CITIZENS FINANCIAL SERVICES INC
Form 10-Q
November 08, 2018
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 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 0 13222

CITIZENS FINANCIAL SERVICES, INC.
(Exact name of registrant as specified in its charter)

PENNSYLVANIA	23 2265045
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

15 South Main Street
Mansfield, Pennsylvania 16933
(Address of principal executive offices)(Zip Code)

Registrant's telephone number, including area code: (570) 662 2121

N/A
(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 to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes __X__ No_____

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted 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 such files). Yes __X__ No_____

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

Large accelerated filer ____ Accelerated filer _X__

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 __X__

The number of outstanding shares of the Registrant's Common Stock, as of October 31, 2018, was 3,509,143.

Citizens Financial Services, Inc.
Form 10-Q

INDEX

CITIZENS FINANCIAL SERVICES, INC.
CONSOLIDATED BALANCE SHEET
(UNAUDITED)

(in thousands except share data)	September 30, 2018	December 31, 2017
ASSETS:		
Cash and due from banks:		
Noninterest-bearing	$15,496	$16,347
Interest-bearing	1,004	2,170
Total cash and cash equivalents	16,500	18,517
Interest bearing time deposits with other banks	14,754	10,283
Equity Securities	291	-
Available-for-sale securities	240,426	254,782
Loans held for sale	960	1,439
Loans (net of allowance for loan losses: 2018, $12,383 and 2017, $11,190)	1,047,948	989,335
Premises and equipment	16,189	16,523
Accrued interest receivable	4,480	4,196
Goodwill	23,296	23,296
Bank owned life insurance	27,350	26,883
Other intangibles	1,703	1,953
Other assets	13,983	14,679
TOTAL ASSETS	$1,407,880	$1,361,886
LIABILITIES:		
Deposits:		
Noninterest-bearing	$173,379	$171,840
Interest-bearing	1,001,464	933,103
Total deposits	1,174,843	1,104,943
Borrowed funds	86,097	114,664
Accrued interest payable	979	897
Other liabilities	11,561	12,371
TOTAL LIABILITIES	1,273,480	1,232,875
STOCKHOLDERS' EQUITY:		
Preferred Stock		
$1.00 par value; authorized 3,000,000 shares at September 30, 2018 and December 31, 2017; none issued in 2018 or 2017	-	-
Common stock		
$1.00 par value; authorized 25,000,000 shares at September 30 2018 and 15,000,000 at December 31, 2017; issued 3,904,212 at September 30, 2018 and 3,869,939 at December 31, 2017	3,904	3,870
Additional paid-in capital	53,122	51,108
Retained earnings	96,754	89,982
Accumulated other comprehensive loss	(6,081)	(3,398)
Treasury stock, at cost: 395,070 shares at September 30, 2018 and 383,065 shares at December 31, 2017	(13,299)	(12,551)

TOTAL STOCKHOLDERS' EQUITY	134,400	129,011
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$1,407,880	$1,361,886

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

1

CITIZENS FINANCIAL SERVICES, INC.
CONSOLIDATED STATEMENT OF INCOME
(UNAUDITED)

	Three Months Ended September 30,		Nine Months Ended September 30,	
(in thousands, except share and per share data)	2018	2017	2018	2017
INTEREST INCOME:				
Interest and fees on loans	$12,666	$10,659	$36,988	$30,680
Interest-bearing deposits with banks	94	49	218	129
Investment securities:				
Taxable	967	762	2,683	2,341
Nontaxable	425	588	1,426	1,857
Dividends	107	62	355	191
TOTAL INTEREST INCOME	14,259	12,120	41,670	35,198
INTEREST EXPENSE:				
Deposits	1,794	1,210	4,695	3,398
Borrowed funds	695	293	2,034	782
TOTAL INTEREST EXPENSE	2,489	1,503	6,729	4,180
NET INTEREST INCOME	11,770	10,617	34,941	31,018
Provision for loan losses	475	500	1,300	1,740
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	11,295	10,117	33,641	29,278
NON-INTEREST INCOME:				
Service charges	1,181	1,145	3,455	3,323
Trust	147	187	548	596
Brokerage and insurance	222	154	571	459
Gains on loans sold	170	134	302	383
Equity security gains (losses), net	(4)	-	9	-
Available for sale security gains (losses), net	(8)	9	(8)	204
Earnings on bank owned life insurance	161	166	467	499
Other	141	126	414	380
TOTAL NON-INTEREST INCOME	2,010	1,921	5,758	5,844
NON-INTEREST EXPENSES:				
Salaries and employee benefits	4,679	4,287	14,251	13,030
Occupancy	500	475	1,606	1,479
Furniture and equipment	130	159	394	444
Professional fees	507	318	1,273	942
FDIC insurance	120	95	327	295
Pennsylvania shares tax	250	243	850	767
Amortization of intangibles	74	74	224	223
OREO expenses	6	139	92	255
Other	1,522	1,457	4,305	4,169
TOTAL NON-INTEREST EXPENSES	7,788	7,247	23,322	21,604
Income before provision for income taxes	5,517	4,791	16,077	13,518
Provision for income taxes	936	1,141	2,558	3,097
NET INCOME	$4,581	$3,650	$13,519	$10,421

