SOUTHERN FIRST BANCSHARES INC
Form 10-Q
November 01, 2018

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 September 30, 2018
OR
TRANSITION REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the Transition Period from to
Commission file number 000-27719

Southern First Bancshares, Inc.
(Exact name of registrant as specified in its charter)

South Carolina	**58-2459561**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
100 Verdae Boulevard, Suite 100 Greenville, S.C.	**29606**
(Address of principal executive offices)	(Zip Code)

864-679-9000
(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 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," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer	Accelerated filer
Non-accelerated filer	Smaller Reporting Company
	Emerging growth company

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the 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: 7,450,270 shares of common stock, par value $0.01 per share, were issued and outstanding as of October 25, 2018.

SOUTHERN FIRST BANCSHARES, INC. AND SUBSIDIARY
September 30, 2018 Form 10-Q

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PART I. CONSOLIDATED FINANCIAL INFORMATION
Item 1. CONSOLIDATED FINANCIAL STATEMENTS

SOUTHERN FIRST BANCSHARES, INC. AND SUBSIDIARY
CONSOLIDATED BALANCE SHEETS

(dollars in thousands, except share data)		**September 30, 2018** (Unaudited)	**December 31, 2017** (Audited)
ASSETS			
Cash and cash equivalents:			
Cash and due from banks	$	15,199	17,171
Federal funds sold		52,956	49,148
Interest-bearing deposits with banks		21,836	25,846
Total cash and cash equivalents		89,991	92,165
Investment securities:			
Investment securities available for sale		66,886	67,603
Other investments		4,929	4,462
Total investment securities		71,815	72,065
Mortgage loans held for sale		9,298	11,790
Loans		1,620,201	1,387,070
Less allowance for loan losses		(16,140)	(15,523)
Loans, net		1,604,061	1,371,547
Bank owned life insurance		33,793	33,132
Property and equipment, net		32,670	32,234
Deferred income taxes		7,998	3,782
Other assets		8,081	7,910
Total assets	$	1,857,707	1,624,625
LIABILITIES			
Deposits	$	1,589,483	1,381,123
Federal Home Loan Bank advances and other borrowings		68,500	67,200
Junior subordinated debentures		13,403	13,403
Other liabilities		19,377	13,213
Total liabilities		1,690,763	1,474,939
SHAREHOLDERS' EQUITY			
Preferred stock, par value $.01 per share, 10,000,000 shares authorized, no shares issued and outstanding		-	-
Common stock, par value $.01 per share, 10,000,000 shares authorized, 7,448,770 and 7,347,851 shares issued and outstanding at September 30, 2018 and December 31, 2017, respectively		74	73
Nonvested restricted stock		(770)	(502)
Additional paid-in capital		102,171	99,986
Accumulated other comprehensive loss		(1,622)	(456)
Retained earnings		67,091	50,585
Total shareholders' equity		166,944	149,686
Total liabilities and shareholders' equity	$	1,857,707	1,624,625

See notes to consolidated financial statements that are an integral part of these consolidated statements.

SOUTHERN FIRST BANCSHARES, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF INCOME

(Unaudited)

(dollars in thousands, except share data)	For the three months ended September 30, 2018	2017	For the nine months ended September 30, 2018	2017
Interest income				
Loans	$ 19,159	15,282	53,314	43,089
Investment securities	487	443	1,284	1,208
Federal funds sold	219	230	980	548
Total interest income	19,865	15,955	55,578	44,845
Interest expense				
Deposits	3,928	2,084	10,191	5,073
Borrowings	436	562	1,232	2,504
Total interest expense	4,364	2,646	11,423	7,577
Net interest income	15,501	13,309	44,155	37,268
Provision for loan losses	400	500	1,300	1,500
Net interest income after provision for loan losses	15,101	12,809	42,855	35,768
Noninterest income				
Mortgage banking income	1,354	1,403	4,311	4,063
Service fees on deposit accounts	257	324	769	886
ATM and debit card income	381	284	1,085	818
Income from bank owned life insurance	221	224	662	590
Other income	320	307	898	799
Total noninterest income	2,533	2,542	7,725	7,156
Noninterest expenses				
Compensation and benefits	6,599	5,698	18,808	16,496
Occupancy	1,350	1,043	3,763	3,042
Outside service and data processing costs	841	794	2,400	2,362
Insurance	376	258	987	845
Professional fees	275	334	1,208	1,029
Marketing	215	199	652	605
Other	532	480	1,554	1,550
Total noninterest expenses	10,188	8,806	29,372	25,929
Income before income tax expense	7,446	6,545	21,208	16,995
Income tax expense	1,664	2,295	4,702	6,030
Net income available to common shareholders	$ 5,782	4,250	16,506	10,965
Earnings per common share				
Basic	$ 0.78	0.58	2.24	1.59
Diluted	$ 0.75	0.55	2.13	1.50
Weighted average common shares outstanding				
Basic	7,400,174	7,281,594	7,369,473	6,905,017
Diluted	7,746,205	7,668,476	7,741,483	7,291,164

See notes to consolidated financial statements that are an integral part of these consolidated statements.

