STEWARDSHIP FINANCIAL CORP
Form 10-Q
August 09, 2016

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

FORM 10-Q

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

For the quarterly period ended June 30, 2016

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

For the transition period from __________ to __________

Commission file number 1-33377
Stewardship Financial Corporation
(Exact name of registrant as specified in its charter)

New Jersey	22-3351447
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
630 Godwin Avenue, Midland Park, NJ	07432
(Address of principal executive offices)	(Zip Code)

(201) 444-7100
(Registrant's telephone number, including area code)

(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 x No o

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

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 the definitions of “large accelerated filer,” “accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act.

Large accelerated filer o	Accelerated filer o
Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company x

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

The number of shares outstanding, net of treasury stock, of the Registrant's Common Stock, no par value, as of August 5, 2016 was 6,114,585.

Stewardship Financial Corporation
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PART I – FINANCIAL INFORMATION

Item 1. Financial Statements

Stewardship Financial Corporation and Subsidiary
Consolidated Statements of Financial Condition

	June 30, 2016 (Unaudited)	December 31, 2015
Assets		
Cash and due from banks	$13,471,000	$10,731,000
Other interest-earning assets	430,000	179,000
Cash and cash equivalents	13,901,000	10,910,000
Securities available-for-sale	98,533,000	93,354,000
Securities held to maturity; estimated fair value of $66,772,000 (2016) and $61,281,000 (2015)	65,666,000	60,738,000
Federal Home Loan Bank of New York stock, at cost	2,650,000	2,608,000
Loans held for sale	581,000	1,522,000
Loans, net of allowance for loan losses of $8,388,000 (at June 30, 2016) and $8,823,000 (at December 31, 2015)	529,225,000	517,556,000
Premises and equipment, net	6,678,000	6,799,000
Accrued interest receivable	1,912,000	1,967,000
Other real estate owned, net	834,000	880,000
Bank owned life insurance	16,320,000	14,111,000
Other assets	6,287,000	7,443,000
Total assets	$742,587,000	$717,888,000
Liabilities and Shareholders' equity		
Liabilities		
Deposits:		
Noninterest-bearing	$160,461,000	$147,828,000
Interest-bearing	466,008,000	456,925,000
Total deposits	626,469,000	604,753,000
Federal Home Loan Bank of New York advances	40,000,000	40,000,000
Subordinated Debentures and Subordinated Notes	23,219,000	23,186,000
Accrued interest payable	782,000	791,000
Accrued expenses and other liabilities	1,431,000	1,585,000
Total liabilities	691,901,000	670,315,000
Shareholders' equity		
Common stock, no par value; 10,000,000 shares authorized; 6,113,030 and 6,085,528 shares issued and outstanding at June 30, 2016, and December 31, 2015, respectively	41,571,000	41,410,000
Retained earnings	8,972,000	7,008,000
Accumulated other comprehensive income (loss), net	143,000	(845,000)
Total Shareholders' equity	50,686,000	47,573,000

Total liabilities and Shareholders' equity	$742,587,000	$717,888,000

See accompanying notes to consolidated financial statements.

Stewardship Financial Corporation and Subsidiary
Consolidated Statements of Income (Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2016	2015	2016	2015
Interest income:				
Loans	$6,116,000	$5,623,000	$11,768,000	$11,069,000
Securities held to maturity:				
Taxable	298,000	227,000	568,000	440,000
Nontaxable	100,000	119,000	203,000	249,000
Securities available-for-sale:				
Taxable	409,000	342,000	786,000	704,000
Nontaxable	6,000	6,000	12,000	12,000
FHLB dividends	31,000	33,000	63,000	63,000
Other interest-earning assets	19,000	10,000	28,000	17,000
Total interest income	6,979,000	6,360,000	13,428,000	12,554,000
Interest expense:				
Deposits	561,000	506,000	1,118,000	958,000
FHLB-NY Borrowings	201,000	211,000	404,000	427,000
Subordinated Debentures and Subordinated Notes	362,000	125,000	775,000	250,000
Total interest expense	1,124,000	842,000	2,297,000	1,635,000
Net interest income before provision for loan losses	5,855,000	5,518,000	11,131,000	10,919,000
Provision for loan losses	(450,000)	(600,000)	(800,000)	(700,000)
Net interest income after provision for loan losses	6,305,000	6,118,000	11,931,000	11,619,000
Noninterest income:				
Fees and service charges	530,000	557,000	1,059,000	1,036,000
Bank owned life insurance	107,000	101,000	208,000	197,000
Gain on calls and sales of securities, net	32,000	—	56,000	152,000
Gain on sales of mortgage loans	19,000	55,000	37,000	65,000
Gain on sale of other real estate owned	6,000	—	6,000	53,000
Miscellaneous	138,000	169,000	285,000	297,000
Total noninterest income	832,000	882,000	1,651,000	1,800,000
Noninterest expenses:				
Salaries and employee benefits	2,742,000	2,688,000	5,457,000	5,396,000
Occupancy, net	404,000	423,000	802,000	890,000
Equipment	148,000	165,000	298,000	321,000
Data processing	477,000	459,000	949,000	912,000
Advertising	157,000	258,000	308,000	470,000
FDIC insurance premium	90,000	117,000	196,000	230,000
Charitable contributions	90,000	70,000	160,000	140,000
Stationery and supplies	47,000	43,000	80,000	60,000
Legal	46,000	105,000	90,000	193,000
Bank-card related services	150,000	131,000	281,000	254,000
Other real estate owned	28,000	75,000	102,000	161,000
Miscellaneous	620,000	571,000	1,178,000	1,127,000
Total noninterest expenses	4,999,000	5,105,000	9,901,000	10,154,000
Income before income tax expense	2,138,000	1,895,000	3,681,000	3,265,000
Income tax expense	776,000	673,000	1,328,000	1,126,000
Net income	1,362,000	1,222,000	2,353,000	2,139,000
Dividends on preferred stock	—	171,000	—	342,000