PER COMMON SHARE DATA:

Net Income - Basic	$1.31	$1.04	$3.85	$2.96
Net Income - Diluted	$1.31	$1.04	$3.85	$2.96
Cash Dividends Paid	$0.440	$0.426	$1.302	$1.228
Number of shares used in computation - basic	3,502,859	3,517,208	3,507,515	3,515,032
Number of shares used in computation - diluted	3,503,020	3,519,493	3,509,676	3,516,906

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

2

CITIZENS FINANCIAL SERVICES, INC.
CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME
(UNAUDITED)

	Three Months Ended September 30,		Nine Months Ended September 30,	
(in thousands)	2018	2017	2018	2017
Net income	$4,581	$3,650	$13,519	$10,421
Other comprehensive income (loss):				
Change in unrealized gains (losses) on available				
For sale securities	(971)	(288)	(3,544)	437
Income tax effect	205	98	744	(149)
Change in unrecognized pension cost	47	56	140	168
Income tax effect	(11)	(19)	(30)	(57)
Less: Reclassification adjustment for investment				
security (gains) losses included in net income	8	(9)	8	(204)
Income tax effect	(2)	3	(2)	69
Other comprehensive income (loss), net of tax	(724)	(159)	(2,684)	264
Comprehensive income	$3,857	$3,491	$10,835	$10,685

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

3

CITIZENS FINANCIAL SERVICES, INC.
CONSOLIDATED STATEMENT OF CASH FLOWS
(UNAUDITED)

	Nine Months Ended September 30,	
(in thousands)	2018	2017
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$13,519	$10,421
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	1,300	1,740
Depreciation and amortization	301	321
Amortization and accretion of investment securities	813	1,089
Deferred income taxes	(260)	(381)
Investment securities (gains) losses, net	1	(204)
Earnings on bank owned life insurance	(467)	(499)
Originations of loans held for sale	(14,709)	(17,144)
Proceeds from sales of loans held for sale	15,374	17,789
Realized gains on loans sold	(302)	(383)
(Increase) decrease in accrued interest receivable	(284)	303
Increase in accrued interest payable	82	11
Other, net	(435)	(360)
Net cash provided by operating activities	14,933	12,703
CASH FLOWS FROM INVESTING ACTIVITIES:		
Available-for-sale securities:		
Proceeds from sales	25,168	30,393
Proceeds from maturity and principal repayments	41,027	47,677
Purchase of securities	(56,289)	(20,548)
Purchase of equity securities	(191)	-
Purchase of interest bearing time deposits with other banks	(5,713)	(6,301)
Proceeds from sale of interest bearing time deposits with other banks	1,239	2,741
Proceeds from matured interest bearing time deposits with other banks	-	496
Proceeds from redemption of regulatory stock	7,874	6,090
Purchase of regulatory stock	(6,751)	(5,668)
Net increase in loans	(59,646)	(107,864)
Purchase of premises and equipment	(228)	(179)
Proceeds from sale of foreclosed assets held for sale	899	312
Net cash used in investing activities	(52,611)	(52,851)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net increase in deposits	69,900	46,602
Proceeds from long-term borrowings	7	7
Repayments of long-term borrowings	(1,000)	-
Net decrease in short-term borrowed funds	(27,574)	(6,041)
Purchase of treasury and restricted stock	(1,098)	(645)
Dividends paid	(4,574)	(3,714)
Net cash provided by financing activities	35,661	36,209
Net decrease in cash and cash equivalents	(2,017)	(3,939)
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	18,517	17,754
CASH AND CASH EQUIVALENTS AT END OF PERIOD	$16,500	$13,815