SOUTHERN FIRST BANCSHARES, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(Unaudited)

	For the three months ended September 30,		For the nine months ended September 30,	
(dollars in thousands)	**2018**	**2017**	**2018**	**2017**
Net income	$ 5,782	$ 4,250	16,506	10,965
Other comprehensive income (loss):				
Unrealized gain (loss) on securities available for sale:				
Unrealized holding gain (loss) arising during the period, pretax	(325)	130	(1,475)	626
Tax (expense) benefit	69	(43)	308	(213)
Reclassification of realized (gain) loss	-	-	1	(2)
Tax expense	-	-	-	-
Other comprehensive income (loss)	(256)	87	(1,166)	411
Comprehensive income	$ 5,526	$ 4,337	15,340	11,376

See notes to consolidated financial statements that are an integral part of these consolidated statements.

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SOUTHERN FIRST BANCSHARES, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY
FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2018 AND 2017
(Unaudited)

(dollars in thousands, except share data)	**Common stock Shares**	**Common stock Amount**	**Preferred stock Shares**	**Preferred stock Amount**	**Nonvested restricted stock**	**Additional paid-in capital**	**Accumulated other comprehensive income (loss)**	**Retained earnings**	**Total**
December 31, 2016	**6,463,789**	**65**	**-**	**-**	**(600)**	**73,371**	**(504)**	**37,540**	**109,872**
Net income	-	-	-	-	-	-	-	10,965	10,965
Net issuance of common stock	805,000	8	-	-	-	24,750	-	-	24,758
Proceeds from exercise of stock options	42,267	-	-	-	-	454	-	-	454
Issuance of restricted stock	3,125	-	-	-	(146)	146	-	-	-
Amortization of deferred compensation on restricted stock	-	-	-	-	246	-	-	-	246
Compensation expense related to stock options, net of tax	-	-	-	-	-	743	-	-	743
Other comprehensive income	-	-	-	-	-	-	411	-	411
September 30, 2017	**7,319,098**	**$ 73**	**-**	**$ -**	**$ (500)**	**$ 99,464**	**$ (93)**	**$ 48,505**	**$ 147,449**
December 31, 2017	**7,347,851**	**73**	**-**	**-**	**(502)**	**99,986**	**(456)**	**50,585**	**149,686**
Net income	-	-	-	-	-	-	-	16,506	16,506
Proceeds from exercise of stock options	89,419	1	-	-	-	809	-	-	810
Issuance of restricted stock	11,500	-	-	-	(501)	501	-	-	-
Amortization of deferred compensation on restricted stock	-	-	-	-	233	-	-	-	233
Compensation expense related to stock options, net of tax	-	-	-	-	-	875	-	-	875
Other comprehensive loss	-	-	-	-	-	-	(1,166)	-	(1,166)
September 30, 2018	**7,448,770**	**$ 74**	**-**	**$ -**	**$ (770)**	**$ 102,171**	**$ (1,622)**	**$ 67,091**	**$ 166,944**

See notes to consolidated financial statements that are an integral part of these consolidated statements.

SOUTHERN FIRST BANCSHARES, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	For the nine months ended September 30,	
(dollars in thousands)	**2018**	**2017**
Operating activities		
Net income	$ 16,506	$ 10,965
Adjustments to reconcile net income to cash provided by (used for) operating activities:		
Provision for loan losses	1,300	1,500
Depreciation and other amortization	1,303	1,053
Accretion and amortization of securities discounts and premium, net	341	422
(Gain) loss on sale of investment securities available for sale	1	(2)
(Gain) loss on sale of real estate owned	(7)	3
(Gain) loss on disposal of fixed assets	-	50
Write-down of real estate owned	-	7
Compensation expense related to stock options and grants	1,108	989
Gain on sale of loans held for sale	(4,093)	(4,520)
Loans originated and held for sale	(161,272)	(144,622)
Proceeds from sale of loans held for sale	167,857	147,819
Increase in cash surrender value of bank owned life insurance	(662)	(590)
Increase in deferred tax asset	(3,906)	(2,472)
Increase in other assets, net	(296)	(72)
Increase in other liabilities	6,164	3,773
Net cash provided by operating activities	24,344	14,303
Investing activities		
Increase (decrease) in cash realized from:		
Origination of loans, net	(233,814)	(165,160)
Purchase of property and equipment	(1,739)	(4,290)
Purchase of investment securities:		
Available for sale	(13,903)	(20,675)
Other	(6,782)	(1,811)
Payments and maturities, calls and repayments of investment securities:		
Available for sale	6,962	6,918
Other	6,315	4,489
Proceeds from sale of investment securities available for sale	5,841	-
Purchase of life insurance policies	-	(6,850)
Proceeds from sale of real estate owned	132	498
Net cash used for investing activities	(236,988)	(186,881)
Financing activities		
Increase (decrease) in cash realized from:		
Increase in deposits, net	208,360	251,426
Increase (decrease) in Federal Home Loan Bank advances and other borrowings	1,300	(76,000)
Proceeds from issuance of common stock	-	24,758
Proceeds from the exercise of stock options and warrants	810	454
Net cash provided by financing activities	210,470	200,638
Net (decrease) increase in cash and cash equivalents	(2,174)	28,060
Cash and cash equivalents at beginning of the period	92,165	46,552
Cash and cash equivalents at end of the period	$ 89,991	$ 74,612
Supplemental information		
Cash paid for		
Interest	$ 10,824	$ 7,404
Income taxes	3,906	5,490
Schedule of non-cash transactions		
Real estate acquired in settlement of loans	-	289
Unrealized gain (loss) on securities, net of income taxes	(1,167)	413

See notes to consolidated financial statements that are an integral part of these consolidated statements.

