FARMERS NATIONAL BANC CORP /OH/
Form 10-Q
August 08, 2017

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

Quarterly Report Pursuant to Section 13 or 15(d) of the

Securities Exchange Act of 1934

For the Quarterly period ended June 30, 2017

Commission file number 001-35296

FARMERS NATIONAL BANC CORP.

(Exact name of registrant as specified in its charter)

OHIO (State or other jurisdiction of incorporation or organization)	34-1371693 (I.R.S. Employer Identification No)
20 South Broad Street Canfield, OH (Address of principal executive offices)	44406 (Zip Code)

(330) 533-3341

(Registrant’s telephone number, including area code)

Not applicable

(Former name, former address and former fiscal year, if changed since last report)

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

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

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

Large accelerated filer		Accelerated filer
Non-accelerated filer	(Do not check if a small reporting company)	Small 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

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

Class	Outstanding at July 31, 2017
Common Stock, No Par Value	27,078,261 shares

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CONSOLIDATED BALANCE SHEETS

FARMERS NATIONAL BANC CORP. AND SUBSIDIARIES

	(In Thousands of Dollars)	
	June 30,	December 31,
(Unaudited)	2017	2016
ASSETS		
Cash and due from banks	$ 20,717	$ 19,678
Federal funds sold and other	43,923	22,100
TOTAL CASH AND CASH EQUIVALENTS	64,640	41,778
Securities available for sale	391,628	369,995
Loans held for sale	583	355
Loans	1,505,273	1,427,635
Less allowance for loan losses	11,746	10,852
NET LOANS	1,493,527	1,416,783
Premises and equipment, net	23,046	23,225
Goodwill	37,164	37,164
Other intangibles	7,261	7,990
Bank owned life insurance	30,440	30,048
Other assets	37,375	38,775
TOTAL ASSETS	$ 2,085,664	$ 1,966,113
LIABILITIES AND STOCKHOLDERS' EQUITY		
Deposits:		
Noninterest-bearing	$ 387,596	$ 366,870
Interest-bearing	1,153,407	1,157,886
TOTAL DEPOSITS	1,541,003	1,524,756
Short-term borrowings	289,184	198,460
Long-term borrowings	9,643	15,036
Other liabilities	19,147	14,645
TOTAL LIABILITIES	1,858,977	1,752,897
Commitments and contingent liabilities		
Stockholders' Equity:		
Common Stock - Authorized 35,000,000 shares; issued 27,713,811 in 2017 and 2016	178,761	178,317
Retained earnings	51,329	42,547
Accumulated other comprehensive income (loss)	1,316	(2,791)
Treasury stock, at cost; 647,219 shares in 2017 and 666,147 in 2016	(4,719)	(4,857)
TOTAL STOCKHOLDERS' EQUITY	226,687	213,216
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$ 2,085,664	$ 1,966,113

See accompanying notes

CONSOLIDATED STATEMENTS OF INCOME

FARMERS NATIONAL BANC CORP. AND SUBSIDIARIES

	(In Thousands except Per Share Data)			
	For the Three Months Ended		For the Six Months Ended	
	June 30,	June 30,	June 30,	June 30,
(Unaudited)	2017	2016	2017	2016
INTEREST AND DIVIDEND INCOME				
Loans, including fees	$17,402	$15,623	$33,885	$30,893
Taxable securities	1,265	1,288	2,383	2,725
Tax exempt securities	1,170	899	2,241	1,788
Dividends	123	113	238	226
Federal funds sold and other interest income	82	27	145	65
TOTAL INTEREST AND DIVIDEND INCOME	20,042	17,950	38,892	35,697
INTEREST EXPENSE				
Deposits	1,117	793	2,031	1,500
Short-term borrowings	501	144	828	319
Long-term borrowings	51	124	129	242
TOTAL INTEREST EXPENSE	1,669	1,061	2,988	2,061
NET INTEREST INCOME	18,373	16,889	35,904	33,636
Provision for loan losses	950	990	2,000	1,770
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	17,423	15,899	33,904	31,866
NONINTEREST INCOME				
Service charges on deposit accounts	989	987	1,940	1,922
Bank owned life insurance income	191	202	392	414
Trust fees	1,523	1,564	3,201	3,060
Insurance agency commissions	672	293	1,346	432
Security gains (losses)	(14)	41	(1)	41
Retirement plan consulting fees	399	496	912	985
Investment commissions	253	356	475	592
Net gains on sale of loans	891	540	1,498	942
Debit card and EFT fees	836	657	1,489	1,283
Other operating income	315	601	690	1,012
TOTAL NONINTEREST INCOME	6,055	5,737	11,942	10,683
NONINTEREST EXPENSES				
Salaries and employee benefits	8,853	7,740	17,140	15,294
Occupancy and equipment	1,631	1,616	3,218	3,280
State and local taxes	424	394	841	787
Professional fees	775	754	1,522	1,283
Merger related costs	104	224	166	513
Advertising	317	363	561	708
FDIC insurance	234	286	469	569
Intangible amortization	364	335	729	672
Core processing charges	717	580	1,372	1,218

Telephone and data	242	233	483	449
Other operating expenses	2,103	2,258	3,876	4,454
TOTAL NONINTEREST EXPENSES	15,764	14,783	30,377	29,227
INCOME BEFORE INCOME TAXES	7,714	6,853	15,469	13,322
INCOME TAXES	2,004	1,833	3,976	3,504
NET INCOME	$5,710	$5,020	$11,493	$9,818
EARNINGS PER SHARE - basic and diluted	$0.21	$0.19	$0.42	$0.36

See accompanying notes

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CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

FARMERS NATIONAL BANC CORP. AND SUBSIDIARIES

	(In Thousands of Dollars)			
	For the Three Months Ended		For the Six Months Ended	
	June 30,	June 30,	June 30,	June 30,
(Unaudited)	2017	2016	2017	2016
NET INCOME	$5,710	$5,020	$11,493	$9,818
Other comprehensive income:				
Net unrealized holding gains on available for sale securities	5,946	5,020	6,321	8,377
Reclassification adjustment for (gains) losses realized in income	14	(41)	1	(41)
Net unrealized holding gains	5,960	4,979	6,322	8,336
Income tax effect	(2,087)	(1,745)	(2,215)	(2,920)
Other comprehensive income, net of tax	3,873	3,234	4,107	5,416
TOTAL COMPREHENSIVE INCOME	$9,583	$8,254	$15,600	$15,234

See accompanying notes

CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY

FARMERS NATIONAL BANC CORP. AND SUBSIDIARIES

(Unaudited)	(In Thousands of Dollars) For the Six Months Ended June 30, 2017
COMMON STOCK	
Beginning balance	$ 178,317
Issued 18,928 shares under the Long Term Incentive Plan	(133)
Stock compensation expense for 603,203 unvested shares	577
Ending balance	178,761
RETAINED EARNINGS	
Beginning balance	42,547
Net income	11,493
Decrease as a result of shares issued under the Long Term Incentive Plan	(5)
Dividends declared at $.05 per share	(2,706)
Ending balance	51,329
ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS)	
Beginning balance	(2,791)
Other comprehensive income	4,107
Ending balance	1,316
TREASURY STOCK, AT COST	
Beginning balance	(4,857)
Shares issued under the Long Term Incentive Plan	138
Ending balance	(4,719)
TOTAL STOCKHOLDERS' EQUITY	$ 226,687

See accompanying notes.

CONSOLIDATED STATEMENTS OF CASH FLOWS

FARMERS NATIONAL BANC CORP. AND SUBSIDIARIES

	(In Thousands of Dollars) Six Months Ended	
	June 30,	June 30,
(Unaudited)	2017	2016
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	$11,493	$9,818
Adjustments to reconcile net income to net cash from operating activities:		
Provision for loan losses	2,000	1,770
Depreciation and amortization	1,767	1,787
Net amortization of securities	1,706	1,100
Security (gains) losses	1	(41)
(Gain) loss on land and building sales, net	18	(262)
Stock compensation expense	577	401
(Gain) loss on sale of other real estate owned	(24)	221
Earnings on bank owned life insurance	(392)	(414)
Origination of loans held for sale	(32,119)	(29,698)
Proceeds from loans held for sale	33,389	30,672
Net gains on sale of loans	(1,498)	(942)
Net change in other assets and liabilities	(2,950)	(6,807)
NET CASH FROM OPERATING ACTIVITIES	13,968	7,605
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from maturities and repayments of securities available for sale	22,659	29,331
Proceeds from sales of securities available for sale	54,482	9,191
Purchases of securities available for sale	(87,203)	(12,252)
Purchase of restricted stock	(892)	0
Loan originations and payments, net	(78,828)	(62,905)
Proceeds from sale of other real estate owned	354	407
Proceeds from land and building sales	0	352
Additions to premises and equipment	(664)	(464)
Net cash (paid) received in business combinations	0	(1,073)
NET CASH FROM INVESTING ACTIVITIES	(90,092)	(37,413)
CASH FLOWS FROM FINANCING ACTIVITIES		
Net change in deposits	16,247	38,395
Net change in short-term borrowings	90,724	2,344
Repayment of long-term borrowings	(5,417)	(2,432)
Cash dividends paid	(2,706)	(2,161)
Proceeds from reissuance of treasury shares	138	0
Repurchase of common shares	0	(168)
NET CASH FROM FINANCING ACTIVITIES	98,986	35,978
NET CHANGE IN CASH AND CASH EQUIVALENTS	22,862	6,170
Beginning cash and cash equivalents	41,778	56,014

