	$8	$8
Non-working capital loans	1,310	9	6
Commercial real estate and multi-family residential loans:			
Construction and land development loans	126	1	1
Owner occupied loans	2,390	2	1
Nonowner occupied loans	2,803	70	59
Agri-business and agricultural loans:			
Loans secured by farmland	283	0	0
Consumer 1-4 family loans:			
Closed end first mortgage loans	213	2	2
Open end and junior lien loans	155	0	0
With an allowance recorded:			
Commercial and industrial loans:			
Working capital lines of credit loans	2,376	11	4
Non-working capital loans	6,855	42	30
Commercial real estate and multi-family residential loans:			
Owner occupied loans	1,544	3	2
Consumer 1-4 family mortgage loans:			
Closed end first mortgage loans	1,028	5	2
Other consumer loans	53	1	0
Total	$19,698	$154	$115

The following table presents loans individually evaluated for impairment by class of loans as of and for the six-month period ended June 30, 2018:

(dollars in thousands)	Average Recorded Investment	Interest Income Recognized	Cash Basis Interest Income Recognized
With no related allowance recorded:			
Commercial and industrial loans:			
Working capital lines of credit loans	$1,011	$13	$16
Non-working capital loans	1,733	31	31
Commercial real estate and multi-family residential loans:			
Construction and land development loans	95	3	3
Owner occupied loans	2,712	16	14
Agri-business and agricultural loans:			
Loans secured by farmland	283	0	0
Consumer 1-4 family loans:			
Closed end first mortgage loans	538	4	4
Open end and junior lien loans	169	0	0
With an allowance recorded:			
Commercial and industrial loans:			
Working capital lines of credit loans	2,307	4	3
Non-working capital loans	3,365	5	6
Commercial real estate and multi-family residential loans:			
Construction and land development loans	606	17	18
Owner occupied loans	1,117	1	1
Consumer 1-4 family mortgage loans:			
Closed end first mortgage loans	981	15	14
Open end and junior lien loans	77	0	0
Other consumer loans	48	1	2
Total	$15,042	$110	$112

The following table presents loans individually evaluated for impairment by class of loans as of and for the six-month period ended June 30, 2017:

(dollars in thousands)	Average Recorded Investment	Interest Income Recognized	Cash Basis Interest Income Recognized
With no related allowance recorded:			
Commercial and industrial loans:			
Working capital lines of credit loans	$570	$15	$15
Non-working capital loans	1,345	17	14
Commercial real estate and multi-family residential loans:			
Construction and land development loans	126	2	2
Owner occupied loans	2,481	3	2
Nonowner occupied loans	3,703	154	143
Agri-business and agricultural loans:			
Loans secured by farmland	283	0	0
Consumer 1-4 family loans:			
Closed end first mortgage loans	202	3	3
Open end and junior lien loans	156	0	0
With an allowance recorded:			
Commercial and industrial loans:			
Working capital lines of credit loans	1,870	22	17
Non-working capital loans	6,777	91	81
Commercial real estate and multi-family residential loans:			
Owner occupied loans	1,605	8	7
Consumer 1-4 family mortgage loans:			
Closed end first mortgage loans	1,050	12	9
Other consumer loans	54	2	1
Total	$20,222	$329	$294

The following table presents the ageing of the recorded investment in past due loans as of June 30, 2018 by class of loans:

(dollars in thousands)	Loans Not Past Due	30-89 Days Past Due	Greater than 90 Days Past Due	Nonaccrual	Total Past Due and Nonaccrual	Total
Commercial and industrial loans:						
Working capital lines of credit loans	$776,348	$30	$0	$4,611	$4,641	$780,989
Non-working capital loans	686,853	0	0	4,087	4,087	690,940
Commercial real estate and multi-family residential loans:						
Construction and land development loans	199,046	324	0	0	324	199,370
Owner occupied loans	565,838	0	0	3,242	3,242	569,080
Nonowner occupied loans	518,475	0	0	0	0	518,475
Multifamily loans	221,160	0	0	0	0	221,160
Agri-business and agricultural loans:						
Loans secured by farmland	148,118	0	0	283	283	148,401
Loans for agricultural production	155,915	0	0	0	0	155,915
Other commercial loans	120,395	0	0	0	0	120,395
Consumer 1-4 family mortgage loans:						
Closed end first mortgage loans	178,347	1,084	0	310	1,394	179,741
Open end and junior lien loans	180,860	66	0	244	310	181,170
Residential construction loans	13,138	57	0	0	57	13,195
Other consumer loans	79,828	54	0	0	54	79,882
Total	$3,844,321	$1,615	$0	$12,777	$14,392	$3,858,713

The following table presents the ageing of the recorded investment in past due loans as of December 31, 2017 by class of loans:

