INDEPENDENT BANK CORP
Form 10-Q
November 03, 2016
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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, 2016
Commission File Number: 1-9047

Independent Bank Corp.
(Exact name of registrant as specified in its charter)

Massachusetts	04-2870273
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

Office Address: 2036 Washington Street, Hanover Massachusetts 02339
Mailing Address: 288 Union Street, Rockland, Massachusetts 02370
(Address of principal executive offices, including zip code)
(781) 878-6100
(Registrant's telephone number, including area code)

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	x	Accelerated Filer	o
Non-accelerated Filer	o	Smaller Reporting Company	o

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

As of November 1, 2016, there were 26,329,185 shares of the issuer's common stock outstanding, par value $0.01 per share.

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PART 1. FINANCIAL INFORMATION
Item 1. Financial Statements
INDEPENDENT BANK CORP.
CONSOLIDATED BALANCE SHEETS
(Unaudited—Dollars in thousands, except share data)

	September 30, 2016	December 31 2015
Assets		
Cash and due from banks	$ 92,185	$ 84,813
Interest-earning deposits with banks	265,618	190,952
Securities		
Securities - trading	809	356
Securities - available for sale	387,008	367,249
Securities - held to maturity (fair value $441,834 and $478,749)	430,763	477,507
Total securities	818,580	845,112
Loans held for sale (at fair value)	13,334	5,990
Loans		
Commercial and industrial	857,713	843,276
Commercial real estate	2,787,660	2,653,434
Commercial construction	376,245	373,368
Small business	115,054	96,246
Residential real estate	632,685	638,606
Home equity - first position	559,867	543,092
Home equity - subordinate positions	405,245	384,711
Other consumer	11,664	14,988
Total loans	5,746,133	5,547,721
Less: allowance for loan losses	(58,205)	(55,825)
Net loans	5,687,928	5,491,896
Federal Home Loan Bank stock	11,304	14,431
Bank premises and equipment, net	76,429	75,663
Goodwill	201,083	201,083
Other intangible assets	9,751	11,826
Cash surrender value of life insurance policies	137,723	134,627
Other real estate owned and other foreclosed assets	1,798	2,159
Other assets	186,276	150,917
Total assets	$ 7,502,009	$ 7,209,469
Liabilities and Stockholders' Equity		
Deposits		
Demand deposits	2,024,235	1,846,593
Savings and interest checking accounts	2,417,195	2,370,141
Money market	1,198,959	1,089,139
Time certificates of deposit of $100,000 and over	257,638	274,701
Other time certificates of deposits	371,433	410,129
Total deposits	6,269,460	5,990,703
Borrowings		
Federal Home Loan Bank borrowings	50,826	102,080
Customer repurchase agreements and other short-term borrowings	140,914	133,958

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Junior subordinated debentures (less unamortized debt issuance costs of $141 and $158)	73,157	73,306
Subordinated debentures (less unamortized debt issuance costs of $376 and $411)	34,624	34,589
Total borrowings	299,521	343,933
Other liabilities	114,786	103,370
Total liabilities	6,683,767	6,438,006
Commitments and contingencies		
Stockholders' equity		
Preferred stock, $.01 par value. authorized: 1,000,000 shares, outstanding: none	—	—
Common stock, $.01 par value. authorized: 75,000,000 shares, issued and outstanding: 26,320,467 shares at September 30, 2016 and 26,236,352 shares at December 31, 2015 (includes 212,673 and 230,900 shares of unvested participating restricted stock awards, respectively)	261	260
Shares held in rabbi trust at cost: 169,075 shares at September 30, 2016 and 173,378 shares at December 31, 2015	(4,199)	(3,958)
Deferred compensation and other retirement benefit obligations	4,199	3,958
Additional paid in capital	409,731	405,486
Retained earnings	404,750	368,169
Accumulated other comprehensive income (loss), net of tax	3,500	(2,452)
Total stockholders’ equity	818,242	771,463
Total liabilities and stockholders' equity	$7,502,009	$7,209,469

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

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INDEPENDENT BANK CORP.
CONSOLIDATED STATEMENTS OF INCOME
(Unaudited—Dollars in thousands, except share and per share data)

	Three Months Ended		Nine Months Ended	
	September 30		September 30	
	2016	2015	2016	2015
Interest income				
Interest and fees on loans	$56,778	$ 54,557	$166,683	$ 160,261
Taxable interest and dividends on securities	5,034	5,455	15,500	14,934
Nontaxable interest and dividends on securities	28	31	89	95
Interest on loans held for sale	81	64	170	173
Interest on federal funds sold and short-term investments	387	121	767	212
Total interest and dividend income	62,308	60,228	183,209	175,675
Interest expense				
Interest on deposits	2,733	2,951	8,339	8,636
Interest on borrowings	1,907	2,232	5,778	6,997
Total interest expense	4,640	5,183	14,117	15,633
Net interest income	57,668	55,045	169,092	160,042
Provision for loan losses	950	800	2,075	1,000
Net interest income after provision for loan losses	56,718	54,245	167,017	159,042
Noninterest income				
Deposit account fees	4,622	4,754	13,563	13,385
Interchange and ATM fees	4,190	3,949	12,050	10,817
Investment management	5,446	4,981	16,183	15,616
Mortgage banking income	1,963	1,480	4,458	3,832
Gain on sale of equity securities	—	—	5	19
Gain on sale of fixed income securities	—	—	—	798
Increase in cash surrender value of life insurance policies	984	958	2,980	2,685
Loan level derivative income	810	968	4,627	2,816
Other noninterest income	2,401	2,157	6,800	6,096
Total noninterest income	20,416	19,247	60,666	56,064
Noninterest expenses				
Salaries and employee benefits	27,395	26,685	81,561	78,291
Occupancy and equipment expenses	5,433	5,443	16,927	17,509
Data processing and facilities management	1,400	1,112	3,831	3,462
FDIC assessment	725	1,020	2,655	2,993
Advertising expense	1,654	1,414	4,134	4,101
Consulting expense	770	867	2,235	2,451
Legal fees	321	746	1,132	1,462
Loss on extinguishment of debt	—	—	437	122
Loss on sale of equity securities	—	—	32	8
Loss on sale of fixed income securities	—	—	—	1,124
Merger and acquisition expense	151	—	691	10,501
Other noninterest expenses	9,008	9,744	26,850	28,628
Total noninterest expenses	46,857	47,031	140,485	150,652
Income before income taxes	30,277	26,461	87,198	64,454
Provision for income taxes	9,793	7,867	27,729	18,949
Net income	$20,484	$ 18,594	$59,469	$ 45,505

Basic earnings per share	$0.78	$ 0.71	$2.26	$ 1.77
Diluted earnings per share	$0.78	$ 0.71	$2.26	$ 1.76
Weighted average common shares (basic)	26,324,316	26,200,621	26,301,340	25,774,571
Common shares equivalents	53,072	63,493	48,354	72,921
Weighted average common shares (diluted)	26,377,388	26,264,114	26,349,694	25,847,492
Cash dividends declared per common share	$0.29	$ 0.26	$0.87	$ 0.78

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

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INDEPENDENT BANK CORP.
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(Unaudited—Dollars in thousands)

	Three Months Ended September 30		Nine Months Ended September 30	
	2016	2015	2016	2015
Net income	$20,484	$18,594	$59,469	$45,505
Other comprehensive income (loss), net of tax				
Net change in fair value of securities available for sale	(816)	1,211	5,119	544
Net change in fair value of cash flow hedges	674	132	653	596
Net change in other comprehensive income for defined benefit postretirement plans	59	110	180	309
Total other comprehensive income (loss)	(83)	1,453	5,952	1,449
Total comprehensive income	$20,401	$20,047	$65,421	$46,954

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

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INDEPENDENT BANK CORP.
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
(Unaudited—Dollars in thousands, except share data)

