UNITY BANCORP INC /NJ/
Form 10-Q
May 11, 2017

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

FORM 10-Q

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

For the quarterly period ended March 31, 2017

OR

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

For the transition period from ____ to ____.

Commission File Number 1-12431

Unity Bancorp, Inc.
(Exact name of registrant as specified in its charter)

New Jersey	22-3282551
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
64 Old Highway 22, Clinton, NJ	08809
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code (908) 730-7630

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, as amended, 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 (as defined in Rule 12b-2 of the Exchange Act):
Large accelerated filer Accelerated filer Nonaccelerated 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 Exchange Act:
Yes No

The number of shares outstanding of each of the registrant's classes of common equity stock, as of April 30, 2017 common stock, no par value: 10,534,865 shares outstanding.

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PART I CONSOLIDATED FINANCIAL INFORMATION
ITEM 1 Consolidated Financial Statements (Unaudited)
Unity Bancorp, Inc.
Consolidated Balance Sheets
(Unaudited)

(In thousands)	March 31, 2017	December 31, 2016
ASSETS		
Cash and due from banks	$18,345	$22,105
Federal funds sold and interest-bearing deposits	84,859	83,790
Cash and cash equivalents	103,204	105,895
Securities:		
Securities available for sale	52,246	40,568
Securities held to maturity (fair value of $20,729 and $20,968 respectively)	20,776	20,979
Total securities	73,022	61,547
Loans:		
SBA loans held for sale	12,163	14,773
SBA loans held for investment	42,403	42,492
SBA 504 loans	25,111	26,344
Commercial loans	519,338	509,171
Residential mortgage loans	305,578	289,093
Consumer loans	96,084	91,541
Total loans	1,000,677	973,414
Allowance for loan losses	(12,681)	(12,579)
Net loans	987,996	960,835
Premises and equipment, net	23,261	23,398
Bank owned life insurance ("BOLI")	13,847	13,758
Deferred tax assets	5,552	5,512
Federal Home Loan Bank ("FHLB") stock	5,992	6,037
Accrued interest receivable	4,483	4,462
Other real estate owned ("OREO")	1,172	1,050
Goodwill and other intangibles	1,516	1,516
Other assets	6,123	5,896
Total assets	$1,226,168	$1,189,906
LIABILITIES AND SHAREHOLDERS' EQUITY		
Liabilities:		
Deposits:		
Noninterest-bearing demand	$220,750	$215,963
Interest-bearing demand	146,091	145,654
Savings	389,802	363,462
Time, under $100,000	124,907	123,724
Time, $100,000 to $250,000	76,835	75,567
Time, $250,000 and over	22,318	21,353
Total deposits	980,703	945,723
Borrowed funds	120,000	121,000
Subordinated debentures	10,310	10,310
Accrued interest payable	405	430
Accrued expenses and other liabilities	5,445	6,152
Total liabilities	1,116,863	1,083,615

Commitments and contingencies		
Shareholders' equity:		
Common stock	85,757	85,383
Retained earnings	23,414	20,748
Accumulated other comprehensive income	134	160
Total shareholders' equity	109,305	106,291
Total liabilities and shareholders' equity	$1,226,168	$1,189,906
Issued and outstanding common shares	10,535	10,477

The accompanying notes to the Consolidated Financial Statements are an integral part of these statements.

Unity Bancorp, Inc.
Consolidated Statements of Income
(Unaudited)

	For the three months ended March 31,	
(In thousands, except per share amounts)	2017	2016
INTEREST INCOME		
Federal funds sold and interest-bearing deposits	$129	$44
FHLB stock	93	52
Securities:		
Taxable	491	363
Tax-exempt	44	62
Total securities	535	425
Loans:		
SBA loans	854	721
SBA 504 loans	301	385
Commercial loans	6,166	5,676
Residential mortgage loans	3,384	2,942
Consumer loans	1,132	931
Total loans	11,837	10,655
Total interest income	12,594	11,176
INTEREST EXPENSE		
Interest-bearing demand deposits	153	137
Savings deposits	583	366
Time deposits	804	951
Borrowed funds and subordinated debentures	664	735
Total interest expense	2,204	2,189
Net interest income	10,390	8,987
Provision for loan losses	250	200
Net interest income after provision for loan losses	10,140	8,787
NONINTEREST INCOME		
Branch fee income	331	333
Service and loan fee income	407	255
Gain on sale of SBA loans held for sale, net	485	308
Gain on sale of mortgage loans, net	637	715
BOLI income	88	94

Net security gains	—	94
Gain on repurchase of subordinated debt	—	2,264
Other income	256	217
Total noninterest income	2,204	4,280
NONINTEREST EXPENSE		
Compensation and benefits	4,095	3,549
Occupancy	600	618
Processing and communications	604	644
Furniture and equipment	511	420
Professional services	226	255
Loan collection and OREO expenses	341	72
Other loan expenses	83	104
Deposit insurance	76	160
Advertising	236	241
Director fees	197	135
Other expenses	471	409
Total noninterest expense	7,440	6,607
Income before provision for income taxes	4,904	6,460
Provision for income taxes	1,712	2,255
Net income	$3,192	$4,205
Net income per common share - Basic	$0.30	$0.45
Net income per common share - Diluted	$0.30	$0.44
Weighted average common shares outstanding - Basic	10,509	9,304
Weighted average common shares outstanding - Diluted	10,705	9,550

The accompanying notes to the Consolidated Financial Statements are an integral part of these statements.

All Share information has been adjusted for the 10% stock dividend paid September 30, 2016.

Unity Bancorp, Inc.
Consolidated Statements of Comprehensive Income
(Unaudited)

	For the three months ended					
	March 31, 2017			March 31, 2016		
(In thousands)	Before tax amount	Income tax expense (benefit)	Net of tax amount	Before tax amount	Income tax expense (benefit)	Net of tax amount
Net income	$4,904	$ 1,712	$3,192	$6,460	$ 2,255	$4,205
Other comprehensive (loss) income						
Investment securities available for sale:						
Unrealized holding (losses) gains on securities arising during the period	(144)	(58)	(86)	152	55	97
Less: reclassification adjustment for gains on securities included in net income	—	—	—	94	33	61
Total unrealized (losses) gains on securities available for sale	(144)	(58)	(86)	58	22	36
Adjustments related to defined benefit plan:						
Amortization of prior service cost	21	9	12	20	—	20
Total adjustments related to defined benefit plan	21	9	12	20	—	20
Net unrealized gains from cash flow hedges:						
Unrealized holding gains (losses) on cash flow hedges arising during the period	81	33	48	(492)	(202)	(290)
Total unrealized gains (losses) on cash flow hedges	81	33	48	(492)	(202)	(290)
Total other comprehensive loss	(42)	(16)	(26)	(414)	(180)	(234)
Total comprehensive income	$4,862	$ 1,696	$3,166	$6,046	$ 2,075	$3,971

The accompanying notes to the Consolidated Financial Statements are an integral part of these statements.