Supplemental Disclosures of Cash Flow Information:		
Interest paid	$6,647	$4,169
Income taxes paid	$1,900	$2,950
Loans transferred to foreclosed property	$381	$785

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

CITIZENS FINANCIAL SERVICES, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

Note 1 - Basis of Presentation

Citizens Financial Services, Inc. (individually and collectively with its direct and indirect subsidiaries, the "Company") is a Pennsylvania corporation and the holding company of its wholly owned subsidiary, First Citizens Community Bank (the "Bank"), and of the Bank's wholly owned subsidiary, First Citizens Insurance Agency, Inc. ("First Citizens Insurance").

The accompanying consolidated financial statements have been prepared pursuant to rules and regulations of the Securities and Exchange Commission ("SEC") and in conformity with U.S. generally accepted accounting principles. Because this report is based on an interim period, certain information and footnote disclosures normally included in financial statements prepared in accordance with U.S. generally accepted accounting principles have been condensed or omitted. Certain of the prior year amounts have been reclassified to conform with the current year presentation. Such reclassifications had no effect on net income or stockholders' equity. All material inter company balances and transactions have been eliminated in consolidation.

In the opinion of management of the Company, the accompanying interim financial statements at September 30, 2018 and for the periods ended September 30, 2018 and 2017 include all adjustments, consisting of only normal recurring adjustments, necessary for a fair presentation of the financial condition and the results of operations at the dates and for the periods presented. In preparing the consolidated financial statements, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the balance sheet and revenues and expenses for the period covered by the Consolidated Income Statement. . The financial performance reported for the Company for the nine month period ended September 30, 2018 is not necessarily indicative of the results to be expected for the full year. This information should be read in conjunction with the Company's Annual Report on Form 10-K for the year ended December 31, 2017.

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 other than additional disclosures in note 2 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.

In January 2016, the FASB finalized ASU 2016-01, Financial Instruments - Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities. This accounting standard (a) requires separate presentation of equity investments (except those accounted for under the equity method of accounting or those that result in consolidation of the investee) on the balance sheet and measured at fair value with changes in fair value recognized in net income; (b) simplifies the impairment assessment of equity investments without readily determinable fair values by requiring a qualitative assessment to identify impairment; (c) eliminates the requirement to disclose the fair value of financial instruments measured at amortized cost for entities that are not public business entities; (d) eliminates the requirement for public business entities to disclose the method(s) and significant assumptions used to estimate the fair value that is required to be disclosed for financial instruments measured at amortized cost on the balance sheet; (e) requires public business entities to use the exit price notion when measuring the fair value of financial instruments for disclosure purposes; (f) requires separate presentation of financial assets and financial liabilities by measurement category and form of financial asset (that is, securities or loans and receivables) on the balance sheet or the accompanying notes to the financial statements; and (g) clarifies 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.

The adoption resulted in the Company recognizing a one-time cumulative effect adjustment of $1,000 between accumulated other comprehensive income and retained earnings on the consolidated balance sheet for the fair value of equity securities included in accumulated other comprehensive income as of the beginning of the period. The adjustment had no impact on net income on any prior periods presented.

The Company has adopted this standard during the reporting period. On a prospective basis, the Company implemented changes to the measurement of the fair value of financial instruments using an exit price notion for disclosure purposes included in Note 12 to the financial statements. The September 30, 2018 fair value of each class of financial instruments disclosure did utilize the exit price notion when measuring fair value and, therefore, may not be comparable to the December 3l, 2017 disclosure.

In March 2017, the FASB issued ASU 2017-07, Compensation-Retirement Benefits (Topic 71S). The amendments in this Update require that an employer report the service cost component in the same line item or items as other compensation costs arising from services rendered by the pertinent employees during the period. The other components of net benefit cost are required to be presented in the income statement separately from the service cost component. The Company adopted the standard on January 1, 2018, which resulted in a reclassification of $(50)and ($150) from Salaries and employee benefits into Other noninterest expenses on the Consolidated Statement of Income for the three and nine month periods ended September 30, 2017. See Note 9 for additional information on the presentation of these pension cost components.

