

FLUSHING FINANCIAL CORP  
Form 10-Q  
August 04, 2017

UNITED STATES

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 **June 30, 2017**

Commission file number **001-33013**

**FLUSHING FINANCIAL CORPORATION**

*(Exact name of registrant as specified in its charter)*

**Delaware**

*(State or other jurisdiction of incorporation or organization)*

**11-3209278**

*(I.R.S. Employer Identification No.)*

**220 RXR Plaza, Uniondale, New York 11556**

*(Address of principal executive offices)*

**(718) 961-5400**

*(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 ☐ No

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

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

Large accelerated filer ☐ Accelerated filer ☒

Non-accelerated filer ☐ 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 Act). ☐ Yes ☒ No

The number of shares of the registrant’s Common Stock outstanding as of July 31, 2017 was 28,803,937.



## **TABLE OF CONTENTS**

	<b><u>PAGE</u></b>
<b><u>PART I — FINANCIAL INFORMATION</u></b>	
<b><u>ITEM 1. Financial Statements - (Unaudited)</u></b>	
<u>Consolidated Statements of Financial Condition</u>	<u>1</u>
<u>Consolidated Statements of Income</u>	<u>2</u>
<u>Consolidated Statements of Comprehensive Income</u>	<u>3</u>
<u>Consolidated Statements of Cash Flows</u>	<u>4</u>
<u>Consolidated Statements of Changes in Stockholders' Equity</u>	<u>5</u>
<u>Notes to Consolidated Financial Statements</u>	<u>6</u>
<b><u>ITEM 2. Management's Discussion and Analysis of Financial Condition and Results of Operations</u></b>	<u>50</u>
<b><u>ITEM 3. Quantitative and Qualitative Disclosures About Market Risk</u></b>	<u>67</u>
<b><u>ITEM 4. Controls and Procedures</u></b>	<u>67</u>
<b><u>PART II — OTHER INFORMATION</u></b>	
<b><u>ITEM 1. Legal Proceedings</u></b>	<u>68</u>
<b><u>ITEM 1A. Risk Factors</u></b>	<u>68</u>
<b><u>ITEM 2. Unregistered Sales of Equity Securities and Use of Proceeds</u></b>	<u>68</u>
<b><u>ITEM 3. Defaults Upon Senior Securities</u></b>	<u>68</u>
<b><u>ITEM 4. Mine Safety Disclosures</u></b>	<u>68</u>
<b><u>ITEM 5. Other Information</u></b>	<u>68</u>
<b><u>ITEM 6. Exhibits</u></b>	<u>69</u>
<b><u>SIGNATURES</u></b>	<u>70</u>



**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Consolidated Statements of Financial Condition**

(Unaudited)

**Item 1. Financial Statements**

	June 30, 2017	December 31, 2016
(Dollars in thousands, except per share data)		
<b><u>ASSETS</u></b>		
Cash and due from banks	\$48,539	\$35,857
Securities held-to-maturity:		
Mortgage-backed securities (none pledged) (fair value of \$7,816 at at June 30, 2017)	7,983	-
Other securities (none pledged) (fair value of \$22,777 and \$35,408 at June 30, 2017 and December 31, 2016, respectively)	24,451	37,735
Securities available for sale:		
Mortgage-backed securities (including assets pledged of \$89,197 and \$145,860 at June 30, 2017 and December 31, 2016, respectively; \$1,801 and \$2,016 at fair value pursuant to the fair value option at June 30, 2017 and December 31, 2016, respectively)	520,012	516,476
Other securities (including assets pledged of \$143,261 and \$82,064 at June 30, 2017 and December 31, 2016, respectively; \$28,706 and \$28,429 at fair value pursuant to the fair value option at June 30, 2017 and December 31, 2016, respectively)	317,693	344,905
Loans held for sale	30,565	-
Loans:		
Multi-family residential	2,243,643	2,178,504
Commercial real estate	1,349,634	1,246,132
One-to-four family mixed-use property	556,906	558,502
One-to-four family residential	181,213	185,767
Co-operative apartments	7,069	7,418
Construction	16,842	11,495
Small Business Administration	10,591	15,198
Taxi medallion	18,303	18,996
Commercial business and other	644,262	597,122
Net unamortized premiums and unearned loan fees	17,217	16,559
Allowance for loan losses	(22,157 )	(22,229 )
Net loans	5,023,523	4,813,464
Interest and dividends receivable	21,439	20,228

Edgar Filing: FLUSHING FINANCIAL CORP - Form 10-Q

Bank premises and equipment, net	26,592	26,561
Federal Home Loan Bank of New York stock	66,630	59,173
Bank owned life insurance	130,631	132,508
Goodwill	16,127	16,127
Other assets	51,051	55,453
Total assets	\$6,285,236	\$6,058,487

**LIABILITIES**

Due to depositors:		
Non-interest bearing	\$349,302	\$333,163
Interest-bearing:		
Certificate of deposit accounts	1,332,377	1,372,115
Savings accounts	325,815	254,283
Money market accounts	837,565	843,370
NOW accounts	1,368,441	1,362,484
Total interest-bearing deposits	3,864,198	3,832,252
Mortgagors' escrow deposits	41,303	40,216
Borrowed funds		
Federal Home Loan Bank advances	1,317,087	1,159,190
Subordinated Debentures	73,555	73,414
Junior subordinated debentures, at fair value	35,137	33,959
Total borrowed funds	1,425,779	1,266,563
Other liabilities	70,563	72,440
Total liabilities	5,751,145	5,544,634

**STOCKHOLDERS' EQUITY**

Preferred stock (\$0.01 par value; 5,000,000 shares authorized; none issued)	-	-
Common stock (\$0.01 par value; 100,000,000 shares authorized; 31,530,595 shares issued at June 30, 2017 and December 31, 2016; 28,803,937 shares and 28,632,904 shares outstanding at June 30, 2017 and December 31, 2016, respectively)	315	315
Additional paid-in capital	216,447	214,462
Treasury stock, at average cost (2,726,658 shares and 2,897,691 shares at June 30, 2017 and December 31, 2016, respectively)	(51,483 )	(53,754 )
Retained earnings	375,388	361,192
Accumulated other comprehensive loss, net of taxes	(6,576 )	(8,362 )
Total stockholders' equity	534,091	513,853
Total liabilities and stockholders' equity	\$6,285,236	\$6,058,487

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

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Consolidated Statements of Income**

(Unaudited)

(Dollars in thousands, except per share data)	For the three months ended June 30,		For the six months ended June 30,	
	2017	2016	2017	2016
<b><u>Interest and dividend income</u></b>				
Interest and fees on loans	\$51,631	\$48,413	\$102,516	\$95,971
Interest and dividends on securities:				
Interest	6,432	6,510	12,527	13,102
Dividends	123	120	244	239
Other interest income	129	48	282	142
Total interest and dividend income	58,315	55,091	115,569	109,454
<b><u>Interest expense</u></b>				
Deposits	9,510	8,097	18,490	16,070
Other interest expense	5,188	5,105	10,073	10,362
Total interest expense	14,698	13,202	28,563	26,432
Net interest income	43,617	41,889	87,006	83,022
Provision for loan losses	-	-	-	-
Net interest income after provision for loan losses	43,617	41,889	87,006	83,022
<b><u>Non-interest income</u></b>				
Banking services fee income	1,014	973	1,888	1,949
Net gain on sale of securities	-	2,363	-	2,363
Net gain on sale of loans	34	3	244	344
Net gain on sale of buildings	-	33,814	-	33,814
Net loss from fair value adjustments	(1,159 )	(1,115 )	(1,537 )	(2,102 )
Federal Home Loan Bank of New York stock dividends	643	582	1,466	1,205
Gain from life insurance proceeds	6	-	1,167	411
Bank owned life insurance	807	694	1,602	1,389
Other income	603	403	807	884
Total non-interest income	1,948	37,717	5,637	40,257
<b><u>Non-interest expense</u></b>				
Salaries and employee benefits	15,424	13,968	32,528	30,229



Edgar Filing: FLUSHING FINANCIAL CORP - Form 10-Q

Occupancy and equipment	2,654	2,352	5,150	4,722
Professional services	1,919	2,027	3,915	4,177
FDIC deposit insurance	503	940	829	1,844
Data processing	1,321	1,199	2,524	2,290
Depreciation and amortization	1,155	1,062	2,320	2,094
Other real estate owned/foreclosure expense (income)	(96 )	405	255	558
Prepayment penalty on borrowings	-	2,082	-	2,082
Other operating expenses	3,185	4,419	8,108	8,955
Total non-interest expense	26,065	28,454	55,629	56,951
Income before income taxes	19,500	51,152	37,014	66,328
<u>Provision for income taxes</u>				
Federal	5,576	15,203	10,325	19,950
State and local	1,199	5,514	1,704	6,382
Total taxes	6,775	20,717	12,029	26,332
Net income	\$12,725	\$30,435	\$24,985	\$39,996
Basic earnings per common share	\$0.44	\$1.05	\$0.86	\$1.38
Diluted earnings per common share	\$0.44	\$1.05	\$0.86	\$1.38
Dividends per common share	\$0.18	\$0.17	\$0.36	\$0.34

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

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Consolidated Statements of Comprehensive Income**

(Unaudited)

(In thousands)	For the three months ended June 30,		For the six months ended June 30,	
	2017	2016	2017	2016
Net income	\$12,725	\$30,435	\$24,985	\$39,996
Other comprehensive income, net of tax:				
Amortization of actuarial losses, net of taxes of (\$64) and (\$82) for the three months ended June 30, 2017 and 2016, respectively and of (\$128) and (\$165) for the six months ended June 30, 2017 and 2016, respectively.	87	110	174	219
Amortization of prior service credits, net of taxes of \$5 for each of the three months ended June 30, 2017 and 2016, respectively and \$9 and \$10 for the six months ended June 30, 2017 and 2016, respectively.	(6 )	(7 )	(13 )	(13 )
Reclassification adjustment for net gains included in income, net of taxes of \$1,013 for the three and six months ended June 30, 2016.	-	(1,350 )	-	(1,350 )
Net unrealized gains on securities, net of taxes of (\$436) and \$2,252 for the three months ended June 30, 2017 and 2016, respectively and of (\$1,247) and (\$7,280) for the six months ended June 30, 2017 and 2016, respectively.	601	3,024	1,749	9,794
Net unrealized loss on cash flow hedge, net of taxes of \$90 for the three and six months ended June 30, 2017.	(124 )	-	(124 )	-
Total other comprehensive income, net of tax	558	1,777	1,786	8,650
Comprehensive income	\$13,283	\$32,212	\$26,771	\$48,646

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

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Consolidated Statements of Cash Flows**

(Unaudited)

	For the six months ended June 30,	
	2017	2016
(Dollars in thousands)		
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Net income	\$24,985	\$39,996
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization of bank premises and equipment	2,320	2,094
Amortization of premium, net of accretion of discount	3,657	4,099
Net loss from fair value adjustments	1,537	2,102
Net gain from sale of loans	(244 )	(344 )
Net gain from sale of securities	-	(2,363 )
Net gain from sale of buildings	-	(33,814 )
Net (gain) loss from sale of OREO	(50 )	897
Income from bank owned life insurance	(1,602 )	(1,389 )
Gain from life insurance proceeds	(1,167 )	(411 )
Stock-based compensation expense	4,190	3,673
Deferred compensation	(1,930 )	(2,629 )
Excess tax benefit from stock-based payment arrangements	-	(421 )
Deferred income tax provision	1,005	83
(Increase) decrease in other assets	(21 )	3,857
Increase in other liabilities	4	16,102
Net cash provided by operating activities	32,684	31,532
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Purchases of bank premises and equipment	(2,351 )	(1,460 )
Net purchases of Federal Home Loan Bank of New York shares	(7,457 )	(11,129 )
Purchases of securities held-to-maturity	(8,030 )	(27,705 )
Proceeds from maturities of securities held-to-maturity	13,330	5,475
Purchases of securities available for sale	(40,641 )	(61,615 )
Proceeds from sales and calls of securities available for sale	27,500	66,996
Proceeds from maturities and prepayments of securities available for sale	38,161	53,856
Proceeds from bank owned life insurance	3,911	2,236
Proceeds from sale of buildings	-	34,332
Net originations of loans	(201,438)	(160,139)
Purchases of loans	(58,431 )	(137,994)