Consolidated Statements of Changes in Shareholders' Equity
For the three months ended March 31, 2017 and 2016
(Unaudited)

(In thousands)	Common stock Shares	Common stock Amount	Retained earnings	Accumulated other comprehensive income (loss)	Total shareholders' equity
Balance, December 31, 2016	10,477	$85,383	$20,748	$ 160	$ 106,291
Net income	—	—	3,192	—	3,192
Other comprehensive loss, net of tax	—	—	—	(26)	(26)
Dividends on common stock ($0.05 per share)	—	33	(526)	—	(493)
Common stock issued and related tax effects (1)	58	341	—	—	341
Balance, March 31, 2017	10,535	$85,757	$23,414	$ 134	$ 109,305

(In thousands)	Common stock Shares	Common stock Amount	Retained earnings	Accumulated other comprehensive (loss)	Total shareholders' equity
Balance, December 31, 2015	9,279	$59,371	$19,566	$ (467)	$ 78,470
Net income	—	—	4,205	—	4,205
Other comprehensive loss, net of tax	—	—	—	(234)	(234)
Dividends on common stock ($0.04 per share)	—	25	(340)	—	(315)
Common stock issued and related tax effects (1)	36	150	—	—	150
Balance, March 31, 2016	9,315	$59,546	$23,431	$ (701)	$ 82,276

(1) Includes the issuance of common stock under employee benefit plans, which includes nonqualified stock options and restricted stock expense related entries, employee option exercises and the tax benefit of options exercised.

The accompanying notes to the Consolidated Financial Statements are an integral part of these statements.

2016 share information has been adjusted for the 10% stock dividend paid September 30, 2016.

Unity Bancorp, Inc.
Consolidated Statements of Cash Flows
(Unaudited)

(In thousands)	For the three months ended March 31, 2017	2016
OPERATING ACTIVITIES:		
Net income	$3,192	$4,205
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	250	200
Net amortization of purchase premiums and discounts on securities	73	92
Depreciation and amortization	249	247
Deferred income tax (benefit) expense	(5)	142
Net security gains	—	(94)
Gain on repurchase of subordinated debentures	—	(2,264)
Stock compensation expense	212	132
Loss (gain) on sale of OREO	253	(88)
Gain on sale of mortgage loans held for sale, net	(454)	(294)
Gain on sale of SBA loans held for sale, net	(485)	(308)
Origination of mortgage loans held for sale	(25,654)	(25,015)
Origination of SBA loans held for sale	(2,451)	(3,734)
Proceeds from sale of mortgage loans held for sale, net	26,108	25,309
Proceeds from sale of SBA loans held for sale, net	6,511	3,759
BOLI income	(88)	(94)
Net change in other assets and liabilities	(905)	1,710
Net cash provided by operating activities	6,806	3,905
INVESTING ACTIVITIES		
Purchases of securities held to maturity	—	—
Purchases of securities available for sale	(15,495)	(2,142)
Purchases of FHLB stock, at cost	(225)	(1,395)
Maturities and principal payments on securities held to maturity	192	296
Maturities and principal payments on securities available for sale	3,611	3,949
Proceeds from sales of securities available for sale	—	2,564
Proceeds from redemption of FHLB stock	270	1,260
Proceeds from sale of OREO	21	1,224
Net (increase) decrease in loans	(31,283)	1,078
Purchases of premises and equipment	(210)	(4,543)
Net cash (used in) provided by investing activities	(43,119)	2,291
FINANCING ACTIVITIES		
Net increase in deposits	34,980	32,326
Proceeds from new borrowings	35,000	20,000
Repayments of borrowings	(36,000)	(17,000)
Repurchase of subordinated debentures	—	(2,891)
Proceeds from exercise of stock options	135	—
Dividends on common stock	(493)	(315)
Net cash provided by financing activities	33,622	32,120
(Decrease) increase in cash and cash equivalents	(2,691)	38,316
Cash and cash equivalents, beginning of period	105,895	88,157
Cash and cash equivalents, end of period	$103,204	$126,473

Unity Bancorp, Inc.
Consolidated Statements of Cash Flows (Continued)
(Unaudited)

	For the three months ended March 31,	
(In thousands)	2017	2016
SUPPLEMENTAL DISCLOSURES		
Cash:		
Interest paid	$2,229	$2,259
Income taxes paid	$1,877	$1,337
Noncash investing activities:		
Transfer of SBA loans held for sale to held to maturity	$13	$—
Capitalization of servicing rights	$176	$529
Transfer of loans to OREO	$396	$852

The accompanying notes to the Consolidated Financial Statements are an integral part of these statements.

Unity Bancorp, Inc.
Notes to the Consolidated Financial Statements (Unaudited)
March 31, 2017

NOTE 1. Significant Accounting Policies

The accompanying Consolidated Financial Statements include the accounts of Unity Bancorp, Inc. (the "Parent Company") and its wholly-owned subsidiary, Unity Bank (the "Bank" or when consolidated with the Parent Company, the "Company"), and reflect all adjustments and disclosures which are generally routine and recurring in nature, and in the opinion of management, necessary for a fair presentation of interim results. The Bank has multiple subsidiaries used to hold part of its investment and loan portfolios and OREO properties. All significant intercompany balances and transactions have been eliminated in consolidation. Certain reclassifications have been made to prior period amounts to conform to the current year presentation, with no impact on current earnings or shareholders' equity. The financial information has been prepared in accordance with U.S. generally accepted accounting principles and has not been audited. In preparing the financial statements, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities and revenues and expenses during the reporting periods. Actual results could differ from those estimates. Amounts requiring the use of significant estimates include the allowance for loan losses, valuation of deferred tax and servicing assets, the carrying value of loans held for sale and other real estate owned, the valuation of securities and the determination of other-than-temporary impairment for securities and fair value disclosures. Management believes that the allowance for loan losses is adequate. While management uses available information to recognize losses on loans, future additions to the allowance for loan losses may be necessary based on changes in economic conditions. The Company has evaluated subsequent events for potential recognition and/or disclosure through the date the Consolidated Financial Statements included in this Quarterly Report on Form 10-Q were available to be issued.