Note 2 – Revenue Recognition

Effective January 1, 2018, the Company adopted Accounting Standards Update ASU 2014-09 Revenue from Contracts with Customers – Topic 606 and all subsequent ASUs that modified ASC 606. The Company has elected to apply the standard to all prior periods presented utilizing the full retrospective approach. The implementation of the new standard had no material impact to the measurement or recognition of revenue of prior periods. Management determined that the primary sources of revenue emanating from interest and dividend income on loans and investments along with noninterest revenue resulting from investment security gains, loan servicing, gains on loans sold and earnings on bank owned life insurances are not within the scope of ASC 606. As a result, no changes were made during the period related to these sources of revenue, which cumulatively comprise 90.0% and 89.8% of the total revenue of the Company for the three and nine months ended September 30, 2018, respectively. The main types of noninterest income within the scope of the standard are as follows:

- Service charges on deposit accounts – The Company has contracts with its deposit customers where fees are charged if certain parameters are not met. These agreements can be cancelled at any time by either the Company or the deposit customer. Revenue from these transactions is recognized on a monthly basis as the Company has an unconditional right to the fee consideration. The Company also has transaction fees related to specific transactions or activities resulting from a customer request or activity that include overdraft fees, online banking fees, interchange fees, ATM fees and other transaction fees. All of these fees are attributable to specific performance obligations of the Company where the revenue is recognized at a defined point in time upon the completion of the requested service/transaction.

- Trust fees – Typical contracts for trust services are based on a fixed percentage of the assets earned ratably over a defined period and billed on a monthly basis. Fees charged to customers' accounts are recognized as revenue over the period during which the Company fulfills its performance obligation under the contract (i.e., holding client asset in a managed fiduciary trust account). For these accounts, the performance obligation of the Company is typically satisfied by holding and managing the customer's assets over time. Other fees related to specific customer requests are attributable to specific performance obligations of the Company where the revenue is recognized at a defined point in time, upon completion of the requested service/transaction.

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Gains (losses) on sale of other real estate owned – Gains and losses are recognized at the completion of the property sale when the buyer obtains control of the real estate and all of the performance obligations of the Company have been satisfied. Evidence of the buyer obtaining control of the asset include transfer of the property title, physical possession of the asset, and the buyer obtaining control of the risks and rewards related to the asset. In situations where the Company agrees to provide financing to facilitate the sale, additional analysis is performed to ensure that the contract for sale identifies the buyer and seller, the asset to be transferred, payment terms, and that the contract has a true commercial substance and that collection of amounts due from the buyer are reasonable. In situations where financing terms are not reflective of current market terms, the transaction price is discounted impacting the gain/loss and the carrying value of the asset.

- Brokerage and insurance – Fees includes commissions from the sales of investments and insurance products recognized on a trade date basis as the performance obligation is satisfied at the point in time in which the trade is processed. Additional fees are based on a percentage of the market value of customer accounts and billed on a monthly or quarterly basis. The Company's performance obligation under the contracts with certain customers is generally satisfied through the passage of time as the Company monitors and manages the assets in the customer's portfolio and is not dependent on certain return or performance level of the customer's portfolio. Fees for these services are billed monthly and are recorded as revenue at the end of the month for which the wealth management service has been performed. Other performance obligations (such as the delivery of account statements to customers) are generally considered immaterial to the overall transaction price.

The following table depicts the disaggregation of revenue derived from contracts with customers to depict the nature, amount, timing, and uncertainty of revenue and cash flows for the three and nine months ended September 30, 2018 (in thousands). All revenue in the table below relates to goods and services transferred at a point in time.

	September 30, 2018	
Revenue stream	Three Months Ended	Nine Months Ended
Service charges on deposit accounts		
Overdraft fees	$395	$ 1,143
Statement fees	50	155
Interchange revenue	566	1,671
ATM income	104	301
Other service charges	66	185
Total Service Charges	1,181	3,455
Trust	147	548
Brokerage and insurance	222	571
Other	84	245
Total	$1,634	$ 4,819

Note 3 - Earnings per Share

The following table sets forth the computation of earnings per share. Earnings per share calculations give retroactive effect to stock dividends declared by the Company.