Ending cash and cash equivalents	$64,640	$62,184
Supplemental cash flow information:		
Interest paid	$2,988	$2,001
Income taxes paid	$2,500	$4,300
Supplemental noncash disclosures:		
Transfer of loans to other real estate	$84	$258
Security purchases not settled	$6,957	$3,105
Issuance of stock awards	$133	$0
Issuance of stock for business combinations	$0	$1,138

See accompanying notes

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

Principles of Consolidation:

Farmers National Banc Corp. (“Company”) is a Financial Holding Company registered under the Bank Holding Company Act of 1956, as amended. The Company provides full banking services through its nationally chartered subsidiary, The Farmers National Bank of Canfield (“Bank”). The Bank acquired Bowers Insurance Agency, Inc. (“Bowers”) and consolidated the activity of the Bowers with Farmers National Insurance (“Insurance”) during 2016. The Company acquired First National Bank of Orrville (“First National Bank”) a subsidiary of National Bancshares Corporation (“NBOH”) and 1st National Community Bank (“FNCB”), a subsidiary of Tri-State 1st Banc, Inc. (“Tri-State”) during 2015 and consolidated all activity of both acquisitions within the Bank. Farmers National Captive, Inc. (“Captive”) was formed during the third quarter of 2016 and is a wholly-owned insurance subsidiary of the Company that provides property and casualty insurance coverage to the Company and its subsidiaries. The Captive pools resources with thirteen other similar insurance company subsidiaries of financial institutions to spread a limited amount of risk among themselves and to provide insurance where not currently available or economically feasible in today’s insurance market place. The consolidated financial statements also include the accounts of the Bank’s subsidiaries; Insurance and Farmers of Canfield Investment Co. (“Investments”). The Company provides trust services through its subsidiary, Farmers Trust Company (“Trust”), retirement consulting services through National Associates, Inc. (“NAI”) and insurance services through the Bank’s subsidiary, Insurance. The consolidated financial statements include the accounts of the Company, the Bank and its subsidiaries, along with the Trust, NAI and Captive. All significant intercompany balances and transactions have been eliminated in the consolidation.

Basis of Presentation:

The unaudited condensed consolidated financial statements have been prepared in conformity with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by U.S. generally accepted accounting principles (“U.S. GAAP”) for complete financial statements. The financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company’s 2016 Annual Report to Shareholders included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2016. The interim consolidated financial statements include all adjustments (consisting of only normal recurring items) that, in the opinion of management, are necessary for a fair presentation of the financial position and results of operations for the periods presented. The results of operations for the interim periods disclosed herein are not necessarily indicative of the results that may be expected for a full year. Certain items included in the prior period financial statements were reclassified to conform to the current period presentation. There was no effect on net income or total stockholders’ equity.

Estimates:

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Segments:

The Company provides a broad range of financial services to individuals and companies in northeastern Ohio. Operations are managed and financial performance is primarily aggregated and reported in three lines of business, the Bank segment, the Trust segment and the Retirement Consulting segment.

Comprehensive Income:

Comprehensive income consists of net income and other comprehensive income. Other comprehensive income consists of unrealized gains and losses on securities available for sale and changes in the funded status of the post-retirement health plan, which are recognized as separate components of stockholders equity, net of tax effects. For all periods presented there was no change in the funded status of the post-retirement health plan.

New Accounting Standards:

During April of 2017, the FASB issued ASU 2017-08, Receivables—Nonrefundable Fees and Other Costs (Subtopic 310-20): Premium Amortization on Purchased Callable Debt Securities. Under current U.S. GAAP, a premium is typically amortized to the maturity date when a callable debt security is purchased at a premium, even if the holder is certain the call will be exercised. As a result, upon the exercise of a call on a callable debt security held at a premium, the unamortized premium is recorded as a loss in earnings. The new standard shortens the amortization period for the premium to the earliest call date to more closely align interest income recorded on bonds held at a premium or a discount with the economics of the underlying instrument. The standard takes effect for public business entities for fiscal years and interim periods within those fiscal years, beginning after December 15, 2018. Early adoption is permitted, including adoption in an interim period. The Company amortizes the premium to the expected call date currently and therefore does not expect the adoption of this ASU to have a material impact on its Consolidated Financial Statements.

In January 2017, the FASB issued ASU 2017-04, Intangibles - Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment. This ASU eliminates Step 2 from the goodwill impairment test. Instead, under the new guidance, an entity is to perform its annual goodwill impairment test by comparing the fair value of a reporting unit with its carrying amount. An impairment charge would be recognized for the amount by which the carrying amount exceeds the reporting unit's fair value. The new guidance is effective for annual reporting periods, and interim reporting periods within those annual periods, beginning after December 15, 2019. Early adoption is permitted for interim or annual goodwill impairment tests performed on testing dates after January 1, 2017. The adoption of this guidance is not expected to have an impact on the Company's Consolidated Financial Statements.

In June 2016, the FASB issued ASU 2016-13: Financial Instruments-Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments. The ASU requires an organization to measure all expected credit losses for financial assets held at the reporting date based on historical experience, current conditions, and reasonable and supportable forecasts. Financial institutions and other organizations will now use forward-looking information to better inform their credit loss estimates. Many of the loss estimation techniques applied today will still be permitted, although the inputs to those techniques will change to reflect the full amount of expected credit losses. Organizations will continue to use judgment to determine which loss estimation method is appropriate for their circumstances. Additionally, the ASU amends the accounting for credit losses on available-for-sale debt securities and purchased financial assets with credit deterioration. ASU 2016-13 is effective for public companies for annual periods beginning after December 15, 2019, including interim periods within those fiscal years. Entities will apply the standard's provisions as a cumulative-effect adjustment to retained earnings as of the beginning of the first reporting period in which the guidance is adopted. The Company has begun to accumulate historical credit information and created a task force in preparation for the adoption of ASU 2016-13, but management has not determined the impact the new standard will have on the Consolidated Financial Statements.

In March 2016, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) 2016-09: Compensation – Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting. The amendments in ASU 2016-09 simplify several aspects of the accounting for employee share-based payment transactions, including the accounting for income taxes, forfeitures and statutory tax withholding requirements, as well as classification in the statement of cash flows. ASU 2016-09 was effective for public companies for interim and annual reporting periods beginning after December 15, 2016, with early adoption permitted. The Company adopted the ASU 2016-09 on January 1, 2017 which had no material impact on the Consolidated Financial Statements and disclosures.

In February 2016, FASB issued ASU 2016-02 (Topic 842): Leases. The main objective of ASU 2016-02 is to provide users with useful, transparent, and complete information about leasing transactions. ASU 2016-02 requires the rights and obligations associated with leasing arrangements be reflected on the balance sheet in order to increase transparency and comparability among organizations. Under the updated guidance, lessees will be required to recognize a right-to-use asset and a liability to make a lease payment and disclose key information about leasing arrangements. ASU 2016-02 is effective for public companies for interim and annual reporting periods beginning after December 15, 2018, with early adoption permitted. The Company expects the adoption of this ASU could require capitalization of certain leases in the amount of $2.6 million on the balance sheet as an asset and a related liability of equal amount with no material income statement effect. Therefore the Company does not expect the adoption of this ASU to have a material impact to its Consolidated Financial Statements.

In January 2016, FASB issued ASU 2016-01: Financial Instruments – Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities. The main objective of ASU 2016-01 is to enhance the reporting model for financial instruments to provide users of financial statements with more decision-useful information. ASU 2016-01 addresses certain aspects of recognition, measurement, presentation, and disclosure of financial instruments. Some of the amendments in ASU 2016-01 include the following: 1) Require equity investments (except those accounted for under the equity method of accounting or those that result in consolidation of the investee) to be measured at fair value with changes in fair value recognized in net income; 2) Simplify the impairment assessment of equity investments without readily determinable fair values by requiring a qualitative assessment to identify impairment; 3) Require public business entities to use the exit price notion when measuring the fair value of financial instruments for disclosure purposes; and 4) Require an entity to present separately in other comprehensive income the portion of the total change in the fair value of a liability resulting from a change in the instrument-specific credit risk when the entity has elected to measure the liability at fair value; among others. The amendments of ASU 2016-01 are effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. Management anticipates the impact of the adoption of this guidance on the Company’s consolidated financial statements to be limited.

In May 2014, FASB issued ASU 2014-09: Revenue from Contracts with Customers (Topic 606). The ASU creates a new topic, Topic 606, to provide guidance on revenue recognition for entities that enter into contracts with customers to transfer goods or services or enter into contracts for the transfer of nonfinancial assets. The core principle of the guidance is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. Additional disclosures are required to provide quantitative and qualitative information regarding the nature, amount, timing, and uncertainty of revenue and cash flows arising from contracts with customers. The new guidance is effective for annual reporting periods, and interim reporting periods within those annual periods, beginning after December 15, 2017. Early adoption is permitted only as of annual reporting periods beginning after December 15, 2016. Management anticipates the impact of the adoption of this guidance on the Company's consolidated financial statements to be limited. There will be no impact to core revenue which is mainly interest income less interest expense. Management is still assessing the impact from other non-interest income sources, specifically, deposit fees, trust income and retirement consulting income.

Business Combinations:

On March 13, 2017, the Company announced the agreement and plan of merger with Monitor Bancorp, Inc. ("Monitor"), the holding company for Monitor Bank. Pursuant to the agreement, the actual consideration to be paid will be calculated based on Monitor's consolidated tangible book value per share as of March 31, 2017, plus the after-tax proceeds of the anticipated sale of Monitor's interest in the Monitor Wealth Group (in aggregate, "March 31 TBV"). Each shareholder of Monitor will be entitled to elect to receive consideration in cash or in Farmers' common shares, subject to an overall limitation of 85% of the shares being exchanged for Farmers' shares and 15% for cash. Based on a current estimate of March 31 TBV, the transaction would be valued at approximately $7.8 million with $1.4 million of goodwill recorded. The merger is expected to qualify as a tax-free reorganization for those Monitor shareholders electing to receive Farmers' shares. The transaction has received customary regulatory approval and is now subject to Monitor shareholder approval. The Company expects the transaction to close in the third quarter of 2017.