Edgar Filing: FLUSHING FINANCIAL CORP - Form 10-Q

Proceeds from sale of real estate owned	583	853
Proceeds from sale of loans	21,575	8,360
Net cash used in investing activities	(213,288)	(227,934)

CASH FLOWS FROM FINANCING ACTIVITIES

Net increase in non-interest bearing deposits	16,139	47,643
Net increase (decrease) in interest-bearing deposits	31,629	(8,448 )
Net increase in mortgagors' escrow deposits	1,087	9,061
Net proceeds from short-term borrowed funds	66,500	215,000
Proceeds from long-term borrowings	173,066	150,000
Repayment of long-term borrowings	(82,049 )	(190,637)
Purchases of treasury stock	(2,599 )	(9,085 )
Excess tax benefit from stock-based payment arrangements	-	421
Proceeds from issuance of common stock upon exercise of stock options	-	127
Cash dividends paid	(10,487 )	(9,878 )
Net cash provided by financing activities	193,286	204,204

Net increase in cash and cash equivalents	12,682	7,802
Cash and cash equivalents, beginning of period	35,857	42,363
Cash and cash equivalents, end of period	\$48,539	\$50,165

SUPPLEMENTAL CASHFLOW DISCLOSURE

Interest paid	\$27,840	\$28,250
Income taxes paid	10,646	9,270
Taxes paid if excess tax benefits were not tax deductible	10,646	9,691
Non-cash activities:		
Loans transferred to Other Real Estate Owned	-	486
Loans held for investment transferred to loans available for sale	30,565	-

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

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Consolidated Statements of Changes in Stockholders' Equity****For the six months ended June 30, 2017 and 2016**

(Unaudited)

(Dollars in thousands, except per share data)	Total	Common Stock	Additional Paid-in Capital	Retained Earnings	Treasury Stock	Accumulated Other Comprehensive Income (Loss)
Balance at December 31, 2016	\$513,853	\$ 315	\$214,462	\$361,192	\$(53,754)	\$ (8,362 )
Net Income	24,985	-	-	24,985	-	-
Award of common shares released from Employee Benefit Trust (111,470 shares)	2,363	-	2,363	-	-	-
Vesting of restricted stock unit awards (258,165 shares)	-	-	(4,562 )	(262 )	4,824	-
Exercise of stock options (4,400 shares)	-	-	(6 )	(40 )	46	-
Stock-based compensation expense	4,190	-	4,190	-	-	-
Purchase of treasury shares (10,000 shares)	(278 )	-	-	-	(278 )	-
Repurchase of shares to satisfy tax obligation (80,303 shares)	(2,321 )	-	-	-	(2,321 )	-
Dividends on common stock (\$0.36 per share)	(10,487 )	-	-	(10,487 )	-	-
Other comprehensive income	1,786	-	-	-	-	1,786
Balance at June 30, 2017	\$534,091	\$ 315	\$216,447	\$375,388	\$(51,483)	\$ (6,576 )
Balance at December 31, 2015	\$473,067	\$ 315	\$210,652	\$316,530	\$(48,868)	\$ (5,562 )
Net Income	39,996	-	-	39,996	-	-
Award of common shares released from Employee Benefit Trust (134,005 shares)	1,912	-	1,912	-	-	-
Vesting of restricted stock unit awards (245,111 shares)	-	-	(4,047 )	(396 )	4,443	-
Exercise of stock options (27,945 shares)	127	-	2	(34 )	159	-
Stock-based compensation expense	3,673	-	3,673	-	-	-
Stock-based income tax benefit	421	-	421	-	-	-
Purchase of treasury shares (378,695 shares)	(7,492 )	-	-	-	(7,492 )	-

Edgar Filing: FLUSHING FINANCIAL CORP - Form 10-Q

Repurchase of shares to satisfy tax obligation (77,212 shares)	(1,593 )	-	-	-	(1,593 )	-
Dividends on common stock (\$0.34 per share)	(9,878 )	-	-	(9,878 )	-	-
Other comprehensive income	8,650	-	-	-	-	8,650
Balance at June 30, 2016	\$508,883	\$ 315	\$212,613	\$346,218	\$(53,351)	\$ 3,088

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

- 5 -

## **PART I – FINANCIAL INFORMATION**

### **FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES**

#### **Notes to Consolidated Financial Statements**

(Unaudited)

#### **1. Basis of Presentation**

The primary business of Flushing Financial Corporation (the “Holding Company”), a Delaware corporation, is the operation of its wholly owned subsidiary, Flushing Bank (the “Bank”).

The unaudited consolidated financial statements presented in this Quarterly Report on Form 10-Q (“Quarterly Report”) include the collective results of the Holding Company and its direct and indirect wholly-owned subsidiaries, including the Bank, Flushing Preferred Funding Corporation, Flushing Service Corporation, and FSB Properties Inc., which are collectively herein referred to as “we,” “us,” “our” and the “Company.”

The Holding Company also owns Flushing Financial Capital Trust II, Flushing Financial Capital Trust III, and Flushing Financial Capital Trust IV (the “Trusts”), which are special purpose business trusts. The Trusts are not included in the Company’s consolidated financial statements, as the Company would not absorb the losses of the Trusts if any losses were to occur.

The accompanying unaudited consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”) and general practices within the banking industry. The information furnished in these interim statements reflects all adjustments that are, in the opinion of management, necessary for a fair statement of the results for such presented periods of the Company. Such adjustments are of a normal recurring nature, unless otherwise disclosed in this Quarterly Report. All inter-company balances and transactions have been eliminated in consolidation. The results of operations in the interim statements are not necessarily indicative of the results that may be expected for the full year.

The accompanying unaudited consolidated financial statements have been prepared in conformity with the instructions to Quarterly Report on Form 10-Q and Article 10, Rule 10-01 of Regulation S-X for interim financial statements. Accordingly, certain information and footnote disclosures normally included in financial statements prepared in accordance with GAAP have been condensed or omitted pursuant to the rules and regulations of the Securities and Exchange Commission (“SEC”). The unaudited consolidated interim financial information should be read in conjunction

with the Company's Annual Report on Form 10-K for the year ended December 31, 2016.

When necessary, certain reclassifications were made to prior-year amounts to conform to the current-year presentation.

## **2. Use of Estimates**

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, and disclosure of contingent assets and liabilities at the date of the financial statements, and reported amounts of revenue and expenses during the reporting period. Estimates that are particularly susceptible to change in the near term are used in connection with the determination of the allowance for loan losses ("ALLL"), the evaluation of goodwill for impairment, the review of the need for a valuation allowance of the Company's deferred tax assets, the fair value of financial instruments and the evaluation of other-than-temporary impairment ("OTTI") on securities. Actual results could differ from these estimates.

## **3. Earnings Per Share**

Basic earnings per common share is computed by dividing net income available to common shareholders by the total weighted average number of common shares outstanding, which includes unvested participating securities. Unvested share-based payment awards that contain nonforfeitable rights to dividends or dividend equivalents (whether paid or unpaid) are participating securities and as such are included in the calculation of earnings per share. The Company's unvested restricted stock unit awards are considered participating securities. Therefore, weighted average common shares outstanding used for computing basic earnings per common share includes common shares outstanding plus unvested restricted stock unit awards. The computation of diluted earnings per share includes the additional dilutive effect of stock options outstanding and other common stock equivalents during the period. Common stock equivalents that are anti-dilutive are not included in the computation of diluted earnings per common share. The numerator for calculating basic and diluted earnings per common share is net income available to common shareholders. The shares held in the Company's Employee Benefit Trust are not included in shares outstanding for purposes of calculating earnings per common share.



## Notes to Consolidated Financial Statements

Earnings per common share have been computed based on the following:

	For the three months ended June 30, 2017		For the three months ended June 30, 2016		For the six months ended June 30, 2017		For the six months ended June 30, 2016	
	(In thousands, except per share data)							
Net income, as reported	\$12,725		\$30,435		\$24,985		\$39,996	
Divided by:								
Weighted average common shares outstanding	29,135		29,022		29,077		29,059	
Weighted average common stock equivalents	1		12		3		14	
Total weighted average common shares outstanding and common stock equivalents	29,136		29,034		29,080		29,073	
Basic earnings per common share	\$0.44		\$1.05		\$0.86		\$1.38	
Diluted earnings per common share <sup>(1)</sup>	\$0.44		\$1.05		\$0.86		\$1.38	
Dividend payout ratio	40.9	%	16.2	%	41.9	%	24.6	%

(1) For the three and six months ended June 30, 2017 and 2016, there were no stock options that were anti-dilutive.

#### 4. Debt and Equity Securities

The Company's investments in equity securities that have readily determinable fair values and all investments in debt securities are classified in one of the following three categories and accounted for accordingly: (1) trading securities, (2) securities available for sale and (3) securities held-to-maturity.

The Company did not hold any trading securities at June 30, 2017 and December 31, 2016. Securities available for sale are recorded at fair value. Securities held-to-maturity are recorded at amortized cost.

The following table summarizes the Company's portfolio of securities held-to-maturity at June 30, 2017:

	Amortized		Gross	Gross
	Cost	Fair Value	Unrealized Gains	Unrealized Losses
	(In thousands)			
Securities held-to-maturity:				
Municipals	\$24,451	\$22,777	\$ -	\$ 1,674
Total other securities	24,451	22,777	-	1,674
FNMA	7,983	7,816	-	167
Total mortgage-backed securities	7,983	7,816	-	167
Total	\$32,434	\$30,593	\$ -	\$ 1,841

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

The following table summarizes the Company's portfolio of securities held-to-maturity at December 31, 2016:

	Amortized		Gross	Gross
	Cost	Fair Value	Unrealized Gains	Unrealized Losses
	(In thousands)			
Securities held-to-maturity:				
Municipals	\$37,735	\$35,408	\$ -	\$ 2,327
Total	\$37,735	\$35,408	\$ -	\$ 2,327

The following table summarizes the Company's portfolio of securities available for sale at June 30, 2017:

	Amortized		Gross	Gross
	Cost	Fair Value	Unrealized Gains	Unrealized Losses
Securities available for sale:	(In thousands)			
Corporate	\$110,000	\$103,191	\$ -	\$ 6,809
Municipals	123,606	126,596	2,990	-
Mutual funds	21,563	21,563	-	-
Collateralized loan obligations	58,379	58,899	520	-
Other	7,444	7,444	-	-
Total other securities	320,992	317,693	3,510	6,809
REMIC and CMO	409,049	408,926	2,248	2,371
GNMA	1,153	1,248	95	-
FNMA	105,011	104,736	540	815
FHLMC	5,131	5,102	24	53
Total mortgage-backed securities	520,344	520,012	2,907	3,239
Total	\$841,336	\$837,705	\$ 6,417	\$ 10,048

Edgar Filing: FLUSHING FINANCIAL CORP - Form 10-Q

The following table summarizes the Company's portfolio of securities available for sale at December 31, 2016:

	Amortized		Gross	Gross
	Cost	Fair Value	Unrealized	Unrealized
			Gains	Losses
Securities available for sale:	(In thousands)			
Corporate	\$110,000	\$102,910	\$ -	\$ 7,090
Municipals	124,984	126,903	1,983	64
Mutual funds	21,366	21,366	-	-
Collateralized loan obligations	85,470	86,365	895	-
Other	7,363	7,361	-	2
Total other securities	349,183	344,905	2,878	7,156
REMIC and CMO	402,636	401,370	1,607	2,873
GNMA	1,319	1,427	108	-
FNMA	109,493	108,351	463	1,605
FHLMC	5,378	5,328	35	85
Total mortgage-backed securities	518,826	516,476	2,213	4,563
Total	\$868,009	\$861,381	\$ 5,091	\$ 11,719

Mortgage-backed securities shown in the table above include one private issue CMO that is collateralized by commercial real estate mortgages with an amortized cost and market value of \$0.1 million and \$0.2 million at June 30, 2017 and December 31, 2016, respectively.

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

The corporate securities held by the Company at June 30, 2017 and December 31, 2016 are issued by U.S. banking institutions.