	Three months ended September 30,		Nine months ended September 30,	
	2018	2017	2018	2017
Net income applicable to common stock	$4,581,000	$3,650,000	$13,519,000	$10,421,000
Basic earnings per share computation				
Weighted average common shares outstanding	3,502,859	3,517,208	3,507,515	3,515,032
Earnings per share - basic	$1.31	$1.04	$3.85	$2.96
Diluted earnings per share computation				
Weighted average common shares outstanding for basic earnings per share	3,502,859	3,517,208	3,507,515	3,515,032
Add: Dilutive effects of restricted stock	161	2,285	2,161	1,874
Weighted average common shares outstanding for dilutive earnings per share	3,503,020	3,519,493	3,509,676	3,516,906
Earnings per share - diluted	$1.31	$1.04	$3.85	$2.96

For the three months ended September 30, 2018 and 2017, there were 4,696 and 1,107 shares, respectively, related to the restricted stock plan that were excluded from the diluted earnings per share calculations since they were anti-dilutive. These anti-dilutive shares had per share prices ranging from $46.69-$62.93 for the three month period ended September 30, 2018 and per share prices ranging from $49.87-$53.15 for the three month period ended September 30, 2017. For the nine months ended September 30, 2018 and 2017, 4,033 and 4,162 shares, respectively, related to the restricted stock plan were excluded from the diluted earnings per share calculations since they were anti-dilutive. These anti-dilutive shares had prices ranging from $46.69-$61.04 for the nine month period ended September 30, 2018 and prices ranging from $46.69-$53.15 for the nine month period ended September 30, 2017.

Note 4 – Investments

The amortized cost, gross unrealized gains and losses, and fair value of investment securities at September 30, 2018 and December 31, 2017 were as follows (in thousands):

September 30, 2018	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available-for-sale securities:				
U.S. agency securities	$ 109,612	$ -	$ (1,343)	$ 108,269
U.S. treasury securities	33,798	-	(961)	32,837
Obligations of state and political subdivisions	51,941	116	(459)	51,598
Corporate obligations	3,000	-	-	3,000
Mortgage-backed securities in government sponsored entities	45,951	2	(1,231)	44,722
Total available-for-sale securities	$ 244,302	$ 118	$ (3,994)	$ 240,426
December 31, 2017				
Available-for-sale securities:				
U.S. agency securities	$ 99,454	$ 26	$ (593)	$ 98,887
U.S. treasury securities	28,782	-	(178)	28,604
Obligations of state and political subdivisions	78,409	820	(139)	79,090
Corporate obligations	3,000	83	-	3,083

Mortgage-backed securities in				
government sponsored entities	45,385	19	(377)	45,027
Equity securities in financial institutions	92	-	(1)	91
Total available-for-sale securities	$ 255,122	$ 948	$ (1,288)	$ 254,782

The following table shows the Company's gross unrealized losses and fair value of the Company's investments with unrealized losses that are not deemed to be other-than-temporarily impaired, aggregated by investment category and length of time, which individual securities have been in a continuous unrealized loss position, at September 30, 2018 and December 31, 2017 (in thousands). As of September 30, 2018, the Company owned 143 securities whose fair value was less than their cost basis.

September 30, 2018	Less than Twelve Months		Twelve Months or Greater		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
U.S. agency securities	$54,399	$ (656)	$40,554	$ (687)	$94,953	$ (1,343)
U.S. treasury securities	32,837	(961)	-	-	32,837	(961)
Obligations of state and political subdivisions	26,648	(249)	8,381	(210)	35,029	(459)
Mortgage-backed securities in government sponsored entities	17,167	(299)	24,056	(932)	41,223	(1,231)
Total securities	$131,051	$ (2,165)	$72,991	$ (1,829)	$204,042	$ (3,994)
December 31, 2017						
U.S. agency securities	$74,952	$ (421)	$16,928	$ (172)	$91,880	$ (593)
U.S. treasury securities	28,604	(178)	-	-	28,604	(178)
Obligations of states and political subdivisions	14,885	(85)	5,958	(54)	20,843	(139)
Mortgage-backed securities in government sponsored entities	27,154	(190)	13,822	(187)	40,976	(377)
Equity securities in financial institutions	91	(1)	-	-	91	(1)
Total securities	$145,686	$ (875)	$36,708	$ (413)	$182,394	$ (1,288)