SOUTHERN FIRST BANCSHARES, INC. AND SUBSIDIARY
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 – Nature of Business and Basis of Presentation

Business Activity
Southern First Bancshares, Inc. (the "Company") is a South Carolina corporation that owns all of the capital stock of Southern First Bank (the "Bank") and all of the stock of Greenville First Statutory Trust I and II (collectively, the "Trusts"). The Trusts are special purpose non-consolidated entities organized for the sole purpose of issuing trust preferred securities. The Bank's primary federal regulator is the Federal Deposit Insurance Corporation (the "FDIC"). The Bank is also regulated and examined by the South Carolina Board of Financial Institutions. The Bank is primarily engaged in the business of accepting demand deposits and savings deposits insured by the FDIC, and providing commercial, consumer and mortgage loans to the general public.

Basis of Presentation
The accompanying consolidated financial statements have been prepared in accordance with generally accepted accounting principles (“GAAP”) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all the information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the three and nine month periods ended September 30, 2018 are not necessarily indicative of the results that may be expected for the year ending December 31, 2018. For further information, refer to the consolidated financial statements and footnotes thereto included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2017 as filed with the Securities and Exchange Commission (“SEC”) on February 28, 2018. The consolidated financial statements include the accounts of the Company and the Bank. In accordance with Financial Accounting Standards Board (“FASB”) Accounting Standards Codification (“ASC”) 810, “Consolidation,” the financial statements related to the Trusts have not been consolidated.

Business Segments
In determining proper segment definition, the Company considers the materiality of a potential segment and components of the business about which financial information is available and regularly evaluated, relative to a resource allocation and performance assessment. The Company accounts for intersegment revenues and expenses as if the revenue/expense transactions were generated to third parties, that is, at current market prices. Please refer to “Note 9 – Reportable Segments” for further information on the reporting for the Company’s three business segments.

Use of Estimates
The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America, or GAAP, requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the date of the consolidated financial statements and the reported amount of income and expenses during the reporting periods. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses, real estate acquired in the settlement of loans, fair value of financial instruments, evaluating other-than-temporary-impairment of investment securities and valuation of deferred tax assets.

Reclassifications
Certain amounts, previously reported, have been reclassified to state all periods on a comparable basis and had no effect on shareholders’ equity or net income.

Subsequent Events
Subsequent events are events or transactions that occur after the balance sheet date but before financial statements are issued. Recognized subsequent events are events or transactions that provide additional evidence about conditions that existed at the date of the balance sheet, including the estimates inherent in the process of preparing financial statements. Non-recognized subsequent events are events that provide evidence about conditions that did not exist at the date of the balance sheet but arose after that date. Management performed an evaluation to determine whether there have been any subsequent events since the balance sheet date and determined that no subsequent events occurred requiring accrual or disclosure.

Revenue from Contracts with Customers
The Company records revenue from contracts with customers in accordance with Accounting Standards Codification Topic 606, "Revenue from Contracts with Customers" ("Topic 606"). Under Topic 606, the Company must identify the contract with a customer, identify the performance obligations in the contract, determine the transaction price, allocate the transaction price to the performance obligations in the contract, and recognize revenue when (or as) the Company satisfies a performance obligation. Significant revenue has not been recognized in the current reporting period that results from performance obligations satisfied in previous periods.

The Company's primary sources of revenue are derived from interest and dividends earned on loans, investment securities, and other financial instruments that are not within the scope of Topic 606. The Company has evaluated the nature of its contracts with customers and determined that further disaggregation of revenue from contracts with customers into more granular categories beyond what is presented in the Consolidated Statements of Income was not necessary. The Company generally fully satisfies its performance obligations on its contracts with customers as services are rendered and the transaction prices are typically fixed; charged either on a periodic basis or based on activity. Our accounting policies will not change materially since the principles of revenue recognition from the Accounting Standards Update are largely consistent with existing guidance and current practices applied by our business. The following is a discussion of revenues within the scope of the new guidance:

Service fees on deposit accounts - The Company earns fees from its deposit clients for various transaction-based, account maintenance, and overdraft or non-sufficient funds ("NSF") services. Transaction-based fees, which include services such as stop payment charges, statement rendering, and ACH fees, are recognized at the time the transaction is executed as that is the point in time the Company fulfills the client's request. Account maintenance fees, which relate primarily to monthly maintenance and account management, are earned over the course of a month, representing the period over which the Company satisfies the performance obligation. Overdraft and NSF fees are recognized at the point in time that the overdraft occurs or the NSF item is presented. Service charges on deposits are withdrawn from the client's account balance.