The following tables detail the amortized cost and fair value of the Company's securities classified as held-to-maturity and available for sale at June 30, 2017 by contractual maturity. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

Securities held-to-maturity:	Amortized	
	Cost	Fair Value
	(In thousands)	
Due in one year or less	\$2,585	\$2,585
Due after ten years	21,866	20,192
Total other securities	24,451	22,777
Mortgage-backed securities	7,983	7,816
Total	\$32,434	\$30,593

Securities available for sale:	Amortized	
	Cost	Fair Value
	(In thousands)	
Due in one year or less	\$-	\$-
Due after one year through five years	1,751	1,762
Due after five years through ten years	123,872	120,810
Due after ten years	173,806	173,558
Mutual funds	21,563	21,563
Total other securities	320,992	317,693
Mortgage-backed securities	520,344	520,012

Total	\$841,336	\$837,705
-------	-----------	-----------

- 9 -

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

The following tables show the Company's securities with gross unrealized losses and their fair value, aggregated by category and length of time that individual securities have been in a continuous unrealized loss position, at the dates indicated:

	At June 30, 2017						
		Total		Less than 12 months		12 months or more	
		Unrealized		Unrealized		Unrealized	
	Count	Fair Value	Losses	Fair Value	Losses	Fair Value	Losses
		(Dollars in thousands)					
Held-to-maturity securities							
Municipals	1	\$20,192	\$ 1,674	\$20,192	\$ 1,674	\$-	\$ -
Total other securities	1	20,192	1,674	20,192	1,674	-	-
FNMA	1	7,816	167	7,816	167	-	-
Total mortgage-backed securities	1	7,816	167	7,816	167	-	-
Total	2	\$28,008	\$ 1,841	\$28,008	\$ 1,841	\$-	\$ -
Available for sale securities							
Corporate	14	\$103,191	\$ 6,809	\$9,475	\$ 525	\$93,716	\$ 6,284
Total other securities	14	103,191	6,809	9,475	525	93,716	6,284
REMIC and CMO	31	188,993	2,371	176,158	1,815	12,835	556
FNMA	14	52,826	815	47,153	605	5,673	210
FHLMC	1	3,981	53	3,981	53	-	-
Total mortgage-backed securities	46	245,800	3,239	227,292	2,473	18,508	766
Total	60	\$348,991	\$ 10,048	\$236,767	\$ 2,998	\$112,224	\$ 7,050

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

	At December 31, 2016						
		Total		Less than 12 months		12 months or more	
		Unrealized	Unrealized	Unrealized	Unrealized	Unrealized	Unrealized
	Coun	Fair Value	Losses	Fair Value	Losses	Fair Value	Losses
	(Dollars in thousands)						
Held-to-maturity securities							
Municipals	1	\$ 19,538	\$ 2,327	\$ 19,538	\$ 2,327	\$ -	\$ -
Total	1	\$ 19,538	\$ 2,327	\$ 19,538	\$ 2,327	\$ -	\$ -
Available for sale securities							
Corporate	14	\$ 102,910	\$ 7,090	\$ 28,476	\$ 1,524	\$ 74,434	\$ 5,566
Municipals	4	16,047	64	16,047	64	-	-
Other	1	298	2	-	-	298	2
Total other securities	19	119,255	7,156	44,523	1,588	74,732	5,568
REMIC and CMO	35	222,807	2,873	208,827	2,268	13,980	605
FNMA	18	80,924	1,605	74,972	1,250	5,952	355
FHLMC	1	3,993	85	3,993	85	-	-
Total mortgage-backed securities	54	307,724	4,563	287,792	3,603	19,932	960
Total	73	\$ 426,979	\$ 11,719	\$ 332,315	\$ 5,191	\$ 94,664	\$ 6,528

OTTI losses on impaired securities must be fully recognized in earnings if an investor has the intent to sell the debt security or if it is more likely than not that the investor will be required to sell the debt security before recovery of its amortized cost. However, even if an investor does not expect to sell a debt security in an unrealized loss position, the investor must evaluate the expected cash flows to be received and determine if a credit loss has occurred. In the event that a credit loss has occurred, only the amount of impairment associated with the credit loss is recognized in earnings in the Consolidated Statements of Income. Amounts relating to factors other than credit losses are recorded in accumulated other comprehensive loss ("AOCL") within Stockholders' Equity. Unrealized losses on available for sale securities, that are deemed to be temporary, are recorded in AOCL, net of tax.

The Company reviewed each investment that had an unrealized loss at June 30, 2017 and December 31, 2016. The unrealized losses in FNMA securities held-to-maturity at June 30, 2017 were caused by movements in interest rates. The unrealized losses in municipal securities held-to-maturity at June 30, 2017 and December 31, 2016 were caused



by illiquidity in the market and movements in interest rates. The unrealized losses in securities available for sale at June 30, 2017 and December 31, 2016 were caused by movements in interest rates.

It is not anticipated that these securities would be settled at a price that is less than the amortized cost of the Company's investment. Each of these securities is performing according to its terms and, in the opinion of management, will continue to perform according to its terms. The Company does not have the intent to sell these securities and it is more likely than not the Company will not be required to sell the securities before recovery of the securities' amortized cost basis. This conclusion is based upon considering the Company's cash and working capital requirements and contractual and regulatory obligations, none of which the Company believes would cause the sale of the securities. Therefore, the Company did not consider these investments to be other-than-temporarily impaired at June 30, 2017 and December 31, 2016.

Realized gains and losses on the sales of securities are determined using the specific identification method. The Company sold available for sale securities totaling \$64.6 million during the three and six months ended June 30, 2016. The Company did not sell any securities available for sale during the three and six months ended June 30, 2017.

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

The following table represents the gross gains and gross losses realized from the sale of securities available for sale for the periods indicated:

	For the three months ended June 30, 2017	For the six months ended June 30, 2017
	(In thousands)	
Gross gains from the sale of securities	\$- \$2,370	\$- \$2,370
Gross losses from the sale of securities	- (7 )	- (7 )
Net gains from the sale of securities	\$- \$2,363	\$- \$2,363

**5. Loans**

Loans are reported at their principal outstanding balance net of any unearned income, charge-offs, deferred loan fees and costs on originated loans and unamortized premiums or discounts on purchased loans. Interest on loans is recognized on the accrual basis. The accrual of income on loans is generally discontinued when certain factors, such as contractual delinquency of 90 days or more, indicate reasonable doubt as to the timely collectability of such income. Uncollected interest previously recognized on non-accrual loans is reversed from interest income at the time the loan is placed on non-accrual status. A non-accrual loan can be returned to accrual status when contractual delinquency returns to less than 90 days delinquent. Subsequent cash payments received on non-accrual loans that do not bring the loan to less than 90 days delinquent are recorded on a cash basis. Subsequent cash payments can also be applied first as a reduction of principal until all principal is recovered and then subsequently to interest, if in management's opinion, it is evident that recovery of all principal due is likely to occur. Loan fees and certain loan origination costs are deferred. Net loan origination costs and premiums or discounts on loans purchased are amortized into interest income over the contractual life of the loans using the level-yield method. Prepayment penalties received on loans which pay in full prior to their scheduled maturity are included in interest income in the period they are collected.

The Company maintains an allowance for loan losses at an amount, which, in management's judgment, is adequate to absorb probable estimated losses inherent in the loan portfolio. Management's judgment in determining the adequacy of the allowance is based on evaluations of the collectability of loans. This evaluation is inherently subjective, as it requires estimates that are susceptible to significant revisions as more information becomes available. An unallocated component is maintained to cover uncertainties that could affect management's estimate of probable losses. The unallocated component of the allowance reflects the margin of imprecision inherent in the underlying assumptions used in the methodologies for estimating specific and general losses in the portfolio. The allowance is established through a provision for loan losses based on management's evaluation of the risk inherent in the various components of the loan portfolio and other factors, including historical loan loss experience (which is updated quarterly), current economic conditions, delinquency and non-accrual trends, classified loan levels, risk in the portfolio and volumes and trends in loan types, recent trends in charge-offs, changes in underwriting standards, experience, ability and depth of the Company's lenders, collection policies and experience, internal loan review function and other external factors. The Company segregated its loans into two portfolios based on year of origination. One portfolio was reviewed for loans originated after December 31, 2009 and a second portfolio for loans originated prior to January 1, 2010. Our decision to segregate the portfolio based upon origination dates was based on changes made in our underwriting standards during 2009. By the end of 2009, all loans were being underwritten based on revised and tightened underwriting standards. Loans originated prior to 2010 have a higher delinquency rate and loss history. Each of the years in the portfolio for loans originated prior to 2010 has a similar delinquency rate. The determination of the amount of the allowance for loan losses includes estimates that are susceptible to significant changes due to changes in appraisal values of collateral, national and local economic conditions and other factors. We review our loan portfolio by separate categories with similar risk and collateral characteristics. Impaired loans are segregated and reviewed separately. All non-accrual loans are classified as impaired loans. The Company's Board of Directors reviews and approves management's evaluation of the adequacy of the allowance for loan losses on a quarterly basis.

The allowance for loan losses is established through charges to earnings in the form of a provision for loan losses. Increases and decreases in the allowance other than charge-offs and recoveries are included in the provision for loan losses. When a loan or a portion of a loan is determined to be uncollectible, the portion deemed uncollectible is charged against the allowance, and subsequent recoveries, if any, are credited to the allowance.

## **PART I – FINANCIAL INFORMATION**

### **FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES**

#### **Notes to Consolidated Financial Statements**

(Unaudited)

The Company recognizes a loan as non-performing when the borrower has demonstrated the inability to bring the loan current, or due to other circumstances which, in management's opinion, indicate the borrower will be unable to bring the loan current within a reasonable time. All loans classified as non-performing, which includes all loans past due 90 days or more, are classified as non-accrual unless there is, in our opinion, compelling evidence the borrower will bring the loan current in the immediate future. Appraisals are obtained and/or updated internal evaluations are prepared as soon as practical, and before the loan becomes 90 days delinquent. The loan balances of collateral dependent impaired loans are compared to the property's updated fair value. The Company considers fair value of collateral dependent loans to be 85% of the appraised or internally estimated value of the property, except for taxi medallion loans. The fair value of the underlying collateral of taxi medallion loans is the value of the underlying medallion based upon the most recently reported arm's length transaction. The balance which exceeds fair value is generally charged-off. In addition, taxi medallion loans on accrual status with a loan-to-value greater than 100% are classified as impaired and allocated a portion of the ALLL in the amount of the excess of the loan-to-value over the loan's principal balance. The 85% is based on the actual net proceeds the Bank has received from the sale of other real estate owned ("OREO") as a percentage of OREO's appraised value.

A loan is considered impaired when, based upon current information, the Company believes it is probable that it will be unable to collect all amounts due, both principal and interest, in accordance with the original terms of the loan. Impaired loans are measured based on the present value of the expected future cash flows discounted at the loan's effective interest rate or at the loan's observable market price or, as a practical expedient, the fair value of the collateral if the loan is collateral dependent. Interest income on impaired loans is recorded on the cash basis.

The Company reviews each impaired loan on an individual basis to determine if either a charge-off or a valuation allowance needs to be allocated to the loan. The Company does not charge-off or allocate a valuation allowance to loans for which management has concluded the current value of the underlying collateral will allow for recovery of the loan balance either through the sale of the loan or by foreclosure and sale of the property.

The Company evaluates the underlying collateral through a third party appraisal, or when a third party appraisal is not available, the Company will use an internal evaluation. The internal evaluations are prepared using an income approach or a sales approach. The income approach is used for income producing properties and uses current revenues less operating expenses to determine the net cash flow of the property. Once the net cash flow is determined, the value of the property is calculated using an appropriate capitalization rate for the property. The sales approach uses comparable sales prices in the market. When an internal evaluation is used, we place greater reliance on the income approach to value the collateral.

In preparing internal evaluations of property values, the Company seeks to obtain current data on the subject property from various sources, including: (1) the borrower; (2) copies of existing leases; (3) local real estate brokers and appraisers; (4) public records (such as for real estate taxes and water and sewer charges); (5) comparable sales and rental data in the market; (6) an inspection of the property and (7) interviews with tenants. These internal evaluations primarily focus on the income approach and comparable sales data to value the property.

As of June 30, 2017, we utilized recent third party appraisals of the collateral to measure impairment for \$41.9 million, or 82.4%, of collateral dependent impaired loans, and used internal evaluations of the property's value for \$8.9 million, or 17.6%, of collateral dependent impaired loans.

The Company may restructure a loan to enable a borrower experiencing financial difficulties to continue making payments when it is deemed to be in the Company's best long-term interest. This restructure may include reducing the interest rate or amount of the monthly payment for a specified period of time, after which the interest rate and repayment terms revert to the original terms of the loan. We classify these loans as Troubled Debt Restructured ("TDR").

