LAKELAND FINANCIAL CORP
Form 10-Q
August 07, 2017
UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10 Q

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

For the quarterly period ended June 30, 2017

OR

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

For the transition period from ____________ to _____________

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

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

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

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

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

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

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

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

Smaller reporting company [ ]   Emerging growth company [ ]

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

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

Number of shares of common stock outstanding at July 31, 2017: 25,194,903

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ITEM 1. FINANCIAL STATEMENTS

CONSOLIDATED BALANCE SHEETS (in thousands except share data)

	June 30, 2017 (Unaudited)	December 31, 2016
ASSETS		
Cash and due from banks	$111,406	$142,408
Short-term investments	25,930	24,872
Total cash and cash equivalents	137,336	167,280
Securities available for sale (carried at fair value)	530,312	504,191
Real estate mortgage loans held for sale	4,221	5,915
Loans, net of allowance for loan losses of $44,563 and $43,718	3,532,441	3,427,209
Land, premises and equipment, net	56,492	52,092
Bank owned life insurance	74,929	74,006
Federal Reserve and Federal Home Loan Bank stock	11,522	11,522
Accrued interest receivable	12,028	11,687
Goodwill	4,970	4,970
Other assets	28,748	31,153
Total assets	$4,392,999	$4,290,025
LIABILITIES AND STOCKHOLDERS' EQUITY		
LIABILITIES		
Noninterest bearing deposits	$762,965	$819,803
Interest bearing deposits	2,852,974	2,758,109
Total deposits	3,615,939	3,577,912
Short-term borrowings		
Securities sold under agreements to repurchase	60,188	50,045
Other short-term borrowings	215,000	180,000
Total short-term borrowings	275,188	230,045
Long-term borrowings	30	32
Subordinated debentures	30,928	30,928
Accrued interest payable	4,809	5,676
Other liabilities	15,645	18,365
Total liabilities	3,942,539	3,862,958
STOCKHOLDERS' EQUITY		
Common stock: 90,000,000 shares authorized, no par value 25,185,619 shares issued and 25,021,759 outstanding as of June 30, 2017 25,096,087 shares issued and 24,937,865 outstanding as of December 31, 2016	105,744	104,405
Retained earnings	347,427	327,873
Accumulated other comprehensive income/(loss)	369	(2,387)
Treasury stock, at cost (2017 - 163,860 shares, 2016 - 158,222 shares)	(3,169)	(2,913)
Total stockholders' equity	450,371	426,978

Noncontrolling interest	89	89
Total equity	450,460	427,067
Total liabilities and equity	$4,392,999	$4,290,025

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

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

	Three Months Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
NET INTEREST INCOME				
Interest and fees on loans				
Taxable	$36,967	$30,918	$71,414	$60,548
Tax exempt	162	111	312	222
Interest and dividends on securities				
Taxable	2,364	2,297	4,684	4,843
Tax exempt	1,274	947	2,436	1,842
Interest on short-term investments	54	82	102	110
Total interest income	40,821	34,355	78,948	67,565
Interest on deposits	6,243	4,694	11,685	8,889
Interest on borrowings				
Short-term	431	99	741	246
Long-term	328	289	642	575
Total interest expense	7,002	5,082	13,068	9,710
NET INTEREST INCOME	33,819	29,273	65,880	57,855
Provision for loan losses	500	0	700	0
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	33,319	29,273	65,180	57,855
NONINTEREST INCOME				
Wealth advisory fees	1,284	1,133	2,534	2,293
Investment brokerage fees	299	212	620	500
Service charges on deposit accounts	3,253	2,843	6,396	5,623
Loan, insurance and service fees	1,897	1,892	3,790	3,730
Merchant card fee income	570	527	1,108	1,024
Bank owned life insurance income	402	489	873	662
Other income	659	587	1,168	515
Mortgage banking income	378	384	509	711
Net securities gains	49	0	52	52
Total noninterest income	8,791	8,067	17,050	15,110
NONINTEREST EXPENSE				
Salaries and employee benefits	11,065	10,592	22,486	20,197
Net occupancy expense	1,154	1,041	2,274	2,137
Equipment costs	1,156	909	2,231	1,810
Data processing fees and supplies	1,974	2,120	3,990	4,152
Corporate and business development	1,196	763	2,698	1,620
FDIC insurance and other regulatory fees	419	557	853	1,080
Professional fees	801	859	1,755	1,686
Other expense	1,587	1,605	3,113	3,148
Total noninterest expense	19,352	18,446	39,400	35,830

INCOME BEFORE INCOME TAX EXPENSE	22,758	18,894	42,830	37,135
Income tax expense	7,394	6,091	12,952	12,053
NET INCOME	$15,364	$12,803	$29,878	$25,082
BASIC WEIGHTED AVERAGE COMMON SHARES	25,183,186	25,045,251	25,167,799	25,032,502
BASIC EARNINGS PER COMMON SHARE	$0.61	$0.51	$1.19	$1.00
DILUTED WEIGHTED AVERAGE COMMON SHARES	25,619,977	25,395,770	25,618,552	25,370,607
DILUTED EARNINGS PER COMMON SHARE	$0.60	$0.50	$1.17	$0.99

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

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(unaudited - in thousands)

	Three months ended June 30,		Six months ended June 30,	
	2017	2016	2017	2016
Net income	$15,364	$12,803	$29,878	$25,082
Other comprehensive income (loss)				
Change in securities available for sale:				
Unrealized holding gain on securities available for sale arising during the period	3,358	4,155	4,070	11,702
Reclassification adjustment for gains included in net income	(49)	0	(52)	(52)
Net securities gain activity during the period	3,309	4,155	4,018	11,650
Tax effect	(1,079)	(1,385)	(1,343)	(3,691)
Net of tax amount	2,230	2,770	2,675	7,959
Defined benefit pension plans:				
Amortization of net actuarial loss	67	54	133	108
Tax effect	(26)	(21)	(52)	(43)
Net of tax amount	41	33	81	65
Total other comprehensive income, net of tax	2,271	2,803	2,756	8,024
Comprehensive income	$17,635	$15,606	$32,634	$33,106