ATM and debit card income - The Company earns interchange fees from debit cardholder transactions conducted through the payment networks. Interchange fees from cardholder transactions represent a percentage of the underlying transaction value and are recognized daily, concurrently with the transaction processing services provided to the cardholder.

Income Taxes
On December 22, 2017, the United States enacted tax reform legislation commonly known as the Tax Cuts and Jobs Act (the "Tax Act"), resulting in significant modifications to existing law. Authoritative guidance and interpretation by regulatory bodies is ongoing, and as such, the accounting for the effects of the Tax Act is not final and the full impact of the new regulation is still being evaluated.

Adoption of New Accounting Standards
In May 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2014-09, "Revenue from Contracts with Customers" ("ASU 2014-09"), which requires an entity to recognize the amount of revenue to which it expects to be entitled for the transfer of promised goods or services to customers. The ASU replaces most existing revenue recognition guidance in GAAP. The new standard was effective for the Company on January 1, 2018. Adoption of ASU 2014-09 did not have a material impact on the Company's consolidated financial statements and related disclosures as the Company's primary sources of revenues are derived from interest and dividends earned on loans, investment securities, and other financial instruments that are not within the scope of ASU 2014-09. The Company's revenue recognition pattern for revenue streams within the scope of ASU 2014-09, including but not limited to service charges on deposit accounts, ATM and debit card income, and gains/losses on the sale of other real estate owned, did not change significantly from current practice. The standard permits the use of either the full retrospective or modified retrospective transition method. The Company elected to use the modified retrospective transition method which requires application of ASU 2014-09 to uncompleted contracts at the date of adoption however, periods prior to the date of adoption will not be retrospectively revised as the impact of the ASU on uncompleted contracts at the date of adoption was not material.

In January 2016, the FASB issued ASU No. 2016-01, “Financial Instruments – Overall: Recognition and Measurement of Financial Assets and Financial Liabilities” (“ASU 2016-01”). The guidance affects the accounting for equity investments, financial liabilities under the fair value option and the presentation and disclosure requirements of financial instruments. ASU 2016-01 was effective for the Company on January 1, 2018 and resulted in the use of an exit price rather than an entrance price to determine the fair value of loans not measured at fair value on a non-recurring basis in the consolidated balance sheets. See Note 7 – Fair Value Accounting for further information regarding the valuation of these loans.

In February 2018, the FASB amended certain aspects of the guidance issued in ASU 2016-01, the Financial Instruments Topic of the ASC. The amendments clarify certain aspects of the guidance issued in ASU 2016-01. The amendments were effective for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years beginning after June 15, 2018 and did not have a material effect on the Company’s financial statements.

In February 2018, the FASB Issued ASU 2018-02, “Income Statement (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income” (“ASU 2018-02”), which requires companies to reclassify the stranded effects in other comprehensive income to retained earnings as a result of the change in the tax rates under the Tax Act. The Company has opted to early adopt this pronouncement by retrospective application to each period (or periods) in which the effect of the change in the tax rate under the Tax Act is recognized. The impact of the reclassification from other comprehensive income to retained earnings did not have a material effect on the Company’s financial statements.

Newly Issued, But Not Yet Effective Accounting Standards
In February 2016, the FASB issued ASU 2016-02, “Leases (Topic 842)” (“ASU 2016-02”). The FASB issued this ASU to increase transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet by lessees for those leases classified as operating leases under current U.S. GAAP and disclosing key information about leasing arrangements. The amendments in this ASU are effective for annual periods, and interim periods within those annual periods, beginning after December 15, 2018. Early application of this ASU is permitted for all entities. The Company leases certain properties under operating leases that will result in the recognition of lease assets and lease liabilities on the Company’s balance sheet under the ASU. At September 30, 2018, the Company had contractual future minimum lease commitments of approximately $15.2 million, before considering renewal options that are generally present, and is currently evaluating the impact of this pronouncement on its financial statements.

In June 2016, the FASB issued ASU 2016-13, “Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments” (“ASU 2016-13”). Among other things, ASU 2016-13 requires the measurement of 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 form 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. In addition, ASU 2016-13 amends the accounting for credit losses on debt securities and purchased financial assets with credit deterioration. The amendments in ASU 2016-13 are effective for fiscal years beginning after December 31, 2019, and interim periods within those years for public business entities that are SEC filers. Early adoption is permitted for fiscal years, and interim periods within those years, beginning after December 15, 2018, however, the Company does not currently plan to early adopt the ASU. We are evaluating the impact of the ASU on our consolidated financial statements. In addition to our allowance for loan losses, we will also record an allowance for credit losses on debt securities instead of applying the impairment model currently utilized. The amount of the adjustments will be impacted by each portfolio’s composition and credit quality at the adoption date as well as economic conditions and forecasts at that time.

In March 2017, the FASB amended the requirement in the Receivables-Nonrefundable Fees and Other Costs Topic of the ASC related to the amortization period for certain purchased callable debt securities held at a premium. The amendments shorten the amortization period for the premium to the earliest call date. The amendments will be effective for the Company for interim and annual periods beginning after December 15, 2018. The Company does not expect these amendments to have a material effect on its financial statements.