As of September 30, 2018 and December 31, 2017, the Company's investment securities portfolio contained unrealized losses on agency securities issued or backed by the full faith and credit of the United States government or are generally viewed as having the implied guarantee of the U.S. government, U.S treasury securities, obligations of states and political subdivisions and mortgage backed securities issued by government sponsored entities. For fixed maturity investments management considers whether the present value of cash flows expected to be collected are less than the security's amortized cost basis (the difference defined as the credit loss), the magnitude and duration of the decline, the reasons underlying the decline and the Company's intent to sell the security or whether it is more likely than not that the Company would be required to sell the security before its anticipated recovery in market value, to determine whether the loss in value is other than temporary. Once a decline in value is determined to be other than temporary, if the Company does not intend to sell the security, and it is more likely than not that it will not be required to sell the security before recovery of the security's amortized cost basis, the charge to earnings is limited to the amount of credit loss. Any remaining difference between fair value and amortized cost (the difference defined as the non-credit portion) is recognized in other comprehensive income, net of applicable taxes. Otherwise, the entire difference between fair value and amortized cost is charged to earnings. The Company has concluded that any impairment of its investment securities portfolio outlined in the above table is not other than temporary and is the result of interest rate changes, sector credit rating changes, or issuer-specific rating changes that are not expected to result in the non-collection of principal and interest during the period.

Proceeds from sales of securities available-for-sale for the nine months ended September 30, 2018 and 2017 were $25,168,000 and $30,393,000, respectively. Proceeds from sales of securities available-for-sale for the three months ended September 30, 2018 were $25,168,000. There were no sales of available for sale securities during the three months ended September 30, 2017. The gross gains and losses were as follows (in thousands):

	Three Months Ended Sept. 30,	Nine Months Ended Sept. 30,

	2018	2017	2018	2017
Gross gains on available for sale securities	$161	$ 9	$161	$211
Gross losses on available for sale securities	(169)	-	(169)	(7)
Net gains	$(8)	$ 9	$(8)	$204

The following table presents the net gains on the Company's equity investments recognized in earnings during the three month and nine month periods ended September 30, 2018, and the portion of unrealized gains for the period that relates to equity investments held at September 30, 2018 (in thousands):

9

Equity Securities	Three Months Ended September 30, 2018	Nine Months Ended September 30, 2018
Net gains (losses) recognized in equity securities during the period	$ (4)	$ 9
Less: Net gains realized on the sale of equity securities during the period	-	-
Net unrealized gains (losses)	$ (4)	$ 9

Investment securities with an approximate carrying value of $237.0 million and $243.4 million at September 30, 2018 and December 31, 2017, respectively, were pledged to secure public funds and certain other deposits.

Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties. The amortized cost and fair value of debt securities (excludes equity securities) at September 30, 2018, by contractual maturity, are shown below (in thousands):

	Amortized Cost	Fair Value
Available-for-sale debt securities:		
Due in one year or less	$ 29,087	$ 29,035
Due after one year through five years	105,536	103,350
Due after five years through ten years	59,609	58,574
Due after ten years	50,070	49,467
Total	$ 244,302	$ 240,426

Note 5 – Loans

The Company grants loans primarily to customers throughout north central, central and south central Pennsylvania and the southern tier of New York. Although the Company had a diversified loan portfolio at September 30, 2018 and December 31, 2017, a substantial portion of its debtors' ability to honor their contracts is dependent on the economic conditions within these regions. The following table summarizes the primary segments of the loan portfolio and how those segments are analyzed within the allowance for loan losses as of September 30, 2018 and December 31, 2017 (in thousands):

September 30, 2018	Total Loans	Individually evaluated for impairment	Loans acquired with deteriorated credit quality	Collectively evaluated for impairment
Real estate loans:				
Residential	$ 213,255	$ 915	$ 30	$ 212,310
Commercial	312,982	14,148	1,345	297,489
Agricultural	280,569	5,038	683	274,848
Construction	30,262	-	-	30,262
Consumer	9,702	-	-	9,702
Other commercial loans	72,219	3,368	518	68,333
Other agricultural loans	39,917	1,448	-	38,469
State and political subdivision loans	101,425	-	-	101,425

Total	1,060,331	24,917	2,576	1,032,838
Allowance for loan losses	12,383	654	-	11,729
Net loans	$1,047,948	$ 24,263	$ 2,576	$1,021,109

December 31, 2017	Total Loans	Individually evaluated for mpairment	Loans acquired with deteriorated credit quality	Collectively evaluated for impairment
Real estate loans:				
Residential	$214,479	$ 1,065	$ 33	$ 213,381
Commercial	308,084	13,864	1,460	292,760
Agricultural	239,957	3,901	702	235,354
Construction	13,502	-	-	13,502
Consumer	9,944	8	-	9,936
Other commercial loans	72,013	4,197	443	67,373
Other agricultural loans	37,809	1,363	-	36,446
State and political subdivision loans	104,737	-	-	104,737
Total	1,000,525	24,398	2,638	973,489
Allowance for loan losses	11,190	410	-	10,780
Net loans	$989,335	$ 23,988	$ 2,638	$ 962,709