(dollars in thousands)	Loans Not Past Due	30-89 Days Past Due	Greater than 90 Days Past Due	Nonaccrual	Total Past Due and Nonaccrual	Total
Commercial and industrial loans:						
Working capital lines of credit loans	$742,205	$11	$0	$1,459	$1,470	$743,675
Non-working capital loans	671,490	0	0	3,462	3,462	674,952
Commercial real estate and multi-family residential loans:						
Construction and land development loans	215,713	8,000	0	0	8,000	223,713
Owner occupied loans	534,648	0	0	3,620	3,620	538,268
Nonowner occupied loans	507,696	0	0	0	0	507,696
Multifamily loans	173,100	244	0	0	244	173,344
Agri-business and agricultural loans:						
Loans secured by farmland	186,160	0	0	283	283	186,443
Loans for agricultural production	196,483	0	0	0	0	196,483
Other commercial loans	123,922	0	0	0	0	123,922
Consumer 1-4 family mortgage loans:						
Closed end first mortgage loans	177,410	1,183	6	342	1,531	178,941
Open end and junior lien loans	183,056	89	0	236	325	183,381
Residential construction loans	13,447	0	0	0	0	13,447

Other consumer loans	74,102	92	0	0	92	74,194
Total	$3,799,432	$9,619	$6	$9,402	$19,027	$3,818,459

Troubled Debt Restructurings:

Troubled debt restructured loans are included in the totals for impaired loans. The Company has allocated $2.1 million and $2.3 million of specific reserves to customers whose loan terms have been modified in troubled debt restructurings as of June 30, 2018 and December 31, 2017, respectively. The Company is not committed to lend additional funds to debtors whose loans have been modified in a troubled debt restructuring.

(dollars in thousands)	June 30 2018	December 31 2017
Accruing troubled debt restructured loans	$3,402	$2,893
Nonaccrual troubled debt restructured loans	7,666	7,750
Total troubled debt restructured loans	$11,068	$10,643

During the three months ended June 30, 2018, one commercial and industrial loan was modified as a troubled debt restructuring due to receiving inadequate compensation for the terms of the restructure and is included in the tables below.

Additional concessions were granted to borrowers with previously identified troubled debt restructured loans during the three-month period ended June 30, 2018. The loan to one of the borrowers is for a commercial real estate building where the collateral value and cash flows from the company occupying the building do not support the loan with a recorded investment of $107,000. The loan to another one of the borrowers is for a vacant commercial real estate building that does not generate cash flow to support the loan with a recorded investment of $875,000. The other loans are to a borrower for an investment in land for residential development which has not had sales activity to support loans with a recorded investment of $484,000. These concessions are not included in table below.

During the three months ended March 31, 2018, certain loans were modified as troubled debt restructurings. The modified terms of these loans include one or a combination of the following: inadequate compensation for the terms of the restructure or renewal; a modification of the repayment terms which delays principal repayment for some period; or renewal terms offered to borrowers in financial distress where no additional credit enhancements were obtained at the time of renewal. These concessions are included in the table below.

Additional concessions were granted to borrowers with previously identified troubled debt restructured loans during the three-month period ended March 31, 2018. The loan to one of the borrowers is for a commercial real estate building where the collateral value and cash flows from the companies occupying the buildings do not support the loan with recorded investments of $341,000. The loans to two other borrowers are for commercial and industrial capital and non-working capital loans with recorded investments of $551,000. These concessions are not included in the table below.

The following table presents loans by class modified as new troubled debt restructurings that occurred during the three months ended June 30, 2018:

	All Modifications			Modified Repayment Terms	
(dollars in thousands)	Number of Loans	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment	Number of Loans	Extension Period or Range (in months)
Troubled Debt Restructurings					

Commercial and industrial loans:					
Non-working capital loans	1	$20	$20	1	0
Total	1	$20	$20	1	0

21

The following table presents loans by class modified as new troubled debt restructurings that occurred during the six months ended June 30, 2018:

	All Modifications			Modified Repayment Terms	
(dollars in thousands)	Number of Loans	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment	Number of Loans	Extension Period or Range (in months)
Troubled Debt Restructurings					
Commercial and industrial loans:					
Working capital lines of credit loans	1	$600	$600	1	0
Non-working capital loans	2	1,420	1,420	2	0
Commercial real estate and multi-family residential loans:					
Construction and land development loans	1	824	824	1	12
Owner occupied loans	1	387	387	1	12
Consumer 1-4 family loans:					
Closed end first mortgage loans	1	198	197	1	239
Total	6	$3,429	$3,428	6	0-239

For the three-month period ended June 30, 2018, the troubled debt restructuring described above did not impact the allowance for loan losses and no charge-off was recorded. For the six-month period ended June 30, 2018, the debt restructurings described above decreased the allowance for loan losses by $166,000, and resulted in charge-offs of $1.6 million.

During the three months ended June 30, 2017, no loans were modified as troubled debt restructurings.