Net income available to common shareholders	$1,362,000	$1,051,000	$2,353,000	$1,797,000
Basic and diluted earnings per common share	$0.22	$0.17	$0.39	$0.30
Weighted average number of basic and diluted common shares outstanding	6,111,729	6,086,474	6,102,040	6,066,191

See accompanying notes to consolidated financial statements.

Stewardship Financial Corporation and Subsidiary
Consolidated Statements of Comprehensive Income
(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2016	2015	2016	2015
Net income	$1,362,000	$1,222,000	$2,353,000	$2,139,000
Other comprehensive income (loss), net of tax:				
Change in unrealized holding gains (losses) on securities available-for-sale	244,000	(325,000)	916,000	138,000
Reclassification adjustment for gains in net income	(20,000)	—	(35,000)	(91,000)
Accretion of loss on securities reclassified to held to maturity	25,000	34,000	70,000	121,000
Change in fair value of interest rate swap	—	37,000	37,000	71,000
Total other comprehensive income (loss)	249,000	(254,000)	988,000	239,000
Total comprehensive income	$1,611,000	$968,000	$3,341,000	$2,378,000

See accompanying notes to consolidated financial statements.

Stewardship Financial Corporation and Subsidiary
Consolidated Statement of Changes in Shareholders' Equity
(Unaudited)

Six Months Ended June 30, 2016

	Preferred Stock	Common Stock Shares	Common Stock Amount	Retained Earnings	Accumulated Other Comprehensive Income (Loss), Net	Total
Balance -- December 31, 2015	$—	6,085,528	$41,410,000	$7,008,000	$ (845,000)	$47,573,000
Cash dividends declared on common stock	—	—	—	(305,000)	—	(305,000)
Payment of discount on dividend reinvestment plan	—	—	(2,000)	—	—	(2,000)
Common stock issued under dividend reinvestment plan	—	6,700	36,000	—	—	36,000
Common stock issued under stock plans	—	1,761	10,000	—	—	10,000
Issuance of restricted stock	—	34,332	198,000	(198,000)	—	—
Amortization of restricted stock, net	—	(15,291)	(86,000)	114,000	—	28,000
Tax benefit from restricted stock vesting	—	—	5,000	—	—	5,000
Net income	—	—	—	2,353,000	—	2,353,000
Other comprehensive income	—	—	—	—	988,000	988,000
Balance -- June 30, 2016	$—	6,113,030	$41,571,000	$8,972,000	$ 143,000	$50,686,000

Six Months Ended June 30, 2015

	Preferred Stock	Common Stock Shares	Common Stock Amount	Retained Earnings	Accumulated Other Comprehensive Income (Loss), Net	Total
Balance -- December 31, 2014	$14,984,000	6,034,933	$41,125,000	$3,817,000	$ (957,000)	$58,969,000
Cash dividends declared on common stock	—	—	—	(242,000)	—	(242,000)
Payment of discount on dividend reinvestment plan	—	—	(2,000)	—	—	(2,000)
Cash dividends declared on preferred stock	—	—	—	(342,000)	—	(342,000)
Common stock issued under dividend reinvestment plan	—	5,635	30,000	—	—	30,000
Common stock issued under stock plans	—	4,219	21,000	—	—	21,000
Issuance of restricted stock	—	50,974	279,000	(279,000)	—	—
Amortization of restricted stock, net	—	(7,062)	(38,000)	75,000	—	37,000
Tax benefit from restricted stock vesting	—	—	3,000	—	—	3,000
Amortization of issuance costs	5,000	—	—	(5,000)	—	—
Net income	—	—	—	2,139,000	—	2,139,000
Other comprehensive income	—	—	—	—	239,000	239,000
Balance -- June 30, 2015	$14,989,000	6,088,699	$41,418,000	$5,163,000	$ (718,000)	$60,852,000

See accompanying notes to consolidated financial statements.