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

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

	Common Stock Shares	Common Stock Stock	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Treasury Stock	Total Stockholders' Equity
Balance at January 1, 2016	24,819,066	$99,123	$294,002	$2,142	$(2,455)	$392,812
Comprehensive income:						
Net income			25,082			25,082
Other comprehensive income (loss), net of tax				8,024		8,024
Cash dividends declared, $0.35 per share			(8,767)			(8,767)
Treasury shares purchased under deferred directors' plan	(7,613)	226			(226)	0
Stock activity under equity compensation plans	82,775	(143)				(143)
Stock based compensation expense		1,796				1,796
Balance at June 30, 2016	24,894,228	$101,002	$310,317	$10,166	$(2,681)	$418,804
Balance at January 1, 2017	24,937,865	$104,405	$327,873	$(2,387)	$(2,913)	$426,978
Comprehensive income:						
Net income			29,878			29,878
Other comprehensive income (loss), net of tax				2,756		2,756
Cash dividends declared, $0.41 per share			(10,324)			(10,324)
Treasury shares purchased under deferred directors' plan	(5,638)	256			(256)	0
Stock activity under equity compensation plans	89,532	(1,736)				(1,736)
Stock based compensation expense		2,819				2,819
Balance at June 30, 2017	25,021,759	$105,744	$347,427	$369	$(3,169)	$450,371

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

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CONSOLIDATED STATEMENTS OF CASH FLOWS (unaudited - in thousands)

Six Months Ended June 30	2017	2016
Cash flows from operating activities:		
Net income	$29,878	$25,082
Adjustments to reconcile net income to net cash from operating activities:		
Depreciation	2,412	2,009
Provision for loan losses	700	0
Net (gain) loss on sale and write down of other real estate owned	(5)	2
Amortization of loan servicing rights	307	296
Loans originated for sale	(40,622)	(27,572)
Net gain on sales of loans	(859)	(814)
Proceeds from sale of loans	42,773	27,391
Net (gain) loss on sales of premises and equipment	(5)	10
Net gain on sales and calls of securities available for sale	(52)	(52)
Net securities amortization	1,407	1,420
Stock based compensation expense	2,819	1,796
Earnings on life insurance	(873)	(662)
Tax benefit of stock option exercises	(932)	(482)
Net change:		
Interest receivable and other assets	1,784	(2,259)
Interest payable and other liabilities	(2,804)	8,613
Total adjustments	6,050	9,696
Net cash from operating activities	35,928	34,778
Cash flows from investing activities:		
Proceeds from sale of securities available for sale	35,845	6,929
Proceeds from maturities, calls and principal paydowns of securities available for sale	30,837	35,591
Purchases of securities available for sale	(90,140)	(53,766)
Purchase of life insurance	(490)	(338)
Net increase in total loans	(106,011)	(117,495)
Proceeds from sales of land, premises and equipment	7	6
Purchases of land, premises and equipment	(6,814)	(4,485)
Purchases of Federal Home Loan Bank Stock	0	(704)
Proceeds from sales of other real estate	42	31
Net cash from investing activities	(136,724)	(134,231)

Cash flows from financing activities:		
Net increase in total deposits	38,027	220,034
Net increase (decrease) in short-term borrowings	45,143	(83,254)
Payments on long-term borrowings	(2)	(2)
Common dividends paid	(10,311)	(8,754)
Preferred dividends paid	(13)	(13)
Payments related to equity incentive plans	(1,736)	(143)
Purchase of treasury stock	(256)	(226)
Net cash from financing activities	70,852	127,642
Net change in cash and cash equivalents	(29,944)	28,189
Cash and cash equivalents at beginning of the period	167,280	80,674
Cash and cash equivalents at end of the period	$137,336	$108,863
Cash paid during the period for:		
Interest	$13,936	$9,080
Income taxes	11,513	8,750
Supplemental non-cash disclosures:		
Loans transferred to other real estate owned	79	64
Securities purchases payable	0	3,885

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

NOTE 1. BASIS OF PRESENTATION

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

The unaudited consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles ("GAAP") for interim financial information and with the instructions for Form 10-Q. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements and are unaudited. In the opinion of management, all adjustments (all of which are normal and recurring in nature) considered necessary for a fair presentation have been included. Operating results for the three-month and six-month periods ended June 30, 2017 are not necessarily indicative of the results that may be expected for any subsequent reporting periods, including the year ending December 31, 2017. The Company's 2016 Annual Report on Form 10-K should be read in conjunction with these statements.

NOTE 2. SECURITIES

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

(dollars in thousands)	Amortized Cost	Gross Unrealized Gain	Gross Unrealized Losses	Fair Value
June 30, 2017				
U.S. Treasury securities	$990	$18	$0	$1,008
U.S. government sponsored agencies	5,895	13	(62)	5,846
Agency residential mortgage-backed securities	355,055	3,779	(1,930)	356,904
State and municipal securities	165,489	2,869	(1,804)	166,554
Total	$527,429	$6,679	$(3,796)	$530,312
December 31, 2016				
U.S. Treasury securities	$990	$13	$0	$1,003
U.S. government sponsored agencies	6,312	10	(81)	6,241
Agency residential mortgage-backed securities	351,108	3,604	(3,144)	351,568
State and municipal securities	146,917	1,784	(3,322)	145,379
Total	$505,327	$5,411	$(6,547)	$504,191

Information regarding the fair value and amortized cost of available for sale debt securities by maturity as of June 30, 2017 is presented below. Maturity information is based on contractual maturity for all securities other than mortgage-backed securities. Actual maturities of securities may differ from contractual maturities because borrowers may have the right to prepay the obligation without a prepayment penalty.