The interim unaudited Consolidated Financial Statements included herein have been prepared in accordance with instructions for Form 10-Q and the rules and regulations of the Securities and Exchange Commission ("SEC") and consist of normal recurring adjustments necessary for the fair presentation of interim results. The results of operations for the three months ended March 31, 2017 are not necessarily indicative of the results which may be expected for the entire year. As used in this Form 10-Q, "we" and "us" and "our" refer to Unity Bancorp, Inc., and its consolidated subsidiary, Unity Bank, depending on the context. Certain information and financial disclosures required by U.S. generally accepted accounting principles have been condensed or omitted from interim reporting pursuant to SEC rules. Interim financial statements should be read in conjunction with the Company's Consolidated Financial Statements and notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2016.

Stock Transactions

On August 26, 2016, the Company declared a 10% stock dividend to shareholders' of record as of September 15, 2016. The 10% stock dividend was paid on September 30, 2016. All share amounts in the following tables have been restated to include the effect of the 10% stock dividend distribution.

Stock Option Plans
The Company has incentive and nonqualified option plans, which allow for the grant of options to officers, employees and members of the Board of Directors. Transactions under the Company's stock option plans for the three months ended March 31, 2017 are summarized in the following table:

	Shares	Weighted average exercise	Weighted average remaining contractual life in years	Aggregate intrinsic value

		price		
Outstanding at December 31, 2016	552,759	$ 7.26	5.7	$4,663,432
Options granted	47,100	16.37		
Options exercised	(17,064)	7.91		
Options forfeited	—	—		
Options expired	(607)	11.48		
Outstanding at March 31, 2017	582,188	$ 7.98	5.9	$5,224,156
Exercisable at March 31, 2017	410,995	$ 6.14	4.5	$4,442,273

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Grants under the Company's incentive and nonqualified option plans generally vest over 3 years and must be exercised within 10 years of the date of grant. The exercise price of each option is the market price on the date of grant. As of March 31, 2017, 2,112,585 shares have been reserved for issuance upon the exercise of options, 582,188 option grants are outstanding, and 1,498,025 option grants have been exercised, forfeited or expired, leaving 32,372 shares available for grant.

The fair values of the options granted during the three months ended March 31, 2017 and 2016 were estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted average assumptions:

	For the three months ended March 31, 2017	2016
Number of options granted	47,100	97,900
Weighted average exercise price	$16.37	$10.06
Weighted average fair value of options	$4.64	$3.19
Expected life in years (1)	6.57	6.85
Expected volatility (2)	28.12 %	31.91 %
Risk-free interest rate (3)	2.18 %	1.79 %
Dividend yield (4)	1.15 %	1.44 %

(1) The expected life of the options was estimated based on historical employee behavior and represents the period of time that options granted are expected to be outstanding.
(2) The expected volatility of the Company's stock price was based on the historical volatility over the period commensurate with the expected life of the options.
(3) The risk-free interest rate is the U.S. Treasury rate commensurate with the expected life of the options on the date of grant.
(4) The expected dividend yield is the projected annual yield based on the grant date stock price.

Upon exercise, the Company issues shares from its authorized but unissued common stock to satisfy the options. The following table presents information about options exercised during the three months ended March 31, 2017 and 2016:

	For the three months ended March 31, 2017	2016
Number of options exercised	17,064	—
Total intrinsic value of options exercised	$147,690	$ —
Cash received from options exercised	$134,955	$ —
Tax deduction realized from options	$60,331	$ —

The following table summarizes information about stock options outstanding and exercisable at March 31, 2017:

	Options outstanding			Options exercisable	
Range of exercise prices	Options outstanding	Weighted average remaining contractual life (in years)	Weighted average exercise price	Options exercisable	Weighted average exercise price
$0.00 - 4.00	96,800	1.9	$ 3.54	96,800	$ 3.54
4.01 - 8.00	242,688	4.4	6.26	242,321	6.25
8.01 - 12.00	166,100	8.5	9.52	71,874	9.27
12.01 - 16.00	46,600	9.7	15.00	—	—

16.01 - 20.00	30,000	9.9	16.75	—	—
Total	582,188	5.9	$ 7.98	410,995	$ 6.14

Financial Accounting Standards Board Accounting Standards Codification ("FASB ASC") Topic 718, "Compensation - Stock Compensation," requires an entity to recognize the fair value of equity awards as compensation expense over the period during which an employee is required to provide service in exchange for such an award (vesting period). Compensation expense related to stock options and the related income tax benefit for the three months ended March 31, 2017 and 2016 are detailed in the following table:

	For the three months ended March 31,	
	2017	2016
Compensation expense	$69,817	$55,983
Income tax benefit	$28,520	$22,869

As of March 31, 2017, unrecognized compensation costs related to nonvested share-based compensation arrangements granted under the Company's stock option plans totaled approximately $571 thousand. That cost is expected to be recognized over a weighted average period of 2.3 years.

Restricted Stock Awards

Restricted stock is issued under the stock bonus program to reward employees and directors and to retain them by distributing stock over a period of time. The following table summarizes nonvested restricted stock activity for the three months ended March 31, 2017:

	Shares	Average grant date fair value
Nonvested restricted stock at December 31, 2016	97,203	$ 9.47
Granted	38,400	16.36
Cancelled	—	—
Vested	(29,016)	8.80
Nonvested restricted stock at March 31, 2017	106,587	$ 12.13

Restricted stock awards granted to date vest over a period of 4 years and are recognized as compensation to the recipient over the vesting period. The awards are recorded at fair market value at the time of grant and amortized into salary expense on a straight line basis over the vesting period. As of March 31, 2017, 518,157 shares of restricted stock were reserved for issuance, of which 111,404 shares are available for grant.