Stewardship Financial Corporation and Subsidiary
Consolidated Statements of Cash Flows
(Unaudited)

	Six Months Ended June 30, 2016	2015
Cash flows from operating activities:		
Net income	$2,353,000	$2,139,000
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization of premises and equipment	185,000	186,000
Amortization of premiums and accretion of discounts, net	285,000	338,000
Amortization of restricted stock	28,000	37,000
Amortization of subordinated debenture issuance costs	33,000	—
Accretion of deferred loan fees	34,000	42,000
Provision for loan losses	(800,000)	(700,000)
Originations of mortgage loans held for sale	(2,825,000)	(5,653,000)
Proceeds from sale of mortgage loans	3,803,000	4,302,000
Gain on sales of mortgage loans	(37,000)	(65,000)
Gain on calls and sales of securities	(56,000)	(152,000)
Gain on sale of other real estate owned	(6,000)	(53,000)
Deferred income tax expense	248,000	210,000
Increase in accrued interest receivable	55,000	88,000
Increase (decrease) in accrued interest payable	(9,000)	58,000
Earnings on bank owned life insurance	(208,000)	(197,000)
Decrease in other assets	339,000	801,000
Decrease in other liabilities	(117,000)	(2,053,000)
Net cash provided by (used in) operating activities	3,305,000	(672,000)
Cash flows from investing activities:		
Purchase of securities available-for-sale	(21,288,000)	(57,000)
Proceeds from maturities and principal repayments on securities available-for-sale	6,305,000	6,258,000
Proceeds from sales and calls on securities available-for-sale	11,050,000	27,845,000
Purchase of securities held to maturity	(24,898,000)	(13,182,000)
Proceeds from maturities and principal repayments on securities held to maturity	3,464,000	4,921,000
Proceeds from calls on securities held to maturity	16,570,000	5,100,000
Sale (purchase) of FHLB-NY stock	(42,000)	944,000
Net increase in loans	(11,055,000)	(29,317,000)
Proceeds from sale of other real estate owned	184,000	1,149,000
Purchase of bank owned life insurance	(2,000,000)	—
Additions to premises and equipment	(64,000)	(584,000)
Net cash provided by (used in) investing activities	(21,774,000)	3,077,000
Cash flows from financing activities:		
Net increase in noninterest-bearing deposits	12,633,000	16,825,000
Net increase in interest-bearing deposits	9,083,000	12,698,000
Net decrease in short term borrowings	—	(21,700,000)
Cash dividends paid on common stock	(305,000)	(242,000)
Cash dividends paid on preferred stock	—	(342,000)
Payment of discount on dividend reinvestment plan	(2,000)	(2,000)
Issuance of common stock for cash	46,000	51,000
Tax benefit from restricted stock vesting	5,000	3,000

Net cash provided by financing activities	21,460,000	7,291,000
Net increase in cash and cash equivalents	2,991,000	9,696,000
Cash and cash equivalents - beginning	10,910,000	10,086,000
Cash and cash equivalents - ending	$13,901,000	$19,782,000

Stewardship Financial Corporation and Subsidiary
Consolidated Statements of Cash Flows (continued)
(Unaudited)

	Six Months Ended June 30,	
	2016	2015
Supplemental disclosures of cash flow information:		
Cash paid during the period for interest	$2,306,000	$1,578,000
Cash paid during the period for income taxes	$746,000	$1,024,000
Transfers from loans to other real estate owned	$152,000	$—

See accompanying notes to consolidated financial statements.

Stewardship Financial Corporation and Subsidiary
Notes to Consolidated Financial Statements
June 30, 2016
(Unaudited)

Note 1. Summary of Significant Accounting Policies

Certain information and note disclosures normally included in the unaudited consolidated financial statements prepared in accordance with U.S. generally accepted accounting principles (“GAAP”) have been omitted pursuant to the rules and regulations of the Securities and Exchange Commission (the “SEC”). These unaudited consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto included in the Stewardship Financial Corporation Annual Report on Form 10-K for the fiscal year ended December 31, 2015, filed with the SEC on March 24, 2016 (the “2015 Annual Report”).

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 SEC and, therefore, do not include information or footnotes necessary for a complete presentation of consolidated financial condition, results of operations, and cash flows in conformity with GAAP. However, all adjustments, consisting only of normal recurring adjustments, which in the opinion of management are necessary for a fair presentation of the interim consolidated financial statements, have been included. The results of operations for the three and six months ended June 30, 2016 are not necessarily indicative of the results which may be expected for the entire year.

Principles of consolidation

The consolidated financial statements include the accounts of Stewardship Financial Corporation and its wholly-owned subsidiary, Atlantic Stewardship Bank (the “Bank”), together referred to as “the Corporation”. The Bank includes its wholly-owned subsidiaries, Stewardship Investment Corporation, Stewardship Realty LLC, Atlantic Stewardship Insurance Company, LLC and several other subsidiaries formed to hold title to properties acquired through foreclosure or deed in lieu of foreclosure. The Bank’s subsidiaries have an insignificant impact on the Bank’s daily operations. All intercompany accounts and transactions have been eliminated in the consolidated financial statements.