On June 1, 2016, the Bank completed the acquisition of the Bowers Insurance Agency, Inc., and merged all activity of Bowers with Insurance, the Bank's wholly-owned insurance agency subsidiary. The Bowers group is engage in selling insurance including commercial, farm, home, and auto property/casualty insurance and will help to meet the needs of all the Company's customers. The transaction involved both cash and 123,280 shares of stock totaling $3.2 million, including up to $1.2 million of future payments, contingent upon Bowers meeting performance targets, with an estimated fair value at the acquisition date of $880 thousand. The first of three contingent payments of cash and stock were made, during July 2017, totaling $316 thousand, which reduce the earnout payable to $564 thousand. The acquisition is part of the Company's plan to increase the levels of noninterest income and to complement the existing insurance services currently being offered.

Goodwill of $1.8 million, which is recorded on the balance sheet, arising from the acquisition consisted largely of synergies and the cost savings resulting from the combining of the companies. The goodwill was determined not to be deductible for income tax purposes. The fair value of other intangible assets of $1.6 million is related to client relationships, company name and noncompetition agreements.

The following table summarizes the consideration paid for Bowers and the amounts of the assets acquired and liabilities assumed on the closing date of the acquisition.

(In Thousands of Dollars)	
Consideration	
Cash	$1,137
Stock	1,138
Contingent consideration	880
Fair value of total consideration transferred	$3,155
Fair value of assets acquired	
Cash	$64
Premises and equipment	290
Other assets	34
Total assets acquired	388
Fair value of liabilities assumed	124
Net assets acquired	$264
Assets and liabilities arising from acquisition	
Identified intangible assets	1,630
Deferred tax liability	(588)
Goodwill created	1,849
Total net assets acquired	$3,155

The following table presents pro forma information as if the above acquisition that occurred during June 2016 actually took place at the beginning of 2016. The pro forma information includes adjustments for merger related costs, amortization of intangibles arising from the transaction and the related income tax effects. The pro forma financial information is not necessarily indicative of the results of operations that would have occurred had the transactions been effective on the assumed date.

(In thousands of dollars except per share results)	For Three Months Ended June 30, 2016	For Six Months Ended
Net interest income	$16,889	$33,636
Net income	$5,003	$9,789
Basic and diluted earnings per share	$0.18	$0.36

Securities:

The following table summarizes the amortized cost and fair value of the available-for-sale investment securities portfolio at June 30, 2017 and December 31, 2016 and the corresponding amounts of unrealized gains and losses recognized in accumulated other comprehensive income:

(In Thousands of Dollars)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
June 30, 2017				
U.S. Treasury and U.S. government sponsored entities	$ 5,467	$ 14	$ (20)	$ 5,461
State and political subdivisions	175,801	3,101	(734)	178,168
Corporate bonds	1,238	7	(4)	1,241
Mortgage-backed securities - residential	171,498	1,153	(895)	171,756
Collateralized mortgage obligations - residential	19,652	3	(558)	19,097
Small Business Administration	15,825	0	(274)	15,551
Equity securities	173	182	(1)	354
Totals	$ 389,654	$ 4,460	$ (2,486)	$ 391,628

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(In Thousands of Dollars)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
December 31, 2016				
U.S. Treasury and U.S. government sponsored entities	$ 5,970	$ 5	$ (54)	$ 5,921
State and political subdivisions	157,014	1,049	(2,760)	155,303
Corporate bonds	1,343	4	(8)	1,339
Mortgage-backed securities - residential	171,215	1,019	(2,552)	169,682
Collateralized mortgage obligations - residential	21,397	1	(705)	20,693
Small Business Administration	17,236	0	(530)	16,706
Equity securities	168	185	(2)	351
Totals	$ 374,343	$ 2,263	$ (6,611)	$ 369,995

Proceeds from the sale of portfolio securities were $11.2 million during the three and $54.5 during the six month period ended June 30, 2017. Gross gains of $168 thousand and $730 thousand along with gross losses of $182 thousand and $731 thousand were realized on these sales during the three and six month periods ended June 30, 2017. Proceeds from the sale of portfolio securities were $9.2 million during the three and six month period ended June 30, 2016. Gross gains were $193 thousand along with gross losses of $152 thousand during the same three and six month period ended June 30, 2016.

The amortized cost and fair value of the debt securities portfolio are shown by expected maturity. Expected maturities may differ from contractual maturities if issuers have the right to call or prepay obligations with or without call or prepayment penalties. Securities not due at a single maturity date are shown separately.

	June 30, 2017	
(In Thousands of Dollars)	Amortized Cost	Fair Value
Maturity		
Within one year	$ 11,945	$ 11,997
One to five years	50,282	51,090
Five to ten years	104,186	105,633
Beyond ten years	16,093	16,150
Mortgage-backed, collateralized mortgage obligations and Small Business Administration securities	206,975	206,404
Total	$ 389,481	$ 391,274

The following table summarizes the investment securities with unrealized losses at June 30, 2017 and December 31, 2016, aggregated by major security type and length of time in a continuous unrealized loss position. Unrealized losses for U.S. Treasury and U.S. government sponsored entities for more than twelve months, rounded to less than $1 thousand in 2016.

(In Thousands of Dollars)	Less than 12 Months Fair Value	Unrealized Loss	12 Months or Longer Fair Value	Unrealized Loss	Total Fair Value	Unrealized Loss
June 30, 2017						
Available-for-sale						
U.S. Treasury and U.S. government sponsored entities	$2,392	$ (20)	$0	$ 0	$2,392	$ (20)
State and political subdivisions	33,517	(727)	291	(7)	33,808	(734)
Corporate bonds	582	(4)	0	0	582	(4)
Mortgage-backed securities - residential	61,503	(856)	1,861	(39)	63,364	(895)
Collateralized mortgage obligations - residential	7,241	(81)	10,271	(477)	17,512	(558)
Small Business Administration	8,176	(77)	7,336	(197)	15,512	(274)
Equity securities	28	(1)	0	0	28	(1)
Total	$113,439	$ (1,766)	$19,759	$ (720)	$133,198	$ (2,486)

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(In Thousands of Dollars)	Less than 12 Months Fair Value	Unrealized Loss	12 Months or Longer Fair Value	Unrealized Loss	Total Fair Value	Unrealized Loss
December 31, 2016						
Available-for-sale						
U.S. Treasury and U.S. government sponsored entities	$4,015	$ (54)	$502	$ 0	$4,517	$ (54)
State and political subdivisions	92,560	(2,745)	286	(15)	92,846	(2,760)
Corporate bonds	786	(8)	0	0	786	(8)
Mortgage-backed securities - residential	98,348	(1,823)	29,743	(729)	128,091	(2,552)
Collateralized mortgage obligations - residential	7,956	(108)	10,972	(597)	18,928	(705)
Small Business Administration	8,770	(205)	7,890	(325)	16,660	(530)
Equity securities	44	(2)	0	0	44	(2)
Total	$212,479	$ (4,945)	$49,393	$ (1,666)	$261,872	$ (6,611)

Other-Than-Temporary-Impairment

Management evaluates securities for other-than-temporary impairment (“OTTI”) at least on a quarterly basis, and more frequently when economic or market conditions warrant such an evaluation. Investment securities are generally evaluated for OTTI under FASB Accounting Standards Codification (“ASC”) 320, Investments – Debt and Equity Securities. Consideration is given to the length of time and the extent to which the fair value has been less than cost, the financial condition and near-term prospects of the issuer, whether the market decline was affected by macroeconomic conditions and whether the Company has the intent to sell the debt security or more likely than not will be required to sell the debt security before its anticipated recovery. In analyzing an issuer’s financial condition, the Company may consider whether the securities are issued by the federal government or its agencies, or U.S. government sponsored enterprises, whether downgrades by bond rating agencies have occurred, and the results of reviews of the issuer’s financial condition. The assessment of whether an other-than-temporary decline exists involves a high degree of subjectivity and judgment, and is based on the information available to management at a point in time.

When OTTI occurs, the amount of the OTTI recognized in earnings depends on whether an entity intends to sell the security or it is more likely than not it will be required to sell the security before recovery of its amortized cost basis. If an entity intends to sell or it is more likely than not it will be required to sell the security before recovery of its amortized cost basis, the OTTI shall be recognized in earnings equal to the entire difference between the investment’s amortized cost basis and its fair value at the balance sheet date. The previous amortized cost basis less the OTTI recognized in earnings becomes the new amortized cost basis of the investment. 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 or loss. The 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, the Company’s security portfolio consisted of 535 securities, 103 of which were in an unrealized loss position. The majority of the unrealized losses on the Company’s securities are related to its holdings of mortgage-backed securities, collateralized mortgage obligations, state and political subdivision securities, and Small

Business Administration securities as discussed below.

Unrealized losses on debt securities issued by state and political subdivisions have not been recognized into income. These securities have maintained their investment grade ratings and management does not have the intent and does not expect to be required to sell these securities before their anticipated recovery. The fair value is expected to recover as the securities approach their maturity date.

All of the Company's holdings of collateralized mortgage obligations and residential mortgage-backed securities were issued by U.S. government-sponsored entities. Unrealized losses on these securities have not been recognized into income. Because the decline in fair value is attributable to changes in interest rates and illiquidity, and not credit quality, the issues are guaranteed by the issuing entity which the U.S. government has affirmed its commitment to support, and because the Company does not have the intent to sell these residential mortgage-backed securities and it is likely that it will not be required to sell the securities before their anticipated recovery, the Company does not consider these securities to be OTTI.