Other accounting standards that have been issued or proposed by the FASB or other standards-setting bodies that do not require adoption until a future date are not expected to have a material impact on the consolidated financial statements upon adoption.

NOTE 2 – Investment Securities

The amortized costs and fair value of investment securities are as follows:

	September 30, 2018				
(dollars in thousands)		Amortized Cost	Gross Unrealized Gains	Losses	Fair Value
Available for sale					
US government agencies	$	8,981	2	349	8,634
SBA securities		3,635	-	163	3,472
State and political subdivisions		8,460	39	127	8,372
Asset-backed securities		6,583	13	10	6,586
Mortgage-backed securities					
FHLMC		8,012	-	361	7,651
FNMA		30,100	1	933	29,168
GNMA		3,168	1	166	3,003
Total mortgage-backed securities		41,280	2	1,460	39,822
Total investment securities available for sale	$	68,939	56	2,109	66,886

	December 31, 2017				
		Amortized Cost	Gross Unrealized Gains	Losses	Fair Value
Available for sale					
US government agencies	$	8,749	1	97	8,653
SBA securities		4,087	-	24	4,063
State and political subdivisions		11,242	179	25	11,396
Mortgage-backed securities					
FHLMC		9,102	-	149	8,953
FNMA		29,383	3	386	29,000
GNMA		5,618	2	82	5,538
Total mortgage-backed securities		44,103	5	617	43,491
Total investment securities available for sale	$	68,181	185	763	67,603

During the first nine months of 2018, there were $5.8 million of investment securities either sold or called, resulting in a loss on sale of $1,000. During the first nine months of 2017, there were $915,000 of investment securities either sold or called, subsequently resulting in a gain on sale of $2,000.

Contractual maturities and yields on the Company's investment securities at September 30, 2018 and December 31, 2017 are shown in the following table. Expected maturities may differ from contractual maturities because issuers may have the right to call or prepay obligations with or without call or prepayment penalties.

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	September 30, 2018									
	Less than one year		One to five years		Five to ten years		Over ten years		Total	
(dollars in thousands)	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield
Available for sale										
US government agencies	$ -	-	2,625	2.12%	6,009	2.75%	-	-	8,634	2.56%
SBA securities	-	-	-	-	-	-	3,472	2.67%	3,472	2.67%
State and political subdivisions	-	-	816	2.60%	4,186	3.09%	3,370	2.83%	8,372	2.94%
Asset-backed securities	-	-	-	-	-	-	6,586	2.91%	6,586	2.91%
Mortgage-backed securities	-	-	3,925	1.83%	9,119	1.80%	26,778	2.48%	39,822	2.26%
Total	$ -	-	7,366	2.02%	19,314	2.37%	40,206	2.59%	66,886	2.47%

	December 31, 2017									
	Less than one year		One to five years		Five to ten years		Over ten years		Total	
	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield
Available for sale										
US government agencies	$ 995	1.15%	1,503	2.04%	6,155	2.40%	-	-	8,653	2.20%
SBA securities	-	-	-	-	-	-	4,063	2.45%	4,063	2.45%
State and political subdivisions	-	-	1,163	1.96%	7,162	2.84%	3,071	2.76%	11,396	2.73%
Mortgage-backed securities	432	0.99%	-	-	11,328	1.84%	31,731	2.06%	43,491	1.99%
Total	$ 1,427	1.10%	2,666	1.59%	24,645	2.27%	38,865	2.15%	67,603	2.17%

The tables below summarize gross unrealized losses on investment securities and the fair market value of the related securities at September 30, 2018 and December 31, 2017, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position.

	September 30, 2018								
		Less than 12 months			12 months or longer			Total	
		Fair	Unrealized		Fair	Unrealized		Fair	Unrealized
(dollars in thousands)	#	value	losses	#	value	losses	#	value	losses
Available for sale									
US government agencies	3	$ 3,368	$ 86	6	$ 4,764	$ 263	9	$ 8,132	$ 349
SBA securities	-	-	-	2	3,472	163	2	3,472	163
State and political subdivisions	4	3,491	48	5	1,935	79	9	5,426	127
Asset-backed securities	2	3,474	10	-	-	-	2	3,474	10
Mortgage-backed securities									
FHLMC	-	-	-	10	7,651	361	10	7,651	361
FNMA	4	5,476	60	23	23,656	873	27	29,132	933
GNMA	1	1,206	70	2	1,776	96	3	2,982	166
Total	14	$ 17,015	$ 274	48	$ 43,254	$ 1,835	62	$ 60,269	$ 2,109

	December 31, 2017								
		Less than 12 months			12 months or longer			Total	
		Fair	Unrealized		Fair	Unrealized		Fair	Unrealized
	#	value	losses	#	value	losses	#	value	losses
Available for sale									
US government agencies	5	$ 4,184	$ 22	4	$ 3,968	$ 75	9	$ 8,152	$ 97
SBA securities	1	2,936	13	1	1,127	11	2	4,063	24
State and political subdivisions	3	1,214	9	2	792	16	5	2,006	25
Mortgage-backed securities									
FHLMC	3	2,897	26	7	6,056	123	10	8,953	149
FNMA	11	14,345	135	13	14,597	251	24	28,942	386
GNMA	2	2,270	40	1	971	42	3	3,241	82
Total	25	$ 27,846	$ 245	28	$ 27,511	$ 518	53	$ 55,357	$ 763