Restricted stock awards granted during the three months ended March 31, 2017 and 2016 were as follows:

	For the three months ended March 31,	
	2017	2016
Number of shares granted	38,400	33,385
Average grant date fair value	$16.36	$10.19

Compensation expense related to restricted stock for the three months ended March 31, 2017 and 2016 is detailed in the following table:

	For the three months ended March 31,

	2017	2016
Compensation expense	$141,804	$76,118
Income tax benefit	$57,927	$31,097

As of March 31, 2017, there was approximately $1.2 million of unrecognized compensation cost related to nonvested restricted stock awards granted under the Company’s stock incentive plans. That cost is expected to be recognized over a weighted average period of 3.2 years.

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401(k) Savings Plan

The Bank has a 401(k) savings plan covering substantially all employees. Under the Plan, an employee can contribute up to 80 percent of their salary on a tax deferred basis. The Bank may also make discretionary contributions to the Plan. The Bank contributed $119 thousand and $89 thousand to the Plan during the three months ended March 31, 2017 and 2016, respectively.

Deferred Fee Plan

The Company has a deferred fee plan for Directors and executive management. Directors of the Company have the option to elect to defer up to 100 percent of their respective retainer and Board of Director fees, and each member of executive management has the option to elect to defer up to 100 percent of their year end cash bonuses. Director and executive deferred fees totaled $120 thousand and $102 thousand during the three months ended March 31, 2017 and 2016, respectively. The interest paid on the deferred balances totaled $10 thousand and $8 thousand during the three months ended March 31, 2017 and 2016, respectively. No fees were distributed in 2017 and 2016, respectively.

Benefit Plans

In addition to the 401(k) savings plan which covers substantially all employees, the Company established in 2015 an unfunded supplemental defined benefit plan to provide additional retirement benefits for the President and Chief Executive Officer ("CEO") and certain key executives.

On June 4, 2015, the Company approved the Supplemental Executive Retirement Plan ("SERP") pursuant to which the President and CEO is entitled to receive certain supplemental nonqualified retirement benefits. On November 21, 2016 the Company approved a change in calculation of the Retirement Benefit payable under the Plan so that the Retirement Benefit shall be an amount equal to forty (40%) percent of the average of Executive's base salary for the thirty-six (36) months immediately preceding executive's separation from service after age 66, adjusted annually thereafter by two (2%). The total benefit is to be made payable in fifteen annual installments. The future payments are estimated to total $3.4 million. A discount rate of 4.00% was used to calculate the present value of the benefit obligation.

The President and CEO commenced vesting to this retirement benefit on January 1, 2014, and vests an additional 3% each year until fully vested on January 1, 2024. In the event that the President and CEO's separation from service from the company were to occur prior to full vesting, the President and CEO would be entitled to and shall be paid the vested portion of the retirement benefit calculated as of the date of separation from service. Notwithstanding the foregoing, upon a Change in Control, and provided that within 6 months following the Change in Control the President and CEO is involuntarily terminated for reasons other than "cause" or the President and CEO resigns for "good reason," as such is defined in the SERP, or the President and CEO voluntarily terminates his employment after being offered continued employment in a position that is not a "Comparable Position," as such is also defined in the SERP, the President and CEO shall become 100% vested in the full retirement benefit.

No contributions or payments have been made during the three months ended March 31, 2017. The following table summarizes the components of the net periodic pension cost of the defined benefit plan recognized during the three months ended March 31, 2017 and 2016:

	For the three months ended March 31,	
(In thousands)	2017	2016
Service cost	$16	$ 15
Interest cost	10	10
Amortization of prior service cost	21	20

Net periodic benefit cost	$47	$ 45

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The following table summarizes the changes in benefit obligations of the defined benefit plan during the three months ended March 31, 2017 and 2016:

(In thousands)	For the three months ended March 31, 2017	2016
Benefit obligation, beginning of year	$1,023	$923
Service cost	16	15
Interest cost	10	10
Actuarial gain (loss)	—	—
Benefit obligation, end of period	$1,049	$948

On October 22, 2015, the Company entered into an Executive Incentive Retirement Plan (the "Plan") with certain key executive officers. The Plan has an effective date of January 1, 2015.

The Plan is an unfunded, nonqualified deferred compensation plan. For any Plan Year, a guaranteed annual Deferral Award percentage of seven and one half percent (7.5%) of the participant's annual base salary will be credited to each Participant's Deferred Benefit Account. A discretionary annual Deferral Award equal to seven and one half percent (7.5%) of the participant's annual base salary may be credited to the Participant's account in addition to the guaranteed Deferral Award, if the Bank exceeds the benchmarks set forth in the Annual Executive Bonus Matrix. The total Deferral Award shall never exceed fifteen percent (15%) of the participant's base salary for any given Plan Year. Each Participant shall be one hundred percent 100% vested in all Deferral Awards as of the date they are awarded.

As of March 31, 2017, the Company had total year to date expenses of $23 thousand related to the Plan. The Plan is reflected on the Company's balance sheet as accrued expenses.

Certain members of management are also enrolled in a split-dollar life insurance plan with a post retirement death benefit of $250 thousand. Total expenses related to this plan were $1 thousand for the three months ended March 31, 2017 and 2016.

Other-Than-Temporary Impairment

The Company has a process in place to identify securities that could potentially incur credit impairment that is other-than-temporary. This process involves monitoring late payments, pricing levels, downgrades by rating agencies, key financial ratios, financial statements, revenue forecasts and cash flow projections as indicators of credit issues. Management evaluates securities for other-than-temporary impairment at least on a quarterly basis, and more frequently when economic or market concern warrants such evaluation. This evaluation considers relevant facts and circumstances in evaluating whether a credit or interest rate-related impairment of a security is other-than-temporary. Relevant facts and circumstances considered include: (1)the extent and length of time the fair value has been below cost; (2) the reasons for the decline in value; (3) the financial position and access to capital of the issuer, including the current and future impact of any specific events and (4) for fixed maturity securities, our intent to sell a security or whether it is more likely than not we will be required to sell the security before the recovery of its amortized cost which, in some cases, may extend to maturity and for equity securities, our ability and intent to hold the security for a forecasted period of time that allows for the recovery in value.