These restructurings have not included a reduction of principal balance. The Company believes that restructuring these loans in this manner will allow certain borrowers to become and remain current on their loans. All loans classified as TDR are considered impaired, however TDR loans which have been current for six consecutive months at the time they are restructured as TDR remain on accrual status and are not included as part of non-performing loans. Loans which were delinquent at the time they are restructured as a TDR are placed on non-accrual status and reported as non-accrual loans until they have made timely payments for six consecutive months.

The allocation of a portion of the allowance for loan losses for a performing TDR loan is based upon the present value of the future expected cash flows discounted at the loan's original effective rate, or for a non-performing TDR, which is collateral dependent, the fair value of the collateral. At June 30, 2017, there were no commitments to lend additional funds to borrowers whose loans were modified to a TDR. The modification of loans to a TDR did not have a significant effect on our operating results, nor did it require a significant allocation of the allowance for loan losses.

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

The following tables shows loans modified and classified as TDR during the periods indicated:

(Dollars in thousands)	For the three and six months ended June 30, 2017			Modification description
	Number	Balance		
Taxi medallion	5	\$4,289		Three received a below market interest rate and a loan amortization extension, while two received an amortization extension.
Total	5	\$4,289		

  

(Dollars in thousands)	For the three and six months ended June 30, 2016			Modification description
	Number	Balance		
One-to-four family - residential	2	\$263		Received below market interest rates and amortization extensions.
Commercial business and other	2	739		One received an amortization extension and one received a below market interest rate and an amortization extension.
Total	4	\$1,002		

The recorded investment of the loans modified and classified as TDR presented in the tables above, were unchanged as there was no principal forgiven in this modification.

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

The following table shows our recorded investment for loans classified as TDR that are performing according to their restructured terms at the periods indicated:

(Dollars in thousands)	June 30, 2017		December 31, 2016	
	Number of contracts	Recorded investment	Number of contracts	Recorded investment
Multi-family residential	9	\$ 2,546	9	\$ 2,572
Commercial real estate	2	2,037	2	2,062
One-to-four family - mixed-use property	5	1,778	5	1,800
One-to-four family - residential	3	581	3	591
Taxi medallion	17	13,870	12	9,735
Commercial business and other	2	566	2	675
Total performing troubled debt restructured	38	\$ 21,378	33	\$ 17,435

The following table shows our recorded investment for loans classified as TDR that are not performing according to their restructured terms at the periods indicated:

(Dollars in thousands)	June 30, 2017		December 31, 2016	
	Number of contracts	Recorded investment	Number of contracts	Recorded investment
Multi-family residential	1	\$ 383	1	\$ 396
Total troubled debt restructurings that subsequently defaulted	1	\$ 383	1	\$ 396

During the three and six months ended June 30, 2017 and 2016 there were no TDR loans transferred to non-performing status.

- 15 -



**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

The following table shows our non-performing loans at the dates indicated:

(In thousands)	June 30, 2017	December 31, 2016
Loans ninety days or more past due and still accruing:		
One-to-four family - mixed-use property	\$-	\$ 386
Construction	602	-
Taxi medallion	727	-
Total	1,329	386
Non-accrual mortgage loans:		
Multi-family residential	1,537	1,837
Commercial real estate	1,948	1,148
One-to-four family - mixed-use property	2,971	4,025
One-to-four family - residential	7,616	8,241
Total	14,072	15,251
Non-accrual non-mortgage loans:		
Small Business Administration	53	1,886
Taxi medallion	-	3,825
Commercial business and other	5	68
Total	58	5,779
Total non-accrual loans	14,130	21,030
Total non-performing loans	\$15,459	\$21,416

The following is a summary of interest foregone on non-accrual loans and loans classified as TDR for the periods indicated:

	For the three months ended June 30, 2017		For the six months ended June 30, 2016	
	2017	2016	2017	2016
	(In thousands)			
Interest income that would have been recognized had the loans performed in accordance with their original terms	\$433	\$476	\$848	\$948
Less: Interest income included in the results of operations	141	101	268	213
Total foregone interest	\$292	\$375	\$580	\$735

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

The following tables show an age analysis of our recorded investment in loans, including loans past maturity, at the periods indicated:

(In thousands)	June 30, 2017			Total Past Due	Current	Total Loans
	30 - 59 Days Past Due	60 - 89 Days Past Due	Greater than 90 Days			
Multi-family residential	\$4,380	\$417	\$1,537	\$6,334	\$2,237,309	\$2,243,643
Commercial real estate	1,106	1,671	1,948	4,725	1,344,909	1,349,634
One-to-four family - mixed-use property	1,807	675	2,971	5,453	551,453	556,906
One-to-four family - residential	789	322	7,426	8,537	172,676	181,213
Co-operative apartments	-	-	-	-	7,069	7,069
Construction loans	-	576	602	1,178	15,664	16,842
Small Business Administration	-	-	-	-	10,591	10,591
Taxi medallion	-	-	727	727	17,576	18,303
Commercial business and other	4	-	5	9	644,253	644,262
Total	\$8,086	\$3,661	\$15,216	\$26,963	\$5,001,500	\$5,028,463

(In thousands)	December 31, 2016			Total Past Due	Current	Total Loans
	30 - 59 Days Past Due	60 - 89 Days Past Due	Greater than 90 Days			
Multi-family residential	\$2,575	\$287	\$1,837	\$4,699	\$2,173,805	\$2,178,504
Commercial real estate	3,363	22	1,148	4,533	1,241,599	1,246,132
One-to-four family - mixed-use property	4,671	762	4,411	9,844	548,658	558,502
One-to-four family - residential	3,831	194	8,047	12,072	173,695	185,767
Co-operative apartments	-	-	-	-	7,418	7,418
Construction loans	-	-	-	-	11,495	11,495
Small Business Administration	13	-	1,814	1,827	13,371	15,198
Taxi medallion	-	-	3,825	3,825	15,171	18,996

Edgar Filing: FLUSHING FINANCIAL CORP - Form 10-Q

Commercial business and other	22	1	-	23	597,099	597,122
Total	\$14,475	\$1,266	\$21,082	\$36,823	\$4,782,311	\$4,819,134

- 17 -

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

The following tables show the activity in the allowance for loan losses for the three month periods indicated:

June 30, 2017

(In thousands)	Multi-family residential	Commercial real estate	One-to-four family - mixed-use property	One-to-four family - residential	Construction loans	Small Business Administration	Taxi medallion and other	Commercial business and other	Unallocated	Total
Allowance for credit losses:										
Beginning balance	\$5,907	\$4,485	\$2,691	\$979	\$94	\$315	\$2,213	\$4,712	\$815	\$22,211
Charge-off's	(148 )	(4 )	(1 )	(170 )	-	(24 )	-	(3 )	-	(350 )
Recoveries	201	-	68	-	-	10	-	17	-	296
Provision (Benefit)	(43 )	207	(190 )	181	36	5	117	(58 )	(255 )	-
Ending balance	\$5,917	\$4,688	\$2,568	\$990	\$130	\$306	\$2,330	\$4,668	\$560	\$22,157

June 30, 2016

(In thousands)	Multi-family residential	Commercial real estate	One-to-four family - mixed-use property	One-to-four family - residential	Construction loans	Small Business Administration	Taxi medallion and other	Commercial business and other	Unallocated	Total
Allowance for credit losses:										
Beginning balance	\$6,298	\$4,201	\$3,507	\$1,042	\$55	\$269	\$335	\$4,591	\$1,695	\$21,993
Charge-off's	(23 )	-	(54 )	(8 )	-	(1 )	-	(15 )	-	(101 )
Recoveries	206	-	18	1	-	43	-	38	-	306
Provision (Benefit)	(304 )	244	(145 )	9	20	263	707	55	(849 )	-
Ending balance	\$6,177	\$4,445	\$3,326	\$1,044	\$75	\$574	\$1,042	\$4,669	\$846	\$22,198

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

The following tables show the activity in the allowance for loan losses for the six month periods indicated:

June 30, 2017

(In thousands)	Multi-family residential	Commercial real estate	One-to-four family - mixed-use property	One-to-four family - residential	Construction loans	Small Business Administration	Taxi medallion and other	Commercial business and other	Unallocated	Total
Allowance for credit losses:										
Beginning balance	\$5,923	\$4,487	\$2,903	\$1,015	\$92	\$481	\$2,243	\$4,492	\$593	\$22,229
Charge-off's	(162 )	(4 )	(35 )	(170 )	-	(89 )	(54 )	(15 )	-	(529 )
Recoveries	231	68	68	-	-	49	-	41	-	457
Provision (Benefit)	(75 )	137	(368 )	145	38	(135 )	141	150	(33 )	-
Ending balance	\$5,917	\$4,688	\$2,568	\$990	\$130	\$306	\$2,330	\$4,668	\$560	\$22,157

June 30, 2016

(In thousands)	Multi-family residential	Commercial real estate	One-to-four family - mixed-use property	One-to-four family - residential	Construction loans	Small Business Administration	Taxi medallion and other	Commercial business and other	Unallocated	Total
Allowance for credit losses:										
Beginning balance	\$6,718	\$4,239	\$4,227	\$1,227	\$50	\$262	\$343	\$4,469	\$-	\$21,535
Charge-off's	(65 )	-	(68 )	(74 )	-	(1 )	-	(40 )	-	(248 )
Recoveries	219	-	205	366	-	74	-	47	-	911
Provision (Benefit)	(695 )	206	(1,038 )	(475 )	25	239	699	193	846	-
Ending balance	\$6,177	\$4,445	\$3,326	\$1,044	\$75	\$574	\$1,042	\$4,669	\$846	\$22,198

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

The following tables show the manner in which loans were evaluated for impairment at the periods indicated:

June 30, 2017

(In thousands)	Multi-family residential	Commercial real estate	One-to-four family - mixed- use property	One-to-four family- residential	Co-operative apartment loans	Construction loans	Small Business Administration	Taxi medallion	Comm business and other
Financing Receivables:									
Ending Balance	\$2,243,643	\$1,349,634	\$556,906	\$181,213	\$7,069	\$16,842	\$10,591	\$18,303	\$644,2
Ending balance: individually evaluated for impairment	\$5,102	\$7,552	\$6,708	\$10,806	\$-	\$602	\$150	\$18,303	\$2,508
Ending balance: collectively evaluated for impairment	\$2,238,541	\$1,342,082	\$550,198	\$170,407	\$7,069	\$16,240	\$10,441	\$-	\$641,7
Allowance for credit losses:									
Ending balance: individually evaluated for impairment	\$328	\$157	\$214	\$57	\$-	\$-	\$-	\$2,330	\$9
Ending balance: collectively evaluated for impairment	\$5,589	\$4,531	\$2,354	\$933	\$-	\$130	\$306	\$-	\$4,659

December 31, 2016

(In thousands)	Multi-family residential	Commercial real estate	One-to-four family - mixed- use property	One-to-four family- residential	Co-operative apartment loans	Construction loans	Small Business Administration	Taxi medallion	Comm business and other
Financing Receivables:									
Ending Balance	\$2,178,504	\$1,246,132	\$558,502	\$185,767	\$7,418	\$11,495	\$15,198	\$18,996	\$597,1
Ending balance: individually evaluated for impairment	\$5,923	\$6,551	\$8,809	\$9,989	\$-	\$-	\$1,937	\$16,282	\$2,492

Edgar Filing: FLUSHING FINANCIAL CORP - Form 10-Q

Ending balance: collectively evaluated for impairment	\$2,172,581	\$1,239,581	\$549,693	\$175,778	\$7,418	\$11,495	\$13,261	\$2,714	\$594,6
Allowance for credit losses:									
Ending balance: individually evaluated for impairment	\$232	\$179	\$417	\$60	\$-	\$-	\$90	\$2,236	\$12
Ending balance: collectively evaluated for impairment	\$5,691	\$4,308	\$2,486	\$955	\$-	\$92	\$391	\$7	\$4,480

- 20 -



**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

The following table shows our recorded investment, unpaid principal balance and allocated allowance for loan losses for impaired loans at the dates indicated:

	June 30, 2017			December 31, 2016		
	Unpaid			Unpaid		
	Recorded	Principal	Related	Recorded	Principal	Related
	Investmen	Balance	Allowance	Investmen	Balance	Allowance
	(In thousands)					
With no related allowance recorded:						
Mortgage loans:						
Multi-family residential	\$2,412	\$2,695	\$ -	\$3,660	\$3,796	\$ -
Commercial real estate	5,516	5,543	-	4,489	4,516	-
One-to-four family mixed-use property	5,459	5,833	-	6,435	6,872	-
One-to-four family residential	10,384	11,649	-	9,560	11,117	-
Construction	602	602	-	-	-	-
Non-mortgage loans:						
Small Business Administration	150	236	-	416	509	-
Taxi medallion	3,746	3,746	-	2,334	2,476	-
Commercial business and other	2,127	2,496	-	2,072	2,443	-
Total loans with no related allowance recorded	30,396	32,800	-	28,966	31,729	-
With an allowance recorded:						
Mortgage loans:						
Multi-family residential	2,690	2,705	328	2,263	2,263	232
Commercial real estate	2,036	2,037	157	2,062	2,062	179
One-to-four family mixed-use property	1,249	1,249	214	2,374	2,376	417
One-to-four family residential	422	422	57	429	429	60
Non-mortgage loans:						
Small Business Administration	-	-	-	1,521	1,909	90
Taxi medallion	14,557	14,557	2,330	13,948	13,948	2,236
Commercial business and other	381	381	9	420	420	12
Total loans with an allowance recorded	21,335	21,351	3,095	23,017	23,407	3,226
Total Impaired Loans:						
Total mortgage loans	\$30,770	\$32,735	\$ 756	\$31,272	\$33,431	\$ 888

Total non-mortgage loans	\$20,961	\$21,416	\$ 2,339	\$20,711	\$21,705	\$ 2,338
--------------------------	----------	----------	----------	----------	----------	----------

- 21 -

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

The following table shows our average recorded investment and interest income recognized for impaired loans for the three months ended:

	June 30, 2017		June 30, 2016	
	Average	Interest	Average	Interest
	Recorded	Income	Recorded	Income
	Investmen	Recognized	Investmen	Recognized
	(In thousands)			
With no related allowance recorded:				
Mortgage loans:				
Multi-family residential	\$2,730	\$ 22	\$5,920	\$ 33
Commercial real estate	6,438	59	5,077	45
One-to-four family mixed-use property	5,560	41	8,928	41
One-to-four family residential	10,263	30	10,649	25
Construction	602	-	570	7
Non-mortgage loans:				
Small Business Administration	160	2	257	3
Taxi medallion	4,352	25	-	-
Commercial business and other	2,187	43	2,313	46
Total loans with no related allowance recorded	32,292	222	33,714	200
With an allowance recorded:				
Mortgage loans:				
Multi-family residential	2,471	50	2,289	29
Commercial real estate	2,043	24	2,222	24
One-to-four family mixed-use property	1,450	16	2,617	34
One-to-four family residential	424	4	389	4
Non-mortgage loans:				
Small Business Administration	-	-	413	10
Taxi medallion	14,216	50	4,237	44
Commercial business and other	391	6	1,225	7
Total loans with an allowance recorded	20,995	150	13,392	152
Total Impaired Loans:				
Total mortgage loans	\$31,981	\$ 246	\$38,661	\$ 242

Total non-mortgage loans	\$21,306	\$ 126	\$8,445	\$ 110
--------------------------	----------	--------	---------	--------

- 22 -

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

The following table shows our average recorded investment and interest income recognized for impaired loans for the six months ended:

	June 30, 2017		June 30, 2016	
	Average	Interest	Average	Interest
	Recorded	Income	Recorded	Income
	Investmen	Recognized	Investmen	Recognized
	(In thousands)			
With no related allowance recorded:				
Mortgage loans:				
Multi-family residential	\$3,040	\$ 45	\$5,861	\$ 67
Commercial real estate	5,788	154	4,655	90
One-to-four family mixed-use property	5,851	78	9,313	88
One-to-four family residential	10,028	56	11,184	52
Construction	401	7	713	14
Non-mortgage loans:				
Small Business Administration	245	4	263	6
Taxi medallion	3,679	55	-	-
Commercial business and other	2,148	87	2,436	93
Total loans with no related allowance recorded	31,180	486	34,425	410
With an allowance recorded:				
Mortgage loans:				
Multi-family residential	2,401	79	2,294	58
Commercial real estate	2,049	48	2,272	49
One-to-four family mixed-use property	1,758	34	2,660	68
One-to-four family residential	425	8	373	7
Non-mortgage loans:				
Small Business Administration	507	-	287	19
Taxi medallion	14,126	93	3,531	88
Commercial business and other	401	12	1,494	14
Total loans with an allowance recorded	21,667	274	12,911	303
Total Impaired Loans:				
Total mortgage loans	\$31,741	\$ 509	\$39,325	\$ 493

Total non-mortgage loans	\$21,106	\$ 251	\$8,011	\$ 220
--------------------------	----------	--------	---------	--------

- 23 -

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

In accordance with our policy and the current regulatory guidelines, we designate loans as “Special Mention,” which are considered “Criticized Loans,” and “Substandard,” “Doubtful,” or “Loss,” which are considered “Classified Loans.” If a loan does not fall within one of the previous mentioned categories, then the loan would be considered “Pass.” These loan designations are updated quarterly. We designate a loan as Substandard when a well-defined weakness is identified that jeopardizes the orderly liquidation of the debt. We designate a loan Doubtful when it displays the inherent weakness of a Substandard loan with the added provision that collection of the debt in full, on the basis of existing facts, is highly improbable. We designate a loan as Loss if it is deemed the debtor is incapable of repayment. The Company does not hold any loans designated as loss, as loans that are designated as Loss are charged-off. Loans that are non-accrual are designated as Substandard, Doubtful or Loss. We designate a loan as Special Mention if the asset does not warrant classification within one of the other classifications, but does contain a potential weakness that deserves closer attention.

The following table sets forth the recorded investment in loans designated as Criticized or Classified at the dates indicated:

(In thousands)	June 30, 2017				
	Special Mention	Substandard	Doubtful	Loss	Total
Multi-family residential	\$8,312	\$ 2,554	\$ -	\$ -	\$10,866
Commercial real estate	2,295	5,516	-	-	7,811
One-to-four family - mixed-use property	3,050	4,929	-	-	7,979
One-to-four family - residential	843	10,225	-	-	11,068
Construction loans	576	602	-	-	1,178
Small Business Administration	525	107	-	-	632
Taxi medallion	-	18,303	-	-	18,303
Commercial business and other	8,772	2,508	-	-	11,280
Total loans	\$24,373	\$ 44,744	\$ -	\$ -	\$69,117

(In thousands)	December 31, 2016				
	Special Mention	Substandard	Doubtful	Loss	Total

Edgar Filing: FLUSHING FINANCIAL CORP - Form 10-Q

Multi-family residential	\$7,133	\$ 3,351	\$ -	\$ -	\$10,484
Commercial real estate	2,941	4,489	-	-	7,430
One-to-four family - mixed-use property	4,197	7,009	-	-	11,206
One-to-four family - residential	1,205	9,399	-	-	10,604
Small Business Administration	540	436	-	-	976
Taxi medallion	2,715	16,228	54	-	18,997
Commercial business and other	9,924	2,493	-	-	12,417
Total loans	\$28,655	\$ 43,405	\$ 54	\$ -	\$72,114

Commitments to extend credit (principally real estate mortgage loans) and lines of credit (principally home equity lines of credit and business lines of credit) amounted to \$77.1 million and \$243.0 million, respectively, at June 30, 2017.

- 24 -



**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

**6. Loans held for sale**

Loans held for sale are carried at the lower of cost or estimated fair value. The Bank had \$30.6 million in loans held for sale at June 30, 2017. The Bank did not have any loans held for sale at December 31, 2016.

The Bank has implemented a strategy of selling certain delinquent and non-performing loans. Once the Bank has decided to sell a loan, the sale usually closes in a short period of time, generally within the same quarter. Loans designated held for sale are reclassified from loans held for investment to loans held for sale. For delinquent and non-performing loan sales, terms of sale include cash due upon the closing of the sale, no contingencies or recourse to the Bank and servicing is released to the buyer.

The following tables show delinquent and non-performing loans sold during the period indicated:

For the three months ended June 30, 2017				
(Dollars in thousands)	Loans sold	Proceeds	Net (charge-offs)	
			recoveries	Net gain
Commercial real estate	1	\$ 335	\$ (4 )	\$ -
Total <sup>(1)</sup>	1	\$ 335	\$ (4 )	\$ -

For the three months ended June 30, 2016				
(Dollars in thousands)	Loans sold	Proceeds	Net (charge-offs)	
			recoveries	Net gain

Edgar Filing: FLUSHING FINANCIAL CORP - Form 10-Q

Multi-family residential	3	\$ 1,174	\$ (8 )	\$ -
One-to-four family - mixed-use property	3	1,271	-	3
Total	6	\$ 2,445	\$ (8 )	\$ 3

For the six months ended

June 30, 2017

Net  
(charge-offs)

(Dollars in thousands)	Loans sold	Proceeds	recoveries	Net gain
One-to-four family - mixed-use property	5	\$ 1,790	\$ (33 )	\$ 28
Commercial real estate	1	335	(4 )	-
Total <sup>(2)</sup>	6	\$ 2,125	\$ (37 )	\$ 28

- 25 -

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

(Dollars in thousands)	For the six months ended June 30, 2016			
	Loans sold	Proceeds	Net (charge-offs) recoveries	Net gain
Multi-family residential	6	\$ 2,049	\$ (8 )	\$ 2
Commercial real estate	2	192	-	-
One-to-four family - mixed-use property	7	2,585	-	23
Total <sup>(3)</sup>	15	\$ 4,826	\$ (8 )	\$ 25

Does not include the sale of four performing Small Business Administration loans for proceeds totaling \$1.5 (1) million, resulting in a net gain totaling \$69,000 and the sale of a participating interest in seven mortgage loans for proceeds totaling \$14.5 million, resulting in a net loss of \$35,000 during the three months ended June 30, 2017.

Does not include the sale of seven performing Small Business Administration loans for proceeds totaling \$4.9 (2) million, resulting in a net gain totaling \$250,000 and the sale of a participating interest in seven mortgage loans for proceeds totaling \$14.5 million, resulting in a net loss of \$35,000 during the six months ended June 30, 2017.

(3) Does not include the sale of six performing Small Business Administration loans for proceeds totaling \$3.5 million during the six months ended June 30, 2016. These loans were sold for a net gain of \$0.3 million.

**7. Other Real Estate Owned**

The following are changes in OREO during the periods indicated:

Edgar Filing: FLUSHING FINANCIAL CORP - Form 10-Q

For the three months ended June 30, 2017	For the six months ended June 30, 2016
---	---

(In thousands)

Balance at beginning of period	\$-	\$4,602	\$533	\$4,932
Acquisitions	-	-	-	486
Write-down of carrying value	-	(934 )	-	(934 )
Sales	-	-	(533)	(816 )
Balance at end of period <sup>(1)</sup>	\$-	\$3,668	\$-	\$3,668

(1) OREO are included in other assets on the Company's Consolidated Statements of Financial Condition.

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

The following table shows the gross gains and write-downs of OREO reported in the Consolidated Statements of Income during the periods indicated:

	For the three months ended June 30, 2017		For the six months ended June 30, 2017	
	2016	2017	2016	2017
	(In thousands)			
Gross gains	\$-	\$-	\$50	\$37
Write-down of carrying value	-	(934)	-	(934)
Total net loss (gain)	\$-	\$(934)	\$50	\$(897)

We may obtain physical possession of residential real estate collateralizing a consumer mortgage loan via foreclosure or an in-substance repossession. During the three and six months ended June 30, 2017, we did not foreclose on any consumer mortgages through in-substance repossession. We did not hold any foreclosed residential real estate properties at June 30, 2017. At December 31, 2016, we held one foreclosed residential real estate property for \$0.5 million. Included within net loans as of June 30, 2017 and December 31, 2016 was a recorded investment of \$9.9 million and \$11.4 million, respectively, of consumer mortgage loans secured by residential real estate properties for which formal foreclosure proceedings were in process according to local requirements of the applicable jurisdiction.

**8. Stock-Based Compensation**

For the three months ended June 30, 2017 and 2016, the Company's net income, as reported, includes \$1.0 million and \$0.6 million, respectively, of stock-based compensation costs and \$0.4 million and \$0.2 million, respectively, of income tax benefits related to the stock-based compensation plans in each of the periods. For the six months ended

June 30, 2017 and 2016, the Company's net income, as reported, includes \$4.1 million and \$3.6 million, respectively, of stock-based compensation costs and \$1.2 million and \$1.4 million, respectively, of income tax benefits related to the stock-based compensation plans. The Company did not issue any restricted stock units during the three months ended June 30, 2017 and 2016. During the six months ended June 30, 2017 and 2016, the Company granted 276,900 and 337,175 restricted stock units, respectively. The Company has not granted stock options since 2009. At June 30, 2017, the Company had 1,200 stock options, all 100% vested, outstanding.