(dollars in thousands)	Amortized Cost	Fair Value
Due in one year or less	$2,293	$2,320
Due after one year through five years	23,660	24,214
Due after five years through ten years	43,811	45,005
Due after ten years	102,610	101,869
	172,374	173,408
Mortgage-backed securities	355,055	356,904
Total debt securities	$527,429	$530,312

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

(dollars in thousands)	Three months ended June 30, 2017	2016	Six months ended June 30, 2017	2016
Sales of securities available for sale				
Proceeds	$19,034	$0	$35,845	$6,929
Gross gains	59	0	256	65
Gross losses	(10)	0	(204)	(13)

The Company sold eight securities with a total book value of $19.0 million and a total fair value of $19.0 million during the second quarter of 2017. The Company sold 35 securities with a total book value of $35.8 million and a total fair value of $35.8 million during the first six months of 2017. The Company sold four securities with a total book value of $6.9 million and a total fair value of $7.0 million during the first six months of 2016.

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

Securities with carrying values of $156.7 million and $168.3 million were pledged as of June 30, 2017 and December 31, 2016, respectively, as collateral for securities sold under agreements to repurchase, borrowings from the Federal Home Loan Bank and for other purposes as permitted or required by law.

Information regarding securities with unrealized losses as of June 30, 2017 and December 31, 2016 is presented below. The tables divide the securities between those with unrealized losses for less than twelve months and those with unrealized losses for twelve months or more.

	Less than 12 months		12 months or more		Total	
(dollars in thousands)	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
June 30, 2017						
U.S. government sponsored agencies	$3,054	$62	$0	$0	$3,054	$62
Agency residential mortgage-backed securities	131,542	1,576	10,254	354	141,796	1,930
State and municipal securities	57,041	1,582	4,456	222	61,497	1,804
Total temporarily impaired	$191,637	$3,220	$14,710	$576	$206,347	$3,796

December 31, 2016						
U.S. government sponsored agencies	$3,290	$81	$0	$0	$3,290	$81
Agency residential mortgage-backed securities	181,699	2,882	7,080	262	188,779	3,144
State and municipal securities	77,434	3,180	2,361	142	79,795	3,322
Total temporarily impaired	$262,423	$6,143	$9,441	$404	$271,864	$6,547

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The total number of securities with unrealized losses as of June 30, 2017 and December 31, 2016 is presented below.

	Less than 12 months	12 months or more	Total
June 30, 2017			
U.S. government sponsored agencies	1	0	1
Agency residential mortgage-backed securities	38	3	41
State and municipal securities	74	6	80
Total temporarily impaired	113	9	122
December 31, 2016			
U.S. government sponsored agencies	1	0	1
Agency residential mortgage-backed securities	59	2	61
State and municipal securities	121	4	125
Total temporarily impaired	181	6	187

The following factors are considered in determining whether or not the impairment of these securities is other-than-temporary. In making this determination, management considers the extent and duration of the unrealized loss, and the financial condition and near-term prospects of the issuer, as well as the underlying fundamentals of the relevant market and the outlook for such market in the near future. Management also assesses whether it intends to sell, or it is more likely than not that it will be required to sell, a security in an unrealized loss position before recovery of its amortized cost basis. If either of the criteria regarding intent or requirement to sell is met, the entire difference between amortized cost and fair value is recognized as impairment through earnings. For debt securities that do not meet the aforementioned criteria, the amount of impairment is split into two components as follows: 1) OTTI related to credit loss, which must be recognized in the income statement and 2) OTTI related to other factors, which is recognized in other comprehensive income. Credit loss is defined as the difference between the present value of the cash flows expected to be collected and the amortized cost basis. For equity securities, the entire amount of impairment is recognized through earnings. As of June 30, 2017 and December 31, 2016, ninety-nine percent of the securities in the Company's portfolio were backed by the U.S. government, government agencies, government sponsored agencies or were A-rated or better, except for certain non-local or local municipal securities, which are not rated. For the government, government-sponsored agency and municipal securities, management did not believe that there would be credit losses or that full principal would not be received. Management considered the unrealized losses on these securities to be primarily interest rate driven and does not expect material losses given current market conditions unless the securities are sold. However, at this time management does not have the intent to sell, and it is more likely than not that the Company will not be required to sell these securities before the recovery of their amortized cost basis.

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NOTE 3. LOANS

(dollars in thousands)	June 30, 2017			December 31, 2016		
Commercial and industrial loans:						
Working capital lines of credit loans	$717,875	20.0	%	$624,404	18.0	%
Non-working capital loans	646,517	18.1		644,086	18.5	
Total commercial and industrial loans	1,364,392	38.1		1,268,490	36.5	
Commercial real estate and multi-family residential loans:						
Construction and land development loans	209,772	5.8		245,182	7.1	
Owner occupied loans	511,425	14.3		469,705	13.5	
Nonowner occupied loans	450,907	12.6		458,404	13.2	
Multifamily loans	170,902	4.8		127,632	3.7	
Total commercial real estate and multi-family residential loans	1,343,006	37.5		1,300,923	37.5	
Agri-business and agricultural loans:						
Loans secured by farmland	156,053	4.4		172,633	5.0	
Loans for agricultural production	175,334	4.9		222,210	6.4	
Total agri-business and agricultural loans	331,387	9.3		394,843	11.4	
Other commercial loans	116,651	3.3		98,270	2.8	
Total commercial loans	3,155,436	88.2		3,062,526	88.2	
Consumer 1-4 family mortgage loans:						
Closed end first mortgage loans	171,495	4.8		163,155	4.7	
Open end and junior lien loans	172,530	4.8		169,664	4.9	
Residential construction and land development loans	10,118	0.3		15,015	0.4	
Total consumer 1-4 family mortgage loans	354,143	9.9		347,834	10.0	
Other consumer loans	68,646	1.9		61,308	1.8	
Total consumer loans	422,789	11.8		409,142	11.8	
Subtotal	3,578,225	100.0	%	3,471,668	100.0	%
Less: Allowance for loan losses	(44,563)			(43,718)		
Net deferred loan fees	(1,221)			(741)		
Loans, net	$3,532,441			$3,427,209		

The recorded investment in loans does not include accrued interest.

The Company had $184,000 in residential real estate loans in the process of foreclosure as of June 30, 2017, compared to $241,000 as of December 31, 2016.