Management does not believe any unrealized losses on Small Business Administration securities represent an OTTI. The securities are issued and backed by the full faith and credit of the U.S. government and the Company does not have the intent and does not anticipate that it will be required to sell these securities before their anticipated recovery. The fair value of these securities is expected to recover as they approach their maturity.

Loans:

Loan balances were as follows:

(In Thousands of Dollars)	June 30, 2017	December 31, 2016
Originated loans:		
Commercial real estate		
Owner occupied	$124,664	$109,750
Non-owner occupied	182,900	165,861
Farmland	50,873	34,155
Other	78,496	70,823
Commercial		
Commercial and industrial	184,854	171,145
Agricultural	30,355	24,598
Residential real estate		
1-4 family residential	246,771	224,222
Home equity lines of credit	66,035	59,642
Consumer		
Indirect	166,835	156,633
Direct	27,995	26,663
Other	8,066	7,611
Total originated loans	$1,167,844	$1,051,103
Acquired loans:		
Commercial real estate		
Owner occupied	$56,330	$60,928
Non-owner occupied	20,969	24,949
Farmland	47,884	54,204
Other	13,485	14,665
Commercial		
	30,822	33,626

Commercial and industrial		
Agricultural	13,575	16,024
Residential real estate		
1-4 family residential	101,690	112,015
Home equity lines of credit	31,495	34,795
Consumer		
Direct	17,429	21,681
Other	129	247
Total acquired loans	$333,808	$373,134
Net Deferred loan costs	3,621	3,398
Allowance for loan losses	(11,746)	(10,852)
Net loans	$1,493,527	$1,416,783

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Purchased credit impaired loans

As part of the NBOH acquisition the Company acquired various loans that displayed evidence of deterioration of credit quality since origination and which was probable that all contractually required payments would not be collected. The carrying amounts and contractually required payments of these loans which are included in the loan balances above are summarized in the following tables:

(In Thousands of Dollars)	June 30, 2017	December 31, 2016
Commercial real estate		
Owner occupied	$707	$ 689
Non-owner occupied	394	436
Commercial		
Commercial and industrial	1,148	1,213
Total outstanding balance	$2,249	$ 2,338
Carrying amount, net of allowance of $0 in 2017 and 2016	$1,815	$ 1,864

Accretable yield, or income expected to be collected, is shown in the table below:

(In Thousands of Dollars)	Six Months Ended June 30, 2017
Beginning balance	$ 247
New loans purchased	0
Accretion of income	(38)
Ending balance	$ 209

The key assumptions considered include probability of default and the amount of actual prepayments after the acquisition date. Prepayments affect the estimated life of the loans and could change the amount of interest income and principal expected to be collected. In reforecasting future estimated cash flows, credit loss expectations are adjusted as necessary. There were no adjustments to forecasted cash flows that impacted the allowance for loan losses for the three and six month periods ended June 30, 2017.

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

Three Months Ended June 30, 2017

(In Thousands of Dollars)	Commercial Real Estate	Commercial	Residential Real Estate	Consumer	Unallocated	Total
Allowance for loan losses						
Beginning balance	$ 3,638	$ 1,846	$ 2,321	$ 2,813	$ 701	$ 11,319
Provision for loan losses	365	198	5	464	(82)	950
Loans charged off	(67)	(113)	(36)	(509)	0	(725)
Recoveries	18	5	20	159	0	202
Total ending allowance balance	$ 3,954	$ 1,936	$ 2,310	$ 2,927	$ 619	$ 11,746

Six Months Ended June 30, 2017

(In Thousands of Dollars)	Commercial Real Estate	Commercial	Residential Real Estate	Consumer	Unallocated	Total
Allowance for loan losses						
Beginning balance	$ 3,577	$ 1,874	$ 2,205	$ 2,766	$ 430	$ 10,852
Provision for loan losses	442	215	114	1,040	189	2,000
Loans charged off	(207)	(215)	(42)	(1,204)	0	(1,668)
Recoveries	142	62	33	325	0	562
Total ending allowance balance	$ 3,954	$ 1,936	$ 2,310	$ 2,927	$ 619	$ 11,746

Three Months Ended June 30, 2016

(In Thousands of Dollars)	Commercial Real Estate	Commercial	Residential Real Estate	Consumer	Unallocated	Total
Allowance for loan losses						
Beginning balance	$ 3,181	$ 1,452	$ 1,914	$ 2,218	$ 625	$9,390
Provision for loan losses	335	212	196	521	(274)	990
Loans charged off	(307)	(37)	(44)	(431)	0	(819)
Recoveries	1	7	15	136	0	159
Total ending allowance balance	$ 3,210	$ 1,634	$ 2,081	$ 2,444	$ 351	$9,720

Six Months Ended June 30, 2016

(In Thousands of Dollars)	Commercial Real Estate	Commercial	Residential Real Estate	Consumer	Unallocated	Total
Allowance for loan losses						
Beginning balance	$ 3,127	$ 1,373	$ 1,845	$ 2,160	$ 473	$8,978
Provision for loan losses	378	276	271	967	(122)	1,770
Loans charged off	(307)	(37)	(78)	(975)	0	(1,397)
Recoveries	12	22	43	292	0	369
Total ending allowance balance	$ 3,210	$ 1,634	$ 2,081	$ 2,444	$ 351	$9,720

The following tables present the balance in the allowance for loan losses and the recorded investment in loans by portfolio segment, based on impairment method as of June 30, 2017 and December 31, 2016. The recorded investment in loans includes the unpaid principal balance and unamortized loan origination fees and costs, but excludes accrued interest receivable, which is not considered to be material:

June 30, 2017

(In Thousands of Dollars)	Commercial Real Estate	Commercial	Residential Real Estate	Consumer	Unallocated	Total
Allowance for loan losses:						
Ending allowance balance attributable to loans:						
Individually evaluated for impairment	$ 29	$ 4	$ 59	$ 0	$ 0	$ 92

Collectively evaluated for impairment	3,889	1,920	2,218	2,923	619	11,569
Acquired loans collectively evaluated for impairment	36	12	33	4	0	85
Acquired with deteriorated credit quality	0	0	0	0	0	0
Total ending allowance balance	$ 3,954	$ 1,936	$ 2,310	$ 2,927	$ 619	$ 11,746
Loans:						
Loans individually evaluated for impairment	$ 1,948	$ 253	$ 3,388	$ 108	$ 0	$ 5,697
Loans collectively evaluated for impairment	433,957	214,691	309,146	208,407	0	1,166,201
Acquired loans	137,534	43,550	132,947	17,529	0	331,560
Acquired with deteriorated credit quality	969	846	0	0	0	1,815
Total ending loans balance	$ 574,408	$ 259,340	$ 445,481	$ 226,044	$ 0	$ 1,505,273

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December 31, 2016

(In Thousands of Dollars)	Commercial Real Estate	Commercial	Residential Real Estate	Consumer	Unallocated	Total
Allowance for loan losses:						
Ending allowance balance attributable to loans:						
Individually evaluated for impairment	$ 86	$ 111	$ 52	$ 0	$ 0	$ 249
Collectively evaluated for impairment	3,491	1,763	2,153	2,766	430	10,603
Acquired loans collectively evaluated for impairment	0	0	0	0	0	0
Acquired with deteriorated credit quality	0	0	0	0	0	0
Total ending allowance balance	$ 3,577	$ 1,874	$ 2,205	$ 2,766	$ 430	$ 10,852
Loans:						
Loans individually evaluated for impairment	$ 3,457	$ 477	$ 3,308	$ 96	$ 0	$ 7,338
Loans collectively evaluated for impairment	376,632	195,146	280,215	196,081	0	1,048,074
Acquired loans	153,228	48,536	146,672	21,923	0	370,359
Acquired with deteriorated credit quality	968	896	0	0	0	1,864
Total ending loans balance	$ 534,285	$ 245,055	$ 430,195	$ 218,100	$ 0	$ 1,427,635

The following tables present information related to impaired loans by class of loans as of June 30, 2017 and December 31, 2016:

(In Thousands of Dollars)	Unpaid Principal Balance	Recorded Investment	Allowance for Loan Losses Allocated
June 30, 2017			
With no related allowance recorded:			
Commercial real estate			
Owner occupied	$ 1,198	$ 681	$ 0
Non-owner occupied	18	18	0
Commercial			
Commercial and industrial	203	182	0
Agricultural	123	0	0
Residential real estate			
1-4 family residential	2,466	2,221	0
Home equity lines of credit	306	284	0
Consumer	207	108	0
Subtotal	4,521	3,494	0
With an allowance recorded:			
Commercial real estate			
Owner occupied	163	163	7
Non-owner occupied	1,086	1,086	22
Commercial			
Commercial and industrial	71	71	4
Residential real estate			
1-4 family residential	831	795	56
Home equity lines of credit	91	88	3
Subtotal	2,242	2,203	92
Total	$ 6,763	$ 5,697	$ 92

(In Thousands of Dollars)	Unpaid Principal Balance	Recorded Investment	Allowance for Loan Losses Allocated
December 31, 2016			
With no related allowance recorded:			
Commercial real estate			
Owner occupied	$ 1,974	$ 1,456	$ 0
Non-owner occupied	332	331	0
Commercial			
Commercial and industrial	205	184	0
Residential real estate			
1-4 family residential	2,650	2,403	0
Home equity lines of credit	195	179	0
Consumer	205	96	0
Subtotal	5,561	4,649	0
With an allowance recorded:			
Commercial real estate			
Owner occupied	173	173	14
Non-owner occupied	1,118	1,118	30
Farmland	380	379	42
Commercial			
Commercial and industrial	75	75	4
Agricultural	219	218	107
Residential real estate			
1-4 family residential	661	642	51
Home equity lines of credit	84	84	1
Subtotal	2,710	2,689	249
Total	$ 8,271	$ 7,338	$ 249