The consolidated financial statements of the Corporation have been prepared in conformity with GAAP. In preparing the consolidated financial statements, management is required to make estimates and assumptions, based on available information, that affect the amounts reported in the consolidated financial statements and disclosures provided. Actual results could differ significantly from those estimates.

Material estimates

Material estimates that are particularly susceptible to significant changes relate to the determination of the allowance for loan losses and deferred income taxes. Management believes the Corporation’s policies with respect to the methodology for the determination of the allowance for loan losses and the evaluation of deferred income taxes involves a higher degree of complexity and requires management to make difficult and subjective judgments, which often require assumptions or estimates about highly uncertain matters. Changes in these judgments, assumptions or estimates could materially impact results of operations. These critical policies and their application are periodically reviewed with the Audit Committee and the Board of Directors.

Adoption of New Accounting Standards

In April 2015, the Financial Accounting Standards Board (the "FASB") issued Accounting Standards Update ("ASU") 2015-03, "Interest – Imputation of Interest (Subtopic 835-30) – Simplifying the Presentation of Debt Issuance Costs." This ASU is part of the FASB's initiative to reduce complexity in accounting standards. To simplify presentation of debt issuance costs, the amendments in this ASU require that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. The recognition and measurement guidance for debt issuance costs are not affected by the amendments in this ASU. The amendments in ASU 2015-03 are effective for fiscal years, including interim periods, beginning after December 15, 2015. The adoption of the amendments in this standard did not have a material impact on the Corporation's consolidated financial statements.

In January 2016, the FASB issued ASU No. 2016-01, "Financial Instruments - Overall: Recognition and Measurement of Financial Assets and Liabilities." This ASU addresses certain aspects of recognition, measurement, presentation, and disclosure of financial instruments. This amendment supersedes the guidance to classify equity securities with readily determinable fair values into different categories, requires equity securities to be measured at fair value with changes in the fair value recognized through net income, and simplifies the impairment assessment of equity investments without readily determinable fair values. The amendment requires public business entities that are required to disclose the fair value of financial instruments measured at amortized cost on the balance sheet to measure that fair value using the exit price notion. The amendment requires an entity to present separately in other comprehensive income the portion of the total change in the fair value of a liability resulting from a change in the instrument-specific credit risk when the entity has elected to measure the liability at fair value in accordance with the fair value option. The amendment requires separate presentation of financial assets and financial liabilities by measurement category and form of financial asset on the balance sheet or in the accompanying notes to the financial statements. The amendment reduces diversity in current practice by clarifying that an entity should evaluate the need for a valuation allowance on a deferred tax asset related to available for sale securities in combination with the entity’s other deferred tax assets. This amendment is effective for fiscal years, including interim periods, beginning after December 15, 2017. Entities should apply the amendment by means of a cumulative-effect adjustment as of the beginning of the fiscal year of adoption, with the exception of the amendment related to equity securities without readily determinable fair values, which should be applied prospectively to equity investments that exist as of the date of adoption. The Corporation intends to adopt the accounting standard during the first quarter of 2018, and is currently evaluating the impact that the adoption of the guidance will have on the Corporation's consolidated financial statements.

In February 2016, the FASB issued ASU 2016-02, “Leases (Subtopic 842).” This ASU requires all lessees to recognize a lease liability and a right-of-use asset, measured at the present value of the future minimum lease payments, at the lease commencement date. Lessor accounting remains largely unchanged under the new guidance. The amendments in ASU 2016-02 are effective for fiscal years, including interim periods, beginning after December 15, 2018. Early adoption of ASU 2016-02 is permitted. The Corporation is currently assessing the impact that the adoption of the guidance will have on the Corporation's consolidated financial statements.

In March 2016, the FASB issued ASU 2016-09, “Compensation – Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting”. The objective of this ASU is to simplify accounting for share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. Under ASU 2016-09, all excess tax benefits and tax deficiencies (including tax benefits of dividends on share-based payment awards) should be recognized as income tax expense or benefit in the income statement. The tax effects of exercised or vested awards should be treated as discrete items in the reporting period in which they occur. An entity also should recognize excess tax benefits regardless of whether the benefit reduces taxes payable in the current period. An entity can make an entity-wide accounting policy election to either estimate the number of awards that are expected to vest (current accounting) or account for forfeitures when they occur. Within the Cash Flow Statement, excess tax benefits should be classified along with other income tax cash flows as an operating activity, and cash paid by an employer when directly withholding shares for tax-withholding purposes should be classified as a financing activity. The amendments in ASU 2016-09 are effective for fiscal years, including interim periods, beginning after December 15, 2016. Early adoption of ASU 2016-09 is permitted. The Corporation is currently assessing the impact that the adoption of the guidance will have on the Corporation'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 main objective of this ASU is to provide financial statement users with more decision-useful information about the expected credit losses on financial instruments by a reporting entity at each reporting date. The amendments in this ASU require financial assets measured at amortized cost to be presented at the net amount expected to be collected. The allowance for credit losses would represent a valuation account that would be deducted from the amortized cost basis of the financial asset(s) to present the net carrying value at the amount expected to be collected on the financial asset. The income statement would reflect the measurement of credit losses for newly recognized financial assets, as well as the expected increases or decreases of expected credit losses that have taken place during the period. The measurement of expected credit losses would be based on relevant information about past events, including historical experience, current conditions, and reasonable and supportable forecasts that affect the collectability of the reported amount. An entity will be required to use judgment in determining the relevant information and estimation methods that are appropriate in its circumstances. The amendments in ASU