	Common Stock Outstanding	Common Stock	Value of Shares Held in Rabbi Trust at Cost	Deferred Compensation and Other Retirement Benefit Obligations	Additional Paid in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total
Balance December 31, 2015	26,236,352	$ 260	$ (3,958)	$ 3,958	$405,486	$368,169	$ (2,452)	$771,463
Net income	—	—	—	—	—	59,469	—	59,469
Other comprehensive income	—	—	—	—	—	—	5,952	5,952
Common dividend declared ($0.87 per share)	—	—	—	—	—	(22,888)	—	(22,888)
Proceeds from exercise of stock options, net of cash paid	9,022	—	—	—	160	—	—	160
Tax benefit related to equity award activity	—	—	—	—	354	—	—	354
Stock based compensation	—	—	—	—	2,308	—	—	2,308
Restricted stock awards issued, net of awards surrendered	32,567	1	—	—	(674)	—	—	(673)
Shares issued under direct stock purchase plan	42,526	—	—	—	1,918	—	—	1,918
Deferred compensation and other retirement benefit obligations	—	—	(241)	241		—	—	—
Tax benefit related to deferred compensation distributions	—	—	—	—	179	—	—	179
Balance September 30, 2016	26,320,467	$ 261	$ (4,199)	$ 4,199	$409,731	$404,750	$ 3,500	$818,242
Balance December 31, 2014	23,998,738	$ 237	$ (3,666)	$ 3,666	$311,978	$330,444	$ (2,132)	$640,527
Net income	—	—	—	—	—	45,505	—	45,505
Other comprehensive income	—	—	—	—	—	—	1,449	1,449
Common dividend declared ($0.78 per share)	—	—	—	—	—	(20,412)	—	(20,412)
Common stock issued for acquisition	2,052,137	21	—	—	86,394	—	—	86,415
Proceeds from exercise of stock options, net of cash	78,240	1	—	—	1,364	—	—	1,365

paid								
Tax benefit related to equity award activity	—	—	—	—	776	—	—	776
Stock based compensation	—	—	—	—	2,028	—	—	2,028
Restricted stock awards issued, net of awards surrendered	36,901	1	—	—	(646)	—	—	(645)
Shares issued under direct stock purchase plan	46,222	—	—	—	2,023	—	—	2,023
Deferred compensation and other retirement benefit obligations	—	—	(217)	217	—	—	—	—
Tax benefit related to deferred compensation distributions	—	—	—	—	172	—	—	172
Balance September 30, 2015	26,212,238	$ 260	$ (3,883)	$ 3,883	$404,089	$355,537	$ (683)	$759,203

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

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INDEPENDENT BANK CORP.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited—Dollars in thousands)

	Nine Months Ended September 30	
	2016	2015
Cash flow from operating activities		
Net income	$59,469	$45,505
Adjustments to reconcile net income to net cash provided by operating activities		
Depreciation and amortization	10,729	9,327
Provision for loan losses	2,075	1,000
Deferred income tax expense	314	5,372
Net loss on sale of securities	27	315
Net loss on fixed assets	10	213
Loss on extinguishment of debt	437	122
Net loss on other real estate owned and foreclosed assets	41	1,070
Realized gain on sale leaseback transaction	(775)	(775)
Stock based compensation	2,308	2,028
Excess tax benefit related to equity award activity	(354)	(776)
Increase in cash surrender value of life insurance policies	(2,980)	(2,685)
Change in fair value on loans held for sale	(60)	(3)
Net change in:		
Trading assets	(453)	(454)
Loans held for sale	(7,284)	(4,585)
Other assets	(42,044)	4,366
Other liabilities	18,314	2,035
Total adjustments	(19,695)	16,570
Net cash provided by operating activities	39,774	62,075
Cash flows used in investing activities		
Proceeds from sales of securities available for sale	285	14,344
Proceeds from maturities and principal repayments of securities available for sale	48,421	60,507
Purchases of securities available for sale	(60,888)	(49,086)
Proceeds from maturities and principal repayments of securities held to maturity	62,005	44,706
Purchases of securities held to maturity	(14,998)	(117,286)
Redemption of Federal Home Loan Bank stock	3,127	—
Investments in low income housing projects	(5,473)	(14,817)
Purchases of life insurance policies	(116)	(115)
Net increase in loans	(198,731)	(65,650)
Cash used in business combinations, net of cash acquired	—	(13,448)
Purchases of bank premises and equipment	(6,022)	(6,846)
Proceeds from the sale of bank premises and equipment	26	1,233
Proceeds from the sale of other real estate owned and foreclosed assets	842	7,378
Net payments relating to other real estate owned and foreclosed assets	(145)	(961)
Net cash used in investing activities	(171,667)	(140,041)
Cash flows provided by financing activities		
Net decrease in time deposits	(55,759)	(54,293)

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Net increase in other deposits	334,516	326,440
Net repayments of short-term Federal Home Loan Bank borrowings	—	(10,000)
Repayments of long-term Federal Home Loan Bank borrowings	(51,641)	(7,000)
Net increase (decrease) in customer repurchase agreements	6,956	(9,441)
Repayments of wholesale repurchase agreements	—	(50,000)
Repayments of subordinated debentures	—	(30,000)
Net proceeds from exercise of stock options	160	1,365
Restricted stock awards issued, net of awards surrendered	(673)	(645)
Excess tax benefit from stock based compensation	354	776
Tax benefit from deferred compensation distribution	179	172
Proceeds from shares issued under direct stock purchase plan	1,918	2,023
Common dividends paid	(22,079)	(19,357)
Net cash provided by financing activities	213,931	150,040
Net increase in cash and cash equivalents	82,038	72,074
Cash and cash equivalents at beginning of year	275,765	178,254
Cash and cash equivalents at end of period	357,803	250,328
Supplemental schedule of noncash investing and financing activities		
Transfer of loans to other real estate owned & foreclosed assets	$ 377	$ 2,134
Other net transfers to other real estate owned	$ —	$ 142
Net increase in capital commitments relating to low income housing project investments	$ 163	$ 2,085
In conjunction with the Peoples Federal Bancshares, Inc. acquisition, assets were acquired and liabilities were assumed as follows		
Common stock issued for acquisition	$ —	$ 86,415
Fair value of assets acquired, net of cash acquired	$ —	$ 598,376
Fair value of liabilities assumed	$ —	$ 498,513

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

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CONDENSED NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 - BASIS OF PRESENTATION

Independent Bank Corp. (the "Company") is a state chartered, federally registered bank holding company, incorporated in 1985. The Company is the sole stockholder of Rockland Trust Company ("Rockland Trust" or the "Bank"), a Massachusetts trust company chartered in 1907.

All material intercompany balances and transactions have been eliminated in consolidation. Certain previously reported amounts may have been reclassified to conform to the current year's presentation.

The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America ("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 of the information and notes required by GAAP for complete financial statements. In the opinion of management, all adjustments considered necessary for a fair presentation of the financial statements, primarily consisting of normal recurring adjustments, have been included. Operating results for the quarter ended September 30, 2016 are not necessarily indicative of the results that may be expected for the year ending December 31, 2016 or any other interim period.

For further information, refer to the consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2015, filed with the Securities and Exchange Commission.

NOTE 2 - RECENT ACCOUNTING STANDARDS UPDATES

Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") Topic 606 "Revenue from Contracts with Customers" Update No. 2014-09. Update No. 2014-09 was issued in May 2014 to address the previous revenue recognition requirements in GAAP that differ from those in International Financial Reporting Standards (IFRS). Accordingly, the FASB and the International Accounting Standards Board (IASB) initiated a joint project to clarify the principles for recognizing revenue and to develop a common revenue standard for U.S. GAAP and IFRS. The largely converged revenue recognition standards will supersede virtually all revenue recognition guidance in GAAP and IFRS. The core principle of the guidance is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. Since the issuance of Update 2014-09, the FASB has finalized various amendments to the standard as summarized below:

FASB ASC Topic 606 "Revenue from Contracts with Customers" Update No. 2016-12
FASB ASC Topic 606 "Revenue from Contracts with Customers" Update No. 2016-10
FASB ASC Topic 606 "Revenue from Contracts with Customers" Update No. 2016-08.
FASB ASC Topic 606 "Revenue from Contracts with Customers" Update No. 2015-14.