The following tables present the average recorded investment in impaired loans by class and interest income recognized by loan class for the three and six month periods ended June 30, 2017 and 2016:

(In Thousands of Dollars)	Average Recorded Investment For Three Months Ended June 30, 2017	2016	Interest Income Recognized For Three Months Ended June 30, 2017	2016
With no related allowance recorded:				
Commercial real estate				
Owner occupied	$682	$1,266	$2	$28
Non-owner occupied	18	334	0	0
Farmland	17	0	0	0
Commercial				
Commercial and industrial	182	331	1	5
Agricultural production	15	0	0	0
Residential real estate				
1-4 family residential	2,251	2,249	35	33
Home equity lines of credit	326	227	3	3
Consumer	105	86	4	3
Subtotal	3,596	4,493	45	72
With an allowance recorded:				
Commercial real estate				
Owner occupied	164	908	2	9
Non-owner occupied	1,092	1,401	14	19
Commercial				
Commercial and industrial	72	78	1	1
Residential real estate				
1-4 family residential	794	845	9	11
Home equity lines of credit	84	86	1	1
Consumer	0	0	0	0
Subtotal	2,206	3,318	27	41
Total	$5,802	$7,811	$72	$113

(In Thousands of Dollars)	Average Recorded Investment For Six Months Ended June 30, 2017	2016	Interest Income Recognized For Six Months Ended June 30, 2017	2016
With no related allowance recorded:				
Commercial real estate				
Owner occupied	$851	$1,786	$5	$38
Non-owner occupied	122	335	1	4
Farmland	24	0	0	0
Commercial				
Commercial and industrial	183	472	2	10
Agricultural	21	0	0	0
Residential real estate				
1-4 family residential	2,315	2,270	72	71
Home equity lines of credit	276	234	7	6
Consumer	90	101	6	6
Subtotal	3,882	5,198	93	135
With an allowance recorded:				
Commercial real estate				
Owner occupied	166	1,248	4	18
Non-owner occupied	1,099	1,435	28	38
Farmland	126	0	0	0
Commercial				
Commercial and industrial	73	79	2	2
Agricultural	100	0	0	0
Residential real estate				
1-4 family residential	784	797	17	20
Home equity lines of credit	84	86	2	2
Subtotal	2,432	3,645	53	80
Total	$6,314	$8,843	$146	$215

Cash basis interest recognized during the three and six month periods ended June 30, 2017 and 2016 was materially equal to interest income recognized.

Nonaccrual loans and loans past due 90 days or more still on accrual include both smaller balance homogeneous loans that are collectively evaluated for impairment and individually classified impaired loans.

The following table presents the recorded investment in nonaccrual and loans past due 90 days or more still on accrual by class of loans as of June 30, 2017 and December 31, 2016:

	June 30, 2017		December 31, 2016	
(In Thousands of Dollars)	Nonaccrual	Loans Past Due 90 Days or More Still Accruing	Nonaccrual	Loans Past Due 90 Days or More Still Accruing
Originated loans:				
Commercial real estate				
Owner occupied	$549	$ 0	$958	$ 0
Non-owner occupied	18	0	343	0
Farmland	51	0	58	0
Commercial				
Commercial and industrial	297	0	400	0
Agricultural	2	0	12	0
Residential real estate				
1-4 family residential	1,667	537	1,929	295
Home equity lines of credit	532	22	202	118
Consumer				
Indirect	396	182	298	438
Direct	6	36	9	65
Other	0	0	0	16
Total originated loans	$3,518	$ 777	$4,209	$ 932
Acquired loans:				
Commercial real estate				
Owner occupied	$34	$ 0	$85	$ 0
Non-owner occupied	185	0	0	0
Other	0	0	24	0
Farmland	0	0	380	0
Commercial				
Commercial and industrial	879	0	961	0
Agricultural	18	0	236	0
Residential real estate				
1-4 family residential	402	124	386	545
Home equity lines of credit	215	38	119	109
Consumer				
Direct	135	30	89	95
Total acquired loans	$1,868	$ 192	$2,280	$ 749
Total loans	$5,386	$ 969	$6,489	$ 1,681

The following tables present the aging of the recorded investment in past due loans as of June 30, 2017 and December 31, 2016 by class of loans:

(In Thousands of Dollars)	30-59 Days Past Due	60-89 Days Past Due	90 Days or More Past Due and Nonaccrual	Total Past Due	Loans Not Past Due	Total
June 30, 2017						
Originated loans:						
Commercial real estate						
Owner occupied	$0	$0	$ 549	$549	$123,757	$124,306
Non-owner occupied	0	0	18	18	182,415	182,433
Farmland	0	0	51	51	50,763	50,814
Other	0	0	0	0	78,184	78,184
Commercial						
Commercial and industrial	121	0	297	418	184,079	184,497
Agricultural	35	0	2	37	30,409	30,446
Residential real estate						
1-4 family residential	1,520	465	2,204	4,189	242,033	246,222
Home equity lines of credit	123	80	554	757	65,314	66,071
Consumer						
Indirect	1,924	430	578	2,932	169,298	172,230
Direct	456	240	42	738	27,452	28,190
Other	30	17	0	47	8,018	8,065
Total originated loans:	$4,209	$1,232	$ 4,295	$9,736	$1,161,722	$1,171,458
Acquired loans:						
Commercial real estate						
Owner occupied	$323	$49	$ 34	$406	$55,925	$56,331
Non-owner occupied	0	0	185	185	20,769	20,954
Farmland	0	0	0	0	47,885	47,885
Other	0	0	0	0	13,501	13,501
Commercial						
Commercial and industrial	69	1	879	949	29,872	30,821
Agricultural	10	0	18	28	13,548	13,576
Residential real estate						
1-4 family residential	479	184	526	1,189	100,504	101,693
Home equity lines of credit	116	0	253	369	31,126	31,495
Consumer						
Direct	341	40	165	546	16,884	17,430
Other	0	0	0	0	129	129
Total acquired loans	$1,338	$274	$ 2,060	$3,672	$330,143	$333,815
Total loans	$5,547	$1,506	$ 6,355	$13,408	$1,491,865	$1,505,273

(In Thousands of Dollars)	30-59 Days Past Due	60-89 Days Past Due	90 Days or More Past Due and Nonaccrual	Total Past Due	Loans Not Past Due	Total
December 31, 2016						
Originated loans:						
Commercial real estate						
Owner occupied	$0	$0	$ 958	$958	$108,475	$109,433
Non-owner occupied	0	0	343	343	165,105	165,448
Farmland	0	0	58	58	34,057	34,115
Other	0	0	0	0	70,542	70,542
Commercial						
Commercial and industrial	90	0	400	490	170,242	170,732
Agricultural	0	29	12	41	24,632	24,673
Residential real estate						
1-4 family residential	3,368	356	2,224	5,948	217,752	223,700
Home equity lines of credit	77	37	320	434	59,248	59,682
Consumer						
Indirect	2,844	696	736	4,276	157,437	161,713
Direct	744	213	74	1,031	25,815	26,846
Other	92	28	16	136	7,476	7,612
Total originated loans	$7,215	$1,359	$ 5,141	$13,715	$1,040,781	$1,054,496
Acquired loans:						
Commercial real estate						
Owner occupied	$8	$205	$ 85	$298	$60,630	$60,928
Non-owner occupied	134	0	0	134	24,815	24,949
Farmland	83	0	380	463	53,741	54,204
Other	0	0	24	24	14,642	14,666
Commercial						
Commercial and industrial	278	0	961	1,239	32,387	33,626
Agricultural	21	0	236	257	15,767	16,024
Residential real estate						
1-4 family residential	1,556	504	931	2,991	109,027	112,018
Home equity lines of credit	152	9	228	389	34,406	34,795
Consumer						
Direct	938	184	184	1,306	20,376	21,682
Other	100	0	0	100	147	247
Total acquired loans	$3,270	$902	$ 3,029	$7,201	$365,938	$373,139
Total loans	$10,485	$2,261	$ 8,170	$20,916	$1,406,719	$1,427,635

Troubled Debt Restructurings:

Total troubled debt restructurings were $5.8 million and $7.0 million at June 30, 2017 and December 31, 2016, respectively. The Company has allocated $92 thousand and $101 thousand of specific reserves to customers whose loan terms have been modified in troubled debt restructurings at June 30, 2017 and December 31, 2016, respectively. There were no commitments to lend additional amounts to borrowers with loans that were classified as troubled debt restructurings at June 30, 2017 and at December 31, 2016.

During the three and six month periods ended June 30, 2017 and 2016, the terms of certain loans were modified as troubled debt restructurings. The modification of the terms of such loans included one or a combination of the following: a reduction of the stated interest rate of the loan; an extension of the maturity date at a stated rate of interest lower than the current market rate for new debt with similar risk; or a legal concession. During the six month period ended June 30, 2017, the terms of such loans included a reduction of the stated interest rate of the loan in the range of 0.49% and 1.89% and extensions of the maturity dates on these and other troubled debt restructurings in the range of 6 to 132 months. During the same six month period in 2016, the terms of such loans included a reduction of the stated interest rate of the loan by 1.24% and an extension of the maturity date by 120 months.