At September 30, 2018, the Company had 14 individual investments with a fair market value of $17.0 million that were in an unrealized loss position for less than 12 months and 48 individual investments with a fair market value of $43.3 million that were in an unrealized loss position for 12 months or longer. The unrealized losses were primarily attributable to changes in interest rates, rather than deterioration in credit quality. The individual securities are each investment grade securities. The Company considers the length of time and extent to which the fair value of available-for-sale debt securities have been less than cost to conclude that such securities are not other-than-temporarily impaired. The Company also considers other factors such as the financial condition of the issuer, including credit ratings and specific events affecting the operations of the issuer, volatility of the security, underlying assets that collateralize the debt security, and other industry and macroeconomic conditions.

As the Company has no intent to sell securities with unrealized losses and it is not more-likely-than-not that the Company will be required to sell these securities before recovery of amortized cost, the Company has concluded that these securities are not impaired on an other-than-temporary basis.

Other investments are comprised of the following and are recorded at cost which approximates fair value.

(dollars in thousands)		September 30, 2018	December 31, 2017
Federal Home Loan Bank stock	$	4,373	3,754
Investment in Trust Preferred securities		403	403
Other investments		153	305
Total other investments	$	4,929	4,462

The Company has evaluated the Federal Home Loan Bank ("FHLB") stock for impairment and determined that the investment in the FHLB stock is not other than temporarily impaired as of September 30, 2018 and ultimate recoverability of the par value of this investment is probable. All of the FHLB stock is used to collateralize advances with the FHLB.

At September 30, 2018, there were no securities pledged as collateral for borrowings or client deposits. At December 31, 2017, $7.7 million of securities were pledged as collateral for repurchase agreements from brokers.

NOTE 3 – Mortgage Loans Held for Sale

Mortgage loans originated and intended for sale in the secondary market are reported as loans held for sale and carried at fair value under the fair value option with changes in fair value recognized in current period earnings. At the date of funding of the mortgage loan held for sale, the funded amount of the loan, the related derivative asset or liability of the associated interest rate lock commitment, less direct loan costs becomes the initial recorded investment in the loan held for sale. Such amount approximates the fair value of the loan. At September 30, 2018, mortgage loans held for sale totaled $9.3 million compared to $11.8 million at December 31, 2017.

Mortgage loans held for sale are considered de-recognized, or sold, when the Company surrenders control over the financial assets. Control is considered to have been surrendered when the transferred assets have been isolated from the Company, beyond the reach of the Company and its creditors; the purchaser obtains the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred assets; and the Company does not maintain effective control over the transferred assets through an agreement that both entitles and obligates the Company to repurchase or redeem the transferred assets before their maturity or the ability to unilaterally cause the holder to return specific assets.

Gains and losses from the sale of mortgage loans are recognized based upon the difference between the sales proceeds and carrying value of the related loans upon sale and are recorded in mortgage banking income in the statement of income. Mortgage banking income also includes the gains and losses associated with the loans held for sale and the gains and losses from derivatives.

Mortgage loans sold by the Company to investors and which were believed to have met investor and agency underwriting guidelines at the time of sale may be subject to repurchase or indemnification in the event of specific default by the borrower or subsequent discovery that underwriting standards were not met. The Company may, upon mutual agreement, agree to repurchase the loans or indemnify the investor against future losses on such loans. In such cases, the Company bears any subsequent credit loss on the loans.

The Company establishes mortgage repurchase reserves related to various representations and warranties that reflect management's estimate of losses based on a combination of factors. The Company establishes a reserve at the time loans are sold and updates the reserve estimate on a quarterly basis during the estimated life of the loan.

NOTE 4 – Loans and Allowance for Loan Losses

The following table summarizes the composition of our loan portfolio. Total gross loans are recorded net of deferred loan fees and costs, which totaled $2.8 million as of September 30, 2018 and $2.3 million as of December 31, 2017.

	September 30, 2018		December 31, 2017	
(dollars in thousands)	Amount	% of Total	Amount	% of Total
Commercial				
Owner occupied RE	$ 372,120	23.0 %	$ 316,818	22.8 %
Non-owner occupied RE	399,166	24.6 %	312,798	22.6 %
Construction	68,415	4.2 %	51,179	3.7 %
Business	244,348	15.1 %	226,158	16.3 %
Total commercial loans	1,084,049	66.9 %	906,953	65.4 %
Consumer				
Real estate	311,271	19.2 %	273,050	19.7 %
Home equity	163,654	10.1 %	156,141	11.3 %
Construction	38,015	2.4 %	28,351	2.0 %
Other	23,212	1.4 %	22,575	1.6 %
Total consumer loans	536,152	33.1 %	480,117	34.6 %
Total gross loans, net of deferred fees	1,620,201	100.0%	1,387,070	100.0%
Less—allowance for loan losses	(16,140)		(15,523)	
Total loans, net	$ 1,604,061		$ 1,371,547	

Maturities and Sensitivity of Loans to Changes in Interest Rates

The information in the following tables summarizes the loan maturity distribution by type and related interest rate characteristics based on the contractual maturities of individual loans, including loans which may be subject to renewal at their contractual maturity. Renewal of such loans is subject to review and credit approval, as well as modification of terms upon maturity. Actual repayments of loans may differ from the maturities reflected below, because borrowers have the right to prepay obligations with or without prepayment penalties.