Management assesses its intent to sell or whether it is more likely than not that it will be required to sell a security before recovery of its amortized cost basis less any current-period credit losses. For debt securities that are considered other-than-temporarily impaired with no intent to sell and no requirement to sell prior to recovery of its amortized cost basis, the amount of the impairment is separated into the amount that is credit related (credit loss component) and the amount due to all other factors. The credit loss component is recognized in earnings and is the difference between the security's amortized cost basis and the present value of its expected future cash flows. The remaining difference between the security's fair value and the present value of future expected cash flows is due to factors that are not credit related and is recognized in other comprehensive income. For debt securities where management has the intent to sell, the amount of the impairment is reflected in earnings as realized losses.

The present value of expected future cash flows is determined using the best estimate cash flows discounted at the effective interest rate implicit to the security at the date of purchase or the current yield to accrete an asset-backed or floating rate security. The methodology and assumptions for establishing the best estimate cash flows vary depending on the type of security. The asset-backed securities cash flow estimates are based on bond specific facts and circumstances that may include collateral characteristics, expectations of delinquency and default rates, loss severity and prepayment speeds and structural support, including subordination and guarantees. The corporate bond cash flow estimates are derived from scenario-based outcomes of expected corporate restructurings or the disposition of assets using bond specific facts and circumstances including timing, security interests and loss severity.

Transfers of Financial Assets

Transfers of financial assets are accounted for as sales, when control over the assets has been surrendered. Control over transferred assets is deemed to be surrendered when (1) the assets have been isolated from the Company, (2) the transferee obtains the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred assets, and (3) the Company does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity.

Loans

Loans Held for Sale

Loans held for sale represent the guaranteed portion of Small Business Administration ("SBA") loans and are reflected at the lower of aggregate cost or market value. The Company originates loans to customers under an SBA program that historically has provided for SBA guarantees of up to 90 percent of each loan. The Company generally sells the guaranteed portion of its SBA loans to a third party and retains the servicing, holding the nonguaranteed portion in its portfolio. The net amount of loan origination fees on loans sold is included in the carrying value and in the gain or loss on the sale. When sales of SBA loans do occur, the premium received on the sale and the present value of future cash flows of the servicing assets are recognized in income. All criteria for sale accounting must be met in order for the loan sales to occur; see details under the "Transfers of Financial Assets" heading above.

Servicing assets represent the estimated fair value of retained servicing rights, net of servicing costs, at the time loans are sold. Servicing assets are amortized in proportion to, and over the period of, estimated net servicing revenues. Impairment is evaluated based on stratifying the underlying financial assets by date of origination and term. Fair value is determined using prices for similar assets with similar characteristics, when available, or based upon discounted cash flows using market-based assumptions. Any impairment, if temporary, would be reported as a valuation allowance.

Serviced loans sold to others are not included in the accompanying Consolidated Balance Sheets. Income and fees collected for loan servicing are credited to noninterest income when earned, net of amortization on the related servicing assets.

Loans Held to Maturity

Loans held to maturity are stated at the unpaid principal balance, net of unearned discounts and deferred loan origination fees and costs. In accordance with the level yield method, loan origination fees, net of direct loan origination costs, are deferred and recognized over the estimated life of the related loans as an adjustment to the loan yield. Interest is credited to operations primarily based upon the principal balance outstanding.

Loans are reported as past due when either interest or principal is unpaid in the following circumstances: fixed payment loans when the borrower is in arrears for two or more monthly payments; open end credit for two or more billing cycles; and single payment notes if interest or principal remains unpaid for 30 days or more.

Nonperforming loans consist of loans that are not accruing interest as a result of principal or interest being in default for a period of 90 days or more or when the ability to collect principal and interest according to the contractual terms is in doubt (nonaccrual loans). When a loan is classified as nonaccrual, interest accruals are discontinued and all past due interest previously recognized as income is reversed and charged against current period earnings. Generally, until the loan becomes current, any payments received from the borrower are applied to outstanding principal until such time as management determines that the financial condition of the borrower and other factors merit recognition of a portion of such payments as interest income. Loans may be returned to an accrual status when the ability to collect is reasonably assured and when the loan is brought current as to principal and interest.

Loans are charged off when collection is sufficiently questionable and when the Company can no longer justify maintaining the loan as an asset on the balance sheet. Loans qualify for charge-off when, after thorough analysis, all possible sources of repayment are insufficient. These include: 1) potential future cash flows, 2) value of collateral, and/or 3) strength of co-makers and guarantors. All unsecured loans are charged off upon the establishment of the loan's nonaccrual status. Additionally, all loans classified as a loss or that portion of the loan classified as a loss is charged off. All loan charge-offs are approved by the Board of Directors.

Troubled debt restructurings ("TDRs") occur when a creditor, for economic or legal reasons related to a debtor's financial condition, grants a concession to the debtor that it would not otherwise consider. These concessions typically include reductions in interest rate, extending the maturity of a loan, or a combination of both. Interest income on accruing TDRs is credited to operations primarily based upon the principal amount outstanding, as stated in the paragraphs above.

The Company evaluates its loans for impairment. A loan is considered impaired when, based on current information and events, it is probable that the Company will be unable to collect all amounts due according to the contractual terms of the loan agreement. The Company has defined impaired loans to be all TDRs and nonperforming loans individually evaluated for impairment. Impairment is evaluated in total for smaller-balance loans of a similar nature (consumer and residential mortgage loans), and on an individual basis for all other loans. Impairment of a loan is measured based on the present value of expected future cash flows, discounted at the loan's effective interest rate, or as a practical expedient, based on a loan's observable market price or the fair value of collateral, net of estimated costs to sell, if the loan is collateral-dependent. If the value of the impaired loan is less than the recorded investment in the loan, the Company establishes a valuation allowance, or adjusts existing valuation allowances, with a corresponding charge to the provision for loan losses.

For additional information on loans, see Note 8 to the Consolidated Financial Statements and the section titled "Loan Portfolio" under Item 2. Management's Discussion and Analysis.

Allowance for Loan Losses and Reserve for Unfunded Loan Commitments

The allowance for loan losses is maintained at a level management considers adequate to provide for probable loan losses as of the balance sheet date. The allowance is increased by provisions charged to expense and is reduced by net charge-offs.

The level of the allowance is based on management's evaluation of probable losses in the loan portfolio, after consideration of prevailing economic conditions in the Company's market area, the volume and composition of the loan portfolio, and historical loan loss experience. The allowance for loan losses consists of specific reserves for individually impaired credits and TDRs, reserves for nonimpaired loans based on historical loss factors and reserves based on general economic factors and other qualitative risk factors such as changes in delinquency trends, industry concentrations or local/national economic trends. This risk assessment process is performed at least quarterly, and, as adjustments become necessary, they are realized in the periods in which they become known.