The following table presents loans by class modified as troubled debt restructurings that occurred during the three and six month periods ended June 30, 2017 and 2016:

Three Months Ended June 30, 2017 (In thousands of Dollars)	Number of Loans	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
Originated loans:			
Residential real estate			
1-4 family residential	1	$ 16	$ 16
Home equity lines of credit	3	70	70
Indirect	10	64	64
Total originated loans	14	$ 150	$ 150
Acquired loans:			
Residential real estate			
1-4 family residential	2	24	24
Consumer	1	29	29
Total acquired loans	3	$ 53	$ 53
Total loans	17	$ 203	$ 203

Six Months Ended June 30, 2017 (In Thousands of Dollars)	Number of Loans	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
Originated loans:			
Residential real estate			
1-4 family residential	7	$ 300	$ 303
Home equity lines of credit	8	164	164
Indirect	14	80	80
Total originated loans	29	$ 544	$ 547
Acquired loans:			
Residential real estate			
1-4 family residential	2	24	24
Home equity lines of credit	1	57	57
Consumer	1	29	29
Total acquired loans	4	$ 110	$ 110
Total loans	33	$ 654	$ 657

Three Months Ended June 30, 2016 (In thousands of Dollars)	Number of Loans	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
Originated loans:			
Residential real estate			
1-4 family residential	3	$ 188	$ 188

Indirect	5		37		37
Total originated loans	8	$	225	$	225
Acquired loans:					
Residential real estate					
1-4 family residential	2		68		68
Total loans	10	$	293	$	293

Six Months Ended June 30, 2016 (In Thousands of Dollars)	Number of Loans	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
Originated loans:			
Residential real estate			
1-4 family residential	6	$ 235	$ 236
Indirect	13	114	114
Total originated loans	19	$ 349	$ 350
Acquired loans:			
Residential real estate			
1-4 family residential	2	68	68
Consumer	1	33	33
Total acquired loans	3	$ 101	$ 101
Total loans	22	$ 450	$ 451

There were $17 thousand and $30 thousand in charge offs and a $17 thousand and $30 thousand increase to the provision for loan losses during the three and six month period ended June 30, 2017, as a result of troubled debt restructurings. There were $316 thousand and $327 thousand in charge offs during the three and six month periods ended June 30, 2016, respectively. There was no increase to the provision for loan losses during the three month period ended June 30, 2016 and an $11 thousand increase to the provision during the six month period ended June 30, 2016, as a result of troubled debt restructuring.

There were no loans for which there was a payment default within twelve months following the modification of the troubled debt restructuring during the three month and six month period ended June 30, 2017. A loan is considered to be in payment default once it is 30 days contractually past due under the modified terms.

There were two commercial loans, one residential real estate loan and one home equity line of credit for which there was a payment default within twelve months following the modification of the troubled debt restructuring during the three month and six month periods ended June 30, 2016. The two commercial loans were past due at June 30, 2016. There was no provision recorded as a result of the defaults during 2016. A loan is considered to be in payment default once it is 30 days contractually past due under the modified terms.

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 establishes a risk rating at origination for all commercial loan and commercial real estate relationships. For relationships over $750 thousand, management monitors the loans on an ongoing basis for any changes in the borrower’s ability to service their debt. Management also affirms the risk ratings for the loans and leases in their respective portfolios on an annual basis. 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. Special mention assets are not adversely classified and do not expose an institution to sufficient risk to warrant adverse classification.

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. Substandard loans are characterized by the distinct possibility that the institution 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 characteristic 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.

As of June 30, 2017 and December 31, 2016, and based on the most recent analysis performed, the risk category of loans by class of loans is as follows:

(In Thousands of Dollars)	Pass	Special Mention	Sub standard	Total
June 30, 2017				
Originated loans:				
Commercial real estate				
Owner occupied	$122,180	$473	$1,653	$124,306
Non-owner occupied	181,833	446	154	182,433
Farmland	50,717	46	51	50,814
Other	77,564	362	258	78,184
Commercial				
Commercial and industrial	181,499	1,977	1,021	184,497
Agricultural	30,151	25	270	30,446
Total originated loans	$643,944	$3,329	$3,407	$650,680
Acquired loans:				
Commercial real estate				
Owner occupied	$54,121	$486	$1,724	$56,331
Non-owner occupied	20,215	388	351	20,954
Farmland	47,114	0	771	47,885
Other	12,813	574	114	13,501
Commercial				
Commercial and industrial	28,591	50	2,180	30,821
Agricultural	12,680	396	500	13,576
Total acquired loans	$175,534	$1,894	$5,640	$183,068
Total loans	$819,478	$5,223	$9,047	$833,748

(In Thousands of Dollars)	Pass	Special Mention	Sub standard	Total
December 31, 2016				
Originated loans:				
Commercial real estate				
Owner occupied	$106,448	$490	$2,495	$109,433
Non-owner occupied	162,465	522	2,461	165,448
Farmland	34,057	0	58	34,115
Other	69,947	325	270	70,542
Commercial				
Commercial and industrial	167,062	2,720	950	170,732
Agricultural	24,395	253	25	24,673
Total originated loans	$564,374	$4,310	$6,259	$574,943

Acquired loans:				
Commercial real estate				
Owner occupied	$58,655	$ 707	$1,566	$60,928
Non-owner occupied	23,577	1,195	177	24,949
Farmland	53,039	0	1,165	54,204
Other	14,060	464	142	14,666
Commercial				
Commercial and industrial	30,543	311	2,772	33,626
Agricultural	14,856	685	483	16,024
Total acquired loans	$194,730	$ 3,362	$6,305	$204,397
Total loans	$759,104	$ 7,672	$12,564	$779,340

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The Company considers the performance of the loan portfolio and its impact on the allowance for loan losses. For residential, consumer indirect and direct loan classes, the Company also evaluates credit quality based on the aging status of the loan, which was previously presented, and by payment activity. In the 1-4 family residential real estate portfolio at June 30, 2017, there were $236 thousand of other real estate owned properties and $748 thousand of properties in foreclosure. Other real estate owned and foreclosure properties were $357 thousand and $371 thousand at December 31, 2016, respectively.

The following tables present the recorded investment in residential, consumer indirect and direct auto loans based on payment activity as of June 30, 2017 and December 31, 2016. Nonperforming loans are loans past due 90 days or more and still accruing interest and nonaccrual loans.

	Residential Real Estate		Consumer		
(In Thousands of Dollars)	1-4 Family Residential	Home Equity Lines of Credit	Indirect	Direct	Other
June 30, 2017					
Originated loans:					
Performing	$244,018	$65,517	$171,652	$28,148	$8,065
Nonperforming	2,204	554	578	42	0
Total originated loans	$246,222	$66,071	$172,230	$28,190	$8,065
Acquired loans:					
Performing	$101,167	$31,242	$0	$17,265	$129
Nonperforming	526	253	0	165	0
Total acquired loans	101,693	31,495	0	17,430	129
Total loans	$347,915	$97,566	$172,230	$45,620	$8,194

	Residential Real Estate		Consumer		
(In Thousands of Dollars)	1-4 Family Residential	Home Equity Lines of Credit	Indirect	Direct	Other
December 31, 2016					
Originated loans:					
Performing	$221,476	$59,362	$160,977	$26,772	$7,596
Nonperforming	2,224	320	736	74	16
Total originated loans	$223,700	$59,682	$161,713	$26,846	$7,612
Acquired loans:					
Performing	$111,087	$34,567	$0	$21,498	$247
Nonperforming	931	228	0	184	0
Total acquired loans	112,018	34,795	0	21,682	247
Total loans	$335,718	$94,477	$161,713	$48,528	$7,859

Interest-Rate Swaps:

The Company uses a program that utilizes interest-rate swaps as part of its asset/liability management strategy. The interest-rate swaps are used to help manage the Company's interest rate risk position and not as derivatives for trading purposes. The notional amount of the interest-rate swaps does not represent amounts exchanged by the parties. The amount exchanged is determined by reference to the notional amount and the other terms of the individual interest-rate swap agreements.

The objective of the interest-rate swaps is to protect the related fixed rate commercial real estate loans from changes in fair value due to changes in interest rates. The Company has a program whereby it lends to its borrowers at a fixed rate with the loan agreement containing a two-way yield maintenance provision, which will be invoked in the event of prepayment of the loan, and is expected to exactly offset the fair value of unwinding the swap. The yield maintenance provision represents an embedded derivative which is bifurcated from the host loan contract and, as such, the swaps and embedded derivatives are not designated as hedges. Accordingly, both instruments are carried at fair value and changes in fair value are reported in current period earnings.

Summary information about these interest-rate swaps at periods ended June 30, 2017 and December 31, 2016 is as follows:

	June 30, 2017	December 31, 2016
Notional amounts (In thousands)	$31,542	$ 34,360
Weighted average pay rate on interest-rate swaps	4.37 %	4.34 %
Weighted average receive rate on interest-rate swaps	3.51 %	3.04 %
Weighted average maturity (years)	4.5	4.8
Fair value of combined interest-rate swaps (In thousands)	$587	$ 685

The fair value of the yield maintenance provisions and interest-rate swaps is recorded in other assets and other liabilities, respectively, in the consolidated balance sheets. Changes in the fair value of the yield maintenance provisions and interest-rate swaps are reported in earnings, as other noninterest income in the consolidated statements of income. For the three month and six month periods ended June 30, 2017 and 2016 there were no net gains or losses recognized in earnings.

Earnings Per Share:

The computation of basic and diluted earnings per share is shown in the following table:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
Basic EPS				
Net income (In thousands)	$5,710	$5,020	$11,493	$9,818
Weighted average shares outstanding	27,337,403	27,086,422	27,309,237	27,056,056
Basic earnings per share	$0.21	$0.19	$0.42	$0.36
Diluted EPS				
Net income (In thousands)	$5,710	$5,020	$11,493	$9,818
Weighted average shares outstanding for basic earnings per share	27,337,403	27,086,422	27,309,237	27,056,056
Dilutive effect of restricted stock awards	57,273	18,110	61,440	14,258
Weighted average shares for diluted earnings per share	27,394,676	27,104,532	27,370,677	27,070,314
Diluted earnings per share	$0.21	$0.19	$0.42	$0.36

There were no restricted stock awards that were considered anti-dilutive for the three and six month periods ended June 30, 2017 and 2016.