2016-13 are effective for fiscal years, including interim periods, beginning after December 15, 2019. Early adoption of ASU 2016-09 is permitted for fiscal years beginning after December 15, 2018. The Corporation is currently evaluating the potential impact that the adoption of the guidance will have on the Corporation's consolidated financial statements.

Note 2. Securities – Available-for-Sale and Held to Maturity

The fair value of the available-for-sale securities and the related gross unrealized gains and losses recognized in accumulated other comprehensive income were as follows:

	June 30, 2016			
	Amortized	Gross Unrealized		Fair
	Cost	Gains	Losses	Value
U.S. government-sponsored agencies	$28,426,000	$164,000	$20,000	$28,570,000
Obligations of state and political subdivisions	1,406,000	26,000	—	1,432,000
Mortgage-backed securities - residential	50,648,000	670,000	32,000	51,286,000
Asset-backed securities (a)	9,291,000	—	205,000	9,086,000
Corporate debt	4,500,000	10,000	85,000	4,425,000
Total debt securities	94,271,000	870,000	342,000	94,799,000
Other equity investments	3,832,000	—	98,000	3,734,000
	$98,103,000	$870,000	$440,000	$98,533,000

	December 31, 2015			
	Amortized	Gross Unrealized		Fair
	Cost	Gains	Losses	Value
U.S. government-sponsored agencies	$31,266,000	$81,000	$393,000	$30,954,000
Obligations of state and political subdivisions	1,409,000	2,000	1,000	1,410,000
Mortgage-backed securities - residential	45,520,000	213,000	496,000	45,237,000
Asset-backed securities (a)	9,877,000	—	176,000	9,701,000
Corporate debt	2,500,000	—	81,000	2,419,000
Total debt securities	90,572,000	296,000	1,147,000	89,721,000
Other equity investments	3,778,000	—	145,000	3,633,000
	$94,350,000	$296,000	$1,292,000	$93,354,000

(a) Collateralized by student loans

Cash proceeds realized from sales and calls of securities available-for-sale for the three and six months ended June 30, 2016 were $9,000,000 and $11,050,000, respectively. There were no cash proceeds realized from sales and calls of securities available-for-sale for the three months ended June 30, 2015. Cash proceeds realized from sales and calls of securities available-for-sale for the six months ended June 30, 2015 were $27,845,000. There were gross gains totaling $7,000 and no gross losses realized on sales and calls during the three and six months ended June 30, 2016. While there were no gross gains and no gross losses realized on sales or calls during the three months ended June 30, 2015, gross gains and gross losses realized on sales and calls during the six months ended June 30, 2015 totaled $213,000 and $61,000, respectively.

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The following is a summary of the held to maturity securities and related gross unrealized gains and losses:

	June 30, 2016			
	Amortized	Gross Unrealized		Fair
	Cost	Gains	Losses	Value
U.S. Treasury	$999,000	$20,000	$—	$1,019,000
U.S. government-sponsored agencies	24,129,000	131,000	10,000	24,250,000
Obligations of state and political subdivisions	10,223,000	167,000	—	10,390,000
Mortgage-backed securities - residential	30,315,000	798,000	—	31,113,000
	$65,666,000	$1,116,000	$10,000	$66,772,000

	December 31, 2015			
	Amortized	Gross Unrealized		Fair
	Cost	Gains	Losses	Value
U.S. Treasury	$999,000	$—	$11,000	$988,000
U.S. government-sponsored agencies	15,109,000	132,000	24,000	15,217,000
Obligations of state and political subdivisions	11,219,000	268,000	—	11,487,000
Mortgage-backed securities - residential	33,411,000	295,000	117,000	33,589,000
	$60,738,000	$695,000	$152,000	$61,281,000

Cash proceeds realized from calls of securities held to maturity for the three and six months ended June 30, 2016 were $10,230,000 and $16,570,000, respectively. Cash proceeds realized from calls of securities held to maturity for the three and six months ended June 30, 2015 were $2,000,000 and $5,100,000, respectively. There were gross gains totaling $25,000 and no gross losses realized on calls during the three months ended June 30, 2016. There were gross gains totaling $49,000 and no gross losses realized on calls during the six months ended June 30, 2016. There were no gross gains and no gross losses realized on calls during the three and six months ended June 30, 2015.