Through Updates 2016-12, 2016-10 and 2016-08, the FASB amended its new revenue guidance on licenses of intellectual property, identification of performance obligations, collectability, noncash consideration and the presentation of sales and other similar taxes. The FASB also clarified the definition of a completed contract at transition and added a practical expedient to ease transition for contracts that were modified prior to adoption. The FASB also amended the new revenue recognition guidance on determining whether an entity is a principal or an agent in an arrangement which affects whether revenue should be reported gross or net.

Following the issuance of Update 2015-14, Update 2014-09, as amended, is effective for the Company for annual reporting periods beginning after December 15, 2017, including interim reporting periods within that reporting period. Earlier adoption is permitted only as of annual reporting periods beginning after December 15, 2016, including interim reporting periods within that reporting period. A full or modified retrospective transition method is required. The Company's revenue is comprised of net interest income on financial assets and liabilities, which is explicitly excluded from the scope of the new guidance, and noninterest income. The Company plans to adopt the revenue recognition guidance in the first quarter of 2018 and is currently evaluating the potential impact on noninterest income

on the Company's consolidated financial position, other presentation and disclosure issues, as well as evaluating its selection of transition method.
FASB ASC Topic 230 "Statement of Cash Flows" Update No. 2016-15. Update No. 2016-15 was issued in August 2016 to reduce diversity of practice in how certain cash receipts and cash payments are presented and classified in the statement of cash flows. The amendments in this update provide guidance on the following eight specific cash flow issues; (1) debt prepayment or debt extinguishment costs, (2) settlement of zero-coupon debt instruments or other debt instruments with coupon interest rates that are insignificant in relation to the effective interest rate of the borrowing, (3) contingent consideration payments made after

a business combination, (4) proceeds from the settlement of insurance claims, (5) proceeds from the settlement of corporate-owned life insurance policies, including bank-owned life insurance policies, (6) distributions received from equity method investees, (7) beneficial interests in securitization transactions, and (8) separately identifiable cash flows and application of the Predominance Principle. The amendments in this topic will provide guidance for these eight issues, thereby reducing the current and potential future diversity in practice. The amendments in this update are effective for annual periods and interim periods within those annual periods beginning after December 31, 2017. Earlier adoption is permitted, including interim reporting periods within that reporting period. If an entity early adopts the amendments in an interim period, any adjustments should be reflected as of the beginning of the fiscal year that includes that interim period. An entity that elects early adoption must adopt all of the amendments in the same period. The adoption of this standard is not expected to have a material impact on the Company's consolidated financial position.

FASB ASC Topic 326 "Financial Instruments - Credit Losses" Update No. 2016-13. Update No. 2016-13 was issued in June 2016 to provide financial statement users with more decision-useful information about the expected credit losses on financial instruments and other commitments to extend credit held by a reporting entity at each reporting date. To achieve this objective, the amendments in this update replace the incurred loss impairment methodology in current GAAP with a methodology that reflects expected credit losses and requires consideration of a broader range of reasonable and supportable information to inform credit loss estimates. The amendments affect entities holding financial assets and net investment in leases that are not accounted for at fair value through net income. The amendments affect loans, debt securities, trade receivables, net investments in leases, off-balance sheet credit exposures, reinsurance receivables, and any other financial assets not excluded from the scope that have the contractual right to receive cash. The amendments in this update are effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years, with earlier adoption permitted as of fiscal years beginning after December 15, 2018, including interim periods with those fiscal years. The Company is currently assessing the impact of the adoption of this standard on the Company's consolidated financial position.

FASB ASC Topic 605 "Revenue Recognition" and Topic 815 "Derivatives and Hedging" Update No. 2016-11. Update No. 2016-11 was issued in May 2016 and is a rescission of SEC guidance because of ASU Updates 2014-09 and 2014-16 pursuant to staff announcements at the March 3, 2016 Emerging Issues Task Force meeting. The amendments in this update are effective upon adoption of Topic 606 "Revenue from Contracts with Customers." The Company is currently assessing the impact of the adoption of this standard on the Company's consolidated financial position.

FASB ASC Topic 718 "Compensation - Stock Compensation" Update No. 2016-09. Update No. 2016-09 was issued in March 2016 and affects all entities that issue share-based awards to their employees. This update was issued as part of the FASB’s simplification initiative. The areas for simplification in this update involve several aspects of the 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. The amendments in this update are effective for fiscal years beginning after December 15, 2016, including interim periods within those fiscal years. The Company is currently assessing the impact of the adoption of this standard on the Company's consolidated financial position.

FASB ASC Topic 323 "Investments -Equity Method and Joint Ventures" Update No. 2016-07. Update No. 2016-07 was issued in March 2016 and eliminates the requirement that when an investment qualifies for use of the equity method as a result of an increase in the level of ownership interest or degree of influence, an investor must adjust the investment, results of operations, and retained earnings retroactively on a step-by-step basis as if the equity method had been in effect during all previous periods that the investment had been held. The amendments require that the equity method investor add the cost of acquiring the additional interest in the investee to the current basis of the investor's previously held interest and adopt the equity method of accounting as of the date the investment becomes qualified for equity method accounting. Therefore, upon qualifying for the equity method of accounting, no retroactive adjustment of the investment is required. The amendments in this update require that an entity that has an available-for-sale equity security that becomes qualified for the equity method of accounting recognize through earnings the unrealized holding gain or loss in accumulated other comprehensive income at the date the investment becomes qualified for use of the equity method. The amendments in this update are effective for fiscal years beginning after December 15, 2016, including interim periods within those fiscal years. The amendments should be applied prospectively upon their effective date to increases in the level of ownership interest or degree of influence that result in the adoption of the equity method. Early adoption is permitted. The adoption of this standard is not expected to have a material impact on the Company's consolidated financial position.

FASB ASC Topic 815 "Derivative and Hedging - Contingent Put and Call Options in Debt Instruments" Update No. 2016-6. Update No. 2016-6 was issued in March 2016 to clarify the requirements for assessing whether contingent call (put) options that can accelerate the payment of principal on debt instruments are clearly and closely related to their debt hosts. An entity performing the assessment under the amendments in this update is required to assess the embedded call (put) options solely in accordance with the four-step decision sequence. For public entities, the amendments in this update are effective for fiscal years beginning after December 15, 2016, including interim periods within those fiscal years. An entity has an option to apply

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the amendments in this update on either a prospective basis or a modified retrospective basis. Early adoption is permitted, including adoption in an interim period. The adoption of this standard is not expected to have a material impact on the Company's consolidated financial position.

FASB ASC Topic 815 "Derivative and Hedging - Effect of Derivative Contract Novations on Existing Hedge Accounting Relationships" Update No. 2016-05. Update No. 2016-05 was issued in March 2016 and applies to all reporting entities for which there is a change in the counterpart to a derivative instrument that has been designated as a hedging instrument under Topic 815. The amendments in this update clarify that a change in the counterparty to a derivative instrument that has been designated as the hedging instrument under Topic 815 does not, in and of itself, require dedesignation of that hedging relationship provided that all other hedge accounting criteria (including those in paragraphs 815-20-35-14 through 35-18) continue to be met. For public entities, the amendments in this update are effective for fiscal years beginning after December 15, 2016, including interim periods within those fiscal years. An entity has an option to apply the amendments in this update on either a prospective basis or a modified retrospective basis. Early adoption is permitted, including adoption in an interim period. The adoption of this standard is not expected to have a material impact on the Company's consolidated financial position.

FASB ASC Topic 842 "Leases" Update No. 2016-02. Update No. 2016-02 was issued in February 2016 and affects any entity that enters into a lease (as that term is defined in this update), with some specified scope exemptions. The core principle of this update is that a lessee should recognize in the statement of financial position a liability to make lease payments and a right-of-use asset representing its right to use the underlying asset for the lease term. For leases with a term of 12 months or less, a lessee is permitted to make an accounting policy election by class of underlying asset not to recognize lease assets and lease liabilities. The recognition, measurement, and presentation of expenses and cash flows arising from a lease have not significantly changed from previous GAAP. In addition, the accounting applied by a lessor is largely unchanged from that applied under previous GAAP. For public companies, the amendments in this update are effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. The Company is currently assessing the impact of the adoption of this standard on the Company's consolidated financial position.