NOTE 4. ALLOWANCE FOR LOAN LOSSES AND CREDIT QUALITY

The following tables present the activity in the allowance for loan losses by portfolio segment for the three-month periods ended June 30, 2017 and 2016:

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

(dollars in thousands)	Commercial and Industrial	Real Estate and Multifamily Residential	Agri-business and Agricultural	Other Commercial	Consumer 1-4 Family Mortgage	Other Consumer	Unallocated	Total
Three Months Ended June 30, 2016								
Beginning balance, April 1	$20,465	$12,752	$2,454	$559	$3,586	$344	$3,124	$43,284
Provision for loan losses	605	(315)	589	(194)	(563)	6	(128)	0
Loans charged-off	(160)	0	0	0	(92)	(45)	0	(297)
Recoveries	25	200	4	0	3	28	0	260
Net (charge-offs)/recoveries	(135)	200	4	0	(89)	(17)	0	(37)
Ending balance	$20,935	$12,637	$3,047	$365	$2,934	$333	$2,996	$43,247

The following tables present the activity in the allowance for loan losses by portfolio segment for the six-month periods ended June 30, 2017 and 2016:

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

(dollars in thousands)	Commercial and Industrial	Commercial Real Estate and Multifamily Residential	Agri-business and Agricultural	Other Commercial	Consumer 1-4 Family Mortgage	Other Consumer	Unallocated	Total
Six Months Ended June 30, 2016								
Beginning balance, January 1	$21,564	$12,473	$2,445	$574	$3,395	$319	$2,840	$43,610
Provision for loan losses	(342)	121	593	(209)	(367)	48	156	0
Loans charged-off	(374)	(168)	0	0	(130)	(90)	0	(762)
Recoveries	87	211	9	0	36	56	0	399
Net (charge-offs)/recoveries	(287)	43	9	0	(94)	(34)	0	(363)
Ending balance	$20,935	$12,637	$3,047	$365	$2,934	$333	$2,996	$43,247

The following tables present the balance in the allowance for loan losses and the recorded investment in loans by portfolio segment and based on impairment method as of June 30, 2017 and December 31, 2016:

(dollars in thousands)	Commercial and Industrial	Commercial Real Estate and Multifamily Residential	Agri-business and Agricultural	Other Commercial	Consumer 1-4 Family Mortgage	Other Consumer	Unallocated	Total
June 30, 2017								
Allowance for loan losses:								
Ending allowance balance attributable to loans:								
Individually evaluated for impairment	$3,734	$561	$0	$0	$286	$44	$0	$4,625
Collectively evaluated for impairment	16,485	13,214	3,870	568	2,403	345	3,053	39,938
Total ending allowance balance	$20,219	$13,775	$3,870	$568	$2,689	$389	$3,053	$44,563
Loans:								
Loans individually evaluated for impairment	$11,192	$6,661	$283	$0	$1,391	$53	$0	$19,580
Loans collectively evaluated for impairment	1,353,075	1,334,473	331,173	116,493	353,809	68,401	0	3,557,424
Total ending loans balance	$1,364,267	$1,341,134	$331,456	$116,493	$355,200	$68,454	$0	$3,577,004

	Commercial and Industrial	Commercial Real Estate and Multi-family Residential	Agri-business and Agricultural	Other Commercial	Consumer 1-4 Family Mortgage	Other Consumer	Unallocated	Total

(dollars in thousands)								
December 31, 2016								
Allowance for loan losses:								
Ending allowance balance attributable to loans:								
Individually evaluated for impairment	$3,191	$576	$0	$0	$296	$51	$0	$4,114
Collectively evaluated for impairment	17,081	12,876	3,532	461	2,531	336	2,787	39,604
Total ending allowance balance	$20,272	$13,452	$3,532	$461	$2,827	$387	$2,787	$43,718
Loans:								
Loans individually evaluated for impairment	$9,776	$9,151	$283	$0	$1,427	$55	$0	$20,692
Loans collectively evaluated for impairment	1,258,682	1,290,131	394,621	98,265	347,408	61,128	0	3,450,235
Total ending loans balance	$1,268,458	$1,299,282	$394,904	$98,265	$348,835	$61,183	$0	$3,470,927

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The following table presents loans individually evaluated for impairment by class of loans as of June 30, 2017:

(dollars in thousands)	Unpaid Principal Balance	Recorded Investment	Allowance for Loan Losses Allocated
With no related allowance recorded:			
Commercial and industrial loans:			
Working capital lines of credit loans	$515	$515	$0
Non-working capital loans	3,052	1,303	0
Commercial real estate and multi-family residential loans:			
Construction and land development loans	126	126	0
Owner occupied loans	2,515	2,267	0
Nonowner occupied loans	2,797	2,797	0
Agri-business and agricultural loans:			
Loans secured by farmland	603	283	0
Consumer 1-4 family loans:			
Closed end first mortgage loans	341	260	0
Open end and junior lien loans	366	154	0
With an allowance recorded:			
Commercial and industrial loans:			
Working capital lines of credit loans	2,839	2,536	1,212
Non-working capital loans	6,839	6,838	2,522
Commercial real estate and multi-family residential loans:			
Owner occupied loans	1,472	1,471	561
Consumer 1-4 family mortgage loans:			
Closed end first mortgage loans	976	977	286
Other consumer loans	53	53	44
Total	$22,494	$19,580	$4,625

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The following table presents loans individually evaluated for impairment by class of loans as of December 31, 2016:

(dollars in thousands)	Unpaid Principal Balance	Recorded Investment	Allowance for Loan Losses Allocated
With no related allowance recorded:			
Commercial and industrial loans:			
Working capital lines of credit loans	$951	$494	$0
Non-working capital loans	3,007	1,358	0
Commercial real estate and multi-family residential loans:			
Construction and land development loans	126	126	0
Owner occupied loans	2,868	2,620	0
Nonowner occupied loans	4,632	4,633	0
Agri-business and agricultural loans:			
Loans secured by farmland	603	283	0
Consumer 1-4 family loans:			
Closed end first mortgage loans	161	147	0
Open end and junior lien loans	408	195	0
With an allowance recorded:			
Commercial and industrial loans:			
Working capital lines of credit loans	1,100	1,099	465
Non-working capital loans	6,827	6,825	2,726
Commercial real estate and multi-family residential loans:			
Owner occupied loans	1,773	1,772	576
Consumer 1-4 family mortgage loans:			
Closed end first mortgage loans	1,152	1,085	296
Other consumer loans	55	55	51
Total	$23,663	$20,692	$4,114