Mortgage-backed securities are a type of asset-backed security secured by a mortgage or collection of mortgages, purchased by government agencies such as the Government National Mortgage Association and government sponsored agencies such as the Federal National Mortgage Association and the Federal Home Loan Mortgage Corporation, which then issue securities that represent claims on the principal and interest payments made by borrowers on the loans in the pool.

Issuers may have the right to call or prepay obligations with or without call or prepayment penalties. This might cause actual maturities to differ from the contractual maturities.

The following table presents the amortized cost and fair value of the debt securities portfolio by contractual maturity. As issuers may have the right to call or prepay obligations with or without call or prepayment premiums, the actual maturities may differ from contractual maturities. Securities not due at a single maturity date, such as mortgage-backed securities and asset-backed securities, are shown separately.

	June 30, 2016	
	Amortized Cost	Fair Value
Available-for-sale		
Within one year	$500,000	$502,000
After one year, but within five years	9,778,000	9,798,000
After five years, but within ten years	17,923,000	18,009,000
After ten years	6,131,000	6,118,000
Mortgage-backed securities - residential	50,648,000	51,286,000
Asset-backed securities	9,291,000	9,086,000
Total	$94,271,000	$94,799,000
Held to maturity		
Within one year	$3,137,000	$3,155,000
After one year, but within five years	8,586,000	8,787,000
After five years, but within ten years	21,676,000	21,716,000
After ten years	1,952,000	2,001,000
Mortgage-backed securities - residential	30,315,000	31,113,000
Total	$65,666,000	$66,772,000

The following tables summarize the fair value and unrealized losses of those investment securities which reported an unrealized loss at June 30, 2016 and December 31, 2015, and if the unrealized loss position was continuous for the twelve months prior to June 30, 2016 and December 31, 2015.

Available-for-Sale

June 30, 2016	Less than 12 Months		12 Months or Longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
U.S. government- sponsored agencies	$1,994,000	$(8,000)	$6,118,000	$(12,000)	$8,112,000	$(20,000)
Obligations of state and political subdivisions	—	—	—	—	—	—
Mortgage-backed securities - residential	6,094,000	(11,000)	3,888,000	(21,000)	9,982,000	(32,000)
Asset-backed securities	6,197,000	(69,000)	2,889,000	(136,000)	9,086,000	(205,000)
Corporate debt	999,000	(1,000)	1,416,000	(84,000)	2,415,000	(85,000)
Other equity investments	—	—	3,674,000	(98,000)	3,674,000	(98,000)
Total temporarily impaired securities	$15,284,000	$(89,000)	$17,985,000	$(351,000)	$33,269,000	$(440,000)

December 31, 2015	Less than 12 Months		12 Months or Longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
U.S. government- sponsored agencies	$18,396,000	$(183,000)	$7,296,000	$(210,000)	$25,692,000	$(393,000)
Obligations of state and political subdivisions	984,000	(1,000)	—	—	984,000	(1,000)
Mortgage-backed securities - residential	8,599,000	(69,000)	16,278,000	(427,000)	24,877,000	(496,000)
Asset-backed securities	6,791,000	(56,000)	2,910,000	(120,000)	9,701,000	(176,000)
Corporate debt	—	—	1,419,000	(81,000)	1,419,000	(81,000)
Other equity investments	—	—	3,573,000	(145,000)	3,573,000	(145,000)
Total temporarily impaired securities	$34,770,000	$(309,000)	$31,476,000	$(983,000)	$66,246,000	$(1,292,000)

Held to Maturity

June 30, 2016	Less than 12 Months		12 Months or Longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
U.S. Treasury	$—	$—	$ —	$ —	$—	$—
U.S. government- sponsored agencies	1,891,000	(10,000)	—	—	1,891,000	(10,000)
Mortgage-backed securities - residential	—	—	—	—	—	—
Total temporarily impaired securities	$1,891,000	$(10,000)	$ —	$ —	$1,891,000	$(10,000)

December 31, 2015	Less than 12 Months		12 Months or Longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
U.S. Treasury	$988,000	$(11,000)	$—	$—	$988,000	$(11,000)
U.S. government- sponsored agencies	4,955,000	(24,000)	—	—	4,955,000	(24,000)
Mortgage-backed securities - residential	15,183,000	(90,000)	1,066,000	(27,000)	16,249,000	(117,000)
Total temporarily impaired securities	$21,126,000	$(125,000)	$1,066,000	$(27,000)	$22,192,000	$(152,000)

Other-Than-Temporary-Impairment

At June 30, 2016, there were available-for-sale investments comprising three U.S. government-sponsored agency securities, five mortgage-backed securities, one asset-backed security, two corporate debt securities, and one other equity investments security in a continuous loss position for twelve months or longer. Management has assessed the securities that were in an unrealized loss position at June 30, 2016 and December 31, 2015 and has determined that any decline in fair value below amortized cost primarily relates to changes in interest rates and market spreads and was temporary.