Although management attempts to maintain the allowance at a level deemed adequate to provide for probable losses, future additions to the allowance may be necessary based upon certain factors including changes in market conditions and underlying collateral values. In addition, various regulatory agencies periodically review the adequacy of the Company's allowance for loan losses. These agencies may require the Company to make additional provisions based on their judgments about information available to them at the time of their examination.

The Company maintains an allowance for unfunded loan commitments that is maintained at a level that management believes is adequate to absorb estimated probable losses. Adjustments to the allowance are made through other expenses and applied to the allowance which is maintained in other liabilities.

For additional information on the allowance for loan losses and unfunded loan commitments, see Note 9 to the Consolidated Financial Statements and the sections titled "Asset Quality" and "Allowance for Loan Losses and Reserve for Unfunded Loan Commitments" under Item 2. Management's Discussion and Analysis.

Income Taxes

The Company accounts for income taxes according to the asset and liability method. Under this method, deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax basis. Deferred tax assets and liabilities are measured using the enacted tax rates applicable to taxable income for the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

Valuation reserves are established against certain deferred tax assets when it is more likely than not that the deferred tax assets will not be realized. Increases or decreases in the valuation reserve are charged or credited to the income tax provision.When tax returns are filed, it is highly certain that some positions taken would be sustained upon examination by the taxing authorities, while others are subject to uncertainty about the merits of the position taken or the amount of the position that ultimately would be sustained. The benefit of a tax position is recognized in the financial statements in the period during which, based on all available evidence, management believes it is more likely than not that the position will be sustained upon examination, including the resolution of appeals or litigation processes, if any. The evaluation of a tax position taken is considered by itself and not offset or aggregated with other positions. Tax positions that meet the more likely than not recognition threshold are measured as the largest amount of tax benefit that is more than 50 percent likely of being realized upon settlement with the applicable taxing authority. The portion of benefits associated with tax positions taken that exceeds the amount measured as described above is reflected as a liability for unrecognized tax benefits in the accompanying balance sheet along with any associated interest and penalties that would be payable to the taxing authorities upon examination.

Interest and penalties associated with unrecognized tax benefits would be recognized in income tax expense on the income statement.

NOTE 2. Litigation

The Company may, in the ordinary course of business, become a party to litigation involving collection matters, contract claims and other legal proceedings relating to the conduct of its business. In the best judgment of management, based upon consultation with counsel, the consolidated financial position and results of operations of the Company will not be affected materially by the final outcome of any pending legal proceedings or other contingent liabilities and commitments.

NOTE 3. Net Income per Share

Basic net income per common share is calculated as net income divided by the weighted average common shares outstanding during the reporting period.

Diluted net income per common share is computed similarly to that of basic net income per common share, except that the denominator is increased to include the number of additional common shares that would have been outstanding if all potentially dilutive common shares, principally stock options, were issued during the reporting period utilizing the Treasury stock method.

The following is a reconciliation of the calculation of basic and diluted income per share:

	For the three months ended March 31,	
(In thousands, except per share amounts)	2017	2016

Net income	$3,192	$4,205
Weighted average common shares outstanding - Basic	10,509	9,304
Plus: Potential dilutive common stock equivalents	196	246
Weighted average common shares outstanding - Diluted	10,705	9,550
Net income per common share - Basic	$0.30	$0.45
Net income per common share - Diluted	0.30	0.44
Stock options and common stock excluded from the income per share calculation as their effect would have been anti-dilutive	56	203

Prior year weighted average share and per share figures shown above have been adjusted for the 10% stock dividend paid September 30, 2016.

NOTE 4. Income Taxes

The Company follows FASB ASC Topic 740, "Income Taxes," which prescribes a threshold for the financial statement recognition of income taxes and provides criteria for the measurement of tax positions taken or expected to be taken in a tax return. ASC 740 also includes guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition of income taxes.

For the quarter ended March 31, 2017, the Company reported income tax expense of $1.7 million for an effective tax rate of 34.9 percent, compared to an income tax expense of $2.3 million and an effective tax rate of 34.9 percent for the prior year's quarter. The Company did not recognize or accrue any interest or penalties related to income taxes during the three months ended March 31, 2017 or 2016. The Company did not have an accrual for uncertain tax positions as of March 31, 2017 or December 31, 2016, as deductions taken and benefits accrued are based on widely understood administrative practices and procedures and are based on clear and unambiguous tax law. Tax returns for all years 2012 and thereafter are subject to future examination by tax authorities.

NOTE 5. Other Comprehensive (Loss) Income

The following tables show the changes in other comprehensive income (loss) for the three months ended March 31, 2017 and 2016, net of tax:

	For the three months ended March 31, 2017			
(In thousands)	Net unrealized losses on securities	Adjustments related to defined benefit plan	Net unrealized gains from cash flow hedges	Accumulated other comprehensive income (loss)
Balance, beginning of period	$(161)	$ (391)	$ 712	$ 160
Other comprehensive (loss) income before reclassifications	(86)	—	48	(38)
Less amounts reclassified from accumulated other comprehensive loss	—	(12)	—	(12)
Period change	(86)	12	48	(26)
Balance, end of period	$(247)	$ (379)	$ 760	$ 134

	For the three months ended March 31, 2016			
(In thousands)	Net unrealized (losses) gains on securities	Adjustments related to defined benefit plan	Net unrealized losses from cash flow hedges	Accumulated other comprehensive income (loss)
Balance, beginning of period	$(2)	$ (448)	$ (17)	$ (467)
Other comprehensive income (loss) before reclassifications	97	—	(290)	(193)
Less amounts reclassified from accumulated other comprehensive loss	61	(20)	—	41
Period change	36	20	(290)	(234)
Balance, end of period	$34	$ (428)	$ (307)	$ (701)

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NOTE 6. Fair Value

Fair Value Measurement

The Company follows FASB ASC Topic 820, "Fair Value Measurement and Disclosures," which requires additional disclosures about the Company's assets and liabilities that are measured at fair value. Fair value is the exchange price that would be received for an asset or paid to transfer a liability (an 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. In determining fair value, the Company uses various methods including market, income and cost approaches. Based on these approaches, the Company often utilizes certain assumptions that market participants would use in pricing the asset or liability, including assumptions about risk and/or the risks inherent in the inputs to the valuation technique. These inputs can be readily observable, market corroborated, or generally unobservable inputs. The Company utilizes techniques that maximize the use of observable inputs and minimize the use of unobservable inputs. The fair value hierarchy ranks the quality and reliability of the information used to determine fair values. Financial assets and liabilities carried at fair value will be classified and disclosed as follows:

Level 1 Inputs
- Unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities.
- Generally, this includes debt and equity securities and derivative contracts that are traded in an active exchange market (i.e. New York Stock Exchange), as well as certain U.S. Treasury, U.S. Government and sponsored entity agency mortgage-backed securities that are highly liquid and are actively traded in over-the-counter markets.