FASB ASC Topic 825-10 "Financial Instruments - Overall Recognition and Measurement of Financial Assets and Financial Liabilities" Update No. 2016-01. Update No. 2016-01 was issued in January 2016 to amend the guidance in U.S. GAAP on the classification and measurement of financial instruments. Although the update retains many current requirements, it significantly revises an entity's accounting related to (1) the classification and measurement of investments in equity securities and (2) the presentation of certain fair value changes for financial liabilities measured at fair value. The update also amends certain disclosure requirements associated with the fair value of financial instruments and various other aspects of recognition, measurement, presentation and disclosure of financial instruments. For public entities, the amendments in this update are effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. Early adoption is permitted for only certain guidance. The Company is currently assessing the impact of the adoption of this standard on the Company's consolidated financial position.

FASB ASC Subtopic 835-30 "Interest - Imputation of Interest" Update No. 2015-03. Update No. 2015-03 was issued in April 2015 to simplify presentation of debt issuance costs. The amendments in this update 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 issuances costs are not affected by the amendments in this update. The amendments in this update were adopted by the Company effective January 1, 2016, with applicable prior period presentation updated as well. The adoption of this standard did not have a material impact on the Company's consolidated financial position.

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NOTE 3 - SECURITIES
Trading Securities

The Company had trading securities of $809,000 and $356,000 as of September 30, 2016 and December 31, 2015, respectively. These securities are held in a rabbi trust and will be used for future payments associated with the Company's non-qualified 401(k) Restoration Plan and Non-Qualified Deferred Compensation Plan.

Available for Sale and Held to Maturity Securities
The following table presents a summary of the amortized cost and gross unrealized holding gains and losses recorded in other comprehensive income and fair value of securities available for sale and securities held to maturity for the periods below:

	September 30, 2016				December 31, 2015			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(Dollars in thousands)							
Available for sale securities								
U.S. government agency securities	$24,502	$804	$—	$25,306	$29,958	$261	$(4)	$30,215
Agency mortgage-backed securities	178,095	7,481	(3)	185,573	207,693	4,227	(983)	210,937
Agency collateralized mortgage obligations	107,466	1,286	(156)	108,596	64,157	179	(752)	63,584
State, county, and municipal securities	4,255	105	—	4,360	4,543	116	—	4,659
Single issuer trust preferred securities issued by banks	2,324	4	(31)	2,297	2,865	8	(81)	2,792
Pooled trust preferred securities issued by banks and insurers	2,200	—	(662)	1,538	2,217	—	(645)	1,572
Small business administration pooled securities	38,678	1,202	—	39,880	40,472	87	(110)	40,449
Equity securities	19,000	701	(243)	19,458	13,235	374	(568)	13,041
Total available for sale securities	$376,520	$11,583	$(1,095)	$387,008	$365,140	$5,252	$(3,143)	$367,249
Held to maturity securities								
U.S. Treasury securities	$1,008	$81	$—	$1,089	$1,009	$55	$—	$1,064
Agency mortgage-backed securities	148,822	6,309	—	155,131	167,134	3,460	(219)	170,375
Agency collateralized mortgage obligations	246,744	4,072	(556)	250,260	267,348	1,195	(3,652)	264,891
State, county, and municipal securities	—	—	—	—	225	2	—	227
Single issuer trust preferred securities issued by banks	1,500	47	—	1,547	1,500	22	—	1,522
Small business administration pooled securities	32,689	1,118	—	33,807	35,291	437	(64)	35,664

Corporate debt securities	—	—	—	—	5,000	6	—	5,006
Total held to maturity securities	$430,763	$ 11,627	$ (556)	$441,834	$477,507	$ 5,177	$ (3,935)	$478,749
Total	$807,283	$ 23,210	$ (1,651)	$828,842	$842,647	$ 10,429	$ (7,078)	$845,998

When securities are sold, the adjusted cost of the specific security sold is used to compute the gain or loss on the sale.

The actual maturities of certain securities may differ from the contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties. A schedule of the contractual maturities of securities available for sale and securities held to maturity as of September 30, 2016 is presented below:

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	Available for Sale		Held to Maturity	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
	(Dollars in thousands)			
Due in one year or less	$999	$1,003	$11	$11
Due after one year to five years	30,422	31,258	16,099	16,739
Due after five to ten years	86,511	89,455	24,594	25,602
Due after ten years	239,588	245,834	390,059	399,482
Total debt securities	$357,520	$367,550	$430,763	$441,834
Equity securities	$19,000	$19,458	$—	$—
Total	$376,520	$387,008	$430,763	$441,834

Inclusive in the table above is $11.9 million of callable securities in the Company’s investment portfolio at September 30, 2016.

The carrying value of securities pledged to secure public funds, trust deposits, repurchase agreements and for other purposes, as required or permitted by law, was $451.7 million and $444.8 million at September 30, 2016 and December 31, 2015, respectively.

At September 30, 2016 and December 31, 2015, the Company had no investments in obligations of individual states, counties, or municipalities which exceeded 10% of stockholders’ equity.

Other-Than-Temporary Impairment ("OTTI")

The Company continually reviews investment securities for the existence of OTTI, taking into consideration current market conditions, the extent and nature of changes in fair value, issuer rating changes and trends, the credit worthiness of the obligor of the security, volatility of earnings, current analysts’ evaluations, the Company’s intent to sell the security, or whether it is more likely than not that the Company will be required to sell the debt security before its anticipated recovery, as well as other qualitative factors. The term “other-than-temporary” is not intended to indicate that the decline is permanent, but indicates that the prospects for a near-term recovery of value is not necessarily favorable, or that there is a lack of evidence to support a realizable value equal to or greater than the carrying value of the investment.

The following tables show the gross unrealized losses and fair value of the Company’s investments in an unrealized loss position, which the Company has not deemed to be OTTI, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position:

	September 30, 2016						
		Less than 12 months		12 months or longer		Total	
	# of holdings	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
	(Dollars in thousands)						
Agency mortgage-backed securities	2	$1,016	$ (3)	$—	$—	$1,016	$ (3)
Agency collateralized mortgage obligations	9	14,530	(30)	51,578	(682)	66,108	(712)
Single issuer trust preferred securities issued by banks and insurers	2	—	—	2,048	(31)	2,048	(31)
Pooled trust preferred securities issued by banks and insurers	1	—	—	1,537	(662)	1,537	(662)
Equity securities	21	515	(16)	6,903	(227)	7,418	(243)
Total temporarily impaired securities	35	$16,061	$ (49)	$62,066	$ (1,602)	$78,127	$ (1,651)

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	December 31, 2015						
		Less than 12 months		12 months or longer		Total	
	# of holdings	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
	(Dollars in thousands)						
U.S.government agency securities	3	$1,990	$(4)	$—	$—	$1,990	$(4)
Agency mortgage-backed securities	57	112,648	(1,062)	4,297	(140)	116,945	(1,202)
Agency collateralized mortgage obligations	23	147,707	(1,420)	80,927	(2,984)	228,634	(4,404)
Single issuer trust preferred securities issued by banks and insurers	2	1,018	(33)	1,018	(48)	2,036	(81)
Pooled trust preferred securities issued by banks and insurers	1	—	—	1,572	(645)	1,572	(645)
Small business administration pooled securities	3	37,986	(174)	—	—	37,986	(174)
Equity securities	34	3,481	(189)	4,971	(379)	8,452	(568)
Total temporarily impaired securities	123	$304,830	$(2,882)	$92,785	$(4,196)	$397,615	$(7,078)

The Company does not intend to sell these investments and has determined based upon available evidence that it is more likely than not that the Company will not be required to sell the security before the recovery of its amortized cost basis. As a result, the Company does not consider these investments to be OTTI. The Company made this determination by reviewing various qualitative and quantitative factors regarding each investment category, such as current market conditions, extent and nature of changes in fair value, issuer rating changes and trends, volatility of earnings, and current analysts' evaluations.