In making this determination management considered the following factors in estimating the cash flows expected to be collected from the security: the period of time the securities were in an unrealized loss position; the percentage decline in comparison to the securities' amortized cost; any adverse conditions specifically related to the security, an industry or a geographic area; the rating or changes to the rating by a credit rating agency; the financial condition of the issuer and guarantor and any recoveries or additional declines in fair value subsequent to the balance sheet date. Management expects to collect all amounts contractually due and none of the debt securities can be prepaid at less than the par values.

Management does not intend to sell these securities in an unrealized loss position and it is not more likely than not that we will be required to sell these securities before the recovery of their amortized cost bases, which may be at maturity.

Note 3. Loans and Allowance for Loan Losses

At June 30, 2016 and December 31, 2015, respectively, the loan portfolio consisted of the following:

	June 30, 2016	December 31, 2015
Commercial:		
Secured by real estate	$35,632,000	$37,993,000
Other	36,388,000	26,867,000
Commercial real estate	337,660,000	334,489,000
Commercial construction	7,097,000	4,609,000
Residential real estate	79,661,000	82,955,000
Consumer:		
Secured by real estate	29,876,000	29,224,000
Other	522,000	580,000
Government Guaranteed Loans - guaranteed portion	10,734,000	9,626,000
Other	68,000	134,000
Total gross loans	537,638,000	526,477,000
Less: Deferred loan costs (fees), net	25,000	98,000
Allowance for loan losses	8,388,000	8,823,000
	8,413,000	8,921,000
Loans, net	$529,225,000	$517,556,000

The Corporation has purchased the guaranteed portion of several government guaranteed loans. Due to the guarantee of the principal amount of these loans, no allowance for loan losses is established for these government guaranteed loans.

At June 30, 2016 and December 31, 2015, loan participations sold by the Corporation to other lending institutions totaled approximately $8,749,000 and $8,527,000, respectively. These amounts are not included in the totals presented above.

Activity in the allowance for loan losses is summarized as follows:

	For the three months ended June 30, 2016				
	Balance, beginning of period	Provision charged to operations	Loans charged off	Recoveries of loans charged off	Balance, end of period
Commercial	$3,720,000	$(386,000)	$(1,000)	$340,000	$3,673,000
Commercial real estate	4,413,000	(156,000)	(64,000)	31,000	4,224,000
Commercial construction	112,000	72,000	—	—	184,000
Residential real estate	106,000	—	—	—	106,000
Consumer	119,000	19,000	(7,000)	1,000	132,000
Other loans	1,000	1,000	(2,000)	—	—
Unallocated	69,000	—	—	—	69,000
Total	$8,540,000	$(450,000)	$(74,000)	$372,000	$8,388,000

	For the six months ended June 30, 2016				
	Balance, beginning of period	Provision charged to operations	Loans charged off	Recoveries of loans charged off	Balance, end of period
Commercial	$3,698,000	$(402,000)	$(3,000)	$380,000	$3,673,000
Commercial real estate	4,660,000	(431,000)	(64,000)	59,000	4,224,000
Commercial construction	114,000	70,000	—	—	184,000
Residential real estate	109,000	(3,000)	—	—	106,000
Consumer	118,000	19,000	(7,000)	2,000	132,000
Other loans	3,000	(1,000)	(2,000)	—	—
Unallocated	121,000	(52,000)	—	—	69,000
Total	$8,823,000	$(800,000)	$(76,000)	$441,000	$8,388,000

	For the three months ended June 30, 2015				
	Balance, beginning of period	Provision charged to operations	Loans charged off	Recoveries of loans charged off	Balance, end of period
Commercial	$3,703,000	$(503,000)	$(1,000)	$118,000	$3,317,000
Commercial real estate	5,116,000	99,000	—	74,000	5,289,000
Commercial construction	106,000	(200,000)	—	108,000	14,000
Residential real estate	146,000	(6,000)	—	—	140,000
Consumer	151,000	(13,000)	—	1,000	139,000
Other loans	—	4,000	(1,000)	—	3,000
Unallocated	378,000	19,000	—	—	397,000
Total	$9,600,000	$(600,000)	$(2,000)	$301,000	$9,299,000

	For the six months ended June 30, 2015				
	Balance, beginning of period	Provision charged to operations	Loans charged off	Recoveries of loans charged off	Balance, end of period
Commercial	$3,704,000	$(341,000)	$(272,000)	$226,000	$3,317,000
Commercial real estate	5,017,000	171,000	—	101,000	5,289,000
Commercial construction	150,000	(477,000)	—	341,000	14,000
Residential real estate	142,000	(2,000)	—	—	140,000
Consumer	189,000	(52,000)	—	2,000	139,000
Other loans	2,000	2,000	(1,000)	—	3,000
Unallocated	398,000	(1,000)	—	—	397,000
Total	$9,602,000	$(700,000)	$(273,000)	$670,000	$9,299,000

The following table presents the balance in the allowance for loan losses and the recorded investment in loans by portfolio segment and based on the impairment method as of June 30, 2016 and December 31, 2015.