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

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

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The following table presents loans individually evaluated for impairment by class of loans as of and for the three-month period ended June 30, 2016:

(dollars in thousands)	Average Recorded Investment	Interest Income Recognized	Cash Basis Interest Income Recognized
With no related allowance recorded:			
Commercial and industrial loans:			
Working capital lines of credit loans	$493	$0	$0
Non-working capital loans	557	0	0
Commercial real estate and multi-family residential loans:			
Owner occupied loans	2,536	0	0
Nonowner occupied loans	4,783	88	89
Agri-business and agricultural loans:			
Loans secured by farmland	471	0	0
Loans for ag production	2,032	5	4
Consumer 1-4 family loans:			
Closed end first mortgage loans	149	0	0
With an allowance recorded:			
Commercial and industrial loans:			
Working capital lines of credit loans	841	5	5
Non-working capital loans	4,077	33	34
Commercial real estate and multi-family residential loans:			
Construction and land development loans	297	4	2
Owner occupied loans	975	0	0
Multifamily loans	383	5	5
Agri-business and agricultural loans:			
Other commercial loans	12	2	0
Consumer 1-4 family mortgage loans:			
Closed end first mortgage loans	1,363	10	14
Open end and junior lien loans	165	0	0
Other consumer loans	58	1	1
Total	$19,192	$153	$154

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

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

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The following table presents loans individually evaluated for impairment by class of loans as of and for the six-month period ended June 30, 2016:

(dollars in thousands)	Average Recorded Investment	Interest Income Recognized	Cash Basis Interest Income Recognized
With no related allowance recorded:			
Commercial and industrial loans:			
Working capital lines of credit loans	$256	$0	$0
Non-working capital loans	615	0	0
Commercial real estate and multi-family residential loans:			
Owner occupied loans	2,630	0	0
Nonowner occupied loans	4,796	117	112
Agri-business and agricultural loans:			
Loans secured by farmland	471	0	0
Loans for ag production	1,016	5	4
Consumer 1-4 family loans:			
Closed end first mortgage loans	98	0	0
With an allowance recorded:			
Commercial and industrial loans:			
Working capital lines of credit loans	1,097	10	10
Non-working capital loans	4,356	67	68
Commercial real estate and multi-family residential loans:			
Construction and land development loans	318	7	5
Owner occupied loans	959	0	0
Nonowner occupied loans	38	0	0
Multifamily loans	384	10	10
Agri-business and agricultural loans:			
Other commercial loans	12	2	0
Consumer 1-4 family mortgage loans:			
Closed end first mortgage loans	1,495	25	25
Open end and junior lien loans	208	0	0
Other consumer loans	58	2	2
Total	$18,807	$245	$236

The following table presents the ageing of the recorded investment in past due loans as of June 30, 2017 by class of loans:

(dollars in thousands)	Loans Not Past Due	30-89 Days Past Due	Greater than 90 Days Past Due	Nonaccrual	Total Past Due	Total
Commercial and industrial loans:						
Working capital lines of credit loans	$716,236	$0	$0	$1,614	$1,614	$717,850
Non-working capital loans	642,356	1	0	4,060	4,061	646,417
Commercial real estate and multi-family residential loans:						
Construction and land development loans	208,881	0	0	0	0	208,881
Owner occupied loans	507,600	48	0	3,471	3,519	511,119
Nonowner occupied loans	450,427	0	0	106	106	450,533
Multifamily loans	170,601	0	0	0	0	170,601
Agri-business and agricultural loans:						
Loans secured by farmland	155,745	30	0	283	313	156,058
Loans for agricultural production	175,398	0	0	0	0	175,398
Other commercial loans	116,493	0	0	0	0	116,493
Consumer 1-4 family mortgage loans:						
Closed end first mortgage loans	169,758	1,198	0	196	1,394	171,152
Open end and junior lien loans	173,646	156	0	154	310	173,956
Residential construction loans	10,092	0	0	0	0	10,092
Other consumer loans	68,325	129	0	0	129	68,454
Total	$3,565,558	$1,562	$0	$9,884	$11,446	$3,577,004

The following table presents the ageing of the recorded investment in past due loans as of December 31, 2016 by class of loans:

(dollars in thousands)	Loans Not Past Due	30-89 Days Past Due	Greater than 90 Days Past Due	Nonaccrual	Total Past Due	Total
Commercial and industrial loans:						
Working capital lines of credit loans	$624,213	$9	$0	$140	$149	$624,362
Non-working capital loans	642,014	0	0	2,082	2,082	644,096
Commercial real estate and multi-family residential loans:						
Construction and land development loans	244,411	0	0	0	0	244,411
Owner occupied loans	465,789	0	0	3,598	3,598	469,387

Nonowner occupied loans	457,880	0	0	122	122	458,002
Multi-family loans	127,482	0	0	0	0	127,482
Agri-business and agricultural loans:						
Loans secured by farmland	172,349	0	0	283	283	172,632
Loans for agricultural production	222,272	0	0	0	0	222,272
Other commercial loans	98,265	0	0	0	0	98,265
Consumer 1-4 family mortgage loans:						
Closed end first mortgage loans	161,499	1,072	53	213	1,338	162,837
Open end and junior lien loans	170,372	448	0	195	643	171,015
Residential construction loans	14,983	0	0	0	0	14,983
Other consumer loans	61,119	64	0	0	64	61,183
Total	$3,462,648	$1,593	$53	$6,633	$8,279	$3,470,927

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Troubled Debt Restructurings:

Troubled debt restructured loans are included in the totals for impaired loans. The Company has allocated $2.9 million and $2.7 million of specific reserves to customers whose loan terms have been modified in troubled debt restructurings as of June 30, 2017 and December 31, 2016. The Company is not committed to lend additional funds to debtors whose loans have been modified in a troubled debt restructuring.