As a result of the Company's review of these qualitative and quantitative factors, the causes of the impairments listed in the table above by category are as follows at September 30, 2016:

- Agency Mortgage-Backed Securities and Agency Collateralized Mortgage Obligations: These portfolios have contractual terms that generally do not permit the issuer to settle the securities at a price less than the current par value of the investment. The decline in market value of these securities is attributable to changes in interest rates and not credit quality. Additionally, these securities are either implicitly or explicitly guaranteed by the U.S. Government or one of its agencies.
- Single Issuer Trust Preferred Securities: This portfolio consists of two securities, one of which is below investment grade. The unrealized loss on these securities is attributable to the illiquid nature of the trust preferred market in the current economic environment. Management evaluates various financial metrics for the issuers, including regulatory capital ratios of the issuers.
- Pooled Trust Preferred Securities: This portfolio consists of one below investment grade security which is performing. The unrealized loss on this security is attributable to the illiquid nature of the trust preferred market in the current economic and regulatory environment. Management evaluates collateral credit and instrument structure, including current and expected deferral and default rates and timing. In addition, discount rates are determined by evaluating comparable spreads observed currently in the market for similar instruments.
- Equity Securities: This portfolio consists of mutual funds and other equity investments. During some periods, the mutual funds in the Company's investment portfolio may have unrealized losses resulting from market fluctuations as well as the risk premium associated with that particular asset class. For example, emerging market equities tend to trade at a higher risk premium than U.S. government bonds and thus, will fluctuate to a greater degree on both the upside and the downside. In the context of a well-diversified portfolio, however, the correlation amongst the various asset classes represented by the funds serves to minimize downside risk. The Company evaluates each mutual fund in the portfolio regularly and measures performance on both an absolute and relative basis. A reasonable recovery period for positions with an unrealized loss is based on management's assessment of general economic data, trends within a particular asset class, valuations, earnings forecasts and bond durations. The Company has the ability and intent to hold these equity securities until a recovery of fair value.

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The following table shows the total OTTI that the Company recorded for the periods indicated:

	Three Months Ended September 30		Nine Months Ended September 30	
	2016	2015	2016	2015
	(Dollars in thousands)			
Gross change in OTTI recorded on certain investments	$ —	$ —	$ —	$ 84
Portion of OTTI recognized in OCI	—	—	—	(84)
Total credit related OTTI recognized in earnings	$ —	$ —	$ —	$ —

The following table shows the cumulative credit related component of OTTI for the periods indicated:

	Three Months Ended September 30		Nine Months Ended September 30	
	2016	2015	2016	2015
	(Dollars in thousands)			
Balance at beginning of period	$ —	$ —	$ —	$ (9,997)
Add				
Incurred on securities not previously impaired	—	—	—	—
Incurred on securities previously impaired	—	—	—	—
Less				
Securities sold during the period	—	—	—	9,997
Reclassification due to changes in Company's intent	—	—	—	—
Increases in cash flow expected to be collected	—	—	—	—
Balance at end of period	$ —	$ —	$ —	$ —

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NOTE 4 - LOANS, ALLOWANCE FOR LOAN LOSSES, AND CREDIT QUALITY

The following tables bifurcate the amount of loans and the allowance allocated to each loan category based on the type of impairment analysis as of the periods indicated:

	September 30, 2016 (Dollars in thousands)								
	Commercial and Industrial	Commercial Real Estate	Commercial Construction	Small Business	Residential Real Estate	Home Equity	Other Consumer	Total	
Financing receivables ending balance:									
Collectively evaluated for impairment	$853,245	$2,759,158	$376,245	$114,085	$609,854	$958,999	$11,244	$5,682,830	
Individually evaluated for impairment	$4,468	$18,077	$—	$969	$14,193	$5,904	$418	$44,029	
Purchased credit impaired loans	$—	$10,425	$—	$—	$8,638	$209	$2	$19,274	
Total loans by group	$857,713	$2,787,660	$376,245	$115,054	$632,685	$965,112	$11,664	$5,746,133	(1)

	December 31, 2015 (Dollars in thousands)								
	Commercial and Industrial	Commercial Real Estate	Commercial Construction	Small Business	Residential Real Estate	Home Equity	Other Consumer	Total	
Financing receivables ending balance:									
Collectively evaluated for impairment	$838,129	$2,619,294	$373,064	$95,225	$614,014	$921,563	$14,427	$5,475,716	
Individually evaluated for impairment	$5,147	$22,986	$304	$1,021	$15,405	$5,989	$558	$51,410	
Purchased credit impaired loans	$—	$11,154	$—	$—	$9,187	$251	$3	$20,595	
Total loans by group	$843,276	$2,653,434	$373,368	$96,246	$638,606	$927,803	$14,988	$5,547,721	(1)

(1) The amount of net deferred fees on loans and net unamortized discounts on acquired loans not deemed to be purchased credit impaired ("PCI") included in the ending balance was $10.9 million at both September 30, 2016 and December 31, 2015 respectively.

The following tables summarize changes in allowance for loan losses by loan category for the periods indicated:

	Three Months Ended September 30, 2016 (Dollars in thousands)							
	Commercial and Industrial	Commercial Real Estate	Commercial Construction	Small Business	Residential Real Estate	Home Equity	Other Consumer	Total
Allowance for loan losses								
Beginning balance	$14,027	$ 29,011	$ 5,216	$1,441	$ 2,578	$ 4,986	$ 468	$57,727

Charge-offs	(27)	(341)	—	(98)	—	(154)	(523)	(1,143)
Recoveries	63	124	—	28	130	24	302	671
Provision (benefit)	(189)	609	117	113	(44)	196	148	950
Ending balance	$13,874	$ 29,403	$ 5,333	$1,484	$ 2,664	$ 5,052	$ 395	$58,205

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	Three Months Ended September 30, 2015 (Dollars in thousands)							
	Commercial and Industrial	Commercial Real Estate	Commercial Construction	Small Business	Residential Real Estate	Home Equity	Other Consumer	Total
Allowance for loan losses								
Beginning balance	$15,279	$26,359	$4,071	$1,248	$2,551	$4,871	$616	$54,995
Charge-offs	(497)	(28)	—	(2)	(40)	(249)	(349)	(1,165)
Recoveries	22	152	—	57	6	130	208	575
Provision (benefit)	(518)	582	422	(20)	75	128	131	800
Ending balance	$14,286	$27,065	$4,493	$1,283	$2,592	$4,880	$606	$55,205

	Nine Months Ended September 30, 2016 (Dollars in thousands)							
	Commercial and Industrial	Commercial Real Estate	Commercial Construction	Small Business	Residential Real Estate	Home Equity	Other Consumer	Total
Allowance for loan losses								
Beginning balance	$13,802	$27,327	$5,366	$1,264	$2,590	$4,889	$587	$55,825
Charge-offs	(31)	(365)	—	(191)	(27)	(491)	(1,152)	(2,257)
Recoveries	850	535	—	122	182	77	796	2,562
Provision (benefit)	(747)	1,906	(33)	289	(81)	577	164	2,075
Ending balance	$13,874	$29,403	$5,333	$1,484	$2,664	$5,052	$395	$58,205
Ending balance: individually evaluated for impairment	$134	$355	$—	$2	$1,156	$223	$23	$1,893
Ending balance: collectively evaluated for impairment	$13,740	$29,048	$5,333	$1,482	$1,508	$4,829	$372	$56,312

	Nine Months Ended September 30, 2015 (Dollars in thousands)							
	Commercial and Industrial	Commercial Real Estate	Commercial Construction	Small Business	Residential Real Estate	Home Equity	Other Consumer	Total
Allowance for loan losses								
Beginning balance	$15,573	$25,873	$3,945	$1,171	$2,834	$4,956	$748	$55,100
Charge-offs	(1,531)	(236)	—	(198)	(242)	(659)	(922)	(3,788)
Recoveries	903	1,006	—	189	52	234	509	2,893
Provision (benefit)	(659)	422	548	121	(52)	349	271	1,000
Ending balance	$14,286	$27,065	$4,493	$1,283	$2,592	$4,880	$606	$55,205
Ending balance: individually evaluated for impairment	$252	$225	$—	$28	$1,313	$245	$27	$2,090
Ending balance: collectively evaluated for impairment	$14,034	$26,840	$4,493	$1,255	$1,279	$4,635	$579	$53,115

For the purpose of estimating the allowance for loan losses, management segregates the loan portfolio into the portfolio segments detailed in the above tables. Each of these loan categories possesses unique risk characteristics that are considered when determining the appropriate level of allowance for each segment. Some of the risk characteristics unique to each loan category include:

Commercial Portfolio

- Commercial and Industrial: Loans in this category consist of revolving and term loan obligations extended to business and corporate enterprises for the purpose of financing working capital and/or capital investment. Collateral generally consists of pledges of business assets including, but not limited to: accounts receivable, inventory, plant and equipment, or real estate, if applicable. Repayment sources consist of primarily, operating cash flow, and secondarily, liquidation of assets.