Level 2 Inputs
- Quoted prices for similar assets or liabilities in active markets.
- Quoted prices for identical or similar assets or liabilities in inactive markets.
- Inputs other than quoted prices that are observable, either directly or indirectly, for the term of the asset or liability (i.e., interest rates, yield curves, credit risks, prepayment speeds or volatilities) or "market corroborated inputs."
- Generally, this includes U.S. Government and sponsored entity mortgage-backed securities, corporate debt securities and derivative contracts.

Level 3 Inputs
- Prices or valuation techniques that require inputs that are both unobservable (i.e. supported by little or no market activity) and that are significant to the fair value of the assets or liabilities.
- These assets and liabilities include financial instruments whose value is determined using pricing models, discounted cash flow methodologies, or similar techniques, as well as instruments for which the determination of fair value requires significant management judgment or estimation.

Fair Value on a Recurring Basis

The following is a description of the valuation methodologies used for instruments measured at fair value on a recurring basis:

Securities Available for Sale
The fair value of available for sale ("AFS") securities is the market value based on quoted market prices, when available, or market prices provided by recognized broker dealers (Level 1). If listed prices or quotes are not available, fair value is based upon quoted market prices for similar or identical assets or other observable inputs (Level 2) or externally developed models that use unobservable inputs due to limited or no market activity of the instrument (Level 3).

As of March 31, 2017, the fair value of the Company's AFS securities portfolio was $52.2 million. Approximately 63 percent of the portfolio was made up of residential mortgage-backed securities, which had a fair value of $32.8 million at March 31, 2017. Approximately $32.1 million of the residential mortgage-backed securities are guaranteed by the Government National Mortgage Association ("GNMA"), the Federal National Mortgage Association ("FNMA") or the Federal Home Loan Mortgage Corporation ("FHLMC"). The underlying loans for these securities are residential mortgages that are geographically dispersed throughout the United States.

All of the Company’s AFS securities were classified as Level 2 assets at March 31, 2017. The valuation of AFS securities using Level 2 inputs was primarily determined using the market approach, which uses quoted prices for similar assets or liabilities in active markets and all other relevant information. It includes model pricing, defined as valuing securities based upon their relationship with other benchmark securities.

There were no changes in the inputs or methodologies used to determine fair value during the period ended March 31, 2017, as compared to the periods ended December 31, 2016 and March 31, 2016.

The tables below present the balances of assets and liabilities measured at fair value on a recurring basis as of March 31, 2017 and December 31, 2016:

	March 31, 2017			
(In thousands)	Level 1	Level 2	Level 3	Total
Securities available for sale:				
U.S. Government sponsored entities	$ —	$ 3,721	$ —	$ 3,721
State and political subdivisions	—	5,863	—	5,863
Residential mortgage-backed securities	—	32,794	—	32,794
Corporate and other securities	—	9,868	—	9,868
Total securities available for sale	$ —	$ 52,246	$ —	$ 52,246
Interest rate swap agreements	—	1,285	—	1,285
Total	$ —	1,285	$ —	$ 1,285

	December 31, 2016			
(In thousands)	Level 1	Level 2	Level 3	Total
Securities available for sale:				
U.S. Government sponsored entities	$ —	$ 3,716	$ —	$ 3,716
State and political subdivisions	—	5,502	—	5,502
Residential mortgage-backed securities	—	21,631	—	21,631
Corporate and other securities	—	9,719	—	9,719
Total securities available for sale	$ —	$ 40,568	$ —	$ 40,568
Interest rate swap agreements	—	1,204	—	1,204
Total	$ —	$ 1,204	$ —	$ 1,204

Fair Value on a Nonrecurring Basis

Certain assets and liabilities are not measured at fair value on an ongoing basis but are subject to fair value adjustments in certain circumstances (for example, when there is evidence of impairment). The following is a description of the valuation methodologies used for instruments measured at fair value on a nonrecurring basis:

Appraisal Policy

All appraisals must be performed in accordance with the Uniform Standards of Professional Appraisal Practice ("USPAP"). Appraisals are certified to the Company and performed by appraisers on the Company’s approved list of appraisers. Evaluations are completed by a person independent of Company management. The content of the appraisal depends on the complexity of the property. Appraisals are completed on a “retail value” and an “as is value.”

The Company requires current real estate appraisals on all loans that become OREO or in-substance foreclosure, loans that are classified substandard, doubtful or loss, or loans that are over $100,000 and nonperforming. Prior to each balance sheet date, the Company values impaired collateral-dependent loans and OREO based upon a third party appraisal, broker's price opinion, drive by appraisal, automated valuation model, updated market evaluation, or a combination of these methods. The amount is discounted for the decline in market real estate values (for original appraisals), for any known damage or repair costs, and for selling and closing costs. The amount of the discount ranges from 10 to 25 percent and is dependent upon the method used to determine the original value. The original appraisal is generally used when a loan is first determined to be impaired. When applying the discount, the Company takes into consideration when the appraisal was performed, the collateral’s location, the type of collateral, any known damage to the property and the type of business. Subsequent to entering impaired status and the Company determining that there is a collateral shortfall, the Company will generally, depending on the type of collateral, order a third party appraisal, broker's price opinion, automated valuation model or updated market evaluation. After receiving the third party results, the Company will discount the value 8 to 10 percent for selling and closing costs.

OREO
The fair value of OREO is determined using appraisals, which may be discounted based on management's review and changes in market conditions (Level 3 Inputs).