During the three months ended March 31, 2017, certain loans were modified as troubled debt restructurings and are reflected in the table presented below. The modified terms of these loans include one or a combination of the following: inadequate compensation for the terms of the restructure or renewal; a modification of the repayment terms which delays principal repayment for some period; or renewal terms offered to borrowers in financial distress where no additional credit enhancements were obtained at the time of renewal.

Additional concessions were granted to borrowers with previously identified troubled debt restructured loans during the three months ended March 31, 2017. The loans to two of the borrowers are for commercial real estate buildings where the collateral value and cash flows from the companies occupying the buildings do not support the loans with recorded investments of $500,000. The loans to two other borrowers are for commercial and industrial non-working capital loans with recorded investments of $690,000. These concessions are not included in table below.

The following table presents loans by class modified as new troubled debt restructurings that occurred during the six months ended June 30, 2017:

All Modifications			Modified Repayment Terms
	Pre-Modification Outstanding	Post-Modification Outstanding	Period or

(dollars in thousands)	Number of Loans	Recorded Investment	Recorded Investment	Number of Loans	Range (in months)
Troubled Debt Restructurings					
Commercial and industrial loans:					
Non-working capital loans	2	$ 1,712	$ 1,712	2	6
Commercial real estate and multi-family residential loans:					
Owner occupied loans	1	486	486	1	6
Consumer 1-4 family loans:					
Closed end first mortgage loans	1	44	46	1	350
Total	4	$ 2,242	$ 2,244	4	6-350

For the three-month period ended June 30, 2017, troubled debt restructurings described above increased the allowance for loan losses by $3,000 and no charge-offs resulted from the modifications. For the six-month period ended June 30, 2017, the troubled debt restructurings described above increased the allowance for loan losses by $86,000 and no charge-offs resulted from the modifications.

There were no troubled debt restructurings that had payment defaults within the twelve months following modification during the three- or six-month periods ended June 30, 2018 and 2017.

Credit Quality Indicators:

The Company categorizes loans into risk categories based on relevant information about the ability of borrowers to service their debt such as: current financial information, historical payment experience, credit documentation, public information and current economic trends, among other factors. The Company analyzes commercial loans individually by classifying the loans as to credit risk. This analysis is performed on a quarterly basis for Special Mention, Substandard and Doubtful grade loans and annually on Pass grade loans over $150,000.

The Company uses the following definitions for risk ratings:

Special Mention. Loans classified as Special Mention have a potential weakness that deserves management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan or of the institution's credit position at some future date.

Substandard. Loans classified as Substandard are inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any. Loans so classified have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the Company will sustain some loss if the deficiencies are not corrected.

Doubtful. Loans classified as Doubtful have all the weaknesses inherent in those classified as Substandard, with the added characteristics that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions, and values, highly questionable and improbable.

Loans not meeting the criteria above that are analyzed individually as part of the above-described process are considered to be Pass rated loans with the exception of consumer troubled debt restructurings which are evaluated and listed with Substandard commercial grade loans and consumer nonaccrual loans which are evaluated individually and listed with Not Rated loans. Loans listed as Not Rated are consumer loans or commercial loans with consumer characteristics included in groups of homogenous loans which are analyzed for credit quality indicators utilizing delinquency status. As of June 30, 2018, and based on the most recent analysis performed, the risk category of loans by class of loans is as follows:

(dollars in thousands)	Pass	Special Mention	Substandard	Doubtful	Not Rated	Total
Commercial and industrial loans:						
Working capital lines of credit loans	$692,253	$64,679	$23,698	$0	$359	$780,989
Non-working capital loans	634,295	27,890	23,657	0	5,098	690,940
Commercial real estate and multi-family residential loans:						
Construction and land development loans	198,605	441	324	0	0	199,370
Owner occupied loans	523,574	23,609	21,897	0	0	569,080
Nonowner occupied loans	515,925	1,883	667	0	0	518,475
Multifamily loans	220,931	229	0	0	0	221,160
Agri-business and agricultural loans:						
Loans secured by farmland	136,465	8,358	3,578	0	0	148,401
Loans for agricultural production	144,728	9,287	1,900	0	0	155,915
Other commercial loans	120,391	0	0	0	4	120,395
Consumer 1-4 family mortgage loans:						
Closed end first mortgage loans	52,761	0	1,467	0	125,513	179,741
Open end and junior lien loans	8,306	0	244	0	172,620	181,170
Residential construction loans	0	0	0	0	13,195	13,195
Other consumer loans	13,832	0	47	0	66,003	79,882
Total	$3,262,066	$136,376	$77,479	$0	$382,792	$3,858,713

As of December 31, 2017, and based on the most recent analysis performed, the risk category of loans by class of loans is as follows:

(dollars in thousands)	Pass	Special Mention	Substandard	Doubtful	Not Rated	Total
Commercial and industrial loans:						
Working capital lines of credit loans	$688,748	$33,337	$21,350	$0	$240	$743,675
Non-working capital loans	624,275	20,171	25,834	0	4,672	674,952
Commercial real estate and multi-family residential loans:						
Construction and land development loans	222,445	441	827	0	0	223,713
Owner occupied loans	496,231	19,361	22,676	0	0	538,268
Nonowner occupied loans	505,033	1,970	693	0	0	507,696
Multifamily loans	173,100	244	0	0	0	173,344
Agri-business and agricultural loans:						
Loans secured by farmland	174,118	7,988	4,337	0	0	186,443
Loans for agricultural production	185,772	9,716	995	0	0	196,483
Other commercial loans	123,917	0	0	0	5	123,922
Consumer 1-4 family mortgage loans:						

Closed end first mortgage loans	52,301	0	1,520	0	125,120	178,941
Open end and junior lien loans	8,259	0	236	0	174,886	183,381
Residential construction loans	0	0	0	0	13,447	13,447
Other consumer loans	18,642	0	50	0	55,502	74,194
Total	$3,272,841	$93,228	$78,518	$0	$373,872	$3,818,459

24

NOTE 5. FAIR VALUE DISCLOSURES

Fair value is the exchange price that would be received for an asset or paid to transfer a liability (exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. There are three levels of inputs that may be used to measure fair values:

Level 1	Quoted prices (unadjusted) for identical assets or liabilities in active markets that the entity has the ability to access as of the measurement date.
Level 2	Significant other observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data.
Level 3	Significant unobservable inputs that reflect a company's own assumptions about the assumptions that market participants would use in pricing an asset or liability.

The Company used the following methods and significant assumptions to estimate the fair value of each type of financial instrument:

Securities: Securities available for sale are valued primarily by a third party pricing service. The fair values of securities available for sale are determined on a recurring basis by obtaining quoted prices on nationally recognized securities exchanges (Level 1 inputs) or pricing models which utilize significant observable inputs such as matrix pricing. This is a mathematical technique widely used in the industry to value debt securities without relying exclusively on quoted prices for the specific securities but rather by relying on the securities' relationship to other benchmark quoted securities (Level 2 inputs). These models utilize the market approach with standard inputs that include, but are not limited to benchmark yields, reported trades, broker/dealer quotes, issuer spreads, two-sided markets, benchmark securities, bids, offers and reference data. For certain municipal securities that are not rated and observable inputs about the specific issuer are not available, fair values are estimated using observable data from other municipal securities presumed to be similar or other market data on other non-rated municipal securities (Level 3 inputs).

The Company's Finance Department, which is responsible for all accounting and SEC compliance, and the Company's Treasury Department, which is responsible for investment portfolio management and asset/liability modeling, are the two areas that determine the Company's valuation policies and procedures. Both of these areas report directly to the Executive Vice President and Chief Financial Officer of the Company. For assets or liabilities that may be considered for Level 3 fair value measurement on a recurring basis, these two departments and the Executive Vice President and Chief Financial Officer determine the appropriate level of the assets or liabilities under consideration. If there are assets or liabilities that are determined to be Level 3 by this group, the Risk Management Committee of the Company and the Audit Committee of the Board of Directors are made aware of such assets at their next scheduled meeting.

Securities pricing is obtained from a third party pricing service and all security prices are tested annually against prices from another third party provider and reviewed with a market value price tolerance variance that varies by sector: municipal securities +/- 5%, government mbs/cmo +/- 3% and U.S. treasuries +/-1%. If any securities fall outside the tolerance threshold, a determination of materiality is made for the amount over the threshold. Any security that would have a material threshold difference would be further investigated to determine why the variance exists and if any action is needed concerning the security pricing for that individual security. Changes in market value are reviewed monthly in aggregate by security type and any material differences are reviewed to determine why they exist. At least annually, the pricing methodology of the pricing service is received and reviewed to support the fair value levels used by the Company. A detailed pricing evaluation is requested and reviewed on any security determined to be fair valued using unobservable inputs by the pricing service.

Mortgage banking derivatives: The fair value of mortgage banking derivatives are based on observable market data as of the measurement date (Level 2).

Interest rate swap derivatives: Our derivatives are traded in an over-the-counter market where quoted market prices are not always available. Therefore, the fair values of derivatives are determined using quantitative models that utilize multiple market inputs. The inputs will vary based on the type of derivative, but could include interest rates, prices and indices to generate continuous yield or pricing curves, prepayment rates, and volatility factors to value the position. The majority of market inputs are actively quoted and can be validated through external sources, including brokers, market transactions and third-party pricing services. The fair value of interest rate swap derivatives is determined by pricing or valuation models using observable market data as of the measurement date (Level 2).