	June 30	December 31
(dollars in thousands)	2017	2016
Accruing troubled debt restructured loans	$8,425	$10,351
Nonaccrual troubled debt restructured loans	6,852	5,633
Total troubled debt restructured loans	$15,277	$15,984

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

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

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

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

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

For the three-month period ended June 30, 2017, the commercial and industrial troubled debt restructurings described above increased the allowance for loan losses by $8,000 and the commercial real estate and multi-family residential loan troubled debt restructuring described above decreased the allowance for loan losses by $5,000. For the six-month period ended June 30, 2017, the commercial and industrial troubled debt restructurings described above increased the allowance for loan losses by $42,000 and the commercial real estate and multi-family residential loan troubled debt restructuring described above increased the allowance for loan losses by $44,000.

No charge-offs resulted from any troubled debt restructurings described above during the three- or six-month periods ended June 30, 2017.

During the three months ended June 30, 2016, certain loans were modified as troubled debt restructurings. The modified terms of these loans include one or a combination of the following: inadequate compensation for the terms of the restructure or renewal; a modification of the repayment terms which delays principal repayment for some period; or renewal terms offered to borrowers in financial distress where no additional credit enhancements were obtained at the time of renewal.

During the three months ended June 30, 2016, there were renewal terms, which are considered additional concessions, offered to three borrowers under financial duress with previously identified troubled debt restructured loans which did not require additional compensation or consideration, and the terms offered would not have been readily available in the marketplace for loans bearing a similar risk profile. In these instances, it was determined that a concession had been granted. The loan to one of the borrowers was for a commercial real estate building where the collateral value and cash flows from the company occupying the building does not support the loan with a recorded investment of $374,000. The loans to the other two borrowers are for commercial and industrial non-working capital loans with recorded investments of $574,000. These concessions are not included in the table below.

Additional concessions were granted to borrowers with previously identified troubled debt restructured loans during the three-months ended March 31, 2016. The loans to two of the borrowers are for commercial real estate buildings where the collateral value and cash flows from the companies occupying the buildings do not support the loans with recorded investments of $542,000. The other loans were to a borrower engaged in land development, where the aggregate recorded investment totaled $484,000. These concessions are not included in table below.

The following table presents loans by class modified as new troubled debt restructurings that occurred during the three months ended June 30, 2016:

				Modified Repayment Terms	
(dollars in thousands)	Number of Loans	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment	Number of Loans	Extension Period or Range (in months)
Troubled Debt Restructurings					
Commercial and industrial loans:					
Non-working capital loans	3	$775	$775	3	9-15
Commercial real estate and multi-family residential loans:					
Owner occupied loans	1	305	305	1	13
Total	4	$1,080	$1,080	4	9-15

The following table presents loans by class modified as new troubled debt restructurings that occurred during the six months ended June 30, 2016:

				Modified Repayment Terms	
(dollars in thousands)	Number of Loans	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment	Number of Loans	Extension Period or Range (in months)
Troubled Debt Restructurings					
Commercial and industrial loans:					

Non-working capital loans	3	$775	$775	3	9-15
Commercial real estate and multi-family residential loans:					
Owner occupied loans	2	640	640	2	13-15
Total	5	$1,415	$1,415	5	9-15

For the three months ended June 30, 2016, the commercial and industrial troubled debt restructurings described above increased the allowance for loan losses by $182,000 and the commercial real estate and multi-family residential loan troubled debt restructuring described above decreased the allowance for loan losses by $145,000. For the six months ended June 30, 2016, the commercial and industrial troubled debt restructurings described above increased the allowance for loan losses by $684,000 and the commercial real estate and multi-family residential loan troubled debt restructuring described above increased the allowance for loan losses by $15,000.

No charge-offs resulted from any troubled debt restructurings described above during the three- or six-month periods ended June 30, 2016.

There were no troubled debt restructurings that had payment defaults within the twelve months following modification during the three- or six-month periods ended June 30, 2017 and 2016.

Credit Quality Indicators:

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

The Company uses the following definitions for risk ratings:

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

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

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

Loans not meeting the criteria above that are analyzed individually as part of the above-described process are considered to be Pass rated loans with the exception of consumer troubled debt restructurings which are evaluated and listed with Substandard commercial grade loans and consumer nonaccrual loans which are evaluated individually and listed with Not Rated loans. Loans listed as Not Rated are consumer loans or commercial loans with consumer characteristics included in groups of homogenous loans which are analyzed for credit quality indicators utilizing delinquency status. As of June 30, 2017, and based on the most recent analysis performed, the risk category of loans by class of loans is as follows:

(dollars in thousands)	Pass	Special Mention	Substandard	Doubtful	Not Rated	Total
Commercial and industrial loans:						
Working capital lines of credit loans	$660,503	$30,547	$26,602	$0	$198	$717,850
Non-working capital loans	596,679	23,539	22,546	0	3,653	646,417
Commercial real estate and multi-family residential loans:						
Construction and land development loans	207,566	1,315	0	0	0	208,881
Owner occupied loans	483,925	14,384	12,810	0	0	511,119
Nonowner occupied loans	445,235	4,475	823	0	0	450,533
Multifamily loans	170,349	252	0	0	0	170,601
Agri-business and agricultural loans:						
Loans secured by farmland	146,607	7,051	2,400	0	0	156,058

Loans for agricultural production	170,484	4,209	705	0	0	175,398
Other commercial loans	116,489	0	0	0	4	116,493
Consumer 1-4 family mortgage loans:						
Closed end first mortgage loans	45,974	0	1,237	0	123,941	171,152
Open end and junior lien loans	7,275	0	0	0	166,681	173,956
Residential construction loans	0	0	0	0	10,092	10,092
Other consumer loans	19,612	0	53	0	48,789	68,454
Total	$3,070,698	$85,772	$67,176	$0	$353,358	$3,577,004

As of December 31, 2016, and based on the most recent analysis performed, the risk category of loans by class of loans is as follows:

(dollars in thousands)	Pass	Special Mention	Substandard	Doubtful	Not Rated	Total
Commercial and industrial loans:						
Working capital lines of credit loans	$577,208	$17,636	$29,396	$0	$122	$624,362
Non-working capital loans	583,135	32,587	24,405	0	3,969	644,096
Commercial real estate and multi-family residential loans:						
Construction and land development loans	242,964	1,447	0	0	0	244,411
Owner occupied loans	444,143	10,285	14,959	0	0	469,387
Nonowner occupied loans	451,390	4,550	2,062	0	0	458,002
Multi-family loans	127,219	263	0	0	0	127,482
Agri-business and agricultural loans:						
Loans secured by farmland	168,660	3,689	283	0	0	172,632
Loans for agricultural production	218,581	3,691	0	0	0	222,272
Other commercial loans	98,261	0	0	0	4	98,265
Consumer 1-4 family mortgage loans:						
Closed end first mortgage loans	44,687	126	1,232	0	116,792	162,837
Open end and junior lien loans	7,028	0	0	0	163,987	171,015
Residential construction loans	0	0	0	0	14,983	14,983
Other consumer loans	17,717	0	55	0	43,411	61,183
Total	$2,980,993	$74,274	$72,392	$0	$343,268	$3,470,927

NOTE 5. FAIR VALUE DISCLOSURES

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

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

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

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

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

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

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

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

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

Mortgage servicing rights: As of June 30, 2017, the fair value of the Company's Level 3 servicing assets for residential mortgage loans was $3.9 million, none of which are currently impaired and therefore are carried at amortized cost. These residential mortgage loans have a weighted average interest rate of 3.82%, a weighted average maturity of 19 years and are secured by homes generally within the Company's market area, which is primarily Northern Indiana. A valuation model is used to estimate fair value by stratifying the portfolios on the basis of certain risk characteristics, including loan type and interest rate. Impairment is estimated based on an income approach. The inputs used include estimates of prepayment speeds, discount rate, cost to service, escrow account earnings, contractual servicing fee income, ancillary income, late fees, and float income. The most significant assumption used to value mortgage servicing rights is prepayment rate. Prepayment rates are estimated based on published industry consensus prepayment rates. The most significant unobservable assumption is the discount rate. At June 30, 2017, the constant prepayment speed (PSA) used was 148 and the discount rate used was 9.4%. At December 31, 2016, the PSA used was 162 and the discount rate used was 9.3%.

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

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

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

	June 30, 2017			
	Fair Value Measurements Using			Assets
(dollars in thousands)	Level 1	Level 2	Level 3	at Fair Value
Assets				
U.S. Treasury securities	$ 1,008	$ 0	$ 0	$ 1,008
U.S. government sponsored agency securities	0	5,846	0	5,846
Mortgage-backed securities	0	356,904	0	356,904
State and municipal securities	0	165,935	619	166,554
Total Securities	1,008	528,685	619	530,312
Mortgage banking derivative	0	264	0	264
Interest rate swap derivative	0	2,693	0	2,693
Total assets	$ 1,008	$ 531,642	$ 619	$ 533,269
Liabilities				
Mortgage banking derivative	0	7	0	7
Interest rate swap derivative	0	2,840	0	2,840
Total liabilities	$ 0	$ 2,847	$ 0	$ 2,847

	December 31, 2016			
	Fair Value Measurements Using			Assets
(dollars in thousands)	Level 1	Level 2	Level 3	at Fair Value
Assets				
U.S. Treasury securities	$ 1,003	$ 0	$ 0	$ 1,003
U.S. government sponsored agency securities	0	6,241	0	6,241
Mortgage-backed securities	0	351,568	0	351,568
State and municipal securities	0	144,709	670	145,379
Total Securities	1,003	502,518	670	504,191
Mortgage banking derivative	0	314	0	314
Interest rate swap derivative	0	2,645	0	2,645
Total assets	$ 1,003	$ 505,477	$ 670	$ 507,150
Liabilities				
Mortgage banking derivative	0	14	0	14
Interest rate swap derivative	0	2,735	0	2,735
Total liabilities	$ 0	$ 2,749	$ 0	$ 2,749

There were no transfers between Level 1 and Level 2 during the six months ended June 30, 2017 and there were no transfers between Level 1 and Level 2 during 2016.

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The table below presents a reconciliation of all assets measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the six months ended June 30, 2017 and 2016:

	State and Municipal Securities	
(dollars in thousands)	2017	2016
Balance of recurring Level 3 assets at January 1	$ 670	$ 551
Transfers into Level 3	0	339
Changes in fair value of securities included in other comprehensive income	(6)	6
Principal payments	(45)	(40)
Balance of recurring Level 3 assets at June 30	$ 619	$ 856

The fair values of two municipal securities with a fair value of $339,000 as of March 31, 2016 were transferred from Level 2 and into Level 3 because of a lack of observable market data for these investments. The Company's policy is to recognize transfers as of the end of the reporting period. As a result the fair value for these municipal securities was transferred on March 31, 2016. The municipal securities measured at fair value included below are non-rated Indiana and Ohio municipal revenue bonds and are not actively traded.