	June 30, 2016								
	Commercial	Commercial Real Estate	Commercial Construction	Residential Real Estate	Consumer	Government Guaranteed	Other Loans	Unallocated	Total
Allowance for loan losses Ending allowance balance attributable to loans									
Individually evaluated for impairment	$79,000	$613,000	$—	$—	$—	$—	$—	$—	$692,000
Collectively evaluated for impairment	3,594,000	3,611,000	184,000	106,000	132,000	—	—	69,000	7,696,000
Total ending allowance balance	$3,673,000	$4,224,000	$184,000	$106,000	$132,000	$—	$—	$69,000	$8,388,000
Loans: Loans individually evaluated for impairment	$2,331,000	$6,768,000	$—	$—	$81,000	$—	$—	$—	$9,180,000
Loans collectively evaluated for impairment	69,689,000	330,892,000	7,097,000	79,661,000	30,317,000	10,734,000	68,000	—	528,458,000
Total ending loan balance	$72,020,000	$337,660,000	$7,097,000	$79,661,000	$30,398,000	$10,734,000	$68,000	$—	$537,638,00

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	December 31, 2015								
	Commercial	Commercial Real Estate	Commercial Construction	Residential Real Estate	Consumer	Government Guaranteed	Other Loans	Unallocated	Total
Allowance for loan losses Ending allowance balance attributable to loans									
Individually evaluated for impairment	$81,000	$638,000	$—	$—	$—	$—	$—	$—	$719,000
Collectively evaluated for impairment	3,617,000	4,022,000	114,000	109,000	118,000	—	3,000	121,000	8,104,000
Total ending allowance balance	$3,698,000	$4,660,000	$114,000	$109,000	$118,000	$—	$3,000	$121,000	$8,823,00
Loans: Loans individually evaluated for impairment	$3,348,000	$8,113,000	$—	$—	$84,000	$—	$—	$—	$11,545,00
Loans collectively evaluated for impairment	61,512,000	326,376,000	4,609,000	82,955,000	29,720,000	9,626,000	134,000	—	514,932,00
Total ending loan balance	$64,860,000	$334,489,000	$4,609,000	$82,955,000	$29,804,000	$9,626,000	$134,000	$—	$526,477,0

The following table presents the recorded investment in nonaccrual loans at the dates indicated:

	June 30, 2016	December 31, 2015

Commercial:		
Secured by real estate	$616,000	$1,300,000
Other	—	14,000
Commercial real estate	252,000	484,000
Consumer:		
Secured by real estate	81,000	84,000
Total nonaccrual loans	$949,000	$1,882,000

At June 30, 2016 and December 31, 2015, there were no loans that were past due 90 days and still accruing.

The following table presents loans individually evaluated for impairment by class of loan at and for the periods indicated:

	At and for the six months ended June 30, 2016				
	Unpaid Principal Balance	Recorded Investment	Allowance for Loan Losses Allocated	Average Recorded Investment	Interest Income Recognized
With no related allowance recorded:					
Commercial:					
Secured by real estate	$2,073,000	$1,853,000		$2,310,000	$47,000
Other	—	—		46,000	—
Commercial real estate	3,824,000	3,563,000		3,197,000	112,000
Consumer:					
Secured by real estate	82,000	81,000		83,000	—
With an allowance recorded:					
Commercial:					
Secured by real estate	190,000	190,000	$68,000	230,000	4,000
Other	288,000	288,000	11,000	256,000	10,000
Commercial real estate	3,205,000	3,205,000	613,000	4,726,000	66,000
	$9,662,000	$9,180,000	$692,000	$10,848,000	$239,000

During the three and six months ended June 30, 2016, no interest income was recognized on a cash basis.

	At and for the year ended December 31, 2015				
	Unpaid Principal Balance	Recorded Investment	Allowance for Loan Losses Allocated	Average Recorded Investment	Interest Income Recognized
With no related allowance recorded:					
Commercial:					
Secured by real estate	$3,244,000	$2,729,000		$3,683,000	$156,000
Other	137,000	137,000		61,000	2,000
Commercial real estate	3,245,000	2,885,000		2,890,000	121,000
Commercial construction	—	—		215,000	—
Residential real estate	—	—		74,000	—
Consumer:					
Secured by real estate	84,000	84,000		226,000	—
With an allowance recorded:					
Commercial:					
Secured by real estate	390,000	308,000	$80,000	405,000	14,000
Other	174,000	174,000	1,000	463,000	31,000
Commercial real estate	5,228,000	5,228,000	638,000	5,534,000	211,000
	$12,502,000	$11,545,000	$719,000	$13,551,000	$535,000

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During the year ended December 31, 2015, no interest income was recognized on a cash basis.

The following table presents the aging of the recorded investment in past due loans by class of loans as of June 30, 2016 and December 31, 2015. Nonaccrual loans are included in the disclosure by payment status.