Impaired loans: Impaired loans with specific allocations of the allowance for loan losses are generally based on the fair value of the underlying collateral if repayment is expected solely from the collateral. Fair value is determined using several methods. Generally, the fair value of real estate is based on appraisals by qualified third party appraisers. These appraisals may utilize a single valuation approach or a combination of approaches including comparable sales and the income approach. Adjustments are routinely made in the appraisal process by the appraisers to adjust for differences between the comparable sales and income data available. Such adjustments are usually significant and result in a Level 3 classification of the inputs for determining fair value. In addition, the Company's management routinely applies internal discount factors to the value of appraisals used in the fair value evaluation of impaired loans. The deductions to the appraisals take into account changing business factors and market conditions, as well as value impairment in cases where the appraisal date predates a likely change in market conditions. Commercial real estate is generally discounted from its appraised value by 0-50% with the higher discounts applied to real estate that is determined to have a thin trading market or to be specialized collateral. In addition to real estate, the Company's management evaluates other types of collateral as follows: (a) raw and finished inventory is discounted from its cost or book value by 35-65%, depending on the marketability of the goods (b) finished goods are generally discounted by 30-60%, depending on the ease of marketability, cost of transportation or scope of use of the finished good (c) work in process inventory is typically discounted by 50-100%, depending on the length of manufacturing time, types of components used in the completion process, and the breadth of the user base (d) equipment is valued at a percentage of depreciated book value or recent appraised value, if available, and is typically discounted at 30-70% after various considerations including age and condition of the equipment, marketability, breadth of use, and whether the equipment includes unique components or add-ons; and (e) marketable securities are discounted by 10-30%, depending on the type of investment, age of valuation report and general market conditions. This methodology is based on a market approach and typically results in a Level 3 classification of the inputs for determining fair value.

Mortgage servicing rights: As of June 30, 2018, the fair value of the Company's Level 3 servicing assets for residential mortgage loans was $4.2 million, none of which are currently impaired and therefore are carried at amortized cost. These residential mortgage loans have a weighted average interest rate of 3.84%, a weighted average maturity of 19 years and are secured by homes generally within the Company's market area, which is primarily Northern Indiana. A valuation model is used to estimate fair value by stratifying the portfolios on the basis of certain risk characteristics, including loan type and interest rate. Impairment is estimated based on an income approach. The inputs used include estimates of prepayment speeds, discount rate, cost to service, escrow account earnings, contractual servicing fee income, ancillary income, late fees, and float income. The most significant assumption used to value mortgage servicing rights is prepayment rate. Prepayment rates are estimated based on published industry consensus prepayment rates. The most significant unobservable assumption is the discount rate. At June 30, 2018, the constant prepayment speed (PSA) used was 95 and the discount rate used was 9.4%. At December 31, 2017, the PSA used was 123 and the discount rate used was 9.4%.

Other real estate owned: Nonrecurring adjustments to certain commercial and residential real estate properties classified as other real estate owned are measured at the lower of carrying amount or fair value, less costs to sell. Fair values are generally based on third party appraisals of the property and are reviewed by the Company's internal appraisal officer. Adjustments are routinely made in the appraisal process by the appraisers to adjust for differences between the comparable properties used to determine value. Such adjustments are usually significant and result in a Level 3 classification. In addition, the Company's management may apply discount factors to the appraisals to take into account changing business factors and market conditions, as well as value impairment in cases where the appraisal date predates a likely change in market conditions. In cases where the carrying amount exceeds the fair value, less costs to sell, an impairment loss is recognized.

Real estate mortgage loans held for sale: Real estate mortgage loans held for sale are carried at the lower of cost or fair value, as determined by outstanding commitments, from third party investors, and result in a Level 2 classification.

The table below presents the balances of assets measured at fair value on a recurring basis:

	June 30, 2018			
	Fair Value Measurements Using			Assets
(dollars in thousands)	Level 1	Level 2	Level 3	at Fair Value
Assets				
U.S. Treasury securities	$ 979	$ 0	$ 0	$ 979
U.S. government sponsored agency securities	0	4,763	0	4,763
Mortgage-backed securities: residential	0	330,781	0	330,781
Mortgage-backed securities: commercial	0	34,134	0	34,134
State and municipal securities	0	191,742	828	192,570
Total Securities	979	561,420	828	563,227
Mortgage banking derivative	0	328	0	328
Interest rate swap derivative	0	4,071	0	4,071
Total assets	$ 979	$ 565,819	$ 828	$ 567,626
Liabilities				
Mortgage banking derivative	0	30	0	30
Interest rate swap derivative	0	4,088	0	4,088
Total liabilities	$ 0	$ 4,118	$ 0	$ 4,118

	December 31, 2017			
	Fair Value Measurements Using			Assets
(dollars in thousands)	Level 1	Level 2	Level 3	at Fair Value
Assets				
U.S. Treasury securities	$ 997	$ 0	$ 0	$ 997
U.S. government sponsored agency securities	0	5,122	0	5,122
Mortgage-backed securities: residential	0	313,774	0	313,774
Mortgage-backed securities: commercial	0	44,211	0	44,211
State and municipal securities	0	173,509	880	174,389
Total Securities	997	536,616	880	538,493
Mortgage banking derivative	0	136	0	136
Interest rate swap derivative	0	2,441	0	2,441
Total assets	$ 997	$ 539,193	$ 880	$ 541,070
Liabilities				
Mortgage banking derivative	0	3	0	3
Interest rate swap derivative	0	2,562	0	2,562
Total liabilities	$ 0	$ 2,565	$ 0	$ 2,565

There were no transfers between Level 1 and Level 2 during the six months ended June 30, 2018 and there were no transfers between Level 1 and Level 2 during 2017.