The Company uses the fair value of the common stock on the date of award to measure compensation cost for restricted stock unit awards. Compensation cost is recognized over the vesting period of the award using the straight-line method.

The 2014 Omnibus Incentive Plan ("2014 Omnibus Plan") became effective on May 20, 2014 after adoption by the Board of Directors and approval by the stockholders. The 2014 Omnibus Plan authorizes the Compensation Committee of the Company's Board of Directors to grant a variety of equity compensation awards as well as long-term and annual cash incentive awards, all of which can, but need not, be structured so as to comply with Section 162(m) of the Internal Revenue Code of 1986, as amended. On May 31, 2017, stockholders approved an amendment to the 2014 Omnibus Plan (the "Amendment") authorizing an additional 672,000 shares available for future issuance. In addition, to increasing the number of shares for future grants, the Amendment eliminates, in the case of stock options and SARs, the ability to recycle shares used to satisfy the exercise price or taxes for such awards. No other amendments to the 2014 Omnibus Plan were made. Including the additional shares authorized from the Amendment, 944,676 shares are available for future issuance under the 2014 Omnibus Plan at June 30, 2017.

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

The following table summarizes the Company's restricted stock unit ("RSU") awards at or for the six months ended June 30, 2017:

	Shares	Weighted-Average Grant-Date Fair Value
Non-vested at December 31, 2016	488,779	\$ 18.99
Granted	276,900	28.21
Vested	(244,272)	21.93
Forfeited	(21,360 )	23.30
Non-vested at June 30, 2017	500,047	\$ 22.48
Vested but unissued at June 30, 2017	270,017	\$ 22.33

As of June 30, 2017, there was \$9.7 million of total unrecognized compensation cost related to RSU awards granted. That cost is expected to be recognized over a weighted-average period of 3.3 years. The total fair value of awards vested for the three months ended June 30, 2017 was \$40,000. No awards vested during the three months ended June 30, 2016. The total fair value of awards vested for the six months ended June 30, 2017 and 2016 was \$7.0 million and \$4.8 million, respectively. The vested but unissued RSU awards consist of awards made to employees and directors who are eligible for retirement. According to the terms of these awards, which provide for vesting upon retirement, these employees and directors have no risk of forfeiture. These shares will be issued at the original contractual vesting and settlement dates.

Cash proceeds, fair value received, tax benefits, and intrinsic value related to stock options exercised, and the weighted average grant date fair value for options granted, during the three and six months ended June 30, 2017 and 2016 are provided in the following table:

For the three months	For the six months ended
----------------------------	--------------------------------

(In thousands)	ended			
	June 30,		June 30,	
	2017	2016	2017	2016
Proceeds from stock options exercised	\$-	\$109	\$-	\$127
Fair value of shares received upon exercise of stock options	37	22	37	350
Tax benefit (expense) related to stock options exercised	39	14	39	(2 )
Intrinsic value of stock options exercised	96	69	96	112

*Phantom Stock Plan:* The Company maintains a non-qualified phantom stock plan as a supplement to its profit sharing plan for officers who have achieved the designated level and completed one year of service. The Company adjusts its liability under this plan to the fair value of the shares at the end of each period.

- 28 -



**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

The following table summarizes the Phantom Stock Plan at or for the six months ended June 30, 2017:

Phantom Stock Plan	Shares	Fair Value
Outstanding at December 31, 2016	89,339	\$29.39
Granted	7,356	27.25
Forfeited	(10 )	28.95
Distributions	(206 )	28.93
Outstanding at June 30, 2017	96,479	\$28.19
Vested at June 30, 2017	96,146	\$28.19

The Company recorded stock-based compensation expense (benefit) for the Phantom Stock Plan of \$144,000 and (\$139,000) for the three months ended June 30, 2017 and 2016, respectively. The total fair value of the distributions from the Phantom Stock Plan was less than \$1,000 for the three months ended June 30, 2017. There were no distributions for the three months ended June 30, 2016.

For the six months ended June 30, 2017 and 2016, the Company recorded stock-based compensation benefit for the Phantom Stock Plan of \$66,000 and \$109,000, respectively. The total fair value of the distributions from the Phantom Stock Plan during the six months ended June 30, 2017 and 2016 was \$6,000 and \$28,000, respectively.

**9. Pension and Other Postretirement Benefit Plans**

The following table sets forth information regarding the components of net expense for the pension and other postretirement benefit plans.



**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

(In thousands)	Three months ended June 30, 2017		Six months ended June 30, 2016	
	2017	2016	2017	2016
<b>Employee Pension Plan:</b>				
Interest cost	\$216	\$226	\$432	\$452
Amortization of unrecognized loss	174	201	348	402
Expected return on plan assets	(348)	(348)	(696)	(696)
Net employee pension expense	\$42	\$79	\$84	\$158
<b>Outside Director Pension Plan:</b>				
Service cost	\$10	\$11	\$20	\$22
Interest cost	23	24	46	48
Amortization of unrecognized gain	(23 )	(21 )	(46 )	(42 )
Amortization of past service liability	10	10	20	20
Net outside director pension expense	\$20	\$24	\$40	\$48
<b>Other Postretirement Benefit Plans:</b>				
Service cost	\$79	\$90	\$158	\$180
Interest cost	76	80	152	160
Amortization of unrecognized loss	-	12	-	24
Amortization of past service credit	(21 )	(22 )	(42 )	(43 )
Net other postretirement expense	\$134	\$160	\$268	\$321

The Company previously disclosed in its Consolidated Financial Statements for the year ended December 31, 2016 that it expects to contribute \$0.3 million and \$0.2 million to the Outside Director Pension Plan (the “Outside Director Pension Plan”) and the other postretirement benefit plans (the “Other Postretirement Benefit Plans”), respectively, during the year ending December 31, 2017. The Company does not expect to make a contribution to the Employee Pension Plan (the “Employee Pension Plan”). As of June 30, 2017, the Company has contributed \$72,000 to the Outside Director Pension Plan and \$41,000 to the Other Postretirement Benefit Plans. As of June 30, 2017, the Company has not revised its expected contributions for the year ending December 31, 2017.

**10. Fair Value of Financial Instruments**

The Company carries certain financial assets and financial liabilities at fair value in accordance with GAAP which defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date, establishes a framework for measuring fair value and expands disclosures about fair value measurements. GAAP permits entities to choose to measure many financial instruments and certain other items at fair value. At June 30, 2017, the Company carried financial assets and financial liabilities under the fair value option with fair values of \$30.5 million and \$35.1 million, respectively. At December 31, 2016, the Company carried financial assets and financial liabilities under the fair value option with fair values of \$30.4 million and \$34.0 million, respectively. The Company did not elect to carry any additional financial assets or financial liabilities under the fair value option during the six months ended June 30, 2017.

- 30 -

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

The following table presents the financial assets and financial liabilities reported at fair value under the fair value option, and the changes in fair value included in the Consolidated Statement of Income – Net gain (loss) from fair value adjustments, at or for the periods ended as indicated:

	Fair Value Measurements at June 30, 2017	Fair Value Measurements at December 31, 2016	Changes in Fair Values For Items Measured at Fair Value Pursuant to Election of the Fair Value Option			
			Three Months Ended		Six Months Ended	
			June 30, 2017	June 30, 2016	June 30, 2017	June 30, 2016
(Dollars in thousands)						
Mortgage-backed securities	\$ 1,801	\$ 2,016	\$ (3 )	\$ (3 )	\$ (10 )	\$ 2
Other securities	28,706	28,429	112	90	144	186
Junior subordinated debentures	35,137	33,959	(595 )	492	(1,165 )	1,546
Net gain (loss) from fair value adjustments <sup>(1) (2)</sup>			\$ (486 )	\$ 579	\$ (1,031 )	\$ 1,734

The net gain (loss) from fair value adjustments presented in the above table does not include net losses of \$0.7 (1) million and \$1.7 million for the three months ended June 30, 2017 and 2016, respectively, from the change in the fair value of interest rate swaps.

The net gain (loss) from fair value adjustments presented in the above table does not include net losses of \$0.5 (2) million and \$3.8 million for the six months ended June 30, 2017 and 2016, respectively, from the change in the fair value of interest rate swaps.

Included in the fair value of the financial assets and financial liabilities selected for the fair value option is the accrued interest receivable or payable for the related instrument. The Company reports as interest income or interest expense in the Consolidated Statement of Income, the interest receivable or payable on the financial instruments selected for the fair value option at their respective contractual rates.

The borrowed funds had a contractual principal amount of \$61.9 million at both June 30, 2017 and December 31, 2016. The fair value of borrowed funds includes accrued interest payable of \$0.2 million and \$0.1 million at June 30, 2017 and December 31, 2016, respectively.

The Company generally holds its earning assets, other than securities available for sale, to maturity and settles its liabilities at maturity. However, fair value estimates are made at a specific point in time and are based on relevant market information. These estimates do not reflect any premium or discount that could result from offering for sale at one time the Company's entire holdings of a particular instrument. Accordingly, as assumptions change, such as interest rates and prepayments, fair value estimates change and these amounts may not necessarily be realized in an immediate sale.

Disclosure of fair value does not require fair value information for items that do not meet the definition of a financial instrument or certain other financial instruments specifically excluded from its requirements. These items include core deposit intangibles and other customer relationships, premises and equipment, leases, income taxes and equity.

Further, fair value disclosure does not attempt to value future income or business. These items may be material and accordingly, the fair value information presented does not purport to represent, nor should it be construed to represent, the underlying "market" or franchise value of the Company.

Financial assets and financial liabilities reported at fair value are required to be measured based on either: (1) quoted prices in active markets for identical financial instruments (Level 1); (2) significant other observable inputs (Level 2); or (3) significant unobservable inputs (Level 3).

A description of the methods and significant assumptions utilized in estimating the fair value of the Company's assets and liabilities that are carried at fair value on a recurring basis are as follows:

Level 1 – where quoted market prices are available in an active market. The Company did not value any of its assets or liabilities that are carried at fair value on a recurring basis as Level 1 at June 30, 2017 and December 31, 2016.

Level 2 – when quoted market prices are not available, fair value is estimated using quoted market prices for similar financial instruments and adjusted for differences between the quoted instrument and the instrument being valued. Fair value can also be estimated by using pricing models, or discounted cash flows. Pricing models primarily use market-based or independently sourced market parameters as inputs, including, but not limited to, yield curves, interest rates, equity or debt prices and credit spreads. In addition to observable market information, models also incorporate maturity and cash flow assumptions. At June 30, 2017 and December 31, 2016, Level 2 included mortgage related securities, corporate debt, municipals and interest rate swaps.

- 31 -

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

Level 3 – when there is limited activity or less transparency around inputs to the valuation, financial instruments are classified as Level 3. At June 30, 2017 and December 31, 2016, Level 3 included trust preferred securities owned and junior subordinated debentures issued by the Company and a single issuer trust preferred security.

The methods described above may produce fair values that may not be indicative of net realizable value or reflective of future fair values. While the Company believes, its valuation methods are appropriate and consistent with those of other market participants, the use of different methodologies, assumptions and models to determine fair value of certain financial instruments could produce different estimates of fair value at the reporting date.