	September 30, 2018			
(dollars in thousands)	One year or less	After one but within five years	After five years	Total
Commercial				
Owner occupied RE	$ 25,962	164,564	181,594	372,120
Non-owner occupied RE	35,003	213,384	150,779	399,166
Construction	19,455	26,137	22,823	68,415
Business	74,091	124,489	45,768	244,348
Total commercial loans	154,511	528,574	400,964	1,084,049
Consumer				
Real estate	37,128	67,254	206,889	311,271
Home equity	11,097	25,556	127,001	163,654
Construction	20,006	887	17,122	38,015
Other	7,961	10,714	4,537	23,212
Total consumer loans	76,192	104,411	355,549	536,152
Total gross loans, net of deferred fees	$ 230,703	632,985	756,513	1,620,201
Loans maturing after one year with:				
Fixed interest rates				$ 1,056,262
Floating interest rates				333,236

(dollars in thousands)	December 31, 2017 One year or less	After one but within five years	After five years	Total
Commercial				
Owner occupied RE	$ 24,171	167,425	125,222	316,818
Non-owner occupied RE	39,519	165,764	107,515	312,798
Construction	13,086	12,796	25,297	51,179
Business	73,588	107,584	44,986	226,158
Total commercial loans	150,364	453,569	303,020	906,953
Consumer				
Real estate	30,172	61,809	181,069	273,050
Home equity	13,331	25,807	117,003	156,141
Construction	14,943	1,737	11,671	28,351
Other	7,203	11,371	4,001	22,575
Total consumer	65,649	100,724	313,744	480,117
Total gross loan, net of deferred fees	$ 216,013	554,293	616,764	1,387,070
Loans maturing after one year with:				
Fixed interest rates				$ 875,991
Floating interest rates				295,066

Portfolio Segment Methodology

Commercial
Commercial loans are assessed for estimated losses by grading each loan using various risk factors identified through periodic reviews. The Company applies historic grade-specific loss factors to each loan class. In the development of statistically derived loan grade loss factors, the Company observes historical losses over 20 quarters for each loan grade. These loss estimates are adjusted as appropriate based on additional analysis of external loss data or other risks identified from current economic conditions and credit quality trends. The allowance also includes an amount for the estimated impairment on nonaccrual commercial loans and commercial loans modified in a troubled debt restructuring ("TDR"), whether on accrual or nonaccrual status.

Consumer
For consumer loans, the Company determines the allowance on a collective basis utilizing historical losses over 20 quarters to represent its best estimate of inherent loss. The Company pools loans, generally by loan class with similar risk characteristics. The allowance also includes an amount for the estimated impairment on nonaccrual consumer loans and consumer loans modified in a TDR, whether on accrual or nonaccrual status.

Credit Quality Indicators

Commercial
We manage a consistent process for assessing commercial loan credit quality by monitoring its loan grading trends and past due statistics. All loans are subject to individual risk assessment. Our risk categories include Pass, Special Mention, Substandard, and Doubtful, each of which is defined by our banking regulatory agencies. Delinquency statistics are also an important indicator of credit quality in the establishment of our allowance for loan losses.

We categorize our loans into risk categories based on relevant information about the ability of the borrower to service their debt such as current financial information, historical payment experience, credit documentation, public information, and current economic trends, among other factors. A description of the general characteristics of the risk grades is as follows:

Pass—These loans range from minimal credit risk to average credit risk; however, still have acceptable credit risk.

Special mention—A special mention loan has potential weaknesses that deserve management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan or the institution's credit position at some future date.

Substandard—A substandard loan is inadequately protected by the current sound worth and paying capacity of the obligor or of the collateral pledged, if any. Loans so classified must have a well-defined weakness, or weaknesses, that may jeopardize the liquidation of the debt. A substandard loan is characterized by the distinct possibility that the Bank will sustain some loss if the deficiencies are not corrected.

Doubtful—A doubtful loan has all of the weaknesses inherent in one classified as substandard with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of the currently existing facts, conditions and values, highly questionable and improbable.

The tables below provide a breakdown of outstanding commercial loans by risk category.

					September 30, 2018
(dollars in thousands)	Owner occupied RE	Non-owner occupied RE	Construction	Business	Total
Pass	$ 368,266	394,880	68,415	238,167	1,069,728
Special mention	725	121	-	3,033	3,879
Substandard	3,129	4,165	-	3,148	10,442
Doubtful	-	-	-	-	-
	$ 372,120	399,166	68,415	244,348	1,084,049

					December 31, 2017
	Owner occupied RE	Non-owner occupied RE	Construction	Business	Total
Pass	$ 312,628	306,965	51,179	215,729	886,501
Special mention	1,770	2,082	-	5,540	9,392
Substandard	2,420	3,751	-	4,889	11,060
Doubtful	-	-	-	-	-
	$ 316,818	312,798	51,179	226,158	906,953

The following tables provide past due information for outstanding commercial loans and include loans on nonaccrual status as well as accruing TDRs.