Stock Based Compensation:

During 2017, the Company, with the approval of shareholders, created the 2017 Equity Incentive Plan (the "2017 Plan"). The 2017 Plan permits the award of up to 800 thousand shares to the Company's directors and employees to attract and retain exceptional personnel, motivate performance and most importantly to help align the interests of Farmers' executives with those of the Company's shareholders. There were 57,748 service time based shares and 64,993 performance based shares granted under the 2017 Plan during the six month period ended June 30, 2017, as shown in the table below. The actual number of performance based stock awards issued will depend on certain performance conditions which are mainly average return on equity compared to a group of peer companies over a three year vesting period.

During 2012, the Company, with the approval of shareholders, created the 2012 Equity Incentive Plan (the "2012 Plan"). The 2012 Plan permitted the award of up to 500 thousand shares to the Company's directors and employees to promote the Company's long-term financial success by motivating performance through long-term incentive compensation and to better align the interests of its employees with those of its shareholders. There were no additional shares granted under the Plan during the six month period ended June 30, 2017 as detailed in the table below. Any new restricted stock awards will be issued under the 2017 Plan described above.

The restricted stock awards were granted with a fair value price equal to the market price of the Company's common stock at the date of the grant. Expense recognized for both Plans was $397 thousand and $577 thousand for the three and six month periods ended June 30, 2017, respectively. During the prior periods, the expense recognized was $200 thousand and $401 thousand for the three and six month periods ended June 30, 2016, respectively. As of June 30, 2017, there was $3 million of total unrecognized compensation expense related to the nonvested shares granted under the Plans. The remaining cost is expected to be recognized over 2.5 years.

The following is the activity under the Plans during the six month period ended June 30, 2017.

	Six Months Ended June 30, 2017			
	2017 Incentive Plan		2012 Incentive Plan	
	Maximum Awarded Units	Weighted Average Grant Date Fair Value	Maximum Awarded Units	Weighted Average Grant Date Fair Value
Beginning unvested units	0	0	499,390	$ 8.30
Granted	122,741	$ 13.67	0	0
Vested	0	0	(18,928)	7.00
Forfeited	0	0	0	0
Ending unvested units	122,741	$ 13.67	480,462	$ 8.35

Other Comprehensive Income:

The following table represents the details of other comprehensive income for the three and six month periods ended June 30, 2017 and 2016.

	Three Months Ended June 30, 2017		
(In Thousands of Dollars)	Pre-tax	Tax	After-Tax
Unrealized holding gains on available-for-sale securities during the period	$5,946	$(2,081)	$ 3,865
Reclassification adjustment for (gains) losses included in net income (1)	14	(6)	8
Net unrealized gains on available-for-sale securities	$5,960	$(2,087)	$ 3,873

	Three Months Ended June 30, 2016		
(In Thousands of Dollars)	Pre-tax	Tax	After-Tax
Unrealized holding gains on available-for-sale securities during the period	$5,020	$(1,759)	$ 3,261
Reclassification adjustment for (gains) losses included in net income (1)	(41)	14	(27)
Net unrealized gains on available-for-sale securities	$4,979	$(1,745)	$ 3,234

Six Months Ended June 30, 2017

(In Thousands of Dollars)	Pre-tax	Tax	After-Tax
Unrealized holding gains on available-for-sale securities during the period	$6,321	$(2,214)	$ 4,107
Reclassification adjustment for (gains) included in net income (1)	1	(1)	0
Net other comprehensive income (loss)	$6,322	$(2,215)	$ 4,107

	Six Months Ended June 30, 2016		
(In Thousands of Dollars)	Pre-tax	Tax	After-Tax
Unrealized holding gains on available-for-sale securities during the period	$8,377	$(2,934)	$ 5,443
Reclassification adjustment for (gains) losses included in net income (1)	(41)	14	(27)
Net unrealized gains on available-for-sale securities	$8,336	$(2,920)	$ 5,416

(1) Pre-tax reclassification adjustments relating to available-for-sale securities are reported in security gains and the tax impact is included in income tax expense on the consolidated statements of income.

Regulatory Capital Matters

Banks and bank holding companies are subject to various regulatory capital requirements administered by the federal banking agencies. Capital adequacy guidelines and, additionally for banks, prompt corrective action regulations, involve quantitative measures of assets, liabilities, and certain off-balance sheet items calculated under regulatory accounting practices. The new minimum capital requirements associated with the Basel Committee on capital and liquidity regulation (Basel III) are being phased in and began on January 1, 2015 and will continue through January 1, 2019. Capital amounts and classifications are also subject to qualitative judgments by regulators. Failure to meet capital requirements can initiate regulatory action by regulators that, if undertaken, could have a direct material effect on the financial statements. Management believes as of June 30, 2017, the Company and the Bank meet all capital adequacy requirements to which they are subject.

The FDIC and other federal banking regulators revised the risk-based capital requirements applicable to financial holding companies and insured depository institutions, including the Company and the Bank, to make them consistent with agreements that were reached by the Basel Committee on Banking Supervision ("Basel III").

The common equity tier 1 capital, tier 1 capital and total capital ratios are calculated by dividing the respective capital amounts by risk-weighted assets. The leverage ratio is calculated by dividing tier 1 capital by adjusted average total assets.

Basel III limits capital distributions and certain discretionary bonus payments if the banking organization does not hold a "capital conservation buffer" consisting of 2.5% of common equity tier 1 capital, tier 1 capital and total capital to risk-weighted assets in addition to the amount necessary to meet minimum risk-based capital requirements. The capital conservation buffer phase in began January 1, 2016 and will increase each year until fully implemented at 2.5% on January 1, 2019. The additional capital conservation buffer is 1.25% for the year of 2017 and was 0.625% during 2016. Excluding the additional buffer, Basel III requires the Company and the Bank to maintain (i) a minimum ratio of common equity tier 1 capital to risk-weighted assets of at least 4.5%, (ii) a minimum ratio of tier 1 capital to risk-weighted assets of at least 6.0%, (iii) a minimum ratio of total capital to risk-weighted assets of at least 8.0% and (iv) a minimum leverage ratio of at least 4.0%.

Prompt corrective action regulations provide five classifications: well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized, and critically undercapitalized, although these terms are not used to represent overall financial condition. If only adequately capitalized, regulatory approval is required to accept brokered deposits. If undercapitalized, capital distributions are limited, as is asset growth and expansion, and capital restoration plans are required. At June 30, 2017 and December 31, 2016, the most recent regulatory notifications categorized the Bank as well capitalized under the regulatory framework for prompt corrective action. There are no conditions or events since that notification that management believes have changed the institution's category.

Actual and required capital amounts and ratios are presented below at June 30, 2017 and December 31, 2016:

	Actual Amount	Ratio	Requirement For Capital Adequacy Purposes: Amount	Ratio	To be Well Capitalized Under Prompt Corrective Action Provisions: Amount	Ratio
June 30, 2017						
Common equity tier 1 capital ratio						
Consolidated	$189,221	11.80%	$72,175	4.5 %	N/A	N/A
Bank	178,540	11.14%	72,134	4.5 %	$104,194	6.5 %
Total risk based capital ratio						
Consolidated	203,152	12.67%	128,311	8.0 %	N/A	N/A
Bank	190,286	11.87%	128,239	8.0 %	160,298	10.0%
Tier I risk based capital ratio						
Consolidated	191,406	11.93%	96,233	6.0 %	N/A	N/A
Bank	178,540	11.14%	96,179	6.0 %	128,239	8.0 %
Tier I leverage ratio						
Consolidated	191,406	9.47 %	80,833	4.0 %	N/A	N/A
Bank	178,540	8.91 %	80,144	4.0 %	100,181	5.0 %
December 31, 2016						
Common equity tier 1 capital ratio						
Consolidated	$180,475	11.69%	$69,474	4.5 %	N/A	N/A
Bank	171,064	11.12%	69,244	4.5 %	$100,020	6.5 %
Total risk based capital ratio						
Consolidated	193,487	12.53%	123,509	8.0 %	N/A	N/A
Bank	181,916	11.82%	123,101	8.0 %	153,877	10.0%
Tier I risk based capital ratio						
Consolidated	182,635	11.83%	92,632	6.0 %	N/A	N/A
Bank	171,064	11.12%	92,326	6.0 %	123,101	8.0 %
Tier I leverage ratio						
Consolidated	182,635	9.41 %	77,596	4.0 %	N/A	N/A
Bank	171,064	8.91 %	76,792	4.0 %	95,990	5.0 %

Fair Value

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 reporting entity'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:

Investment Securities: The Company uses a third party service to estimate fair value on available for sale securities on a monthly basis. This service provider is considered a leading evaluation pricing service for U.S. domestic fixed income securities. They subscribe to multiple third-party pricing vendors, and supplement that information with matrix pricing methods. The fair values for investment securities are determined by quoted market prices in active markets, if available (Level 1). For securities where quoted prices are not available, fair values are calculated based on quoted prices for similar assets in active markets, quoted prices for similar assets in markets that are not active or inputs other than quoted prices, which provide a reasonable basis for fair value determination.