Purchased loans are recorded at fair value on their purchase date without a carryover of the related allowance for loan losses. Upon acquisition, the Company evaluates whether an acquired loan was within the scope of ASC 310-30, Receivables-Loans and Debt Securities Acquired with Deteriorated Credit Quality. Purchased credit-impaired ("PCI") loans are loans that have evidence of credit deterioration since origination and it is probable at the date of acquisition that the Company will not collect all contractually required principal and interest payments. Based upon management's review, there were no material decreases in the expected cash flows of these loans between the acquisition date and September 30, 2018. The fair value of PCI loans, on the acquisition date, was determined, primarily based on the fair value of the loans' collateral. The carrying value of PCI loans was $2,576,000 and $2,638,000 at September 30, 2018 and December 31, 2017, respectively. The carrying value of the PCI loans was determined by projected discounted contractual cash flows and collateral valuations.

Changes in the accretable yield for PCI loans were as follows for the three and nine months ended September 30, 2018 and 2017, respectively (in thousands):

	Three months ended September 30,		Nine months ended September 30,	
	2018	2017	2018	2017
Balance at beginning of period	$59	$167	$106	$389
Accretion	(24)	(90)	(71)	(312)
Reclassification of non-accretable discount	93	-	93	-
Balance at end of period	$128	$77	$128	$77

The following table presents additional information regarding loans acquired with specific evidence of deterioration in credit quality under ASC 310-30 (in thousands):

September 30, 2018	December 31, 2017

Outstanding balance	$ 5,340	$ 5,295
Carrying amount	2,576	2,638

The segments of the Company's loan portfolio are disaggregated into classes to a level that allows management to monitor risk and performance. Residential real estate mortgages consist primarily of 15 to 30 year first mortgages on residential real estate, while residential real estate home equity loans are consumer purpose installment loans or lines of credit with terms of 15 years or less secured by a mortgage which is often a second lien on residential real estate. Commercial real estate loans are business purpose loans secured by a mortgage on commercial real estate. Agricultural real estate loans are loans secured by a mortgage on real estate used in agriculture production. Construction real estate loans are loans secured by residential, commercial or agricultural real estate used during the construction phase of residential, commercial or agricultural projects. Consumer loans are typically unsecured or primarily secured by assets other than real estate and overdraft lines of credit are typically secured by customer deposit accounts. Other commercial loans are loans for commercial purposes primarily secured by non-real estate collateral. Other agricultural loans are loans for agricultural purposes primarily secured by non-real estate collateral. State and political subdivision loans are loans to state and local municipalities for capital and operating expenses or tax free loans used to finance commercial development.

Management considers other commercial loans, other agricultural loans, state and political subdivision loans, commercial real estate loans and agricultural real estate loans which are 90 days or more past due to be impaired. Management will also consider a loan impaired based on other factors it becomes aware of, including the customer's results of operations and cash flows or if the loan is modified in a troubled debt restructuring. In addition, certain residential mortgages, home equity and consumer loans that are cross collateralized with commercial relationships that are determined to be impaired may also be classified as impaired. Impaired loans are analyzed to determine if it is probable that all amounts will not be collected according to the contractual terms of the loan agreement. If management determines that the value of the impaired loan is less than the recorded investment in the loan (net of previous charge-offs, deferred loan fees or costs and unamortized premium or discount), impairment is recognized through an allocation of the allowance for loan losses or a charge-off to the allowance for loan losses.

The following table includes the recorded investment and unpaid principal balances for impaired financing receivables by class, excluding PCI loans, with the associated allowance amount, if applicable (in thousands):

September 30, 2018	Unpaid Principal Balance	Recorded Investment With No Allowance	Recorded Investment With Allowance	Total Recorded Investment	Related Allowance
Real estate loans:					
Mortgages	$ 939	$ 360	$ 466	$ 826	$ 12
Home Equity	108	12	77	89	15
Commercial	17,043	12,595	1,553	14,148	224
Agricultural	5,050	1,752	3,286	5,038	86
Construction	-	-	-	-	-
Consumer	-	-	-	-	-
Other commercial loans	3,956	2,990	378	3,368	152
Other agricultural loans					