					September 30, 2018
(dollars in thousands)	Owner occupied RE	Non-owner occupied RE	Construction	Business	Total
Current	$ 372,120	398,973	68,415	244,246	1,083,754
30-59 days past due	-	-	-	13	13
60-89 days past due	-	-	-	-	-
Greater than 90 Days	-	193	-	89	282
	$ 372,120	399,166	68,415	244,348	1,084,049

					December 31, 2017
	Owner occupied RE	Non-owner occupied RE	Construction	Business	Total
Current	$ 316,818	312,477	51,179	224,861	905,335
30-59 days past due	-	129	-	416	545
60-89 days past due	-	-	-	-	-
Greater than 90 Days	-	192	-	881	1,073
	$ 316,818	312,798	51,179	226,158	906,953

Consumer
The Company manages a consistent process for assessing consumer loan credit quality by monitoring its loan grading trends and past due statistics. All loans are subject to individual risk assessment. The Company's categories include Pass, Special Mention, Substandard, and Doubtful, which are defined above. Delinquency statistics are also an important indicator of credit quality in the establishment of the allowance for loan losses.

The tables below provide a breakdown of outstanding consumer loans by risk category.

					September 30, 2018
(dollars in thousands)	**Real estate**	**Home equity**	**Construction**	**Other**	**Total**
Pass	$ 305,496	160,544	38,015	22,999	527,054
Special mention	1,886	526	-	156	2,568
Substandard	3,889	2,584	-	57	6,530
Doubtful	-	-	-	-	-
	$ 311,271	163,654	38,015	23,212	536,152

					December 31, 2017
	Real estate	**Home equity**	**Construction**	**Other**	**Total**
Pass	$ 269,422	152,545	28,351	22,367	472,685
Special mention	715	1,025	-	88	1,828
Substandard	2,913	2,571	-	120	5,604
Doubtful	-	-	-	-	-
	$ 273,050	156,141	28,351	22,575	480,117

The following tables provide past due information for outstanding consumer loans and include loans on nonaccrual status as well as accruing TDRs.

					September 30, 2018
(dollars in thousands)	**Real estate**	**Home equity**	**Construction**	**Other**	**Total**
Current	$ 310,665	163,309	38,015	23,082	535,071
30-59 days past due	249	345	-	55	649
60-89 days past due	357	-	-	75	432
Greater than 90 Days	-	-	-	-	-
	$ 311,271	163,654	38,015	23,212	536,152

					December 31, 2017
	Real estate	**Home equity**	**Construction**	**Other**	**Total**
Current	$ 271,284	154,821	28,351	22,506	476,962
30-59 days past due	681	325	-	69	1,075
60-89 days past due	131	995	-	-	1,126
Greater than 90 Days	954	-	-	-	954
	$ 273,050	156,141	28,351	22,575	480,117

As of September 30, 2018 and December 31, 2017, total loans 30 days or more past due represented 0.08% and 0.34% of the Company's total loan portfolio, respectively. Commercial loans 30 days or more past due were 0.02% and 0.12% of the Company's total loan portfolio as of September 30, 2018 and December 31, 2017, respectively. As of September 30, 2018 and December 31, 2017, consumer loans 30 days or more past due were 0.07% and 0.23% of total loans, respectively.

Nonperforming assets

The following table shows the nonperforming assets and the related percentage of nonperforming assets to total assets and gross loans. Generally, a loan is placed on nonaccrual status when it becomes 90 days past due as to principal or interest, or when the Company believes, after considering economic and business conditions and collection efforts, that the borrower's financial condition is such that collection of the contractual principal or interest on the loan is doubtful. A payment of interest on a loan that is classified as nonaccrual is recognized as a reduction in principal when received.

Following is a summary of our nonperforming assets, including nonaccruing TDRs.

(dollars in thousands)	September 30, 2018	December 31, 2017
Commercial		
Owner occupied RE	$ -	-
Non-owner occupied RE	1,680	1,581
Construction	-	-
Business	89	910
Consumer		
Real estate	1,153	992
Home equity	850	1,144
Construction	-	-
Other	-	1
Nonaccruing troubled debt restructurings	2,194	2,673
Total nonaccrual loans, including nonaccruing TDRs	5,966	7,301
Other real estate owned	117	242
Total nonperforming assets	$ 6,083	7,543
Nonperforming assets as a percentage of:		
Total assets	0.33%	0.46%
Gross loans	0.38%	0.54%
Total loans over 90 days past due	282	2,027
Loans over 90 days past due and still accruing	-	-
Accruing troubled debt restructurings	$ 6,699	5,145

Impaired Loans

The table below summarizes key information for impaired loans. The Company's impaired loans include loans on nonaccrual status and loans modified in a TDR, whether on accrual or nonaccrual status. These impaired loans may have estimated impairment which is included in the allowance for loan losses. The Company's commercial and consumer impaired loans are evaluated individually to determine the related allowance for loan losses.