Quantitative Information about Level 3 Fair Value Measurements

(dollars in thousands)	Fair Value at June 30, 2017	Valuation Technique	Unobservable Input	Range of Inputs (Average)
State and municipal securities	$ 619	Price to type, par, call	Discount to benchmark index	0-5% (2.01%)

Quantitative Information about Level 3 Fair Value Measurements

(dollars in thousands)	Fair Value at December 31, 2016	Valuation Technique	Unobservable Input	Range of Inputs (Average)
State and municipal securities	$ 670	Price to type, par, call	Discount to benchmark index	0-5% (2.98%)

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

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

	June 30, 2017			
	Fair Value Measurements Using			Assets
(dollars in thousands)	Level 1	Level 2	Level 3	at Fair Value
Assets				
Impaired loans:				
Commercial and industrial loans:				
Working capital lines of credit loans	$ 0	$ 0	$ 1,341	$ 1,341
Non-working capital loans	0	0	4,013	4,013
Commercial real estate and multi-family residential loans:				
Owner occupied loans	0	0	910	910
Total impaired loans	$ 0	$ 0	$ 6,264	$ 6,264
Other real estate owned	0	0	75	75
Total assets	$ 0	$ 0	$ 6,339	$ 6,339

	December 31, 2016			
	Fair Value Measurements Using			Assets
(dollars in thousands)	Level 1	Level 2	Level 3	at Fair Value
Assets				
Impaired loans:				
Commercial and industrial loans:				
Working capital lines of credit loans	$ 0	$ 0	$ 621	$ 621
Non-working capital loans	0	0	3,889	3,889
Commercial real estate and multi-family residential loans:				
Owner occupied loans	0	0	1,195	1,195
Consumer 1-4 family mortgage loans:				
Closed end first mortgage loans	0	0	62	62
Total impaired loans	$ 0	$ 0	$ 5,767	$ 5,767
Other real estate owned	0	0	75	75
Total assets	$ 0	$ 0	$ 5,842	$ 5,842

The following table presents the valuation methodology and unobservable inputs for Level 3 assets measured at fair value on a non-recurring basis at June 30, 2017:

(dollars in thousands)	Fair Value	Valuation Methodology	Unobservable Inputs	Average	Range of Inputs
Impaired loans:					
Commercial and industrial	$ 5,354	Collateral based measurements	Discount to reflect current market conditions and ultimate collectability	37%	(23% - 100%)
Impaired loans:					
Commercial real estate and multi-family residential loans	910	Collateral based measurements	Discount to reflect current market conditions and ultimate collectability	38%	(3% - 60%)
Other real estate owned	75	Appraisals	Discount to reflect current market conditions	49%	

The following table presents the valuation methodology and unobservable inputs for Level 3 assets measured at fair value on a non-recurring basis at December 31, 2016:

(dollars in thousands)	Fair Value	Valuation Methodology	Unobservable Inputs	Average	Range of Inputs
Impaired loans:					
Commercial and industrial	$ 4,510	Collateral based measurements	Discount to reflect current market conditions and ultimate collectability	44%	(22% - 100%)
Impaired loans:					
Commercial real estate	1,195	Collateral based measurements	Discount to reflect current market conditions and ultimate collectability	30%	(6% - 59%)
Impaired loans:					
Consumer 1-4 family mortgage	62	Collateral based measurements	Discount to reflect	15%	

			current market conditions and ultimate collectability	
Other real estate owned	75	Appraisals	Discount to reflect current market conditions	49%

Impaired loans, which are measured for impairment using the fair value of the collateral for collateral dependent loans, had a gross carrying amount of $10.0 million, with a valuation allowance of $3.7 million at June 30, 2017, resulting in a net reduction in the provision for loan losses of $200,000 in the three months ended June 30, 2017 and a net increase in the provision for loan losses of $600,000 in the six months ended June 30, 2017. At June 30, 2016, impaired loans had a gross carrying amount of $6.4 million, with a valuation allowance of $2.5 million, resulting in a net increase in the provision for loan losses of $0 and $100,000 for the three and six months ended June 30, 2016.

Other real estate owned measured at fair value less costs to sell, at both June 30, 2017 and June 30, 2016, had a net carrying amount of $75,000, which is made up of the outstanding balance of $147,000, net of a valuation allowance of $72,000, all of which was written down during 2012.

The following table contains the estimated fair values and the related carrying values of the Company's financial instruments. Items which are not financial instruments are not included.

	June 30, 2017				
	Carrying	Estimated Fair Value			
(dollars in thousands)	Value	Level 1	Level 2	Level 3	Total
Financial Assets:					
Cash and cash equivalents	$ 137,336	$ 135,131	$ 2,207	$ 0	$ 137,338
Securities available for sale	530,312	1,008	528,685	619	530,312
Real estate mortgages held for sale	4,221	0	4,294	0	4,294
Loans, net	3,532,441	0	0	3,502,029	3,502,029
Federal Home Loan Bank stock	8,102	N/A	N/A	N/A	N/A
Federal Reserve Bank stock	3,420	N/A	N/A	N/A	N/A
Accrued interest receivable	12,028	3	2,924	9,101	12,028
Financial Liabilities:					
Certificates of deposit	(1,254,976)	0	(1,261,314)	0	(1,261,314)
All other deposits	(2,360,963)	(2,360,963)	0	0	(2,360,963)
Securities sold under agreements to repurchase	(60,188)	0	(60,188)	0	(60,188)
Other short-term borrowings	(215,000)	0	(214,985)	0	(214,985)
Long-term borrowings	(30)	0	(31)	0	(31)
Subordinated debentures	(30,928)	0	0	(31,206)	(31,206)
Standby letters of credit	(427)	0	0	(427)	(427)
Accrued interest payable	(4,809)	(103)	(4,702)	(4)	(4,809)

	December 31, 2016				
	Carrying	Estimated Fair Value			
(dollars in thousands)	Value	Level 1	Level 2	Level 3	Total
Financial Assets:					
Cash and cash equivalents	$ 167,280	$ 165,385	$ 1,899	$ 0	$ 167,284
Securities available for sale	504,191	1,003	502,518	670	504,191
Real estate mortgages held for sale	5,915	0	5,994	0	5,994
Loans, net	3,427,209	0	0	3,411,121	3,411,121
Federal Home Loan Bank stock	8,102	N/A	N/A	N/A	N/A
Federal Reserve Bank stock	3,420	N/A	N/A	N/A	N/A
Accrued interest receivable	11,687	3	2,688	8,996	11,687
Financial Liabilities:					
Certificates of deposit	(1,163,818)	0	(1,169,905)	0	(1,169,905)
All other deposits	(2,414,094)	(2,414,094)	0	0	(2,414,094)
Securities sold under agreements to repurchase	(50,045)	0	(50,045)	0	(50,045)
Other short-term borrowings	(180,000)	0	(180,005)	0	(180,005)
Long-term borrowings	(32)	0	(34)	0	