The following table sets forth the assets and liabilities that are carried at fair value on a recurring basis and the method that was used to determine their fair value, at June 30, 2017 and December 31, 2016:

	Quoted Prices in Active Markets for Identical Assets (Level 1)		Significant Other Observable Inputs (Level 2)		Significant Other Unobservable Inputs (Level 3)		Total carried at fair value on a recurring basis	
	2017	2016	2017	2016	2017	2016	2017	2016
(In thousands)								
<b>Assets:</b>								
Mortgage-backed Securities	\$-	\$ -	\$520,012	\$516,476	\$-	\$-	\$520,012	\$516,476
Other securities	-	-	310,249	337,544	7,444	7,361	317,693	344,905
Interest rate swaps	-	-	5,648	6,350	-	-	5,648	6,350
<b>Total assets</b>	<b>\$-</b>	<b>\$ -</b>	<b>\$835,909</b>	<b>\$860,370</b>	<b>\$7,444</b>	<b>\$7,361</b>	<b>\$843,353</b>	<b>\$867,731</b>
<b>Liabilities:</b>								
Junior subordinated debentures	\$-	\$ -	\$-	\$-	\$35,137	\$33,959	\$35,137	\$33,959
Interest rate swaps	-	-	4,624	3,386	-	-	4,624	3,386



Total liabilities	\$-	\$ -	\$4,624	\$3,386	\$35,137	\$33,959	\$39,761	\$37,345
-------------------	-----	------	---------	---------	----------	----------	----------	----------

- 32 -

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

The following tables set forth the Company's assets and liabilities that are carried at fair value on a recurring basis, classified within Level 3 of the valuation hierarchy for the periods indicated:

	For the three months ended		June 30, 2016	
	Trust	Junior	Trust	Junior
	preferred	subordinated	preferred	subordinated
	securities	debentures	securities	debentures
	(In thousands)			
Beginning balance	\$7,394	\$ 34,536	\$7,150	\$ 27,977
Net gain from fair value adjustment of financial assets <sup>(1)</sup>	48	-	15	-
Net loss (gain) from fair value adjustment of financial liabilities <sup>(1)</sup>	-	594	-	(491)
Decrease in accrued interest payable	-	7	-	(1)
Change in unrealized gains included in other comprehensive income	2	-	2	-
Ending balance	\$7,444	\$ 35,137	\$7,167	\$ 27,485
Changes in unrealized gains held at period end	\$2	\$ -	\$2	\$ -

  

	For the six months ended		June 30, 2016	
	Trust	Junior	Trust	Junior
	preferred	subordinated	preferred	subordinated
	securities	debentures	securities	debentures
	(In thousands)			
Beginning balance	\$7,361	\$ 33,959	\$7,212	\$ 29,018
Net gain (loss) from fair value adjustment of financial assets <sup>(1)</sup>	81	-	(45)	-
Net loss (gain) from fair value adjustment of financial liabilities <sup>(1)</sup>	-	1,165	-	(1,547)
Increase in accrued interest payable	-	13	-	14
	2	-	-	-

Edgar Filing: FLUSHING FINANCIAL CORP - Form 10-Q

Change in unrealized gains included in other comprehensive income

Ending balance	\$7,444	\$ 35,137	\$7,167	\$ 27,485
Changes in unrealized gains held at period end	\$2	\$ -	\$-	\$ -

(1) These totals in the table above are presented in the Consolidated Statement of Income under net gains (losses) from fair value adjustments.

During the three and six months ended June 30, 2017 and 2016, there were no transfers between Levels 1, 2 and 3.

- 33 -

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

The following tables present the quantitative information about recurring Level 3 fair value of financial instruments and the fair value measurements at the periods indicated:

June 30, 2017							
	Fair Value (Dollars in thousands)	Valuation Technique	Unobservable Input	Range		Weighted Average	
Assets:							
Trust preferred securities	\$7,444	Discounted cash flows	Discount rate	6.0% - 6.9%	6.8	%	
Liabilities:							
Junior subordinated debentures	\$35,137	Discounted cash flows	Discount rate	6.0%	6.0	%	
December 31, 2016							
	Fair Value (Dollars in thousands)	Valuation Technique	Unobservable Input	Range		Weighted Average	
Assets:							
Trust preferred securities	\$7,361	Discounted cash flows	Discount rate	6.3% - 7.1%	7.0	%	
Liabilities:							
Junior subordinated debentures	\$33,959	Discounted cash flows	Discount rate	6.3%	6.3	%	

The significant unobservable inputs used in the fair value measurement of the Company's trust preferred securities and junior subordinated debentures valued under Level 3 at June 30, 2017 and December 31, 2016, is the effective yields

used in the cash flow models. Significant increases or decreases in the effective yield in isolation would result in a significantly lower or higher fair value measurement.

The following table sets forth the Company's assets and liabilities that are carried at fair value on a non-recurring basis and the method that was used to determine their fair value at June 30, 2017 and December 31, 2016:

	Quoted Prices in Active Markets for Identical Assets (Level 1)		Significant Other Observable Inputs (Level 2)		Significant Other Unobservable Inputs (Level 3)		Total carried at fair value on a recurring basis	
	2017	2016	2017	2016	2017	2016	2017	2016
	(In thousands)							
Assets:								
Impaired loans	\$ -	\$ -	\$ -	\$ -	\$ 14,418	\$ 14,968	\$ 14,418	\$ 14,968
Other real estate owned	-	-	-	-	-	533	-	533
Total assets	\$ -	\$ -	\$ -	\$ -	\$ 14,418	\$ 15,501	\$ 14,418	\$ 15,501

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

The following tables present the quantitative information about non-recurring Level 3 fair value of financial instruments and the fair value measurements at the dates indicated:

At June 30, 2017					
	Fair Value	Valuation Technique	Unobservable Input	Range	Weighted Average
(Dollars in thousands)					
Assets:					
Impaired loans	\$1,773	Income approach	Capitalization rate	6.0% to 7.5%	6.8%
			Reduction for planned expedited disposal	15.0%	15.0%
Impaired loans	\$7,674	Sales approach	Adjustment to sales comparison value to reconcile differences between comparable sales	-40.0% to	16.2% -2.0%
			Reduction for planned expedited disposal	0% to 15.0%	7.7%
Impaired loans	\$4,971	Blended income and sales approach	Adjustment to sales comparison value to reconcile differences between comparable sales	-30.0% to	25.0% -1.6%
			Capitalization rate	5.0% to	9.8% 7.4%
			Reduction planned for expedited disposal	14.5% to	15.0% 15.0%

At December 31, 2016					
	Fair Value	Valuation Technique	Unobservable Input	Range	Weighted Average
(Dollars in thousands)					
Assets:					
Impaired loans	\$2,007	Income approach	Capitalization rate	6.0% to 7.5%	7.0%
			Reduction for planned expedited disposal	15.0%	15.0%

Edgar Filing: FLUSHING FINANCIAL CORP - Form 10-Q

Impaired loans	\$8,703	Sales approach	Adjustment to sales comparison value to reconcile differences between comparable sales	-40.0% to	16.2%	-1.5%
			Reduction for planned expedited disposal	0% to	15.0%	7.7%
Impaired loans	\$4,258	Blended income and sales approach	Adjustment to sales comparison value to reconcile differences between comparable sales	-50.0% to	25.0%	-0.6%
			Capitalization rate	5.3% to	9.5%	7.2%
			Reduction planned for expedited disposal	15.0%	15.0%	
Other real estate owned	\$533	Sales approach	Adjustment to sales comparison value to reconcile differences between comparable sales	3.3% to	18.6%	11.0%

**PART I – FINANCIAL INFORMATION**

**FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES**

**Notes to Consolidated Financial Statements**

(Unaudited)

The Company did not have any liabilities that were carried at fair value on a non-recurring basis at June 30, 2017 and December 31, 2016.

The methods and assumptions used to estimate fair value at June 30, 2017 and December 31, 2016 are as follows:

**Cash and Due from Banks, Overnight Interest-Earning Deposits and Federal Funds Sold:**

The fair values of financial instruments that are short-term or reprice frequently and have little or no risk are considered to have a fair value that approximates carrying value.

**FHLB-NY stock:**

The fair value is based upon the par value of the stock, which equals its carrying value.

**Securities:**

The fair values of securities are contained in Note 4 of Notes to Consolidated Financial Statements. Fair value is based upon quoted market prices, where available. If a quoted market price is not available, fair value is estimated using quoted market prices for similar securities and adjusted for differences between the quoted instrument and the instrument being valued. When there is limited activity or less transparency around inputs to the valuation, securities are valued using discounted cash flows.

**Loans held for sale:**



The fair value of non-performing loans held for sale is estimated through a negotiated sales price.

**Loans:**

The fair value of loans is estimated by discounting the expected future cash flows using the current rates at which similar loans would be made to borrowers with similar credit ratings and remaining maturities.

For non-accruing loans, fair value is generally estimated by discounting management's estimate of future cash flows with a discount rate commensurate with the risk associated with such assets or for collateral dependent loans 85% of the appraised or internally estimated value of the property, except for taxi medallion loans. The fair value of the underlying collateral of taxi medallion loans is the most recent reported arm's length transaction. When there is no recent sale activity, the fair value is calculated using capitalization rates.

**Other Real Estate Owned:**

OREO are carried at fair value less selling costs. The fair value is based on appraised value through a current appraisal, or sometimes through an internal review, additionally adjusted by the estimated costs to sell the property.

**Accrued Interest Receivable:**

The carrying amount is a reasonable estimate of fair value due to its short-term nature and is valued at the input level for its underlying financial asset.

**Due to Depositors:**

The fair values of demand, passbook savings, NOW, money market deposits and escrow deposits are, by definition, equal to the amount payable on demand at the reporting dates (i.e. their carrying value). The fair value of certificates of deposits are estimated by discounting the expected future cash flows using the rates currently offered for deposits of similar remaining maturities.

**Borrowings:**

The fair value of borrowings is estimated by discounting the contractual cash flows using interest rates in effect for borrowings with similar maturities and collateral requirements or using a market-standard model. The fair value of the junior subordinated debentures was developed using a credit spread based on the subordinated debt issued by the Company adjusting for differences in the junior subordinated debt's credit rating, liquidity and time to maturity.

- 36 -

**PART I – FINANCIAL INFORMATION**

**FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES**

**Notes to Consolidated Financial Statements**

(Unaudited)

**Accrued Interest Payable:**

The carrying amount is a reasonable estimate of fair value due to its short-term nature and is valued at the input level for its underlying financial liability.

**Interest Rate Swaps:**

The fair value of interest rate swaps is based upon broker quotes.

**Other Financial Instruments:**

The fair values of commitments to sell, lend or borrow are estimated using the fees currently charged or paid to enter into similar agreements, taking into account the remaining terms of the agreements and the present creditworthiness of the counterparties or on the estimated cost to terminate them or otherwise settle with the counterparties at the reporting date. For fixed-rate loan commitments to sell, lend or borrow, fair values also consider the difference between current levels of interest rates and committed rates (where applicable). At June 30, 2017 and December 31, 2016, the fair values of the above financial instruments approximate the recorded amounts of the related fees and were not considered to be material.

The following tables set forth the carrying amounts and estimated fair values of selected financial instruments based on the assumptions described above used by the Company in estimating fair value at the periods indicated:

June 30, 2017					
Carrying	Fair				
Amount	Value	Level 1	Level 2	Level 3	

Edgar Filing: FLUSHING FINANCIAL CORP - Form 10-Q

(In thousands)

Assets:

Cash and due from banks	\$48,539	48,539	\$48,539	\$-	\$-
Securities held-to-maturity					
Mortgage-backed securities	7,983	7,816	-	7,816	-
Other securities	24,451	22,777	-	-	22,777
Securities available for sale					
Mortgage-backed securities	520,012	520,012	-	520,012	-
Other securities	317,693	317,693	-	310,249	7,444
Loans held for sale	30,565	30,565			30,565
Loans	5,045,680	5,021,555	-	-	5,021,555
FHLB-NY stock	66,630	66,630	-	66,630	-
Accrued interest receivable	21,439	21,439	-	21,439	-
Interest rate swaps	5,648	5,648	-	5,648	-
Total assets	\$6,088,640	\$6,062,674	\$48,539	\$931,794	\$5,082,341

Liabilities:

Deposits	\$4,254,803	\$4,256,788	\$2,922,426	\$1,334,362	\$-
Borrowings	1,425,779	1,422,040	-	1,386,903	35,137
Accrued interest payable	2,587	2,587	-	2,587	-
Interest rate swaps	4,624	4,624	-	4,624	-
Total liabilities	\$5,687,793	\$5,686,039	\$2,922,426	\$2,728,476	\$35,137

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

	December 31, 2016				
	Carrying	Fair			
	Amount	Value	Level 1	Level 2	Level 3
	(In thousands)				
Assets:					
Cash and due from banks	\$35,857	\$35,857	\$35,857	\$-	\$-
Securities held-to-maturity					
Other securities	37,735	35,408	-	-	35,408
Securities available for sale					
Mortgage-backed securities	516,476	516,476	-	516,476	-
Other securities	344,905	344,905	-	337,544	7,361
Loans	4,835,693	4,814,840	-	-	4,814,840
FHLB-NY stock	59,173	59,173	-	59,173	-
Interest rate swaps	6,350	6,350	-	6,350	-
Total assets	\$5,836,189	\$5,813,009	\$35,857	\$919,543	\$4,857,609
Liabilities:					
Deposits	\$4,205,631	\$4,213,714	\$2,833,516	\$1,380,198	\$-
Borrowings	1,266,563	1,255,283	-	1,221,324	33,959
Interest rate swaps	3,386	3,386	-	3,386	-
Total liabilities	\$5,475,580	\$5,472,383	\$2,833,516	\$2,604,908	\$33,959

**11. Derivative Financial Instruments**

At June 30, 2017 and December 31, 2016, the Company's derivative financial instruments consist of interest rate swaps. The Company's interest rate swaps are used for three purposes: 1) to mitigate the Company's exposure to rising interest rates on a portion (\$18.0 million) of its floating rate junior subordinated debentures that have a contractual value of \$61.9 million, at June 30, 2017 and December 31, 2016; 2) mitigate the Company's exposure to rising interest rates on certain fixed rate loans totaling \$277.7 million and \$235.4 million at June 30, 2017 and December 31, 2016, respectively; and 3) to mitigate exposure to rising interest rates on certain short-term advances totaling \$50.0 million

at June 30, 2017.