- Commercial Real Estate: Loans in this category consist of mortgage loans to finance investment in real property such as multi-family residential, commercial/retail, office, industrial, hotels, educational and healthcare facilities and other specific use properties. Loans are typically written with amortizing payment structures. Collateral values are determined based upon third party appraisals and evaluations. Loan to value ratios at origination are governed by established policy and regulatory guidelines. Repayment sources consist of primarily, cash flow from operating leases and rents, and secondarily, liquidation of assets.

- Commercial Construction: Loans in this category consist of short-term construction loans, revolving and nonrevolving credit lines and construction/permanent loans to finance the acquisition, development and construction or rehabilitation of real property. Project types include residential 1-4 family, condominium and multi-family homes, commercial/retail, office, industrial, hotels, educational and healthcare facilities and other specific use properties. Loans may be written with nonamortizing or hybrid payment structures depending upon the type of project. Collateral values are determined based upon third party appraisals and evaluations. Loan to value ratios at origination are governed by established policy and regulatory guidelines. Repayment sources vary depending upon the type of project and may consist of sale or lease of units, operating cash flows or liquidation of other assets.
- Small Business: Loans in this category consist of revolving, term loan and mortgage obligations extended to sole proprietors and small businesses for purposes of financing working capital and/or capital investment. Collateral generally consists of pledges of business assets including, but not limited to, accounts receivable, inventory, plant and equipment, or real estate if applicable. Repayment sources consist primarily of operating cash flows, and secondarily, liquidation of assets.

For the commercial portfolio it is the Company’s policy to obtain personal guarantees for payment from individuals holding material ownership interests of the borrowing entities.

Consumer Portfolio

- Residential Real Estate: Residential mortgage loans held in the Company’s portfolio are made to borrowers who demonstrate the ability to make scheduled payments with full consideration to underwriting factors such as current and expected income, employment status, current assets, other financial resources, credit history and the value of the collateral. Collateral consists of mortgage liens on 1-4 family residential properties. The Company does not originate or purchase sub-prime loans.
- Home Equity: Home equity loans and lines are made to qualified individuals and are primarily secured by senior or junior mortgage liens on owner-occupied 1-4 family homes, condominiums or vacation homes. The home equity loan has a fixed rate and is billed in equal payments comprised of principal and interest. The home equity line of credit has a variable rate and is billed in interest-only payments during the draw period. At the end of the draw period, the home equity line of credit is billed as a percentage of the principal balance plus all accrued interest. Additionally, the Company has the option of renewing the line of credit for additional draw periods. Borrower qualifications include favorable credit history combined with supportive income requirements and combined loan to value ratios within established policy guidelines.
- Other Consumer: Other consumer loan products include personal lines of credit and amortizing loans made to qualified individuals for various purposes such as education, debt consolidation, personal expenses or overdraft protection. Borrower qualifications include favorable credit history combined with supportive income and collateral requirements within established policy guidelines. These loans may be secured or unsecured.

Credit Quality

The Company continually monitors the asset quality of the loan portfolio using all available information. Based on this information, loans demonstrating certain payment issues or other weaknesses may be categorized as delinquent, impaired, nonperforming and/or put on nonaccrual status. Additionally, in the course of resolving such loans, the Company may choose to restructure the contractual terms of certain loans to match the borrower’s ability to repay the loan based on their current financial condition. If a restructured loan meets certain criteria, it may be categorized as a troubled debt restructuring (“TDR”).

The Company reviews numerous credit quality indicators when assessing the risk in its loan portfolio. For the commercial portfolio, the Company utilizes a 10-point commercial risk-rating system, which assigns a risk-grade to each borrower based on a number of quantitative and qualitative factors associated with a commercial loan transaction. Factors considered include industry and market conditions, position within the industry, earnings trends, operating cash flow, asset/liability values, debt capacity, guarantor strength, management and controls, financial reporting, collateral, and other considerations. The risk-ratings categories are defined as follows:

- 1- 6 Rating — Pass: Risk-rating grades “1” through “6” comprise those loans ranging from ‘Substantially Risk Free’ which indicates borrowers are of unquestioned credit standing and the pinnacle of credit quality, well established companies with a very strong financial condition, and loans fully secured by cash collateral, through ‘Acceptable Risk’, which indicates borrowers may exhibit declining earnings, strained cash flow, increasing or above average leverage and/or weakening market fundamentals that indicate below average asset quality, margins and market share. Collateral coverage is protective.

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- 7 Rating — Potential Weakness: Borrowers exhibit potential credit weaknesses or downward trends deserving management's close attention. If not checked or corrected, these trends will weaken the Company's asset and position. While potentially weak, currently these borrowers are marginally acceptable; no loss of principal or interest is envisioned.
- 8 Rating — Definite Weakness Loss Unlikely: Borrowers exhibit well defined weaknesses that jeopardize the orderly liquidation of debt. Loan may be inadequately protected by the current net worth and paying capacity of the obligor or by the collateral pledged, if any. Normal repayment from the borrower is in jeopardy, although no loss of principal is envisioned. However, there is a distinct possibility that a partial loss of interest and/or principal will occur if the deficiencies are not corrected. Collateral coverage may be inadequate to cover the principal obligation.
- 9 Rating — Partial Loss Probable: Borrowers exhibit well defined weaknesses that jeopardize the orderly liquidation of debt with the added provision that the weaknesses make collection of the debt in full, on the basis of currently existing facts, conditions, and values, highly questionable and improbable. Serious problems exist to the point where partial loss of principal is likely.
- 10 Rating — Definite Loss: Borrowers deemed incapable of repayment. Loans to such borrowers are considered uncollectible and of such little value that continuation as active assets of the Company is not warranted.

The credit quality of the commercial loan portfolio is actively monitored and any changes in credit quality are reflected in risk-rating changes. Risk-ratings are assigned or reviewed for all new loans, when advancing significant additions to existing relationships (over $50,000), at least quarterly for all actively managed loans, and any time a significant event occurs, including at renewal of the loan.

The Company utilizes a comprehensive strategy for monitoring commercial credit quality. Borrowers are required to provide updated financial information at least annually which is carefully evaluated for any changes in credit quality. Larger loan relationships are subject to a full annual credit review by an experienced credit analysis group. Additionally, the Company retains an independent loan review firm to evaluate the credit quality of the commercial loan portfolio. The independent loan review process achieves significant penetration into the commercial loan portfolio and reports the results of these reviews to the Audit Committee of the Board of Directors on a quarterly basis.

The following table details the amount of outstanding principal balances relative to each of the risk-rating categories for the Company's commercial portfolio:

		September 30, 2016				
Category	Risk Rating	Commercial and Industrial	Commercial Real Estate	Commercial Construction	Small Business	Total
		(Dollars in thousands)				
Pass	1 - 6	$746,616	$2,648,658	$ 370,149	$ 112,442	$3,877,865
Potential weakness	7	83,166	86,408	4,516	1,965	176,055
Definite weakness-loss unlikely	8	27,909	50,162	1,580	619	80,270
Partial loss probable	9	22	2,432	—	28	2,482
Definite loss	10	—	—	—	—	—
Total		$857,713	$2,787,660	$ 376,245	$ 115,054	$4,136,672

		December 31, 2015				
Category	Risk Rating	Commercial and Industrial	Commercial Real Estate	Commercial Construction	Small Business	Total
		(Dollars in thousands)				
Pass	1 - 6	$765,753	$2,484,025	$ 363,781	$ 93,008	$3,706,567
Potential weakness	7	54,375	112,022	7,678	2,444	176,519
Definite weakness-loss unlikely	8	23,073	56,276	1,909	732	81,990