Impaired Collateral-Dependent Loans
The fair value of impaired collateral-dependent loans is derived in accordance with FASB ASC Topic 310, "Receivables." Fair value is determined based on the loan's observable market price or the fair value of the collateral. Partially charged-off loans are measured for impairment based upon an appraisal for collateral-dependent loans. When an updated appraisal is received for a nonperforming loan, the value on the appraisal is discounted in the manner discussed above. If there is a deficiency in the value after the Company applies these discounts, management applies a specific reserve and the loan remains in nonaccrual status. The receipt of an updated appraisal would not qualify as a reason to put a loan back into accruing status. The Company removes loans from nonaccrual status generally when the borrower makes nine months of contractual payments and demonstrates the ability to service the debt going forward. Charge-offs are determined based upon the loss that management believes the Company will incur after evaluating collateral for impairment based upon the valuation methods described above and the ability of the borrower to pay any deficiency.

The valuation allowance for impaired loans is included in the allowance for loan losses in the consolidated balance sheets. At March 31, 2017, the valuation allowance for impaired loans was $296 thousand, an increase of $16 thousand from $280 thousand at December 31, 2016.

The following tables present the assets and liabilities subject to fair value adjustments (impairment) on a non-recurring basis carried on the balance sheet by caption and by level within the hierarchy (as described above):

	Fair value at March 31, 2017			
(In thousands)	Level 1	Level 2	Level 3	Total
Financial assets:				
OREO	$—	$—	$1,172	$1,172
Impaired collateral-dependent loans	—	—	2,619	2,619

	Fair value at December 31, 2016			
(In thousands)	Level 1	Level 2	Level 3	Total
Financial assets:				
OREO	$—	$—	$1,050	$1,050
Impaired collateral-dependent loans	—	—	1,767	1,767

Fair Value of Financial Instruments

FASB ASC Topic 825, "Financial Instruments," requires the disclosure of the estimated fair value of certain financial instruments, including those financial instruments for which the Company did not elect the fair value option. These estimated fair values as of March 31, 2017 and December 31, 2016 have been determined using available market information and appropriate valuation methodologies. Considerable judgment is required to interpret market data to develop estimates of fair value. The estimates presented are not necessarily indicative of amounts the Company could realize in a current market exchange. The use of alternative market assumptions and estimation methodologies could have had a material effect on these estimates of fair value. The methodology for estimating the fair value of financial assets and liabilities that are measured on a recurring or nonrecurring basis are discussed above. The following methods and assumptions were used to estimate the fair value of other financial instruments for which it is practicable to estimate that value:

Cash and Cash Equivalents

For these short-term instruments, the carrying value is a reasonable estimate of fair value.

Securities

The fair value of securities is based upon quoted market prices for similar or identical assets or other observable inputs (Level 2) or externally developed models that use unobservable inputs due to limited or no market activity of the instrument (Level 3).

SBA Loans Held for Sale

The fair value of SBA loans held for sale is estimated by using a market approach that includes significant other observable inputs.

Loans
The fair value of loans is estimated by discounting the future cash flows using current market rates that reflect the interest rate risk inherent in the loan, except for previously discussed impaired loans.

FHLB Stock
Federal Home Loan Bank stock is carried at cost. Carrying value approximates fair value based on the redemption provisions of the issues.

Servicing Assets
Servicing assets do not trade in an active, open market with readily observable prices. The Company estimates the fair value of servicing assets using discounted cash flow models incorporating numerous assumptions from the perspective of a market participant including market discount rates and prepayment speeds.

Accrued Interest
The carrying amounts of accrued interest approximate fair value.

OREO
The fair value of OREO is determined using appraisals, which may be discounted based on management's review and changes in market conditions (Level 3 Inputs).

Deposit Liabilities
The fair value of demand deposits and savings accounts is the amount payable on demand at the reporting date (i.e. carrying value). The fair value of fixed-maturity certificates of deposit is estimated by discounting the future cash flows using current market rates.

Borrowed Funds and Subordinated Debentures
The fair value of borrowings is estimated by discounting the projected future cash flows using current market rates.

Standby Letters of Credit
At March 31, 2017 and December 31, 2016, the Bank had standby letters of credit outstanding of $4.1 million. The fair value of these commitments is nominal.

The table below presents the carrying amount and estimated fair values of the Company's financial instruments presented as of March 31, 2017 and December 31, 2016:

		March 31, 2017		December 31, 2016	
(In thousands)	Fair value level	Carrying amount	Estimated fair value	Carrying amount	Estimated fair value
Financial assets:					
Cash and cash equivalents	Level 1	$103,204	$103,204	$105,895	$105,895
Securities (1)	Level 2	73,022	72,975	61,547	61,536
SBA loans held for sale	Level 2	12,163	13,665	14,773	16,440
Loans, net of allowance for loan losses (2)	Level 2	975,833	975,009	946,062	944,772
FHLB stock	Level 2	5,992	5,992	6,037	6,037
Servicing assets	Level 3	2,150	2,150	2,086	2,086
Accrued interest receivable	Level 2	4,483	4,483	4,462	4,462
OREO	Level 3	1,172	1,172	1,050	1,050
Financial liabilities:					
Deposits	Level 2	980,703	979,793	945,723	944,886
Borrowed funds and subordinated debentures	Level 2	130,310	129,834	131,310	130,319
Accrued interest payable	Level 2	405	405	430	430

(1) Includes held to maturity ("HTM") corporate securities that are considered Level 3. These securities had book values of $3.8 million at March 31, 2017 and December 31, 2016, and market values of $3.6 million at March 31, 2017 and December 31, 2016.

(2) Includes collateral-dependent impaired loans that are considered Level 3 and reported separately in the tables under the "Fair Value on a Nonrecurring Basis" heading. Collateral-dependent impaired loans, net of specific reserves totaled $2.6 million and $1.8 million at March 31, 2017 and December 31, 2016, respectively.

NOTE 7. Securities

This table provides the major components of securities available for sale ("AFS") and held to maturity ("HTM") at amortized cost and estimated fair value at March 31, 2017 and December 31, 2016:

	March 31, 2017				December 31, 2016			
(In thousands)	Amortized cost	Gross unrealized gains	Gross unrealized losses	Estimated fair value	Amortized cost	Gross unrealized gains	Gross unrealized losses	Estimated fair value
Available for sale:								
U.S. Government sponsored entities	$3,745	$ 2	$ (26)	$ 3,721	$			