At June 30, 2017, we held derivatives designated as cash flow hedges, fair value hedges and certain derivatives not designated as hedges. At December 31, 2016, we held fair value hedges and certain derivatives not designated as hedges.

The Company's derivative instruments are carried at fair value in the Company's financial statements as part of Other Assets for derivatives with positive fair values and Other Liabilities for derivatives with negative fair values. The accounting for changes in the fair value of a derivative instrument is dependent upon whether or not it qualifies and has been designated as a hedge for accounting purposes, and further, by the type of hedging relationship.

At June 30, 2017 and December 31, 2016, derivatives with a combined notional amount of \$36.3 million were not designated as hedges. At June 30, 2017 and December 31, 2016, derivatives with a combined notional amount of \$259.4 million and \$217.1 million were designated as fair value hedges. At June 30, 2017, derivatives with a combined notional amount of \$50.0 million were designated as cash flow hedges. At December 31, 2016, the Company did not have any cash flow hedges.

For cash flow hedges, the effective portion of changes in the fair value of the derivative is reported in AOCL, net of tax, but the ineffective portion of changes in the fair value of the derivative is recognized directly in earnings. Changes in the fair value of interest rate swaps not designated as hedges are reflected in "Net gain/loss from fair value adjustments" in the Consolidated Statements of Income.

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

The following table sets forth information regarding the Company's derivative financial instruments at the periods indicated:

	June 30, 2017		December 31, 2016	
	Notional Amount	Net Carrying Value <sup>(1)</sup>	Notional Amount	Net Carrying Value <sup>(1)</sup>
Interest rate swaps (fair value hedge)	\$174,210	\$5,648	\$182,177	\$6,350
Interest rate swaps (fair value hedge)	85,216	(1,421 )	34,916	(658 )
Interest rate swaps (non-hedge)	36,321	(2,989 )	36,321	(2,728 )
Interest rate swaps (cash flow hedge)	50,000	(214 )	-	-
Total derivatives	\$345,747	\$1,024	\$253,414	\$2,964

<sup>(1)</sup> Derivatives in a net positive position are recorded as "Other assets" and derivatives in a net negative position are recorded as "Other liabilities" in the Consolidated Statements of Financial Condition.

The following table sets forth the effect of derivative instruments on the Consolidated Statements of Income for the periods indicated:

	For the three months ended June 30, 2017		For the six months ended June 30, 2017		2016	
(In thousands)						
Financial Derivatives:						
Interest rate swaps (non-hedge)	\$(493)	\$(1,319)	\$(260)	\$(3,421)		
Interest rate swaps (fair value hedge)	(180)	(375 )	(246)	(415 )		
Net loss <sup>(1)</sup>	\$(673)	\$(1,694)	\$(506)	\$(3,836)		

- (1) Net gains and losses are recorded as part of “Net gain/loss from fair value adjustments” in the Consolidated Statements of Income.

During the three months and six months ended June 30, 2017 and 2016, the Company did not record any hedge ineffectiveness.

The Company’s interest rate swaps are subject to master netting arrangements between the Company and its two designated counterparties. The Company has not made a policy election to offset its derivative positions.

The following tables present the effect of the master netting arrangements on the presentation of the derivative assets and liabilities in the Consolidated Statements of Condition as of the dates indicated:

June 30, 2017				Gross Amounts Not Offset in the Consolidated Statement of Condition		
(In thousands)	Gross Amount of Recognized Assets	Gross Amount Offset in the Statement of Condition	Net Amount of Assets Presented in the Statement of Condition	Financial Instruments	Cash Collateral Received	Net Amount
Interest rate swaps	\$5,648	\$ -	\$ 5,648	\$ -	\$ -	\$ 5,648



**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

(In thousands)	Gross Amount of Recognized Liabilities	Gross Amount Offset in the Statement of Condition	Net Amount of Liabilities Presented in the Statement of Condition	Gross Amounts Not Offset in the Consolidated Statement of Condition		
				Financial Instruments	Cash Collateral Pledged	Net Amount
Interest rate swaps	\$ 4,624	\$ -	\$ 4,624	\$ 2,023	\$ -	\$ 2,601

December 31, 2016

(In thousands)	Gross Amount of Recognized Assets	Gross Amount Offset in the Statement of Condition	Net Amount of Assets Presented in the Statement of Condition	Gross Amounts Not Offset in the Consolidated Statement of Condition		
				Financial Instruments	Cash Collateral Received	Net Amount
Interest rate swaps	\$6,350	\$ -	\$ 6,350	\$ -	\$ 2,964	\$ 3,386

(In thousands)	Gross Amount of Recognized Liabilities	Gross Amount Offset in the Statement of Condition	Net Amount of Liabilities Presented in the Statement of Condition	Gross Amounts Not Offset in the Consolidated Statement of Condition		
				Financial Instruments	Cash Collateral Pledged	Net Amount

Condition

Interest rate swaps	\$ 3,386	\$ -	\$ 3,386	\$ -	\$ -	\$ 3,386
---------------------	----------	------	----------	------	------	----------

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

**12. Income Taxes**

Flushing Financial Corporation files consolidated Federal and combined New York State and New York City income tax returns with its subsidiaries, with the exception of the Company's trusts, which file separate Federal income tax returns as trusts, and Flushing Preferred Funding Corporation, which files a separate Federal income tax return as a real estate investment trust. Additionally, the Bank files New Jersey State tax returns.

Income tax provisions are summarized as follows:

(In thousands)	For the three months ended June 30,		For the six months ended June 30,	
	2017	2016	2017	2016
Federal:				
Current	\$6,653	\$16,228	\$9,605	\$19,888
Deferred	(1,077)	(1,025)	720	62
Total federal tax provision	5,576	15,203	10,325	19,950
State and Local:				
Current	1,618	5,976	1,419	6,361
Deferred	(419)	(462)	285	21
Total state and local tax provision	1,199	5,514	1,704	6,382
Total income tax provision	\$6,775	\$20,717	\$12,029	\$26,332

The effective tax rate was 34.7% and 40.5% for the three months ended June 30, 2017 and 2016, respectively, and 32.5% and 39.7% for the six months ended June 30, 2017 and 2016, respectively. The decrease in the effective tax rate reflects the impact of a change in the treatment of deductible stock compensation expense from prior periods. In prior periods the tax impact of deductible stock compensation expense flowed through additional paid-in-capital and did not have an impact on the Company's effective tax rate, in contrast, in 2017 the impact is passed through the provision for income taxes. Additionally, the effective tax rate for 2016 reflects the reduced impact of preferential tax items, because of the gain on sale on one of our properties in Flushing, Queens recorded during the three months

ended June 30, 2016.

The effective rates differ from the statutory federal income tax rate as follows:

(dollars in thousands)	For the three months ended June 30,		For the six months ended June 30,	
	2017	2016	2017	2016
Taxes at federal statutory rate	\$6,825	35.0%	\$17,903	35.0%
Increase (reduction) in taxes resulting from:				
State and local income tax, net of Federal income tax benefit	780	4.0	3,584	7.0
Other	(830 )	(4.3 )	(770 )	(1.5 )
Taxes at effective rate	\$6,775	34.7%	\$20,717	40.5%

The Company has recorded a deferred tax asset of \$32.4 million at June 30, 2017, which is included in “Other Assets” in the Consolidated Statements of Financial Condition. This represents the anticipated net federal, state and local tax benefits expected to be realized in future years upon the utilization of the underlying tax attributes comprising this balance. The Company has reported taxable income for federal, state, and local tax purposes in each of the past three fiscal years. In management’s opinion, in view of the Company’s previous, current and projected future earnings trend, the probability that some of the Company’s \$16.9 million deferred tax liability can be used to offset a portion of the deferred tax asset, as well as certain tax planning strategies, it is more likely than not that the deferred tax asset will be fully realized. Accordingly, no valuation allowance was deemed necessary for the deferred tax asset at June 30, 2017.

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

**13. Accumulated Other Comprehensive Loss:**

The following table sets forth the changes in accumulated other comprehensive loss by component for the three months ended June 30, 2017:

	Unrealized Gains (Losses) on Available for Sale Securities (In thousands)	Unrealized Gains (Losses) on Cash flow Hedges	Defined Benefit Pension Items	Total
Beginning balance, net of tax	\$(2,711)	\$ -	\$(4,423)	\$(7,134)
Other comprehensive income before reclassifications, net of tax	601	(124 )	-	\$477
Amounts reclassified from accumulated other comprehensive income, net of tax	-	-	81	81
Net current period other comprehensive income, net of tax	601	(124 )	81	558
Ending balance, net of tax	\$(2,110)	\$ (124 )	\$(4,342)	\$(6,576)

The following table sets forth the changes in accumulated other comprehensive loss by component for the three months ended June 30, 2016:

Unrealized  
Gains

Edgar Filing: FLUSHING FINANCIAL CORP - Form 10-Q

	(Losses) on Available Defined for Sale Benefit Securities Pension Items Total (In thousands)		
Beginning balance, net of tax	\$6,249	\$(4,938)	\$1,311
Other comprehensive income before reclassifications, net of tax	3,024	-	\$3,024
Amounts reclassified from accumulated other comprehensive income, net of tax	(1,350)	103	(1,247)
Net current period other comprehensive income, net of tax	1,674	103	1,777
Ending balance, net of tax	\$7,923	\$(4,835)	\$3,088

- 42 -

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

The following table sets forth the changes in accumulated other comprehensive loss by component for the six months ended June 30, 2017:

	Unrealized Gains (Losses) on Available for Sale Securities (In thousands)	Unrealized Gains (Losses) on Cash flow Hedges Pension Items	Defined Benefit Pension Items	Total
Beginning balance, net of tax	\$(3,859)	\$ -	\$(4,503)	\$(8,362)
Other comprehensive income before reclassifications, net of tax	1,749	(124 )	-	\$1,625
Amounts reclassified from accumulated other comprehensive income, net of tax	-	-	161	161
Net current period other comprehensive income, net of tax	1,749	(124 )	161	1,786
Ending balance, net of tax	\$(2,110)	\$ (124 )	\$(4,342)	\$(6,576)

The following table sets forth the changes in accumulated other comprehensive income by component for the six months ended June 30, 2016:

Unrealized Gains (Losses) on Available for Sale Securities	Defined Benefit Pension Items	Total
--	--	-------

Edgar Filing: FLUSHING FINANCIAL CORP - Form 10-Q

	(In thousands)		
Beginning balance, net of tax	\$(521 )	\$(5,041)	\$(5,562)
Other comprehensive income before reclassifications, net of tax	9,794	-	\$9,794
Amounts reclassified from accumulated other comprehensive income, net of tax	(1,350)	206	(1,144)
Net current period other comprehensive income, net of tax	8,444	206	8,650
Ending balance, net of tax	\$7,923	\$(4,835)	\$3,088

- 43 -



**PART I – FINANCIAL INFORMATION**

**FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES**

**Notes to Consolidated Financial Statements**

(Unaudited)

The following tables set forth significant amounts reclassified from accumulated other comprehensive loss by component for the periods indicated:

For the three months ended June 30, 2017

Details about Accumulated Other Comprehensive Loss Components	Amounts Reclassified from Accumulated Other Comprehensive Loss (In thousands)	Affected Line Item in the Statement Where Net Income is Presented
Amortization of defined benefit pension items:		
Actuarial losses	\$ (151 ) (1)	Other operating expense
Prior service credits	11	