The table below presents a reconciliation of all assets measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the six months ended June 30, 2018 and 2017:

	State and Municipal Securities			
(dollars in thousands)	2018		2017	
Balance of recurring Level 3 assets at January 1	$	880	$	670
Changes in fair value of securities				
included in other comprehensive income	(7)		(6)	
Principal payments	(45)		(45)	
Balance of recurring Level 3 assets at June 30	$	828	$	619

The state and municipal securities measured at fair value included below are non-rated Indiana municipal revenue bonds and are not actively traded.

Quantitative Information about Level 3 Fair Value Measurements

(dollars in thousands)	Fair Value at 6/30/2018		Valuation Technique	Unobservable Input	Range of Inputs (Average)
State and municipal securities	$	828	Price to type, par, call	Discount to benchmark index	0-5% (0.92%)

Quantitative Information about Level 3 Fair Value Measurements

(dollars in thousands)	Fair Value at 12/31/2017		Valuation Technique	Unobservable Input	Range of Inputs (Average)
State and municipal securities	$	880	Price to type, par, call	Discount to benchmark index	0-5% (2.03%)

The primary methodology used in the fair value measurement of the Company's state and municipal securities classified as Level 3 is a discount to the AAA municipal benchmark index. Significant increases or (decreases) in this index as well as the degree to which the security differs in ratings, coupon, call and duration will result in a higher or (lower) fair value measurement for those securities that are not callable. For those securities that are continuously callable, a slight premium to par is used.

The table below presents the balances of assets measured at fair value on a nonrecurring basis:

	June 30, 2018							
	Fair Value Measurements Using						Assets	
(dollars in thousands)	Level 1		Level 2		Level 3		at Fair Value	
Assets								
Impaired loans:								
Commercial and industrial loans:								
Working capital lines of credit loans	$	0	$	0	$	3,888	$	3,888
Non-working capital loans	0		0		2,354		2,354	
Commercial real estate and multi-family								

residential loans:				
Construction and land development loans	0	0	200	200
Owner occupied loans	0	0	918	918
Consumer 1-4 family mortgage loans:				
Closed end first mortgage loans	0	0	138	138
Total assets	$ 0	$ 0	$ 7,498	$ 7,498

(dollars in thousands)	December 31, 2017 Fair Value Measurements Using Level 1	Level 2	Level 3	Assets at Fair Value
Assets				
Impaired loans:				
Commercial and industrial loans:				
Working capital lines of credit loans	$ 0	$ 0	$ 934	$ 934
Non-working capital loans	0	0	1,693	1,693
Commercial real estate and multi-family residential loans:				
Construction and land development loans	0	0	477	477
Owner occupied loans	0	0	1,133	1,133
Consumer 1-4 family mortgage loans:				
Open end and junior lien loans	0	0	195	195
Total assets	$ 0	$ 0	$ 4,432	$ 4,432

The following table presents the valuation methodology and unobservable inputs for Level 3 assets measured at fair value on a non-recurring basis at June 30, 2018:

(dollars in thousands)	Fair Value	Valuation Methodology	Unobservable Inputs	Average	Range of Inputs
Impaired loans:					
Commercial and industrial	$ 6,242	Collateral based measurements	Discount to reflect current market conditions and ultimate collectability	20%	9% - 100%
Impaired loans:					
Commercial real estate	1,118	Collateral based measurements	Discount to reflect current market conditions and ultimate collectability	32%	9% - 50%
Impaired loans:					
Consumer 1-4 family mortgage	138	Collateral based measurements	Discount to reflect current market conditions and ultimate collectability	5%	2% - 7%

The following table presents the valuation methodology and unobservable inputs for Level 3 assets measured at fair value on a non-recurring basis at December 31, 2017:

(dollars in thousands)	Fair Value	Valuation Methodology	Unobservable Inputs	Average	Range of Inputs
Impaired loans:					
Commercial and industrial	$ 2,627	Collateral based	Discount to reflect	37%	23% - 100%

		measurements	current market conditions and ultimate collectability		
Impaired loans: Commercial real estate	1,610	Collateral based measurements	Discount to reflect current market conditions and ultimate collectability	33%	2% - 58%
Impaired loans: Consumer 1-4 family mortgage	195	Collateral based measurements	Discount to reflect current market conditions and ultimate collectability	17%	

Impaired loans, which are measured for impairment using the fair value of the collateral for collateral dependent loans, had a gross carrying amount of $9.6 million, with a valuation allowance of $2.1 million at June 30, 2018, resulting in a net increase in the provision for loan losses of $4.5 million in the six months ended June 30, 2018 and a net increase in the provision for loan losses of $200,000 in the three months ended June 30, 2018. At June 30, 2017, impaired loans had a gross carrying amount of $10.0 million, with a valuation allowance of $3.7 million, resulting in a net increase in the provision for loan losses of $600,000 in the six months ended June 30, 2017, and a net reduction in the provision for loan losses of $200,000 in the three months ended June 30, 2017.