Such inputs may include interest rates and yield curves, volatilities, prepayment speeds, credit risks and default rates. Inputs used are derived principally from observable market data (Level 2). For securities where quoted prices or market prices of similar securities are not available, fair values are calculated using discounted cash flows or other market indicators (Level 3). The fair values of Level 3 investment securities are determined by using unobservable inputs to measure fair value of assets for which there is little, if any market activity at the measurement date, using reasonable inputs and assumptions based on the best information at the time, to the extent that inputs are available without undue cost and effort. For the period ended June 30, 2017 and for the year ended December 31, 2016, the fair value of Level 3 investment securities was immaterial.

Derivative Instruments: The fair values of derivative instruments are based on valuation models using observable market data as of the measurement date (Level 2).

Impaired Loans: At the time loans are considered impaired, collateral dependent impaired loans are valued at the lower of cost or fair value and non-collateral dependent loans are valued based on discounted cash flows. Impaired loans carried at fair value generally receive specific allocations of the allowance for loan losses. For collateral dependent loans fair value is commonly based on recent real estate appraisals. 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 typically result in a Level 3 classification of the inputs for determining fair value. Non-real estate collateral may be valued using an appraisal, net book value per the borrower’s financial statements, or aging reports, adjusted or discounted based on management’s historical knowledge, changes in market conditions from the time of the valuation, and management’s expertise and knowledge of the client and client’s business, resulting in a Level 3 fair value classification. Impaired loans are evaluated on a quarterly basis for additional impairment and adjusted accordingly.

Other Real Estate Owned: Assets acquired through or instead of loan foreclosure are initially recorded at fair value less costs to sell when acquired, establishing a new cost basis. These assets are subsequently accounted for at lower of cost or fair value less estimated costs to sell. Fair values are commonly based on recent real estate appraisals. These appraisals may use 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 independent appraisers to adjust for differences between the comparable sales and income data available. Such adjustments are usually significant and typically result in a Level 3 classification of the inputs for determining fair value.

Appraisals for both collateral-dependent impaired loans and other real estate owned are performed by certified general appraisers (for commercial and commercial real estate properties) or certified residential appraisers (for residential properties) whose qualifications and licenses have been reviewed and verified by the Company. Once received, a member of the Appraisal Department reviews the assumptions and approaches utilized in the appraisal as well as the overall resulting fair value in comparison with independent data sources such as recent market data or industry-wide statistics. On an annual basis, the Company compares the actual selling price of collateral that has been sold to the most recent appraised value to determine what adjustments should be made to appraisals to arrive at fair value.

Assets measured at fair value on a recurring basis are summarized below:

	Fair Value Measurements at June 30, 2017 Using:			
(In Thousands of Dollars)	Carrying Value	Quoted Prices in Active Markets	Significant Other Observable Inputs	Significant Unobservable Inputs

		for Identical Assets (Level 1)	(Level 2)	(Level 3)
Financial Assets				
Investment securities available-for sale				
U.S. Treasury and U.S. government sponsored entities	$5,461	$ 0	$ 5,461	$ 0
State and political subdivisions	178,168	0	178,168	0
Corporate bonds	1,241	0	1,241	0
Mortgage-backed securities-residential	171,756	0	171,746	10
Collateralized mortgage obligations	19,097	0	19,097	0
Small Business Administration	15,551	0	15,551	0
Equity securities	354	354	0	0
Total investment securities	$391,628	$ 354	$ 391,264	$ 10
Loan yield maintenance provisions	$587	$ 0	$ 587	$ 0
Financial Liabilities				
Interest rate swaps	$587	$ 0	$ 587	$ 0

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(In Thousands of Dollars)	Carrying Value	Fair Value Measurements at December 31, 2016 Using: Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Financial Assets				
Investment securities available-for sale				
U.S. Treasury and U.S. government sponsored entities	$5,921	$ 0	$ 5,921	$ 0
State and political subdivisions	155,303	0	155,303	0
Corporate bonds	1,339	0	1,339	0
Mortgage-backed securities-residential	169,682	0	169,670	12
Collateralized mortgage obligations	20,693	0	20,693	0
Small Business Administration	16,706	0	16,706	0
Equity securities	351	351	0	0
Total investment securities	$369,995	$ 351	$ 369,632	$ 12
Loan yield maintenance provisions	$685	$ 0	$ 685	$ 0
Financial Liabilities				
Interest rate swaps	$685	$ 0	$ 685	$ 0

There were no significant transfers between Level 1 and Level 2 during the three and six month periods ended June 30, 2017 and 2016. For additional information related to yield maintenance provisions and interest rate swaps see Interest –Rate Swaps note.

The table below presents a reconciliation of all assets measured at fair value on a recurring basis using significant unobservable inputs (Level 3):

(In Thousands of Dollars)	Investment Securities Available-for-sale (Level 3) Three Months ended June 30, 2017	2016	Six Months ended June 30, 2017	2016
Beginning Balance	$11	$14	$12	$15
Total unrealized gains or losses:				
Included in other comprehensive income	0	0	0	0
Transfers from level 2	0	1,806	0	1,806

Repayments, calls and maturities	(1)	0	(2)	(1)
Ending Balance	$10	$1,820	$10	$1,820

Assets measured at fair value on a non-recurring basis are summarized below:

	Fair Value Measurements at June 30, 2017 Using:			
(In Thousands of Dollars)	Carrying Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Financial Assets				
Impaired loans				
Commercial real estate				
Owner occupied	$23	$ 0	$ 0	$ 23
1–4 family residential	158	0	0	158
Consumer	6	0	0	6

		Fair Value Measurements at December 31, 2016 Using:		
(In Thousands of Dollars)	Carrying Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Financial Assets				
Impaired loans				
Commercial real estate				
Owner occupied	$23	$ 0	$ 0	$ 23
Farmland	339	0	0	339
Commercial				
Agricultural	113	0	0	113
1–4 family residential	77	0	0	77
Consumer	2	0	0	2
Other real estate owned				
1–4 family residential	16	0	0	16

Impaired loans that are measured for impairment using the fair value of the collateral for collateral dependent loans, had a principal balance of $207 thousand with a valuation allowance of $21 thousand at June 30, 2017, resulting in $153 thousand in additional provision for loan losses for the three month period. At December 31, 2016, impaired loans had a principal balance of $727 thousand, with a valuation allowance of $173 thousand. Loans measured at fair value at June 30, 2016 resulted in no additional provision for loan losses for the six month period ending June 30, 2016. Excluded from the fair value of impaired loans, at June 30, 2017 and December 31, 2016, discussed above are $2.0 million of loans classified as troubled debt restructurings and measured using the present value of cash flows, which is not considered an exit price.

Impaired commercial real estate loans, both owner-occupied and non-owner occupied are valued by independent external appraisals. These external appraisals are prepared using the sales comparison approach and income approach valuation techniques. Management makes subsequent unobservable adjustments to the impaired loan appraisals. Impaired loans other than commercial real estate and other real estate owned are not considered material.

The following table presents quantitative information about Level 3 fair value measurements for financial instruments measured at fair value on a non-recurring basis at the periods ended June 30, 2017 and December 31, 2016:

June 30, 2017	Fair value	Valuation Technique(s)	Unobservable Input(s)	Range (Weighted Average)
Impaired loans				
Commercial real estate	$ 23	Sales Comparison	Adjustment for differences between comparable sales	(24.02%)
Residential	158	Sales comparison	Adjustment for differences between comparable sales	(28.20%) - 20.17%

				0.48%
Consumer	6	Sales comparison	Adjustment for differences between comparable sales	(20.50%) - 20.50% 0.00%

December 31, 2016	Fair value	Valuation Technique(s)	Unobservable Input(s)	Range (Weighted Average)
Impaired loans				
Commercial real estate	$ 23	Sales comparison	Adjustment for differences between comparable sales	(24.02%)
	339	Quoted price for loan relationship	Offer price	35.77%
Commercial	113	Quoted price for loan relationship	Offer price	34.98%
Residential	77	Sales comparison	Adjustment for differences between comparable sales	(12.97%) - 14.22% (3.38%)
Consumer	2	Sales comparison	Adjustment for differences between comparable sales	(20.00%) - 20.00% (0.00%)
Other Real Estate owned residential	16	Sales comparison	Adjustment for differences between comparable sales	(10.36%) - 17.10% (1.90%)

The carrying amounts and estimated fair values of financial instruments not previously disclosed at June 30, 2017 and December 31, 2016 are as follows:

		Fair Value Measurements at June 30, 2017 Using:			
(In Thousands of Dollars)	Carrying Amount	Level 1	Level 2	Level 3	Total
Financial assets					
Cash and cash equivalents	$ 64,640	$20,717	$43,923	$0	$64,640
Restricted stock	10,475	n/a	n/a	n/a	n/a
Loans held for sale	583	0	583	0	583
Loans, net	1,493,527	0	0	1,498,659	1,498,659
Mortgage servicing rights	1,068	0	1,068	0	1,068
Accrued interest receivable	5,910	0	2,082	3,828	5,910
Financial liabilities					
Deposits	1,541,003	1,301,709	236,451	0	1,538,160
Short-term borrowings	289,184	0	289,184	0	289,184
Long-term borrowings	9,643	0	9,582	0	9,582
Accrued interest payable	602	34	568	0	602

Fair Value Measurements at December 31, 2016 Using:

(In Thousands of Dollars)	Carrying Amount	Level 1	Level 2	Level 3	Total
Financial assets					
Cash and cash equivalents	$ 41,778	$19,678	$22,100	$0	$41,778
Restricted stock	9,583	n/a	n/a	n/a	n/a
Loans held for sale	355	0	365	0	365
Loans, net	1,416,783	0	0	1,406,951	1,406,951
Mortgage servicing rights	854	0	854	0	854
Accrued interest receivable	5,504	0	1,924	3,580	5,504
Financial liabilities					
Deposits	1,524,756	1,289,037	232,410	0	1,521,447
Short-term borrowings	198,460	0	198,460		