Partial loss probable	9	75	1,111	—	62	1,248
Definite loss	10	—	—	—	—	—
Total		$843,276	$2,653,434	$ 373,368	$ 96,246	$3,966,324

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For the Company's consumer portfolio, the quality of the loan is best indicated by the repayment performance of an individual borrower. However, the Company does supplement performance data with current Fair Isaac Corporation ("FICO") scores and Loan to Value ("LTV") estimates. Current FICO data is purchased and appended to all consumer loans on a quarterly basis. In addition, automated valuation services and broker opinions of value are used to supplement original value data for the residential and home equity portfolios, periodically. The following table shows the weighted average FICO scores and the weighted average combined LTV ratios as of the periods indicated below:

	September 30, 2016		December 31, 2015	
Residential portfolio				
FICO score (re-scored)(1)	743		742	
LTV (re-valued)(2)	62.7	%	61.4	%
Home equity portfolio				
FICO score (re-scored)(1)	767		765	
LTV (re-valued)(2)	56.2	%	55.8	%

(1) The average FICO scores for September 30, 2016 are based upon rescores available from August 31, 2016 and origination score data for loans booked between September 1, 2016 and September 30, 2016. The average FICO scores for December 31, 2015 are based upon rescores available from November 30, 2015 and origination score data for loans booked between December 1, 2015 and December 31, 2015.

(2) The combined LTV ratios for September 30, 2016 are based upon updated automated valuations as of March 31, 2015 and origination value data for loans booked between April 1, 2015 and September 30, 2016. The combined LTV ratios for December 31, 2015 are based upon updated automated valuations as of March 31, 2015 and actual score data for loans booked from April 1, 2015 through December 31, 2015. For home equity loans and lines in a subordinate lien position, the LTV data represents a combined LTV, taking into account the senior lien data for loans and lines.

Asset Quality

The Company's philosophy toward managing its loan portfolios is predicated upon careful monitoring, which stresses early detection and response to delinquent and default situations. Delinquent loans are managed by a team of seasoned collection specialists and the Company seeks to make arrangements to resolve any delinquent or default situation over the shortest possible time frame. As a general rule, loans more than 90 days past due with respect to principal or interest are classified as nonaccrual loans. The Company also may use discretion regarding other loans over 90 days delinquent if the loan is well secured and/or in process of collection. Set forth is information regarding the Company's nonperforming loans at the period shown:

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The following table shows information regarding nonaccrual loans at the dates indicated:

	September 30, 2016	December 31, 2015
	(Dollars in thousands)	
Commercial and industrial	$3,065	$ 3,699
Commercial real estate	7,399	7,856
Commercial construction	—	304
Small business	288	239
Residential real estate	7,684	8,795
Home equity	6,311	6,742
Other consumer	44	55
Total nonaccrual loans(1)	$24,791	$ 27,690

(1) Included in these amounts were $5.9 million and $5.2 million of nonaccruing TDRs at September 30, 2016 and December 31, 2015, respectively.

The following table shows information regarding foreclosed residential real estate property at the dates indicated:

	September 30, 2016	December 31, 2015
	(Dollars in thousands)	
Foreclosed residential real estate property held by the creditor	$1,384	$ 1,430
Recorded investment in mortgage loans collateralized by residential real estate property that are in the process of foreclosure	$1,557	$ 1,059

The following table shows the age analysis of past due financing receivables as of the dates indicated:

	September 30, 2016										
	30-59 days		60-89 days		90 days or more		Total Past Due				
	Number of Loans	Principal Balance	Number of Loans	Principal Balance	Number of Loans	Principal Balance	Number of Loans	Principal Balance	Current	Total Financing Receivables	Recorded Investment >90 Days and Accruing
	(Dollars in thousands)										
Loan Portfolio											
Commercial and industrial	5	$ 436	2	$ 205	6	$ 2,584	13	$ 3,225	$ 854,488	$ 857,713	$ —
Commercial real estate	6	3,396	9	2,200	8	3,772	23	9,368	2,778,292	2,787,660	—
Commercial construction	—	—	—	—	—	—	—	—	376,245	376,245	—
Small business	16	218	5	90	18	203	39	511	114,543	115,054	—
Residential real estate	13	2,621	11	1,692	27	4,222	51	8,535	624,150	632,685	—
Home equity	14	1,199	11	611	30	1,794	55	3,604	961,508	965,112	—
Other consumer (1)	250	230	19	32	15	11	284	273	11,391	11,664	2
Total	304	$ 8,100	57	$ 4,830	104	$ 12,586	465	$ 25,516	$ 5,720,617	$ 5,746,133	$ 2

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	December 31, 2015										
	30-59 days		60-89 days		90 days or more		Total Past Due		Current	Total Financing Receivables	Recorded Investment >90 Days and Accruing
	Number of Loans	Principal Balance	Number of Loans	Principal Balance	Number of Loans	Principal Balance	Number of Loans	Principal Balance			
	(Dollars in thousands)										
Loan Portfolio											
Commercial and industrial	9	$399	4	$ 1,021	8	$3,039	21	$4,459	$838,817	$843,276	$ —
Commercial real estate	19	7,349	6	1,627	13	4,458	38	13,434	2,640,000	2,653,434	—
Commercial construction	—	—	—	—	1	304	1	304	373,064	373,368	—
Small business	11	93	4	9	13	69	28	171	96,075	96,246	—
Residential real estate	20	3,119	11	2,049	19	3,433	50	8,601	630,005	638,606	—
Home equity	21	1,526	11	903	20	1,338	52	3,767	924,036	927,803	—
Other consumer (1)	297	231	12	65	13	25	322	321	14,667	14,988	—
Total	377	$12,717	48	$ 5,674	87	$12,666	512	$31,057	$5,516,664	$5,547,721	$ —

(1) Other consumer portfolio is inclusive of deposit account overdrafts recorded as loan balances.

Troubled Debt Restructurings

In the course of resolving nonperforming loans, the Bank may choose to restructure the contractual terms of certain loans. The Bank attempts to work out an alternative payment schedule with the borrower in order to avoid foreclosure actions. Any loans that are modified are reviewed by the Bank to identify if a TDR has occurred, which is when, for economic or legal reasons related to a borrower's financial difficulties, the Bank grants a concession to the borrower that it would not otherwise consider. Terms may be modified to fit the ability of the borrower to repay in line with its current financial status and the restructuring of the loan may include the transfer of assets from the borrower to satisfy the debt, a modification of loan terms, or a combination of the two.

The following table shows the Company's total TDRs and other pertinent information as of the dates indicated:

	September 30, 2016	December 31, 2015
	(Dollars in thousands)	
TDRs on accrual status	$27,644	$ 32,849
TDRs on nonaccrual	5,910	5,225
Total TDRs	$33,554	$ 38,074
Amount of specific reserves included in the allowance for loan losses associated with TDRs	$1,515	$ 1,628
Additional commitments to lend to a borrower who has been a party to a TDR	$1,097	$ 972

The Company's policy is to have any restructured loan which is on nonaccrual status prior to being modified remain on nonaccrual status for six months subsequent to being modified before management considers its return to accrual status. If the restructured loan is on accrual status prior to being modified, it is reviewed to determine if the modified loan should remain on accrual status. Additionally, loans classified as TDRs are adjusted to reflect the changes in value of the recorded investment in the loan, if any, resulting from the granting of a concession. For all residential loan modifications, the borrower must perform during a 90 day trial period before the modification is finalized.

The following table shows the modifications which occurred during the periods indicated and the change in the recorded investment subsequent to the modifications occurring:

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	Three Months Ended September 30, 2016			Nine Months Ended September 30, 2016		
	Number of Contracts	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment (1)	Number of Contracts	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment (1)
	(Dollars in thousands)					
Troubled debt restructurings						
Commercial and industrial	—	$ —	$ —	7	$ 528	$ 528
Commercial real estate	3	986	986	9	2,329	2,329
Small business	1	59	59	3	168	168
Residential real estate	—	—	—	5	1,167	1,209
Home equity	4	328	328	8	632	632
Other consumer	—	—	—	5	107	107
Total	8	$ 1,373	$ 1,373	37	$ 4,931	$ 4,973

	Three Months Ended September 30, 2015			Nine Months Ended September 30, 2015		
	Number of Contracts	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment (1)	Number of Contracts	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment (1)
	(Dollars in thousands)					
Troubled debt restructurings						
Commercial and industrial	1	$ 100	$ 100	10	$ 1,153	$ 1,153
Commercial real estate	1	653	653	6	2,963	2,963
Small business	2	103	103	7	269	269
Residential real estate	2	218	245	5	376	403
Home equity	1	36	36	4	251	251
Total	7	$ 1,110	$ 1,137	32	$ 5,012	$ 5,039

(1) The post-modification balances represent the legal principal balance of the loan on the date of modification. These amounts may show an increase when modifications include a capitalization of interest.