The following table contains the estimated fair values and the related carrying values of the Company's financial instruments. Items which are not financial instruments are not included. Due to the adoption of ASU 2016-01 as of January 1, 2018, the fair value as presented below is measured using the exit price notion in the periods after adoption and may not be comparable with prior periods presented as a result of the change in methodology.

	June 30, 2018				
	Carrying	Estimated Fair Value			
(dollars in thousands)	Value	Level 1	Level 2	Level 3	Total
Financial Assets:					
Cash and cash equivalents	$ 180,225	$ 177,480	$ 2,714	$ 0	$ 180,194
Securities available for sale	563,227	979	561,420	828	563,227
Real estate mortgages held for sale	6,097	0	6,200	0	6,200
Loans, net	3,811,007	0	0	3,742,781	3,742,781
Federal Home Loan Bank stock	10,352	N/A	N/A	N/A	N/A
Federal Reserve Bank stock	3,420	N/A	N/A	N/A	N/A
Accrued interest receivable	15,223	3	3,118	12,102	15,223
Financial Liabilities:					
Certificates of deposit	(1,416,735)	0	(1,418,805)	0	(1,418,805)
All other deposits	(2,518,218)	(2,518,218)	0	0	(2,518,218)
Securities sold under agreements to repurchase	(106,239)	0	(106,239)	0	(106,239)
Federal Home Loan Bank advances	(175,000)	0	(175,000)	0	(175,000)
Subordinated debentures	(30,928)	0	0	(31,211)	(31,211)
Standby letters of credit	(611)	0	0	(611)	(611)
Accrued interest payable	(7,328)	(125)	(7,198)	(5)	(7,328)

	December 31, 2017				
	Carrying	Estimated Fair Value			
(dollars in thousands)	Value	Level 1	Level 2	Level 3	Total
Financial Assets:					
Cash and cash equivalents	$ 176,180	$ 174,045	$ 2,127	$ 0	$ 176,172
Securities available for sale	538,493	997	536,616	880	538,493
Real estate mortgages held for sale	3,346	0	3,390	0	3,390
Loans, net	3,771,338	0	0	3,744,842	3,744,842
Federal Home Loan Bank stock	10,352	N/A	N/A	N/A	N/A
Federal Reserve Bank stock	3,420	N/A	N/A	N/A	N/A
Accrued interest receivable	14,093	3	2,925	11,165	14,093
Financial Liabilities:					
Certificates of deposit	(1,412,583)	0	(1,417,075)	0	(1,417,075)
All other deposits	(2,596,072)	(2,596,072)	0	0	(2,596,072)
Securities sold under agreements to repurchase	(70,652)	0	(70,652)	0	(70,652)
Federal Home Loan Bank advances	(80,030)	0	(80,035)	0	(80,035)
Subordinated debentures	(30,928)	0	0	(31,194)	(31,194)
Standby letters of credit	(758)	0	0	(758)	(758)
Accrued interest payable	(6,311)	(149)	(6,158)	(4)	(6,311)

NOTE 6. SECURITIES SOLD UNDER AGREEMENTS TO REPURCHASE

Securities sold under agreements to repurchase represent collateralized borrowings with customers located primarily within the Company's service area. These repurchase liabilities are not covered by federal deposit insurance and are secured by securities owned. The Company retains the right to substitute similar type securities and has the right to withdraw all excess collateral applicable to the repurchase liabilities whenever the collateral values are in excess of the related repurchase liabilities. However, as a means of mitigating market risk, the Company maintains excess collateral to cover normal changes in the repurchase liability by monitoring daily usage. The Company maintains control of the securities through the use of third-party safekeeping arrangements.

Securities sold under agreements to repurchase of $106.2 million and $70.7 million, which mature on demand, are secured by mortgage-backed securities with a carrying amount of $121.7 million and $98.0 million at June 30, 2018 and December 31, 2017, respectively. Additional information concerning recognition of these liabilities is disclosed in Note 8.

NOTE 7. EMPLOYEE BENEFIT PLANS

Components of net periodic benefit cost:

	Three Months Ended June 30,				Six Months Ended June 30,			
	Pension Benefits		SERP Benefits		Pension Benefits		SERP Benefits	
(dollars in thousands)	2018	2017	2018	2017	2018	2017	2018	2017
Service cost	$0	$0	$0	$0	$0	$0	$0	$0
Interest cost	24	26	8	10	47	52	17	20
Expected return on plan assets	(35)	(37)	(16)	(15)	(69)	(72)	(31)	(31)
Recognized net actuarial (gain) loss	48	47	19	20	96	93	37	40
Net pension expense (benefit)	$37	$36	$11	$15	$74	$73	$23	$29

The Company previously disclosed in its financial statements for the year ended December 31, 2017 that it expected to contribute $0 to its pension plan and $0 to its Supplemental Executive Retirement Plan ("SERP") in 2018. The Company has contributed $368,200 to its pension plan and $0 to its SERP as of June 30, 2018. The Company does not expect to make any additional contributions to its pension plan or SERP during the remainder of 2018. As a result of freezing the plan effective April 1, 2000, there is no service cost to record on the pension plan or the SERP for the six-month periods ending June 30, 2018 and 2017. All other components of cost noted in the table above were recorded in other expense under noninterest expenses on the Consolidated Statements of Income for all periods presented.

NOTE 8. OFFSETTING ASSETS AND LIABILITIES

The following tables summarize gross and net information about financial instruments and derivative instruments that are offset in the statement of financial position or that are subject to an enforceable master netting arrangement at June 30, 2018 and December 31, 2017.

	June 30, 2018			
	Gross Amounts of	Gross Amounts Offset in the	Net Amounts of Assets presented in	Gross Amounts Not Offset in the Statement

(dollars in thousands)	Recognized Assets/ Liabilities	Statement of Financial Position	the Statement of Financial Position	of Financial Position Financial Instruments	Cash Collateral Received	Net Amount
Assets						
Interest Rate Swap Derivatives	$4,071	$0	$4,071	$0	$0	$4,071
Total Assets	$4,071	$0	$4,071	$0	$0	$4,071
Liabilities						
Interest Rate Swap Derivatives	$4,088	$0	$4,088	$0	$(2,440)	$1,648
Repurchase Agreements	106,239	0	106,239	(106,239)	0	0
Total Liabilities	$110,327	$0	$110,327	$(106,239)	$(2,440)	$1,648

	December 31, 2017					
(dollars in thousands)	Gross Amounts of Recognized Assets/ Liabilities	Gross Amounts Offset in the Statement of Financial Position	Net Amounts of Assets presented in the Statement of Financial Position	Gross Amounts Not Offset in the Statement of Financial Position Financial Instruments	Cash Collateral Received	Net Amount
Assets						
Interest Rate Swap Derivatives	$2,441	$0	$2,441	$0	$0	$2,441
Total Assets	$2,441	$0	$2,441	$0	$0	$2,441
Liabilities						
Interest Rate Swap Derivatives	$2,562	$0	$2,562	$0	$(750)	$1,812
Repurchase Agreements	70,652	0	70,652	(70,652)	0	0
Total Liabilities	$73,214	$0	$73,214	$(70,652)	$(750)	$1,812

If an event of default occurs causing an early termination of an interest rate swap derivative, any early termination amount payable to one party by the other party may be reduced by set-off against any other amount payable by the one party to the other party. If a default in performance of any obligation of a repurchase agreement occurs, each party will set-off property held in respect of transactions against obligations owing in respect of any other transactions.

NOTE 9. EARNINGS PER SHARE

Basic earnings per common share is net income available to common shareholders divided by the weighted average number of common shares outstanding during the period, including shares held in treasury on behalf of participants in the Company's Directors Fee Deferral Plan. Diluted earnings per common share includes the dilutive effect of additional potential common shares issuable under stock options, stock awards and warrants, none of which were antidilutive.

	Three Months Ended June 30,		Six Months Ended June 30,	
	2018	2017	2018	2017
Weighted average shares outstanding for basic earnings per common share	25,293,329	25,183,186	25,275,471	25,167,799
Dilutive effect of stock options, awards and warrants	415,887	436,791	429,034	450,753
Weighted average shares outstanding for diluted earnings per common share	25,709,216	25,619,977	25,704,505	25,618,552
Basic earnings per common share	$0.80	$0.61	$1.52	$1.19
Diluted earnings per common share	$0.78	$0.60	$1.50	$1.17

NOTE 10. ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS)

The following tables summarize the changes within each classification of accumulated other comprehensive income (loss) net of tax for the six months ended June 30, 2018 and 2017:

(dollars in thousands)	Unrealized Gains and Losses on Available-for-Sales Securities	Defined Benefit Pension Items	Total
Balance at December 31, 2017	$784	$(1,454)	$(670)
Other comprehensive income before reclassification	(8,903)	0	(8,903)
Amounts reclassified from accumulated other comprehensive income (loss)	6	98	104
Net current period other comprehensive income	(8,897)	98	(8,799)
Adoption of ASU 2018-02 (See Note 1)	140		