The following table shows the Company’s post-modification balance of TDRs listed by type of modification as of the periods indicated:

	Three Months Ended September 30		Nine Months Ended September 30	
	2016	2015	2016	2015
	(Dollars in thousands)		(Dollars in thousands)	
Extended maturity	$256	$855	$ 2,638	$ 2,204
Adjusted interest rate	—	—	92	—
Combination rate and maturity	730	246	990	2,769
Court ordered concession	387	36	1,253	66
Total	$1,373	$1,137	$ 4,973	$ 5,039

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The Company considers a loan to have defaulted when it reaches 90 days past due. The following table shows loans that have been modified during the past twelve months which have subsequently defaulted during the periods indicated:

	Three Months Ended September 30					
	2016			2015		
	Number of Contracts	Recorded Investment		Number of Contracts	Recorded Investment	
	(Dollars in thousands)					
Troubled debt restructurings that subsequently defaulted						
Home equity	1	$	141	—	$	—
	1	$	141	—	$	—

	Nine Months Ended September 30					
	2016			2015		
	Number of Contracts	Recorded Investment		Number of Contracts	Recorded Investment	
	(Dollars in thousands)					
Troubled debt restructurings that subsequently defaulted						
Commercial real estate	—	$	—	2	$	880
Commercial and industrial	—		—	3		339
Home equity	1	$	141	—	$	—
	1	$	141	5	$	1,219

All TDR loans are considered impaired and therefore are subject to a specific review for impairment. The impairment analysis appropriately discounts the present value of the anticipated cash flows by the loan's contractual rate of interest in effect prior to the loan's modification. The amount of impairment, if any, is recorded as a specific loss allocation to each individual loan in the allowance for loan losses. Commercial loans (commercial and industrial, commercial construction, commercial real estate and small business loans), residential loans, and home equity loans that have been classified as TDRs and which subsequently default are reviewed to determine if the loan should be deemed collateral dependent. In such an instance, any shortfall between the value of the collateral and the carrying value of the loan is determined by measuring the recorded investment in the loan against the fair value of the collateral less costs to sell. The Company charges off the amount of any confirmed loan loss in the period when the loans, or portion of loans, are deemed uncollectible. Smaller balance consumer TDR loans are reviewed for performance to determine when a charge-off is appropriate.

Impaired Loans

A loan is considered impaired when, based on current information and events, it is probable that the Company will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed.

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The tables below set forth information regarding the Company's impaired loans by loan portfolio at the dates indicated:

	September 30, 2016		
	Recorded Investment	Unpaid Principal Balance	Related Allowance
	(Dollars in thousands)		
With no related allowance recorded			
Commercial and industrial	$2,382	$2,750	$ —
Commercial real estate	11,481	12,567	—
Small business	612	703	—
Residential real estate	4,226	4,399	—
Home equity	4,611	4,733	—
Other consumer	158	159	—
Subtotal	23,470	25,311	—
With an allowance recorded			
Commercial and industrial	$2,086	$2,252	$ 134
Commercial real estate	6,596	7,023	355
Small business	357	369	2
Residential real estate	9,967	10,968	1,156
Home equity	1,293	1,459	223
Other consumer	260	261	23
Subtotal	20,559	22,332	1,893
Total	$44,029	$47,643	$ 1,893

	December 31, 2015		
	Recorded Investment	Unpaid Principal Balance	Related Allowance
	(Dollars in thousands)		
With no related allowance recorded			
Commercial and industrial	$2,613	$3,002	$ —
Commercial real estate	12,008	13,128	—
Commercial construction	304	305	—
Small business	527	618	—
Residential real estate	3,874	4,033	—
Home equity	4,893	5,005	—
Other consumer	184	185	—
Subtotal	24,403	26,276	—
With an allowance recorded			
Commercial and industrial	$2,534	$2,648	$ 183
Commercial real estate	10,978	11,047	204
Small business	494	523	4
Residential real estate	11,531	12,652	1,278
Home equity	1,096	1,287	238
Other consumer	374	389	23
Subtotal	27,007	28,546	1,930
Total	$51,410	$54,822	$ 1,930

The following tables set forth information regarding interest income recognized on impaired loans, by portfolio, for the periods indicated:

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	Three Months Ended September 30, 2016		Nine Months Ended September 30, 2016	
	Average Recorded Investment	Interest Income Recognized	Average Recorded Investment	Interest Income Recognized
	(Dollars in thousands)			
With no related allowance recorded				
Commercial and industrial	$2,444	$ 16	$2,584	$ 48
Commercial real estate	11,549	115	11,775	348
Small business	646	5	679	18
Residential real estate	4,255	42	4,286	134
Home equity	4,616	45	4,677	138
Other consumer	162	3	168	9
Subtotal	23,672	226	24,169	695
With an allowance recorded				
Commercial and industrial	$2,097	$ 4	$2,135	$ 13
Commercial real estate	6,854	42	6,977	126
Small business	367	6	384	17
Residential real estate	10,004	92	10,071	272
Home equity	1,299	13	1,310	36
Other consumer	265	2	272	6
Subtotal	20,886	159	21,149	470
Total	$44,558	$ 385	$45,318	$ 1,165

	Three Months Ended September 30, 2015		Nine Months Ended September 30, 2015	
	Average Recorded Investment	Interest Income Recognized	Average Recorded Investment	Interest Income Recognized
	(Dollars in thousands)			
With no related allowance recorded				
Commercial and industrial	$2,080	$ 11	$2,204	$ 41
Commercial real estate	13,876	89	14,433	337
Commercial construction	307	—	309	—
Small business	465	4	484	14
Residential real estate	3,566	42	3,601	123
Home equity	4,585	44	4,670	134
Other consumer	198	4	207	12
Subtotal	25,077	194	25,908	661
With an allowance recorded				
Commercial and industrial	$3,687	$ 10	$3,894	$ 57
Commercial real estate	15,830	204	15,993	609
Small business	540	7	564	22
Residential real estate	11,698	106	11,764	358
Home equity	1,221	4	1,238	13
Other consumer	421	4	443	11
Subtotal	33,397	335	33,896	1,070
Total	$58,474	$ 529	$59,804	$ 1,731

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Purchased Credit Impaired Loans

Certain loans acquired by the Company may have shown evidence of deterioration of credit quality since origination and it was therefore deemed unlikely that the Company would be able to collect all contractually required payments. As such, these loans were deemed to be PCI loans and the carrying value and prospective income recognition are predicated upon future cash flows expected to be collected. The following table displays certain information pertaining to PCI loans at the dates indicated:

	September 30, 2016	December 31, 2015
	(Dollars in thousands)	
Outstanding balance	$21,481	$ 23,199
Carrying amount	$19,274	$ 20,595

The following table summarizes activity in the accretable yield for the PCI loan portfolio:

	Three Months Ended September 30		Nine Months Ended September 30	
	2016	2015	2016	2015
	(Dollars in thousands)			
Beginning balance	$2,625	$2,527	$2,827	$2,974
Acquisition	—	—	—	319
Accretion	(359)	(592)	(1,188)	(2,138)
Other change in expected cash flows (1)	213	278	744	978
Reclassification from nonaccretable difference for loans which have paid off (2)	—	218	96	298
Ending balance	$2,479	$2,431	$2,479	$2,431

(1) Represents changes in cash flows expected to be collected and resulting in increased interest income as a prospective yield adjustment over the remaining life of the loan(s).
(2) Results in increased interest income during the period in which the loan paid off at amount greater than originally expected.

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NOTE 5 -EARNINGS PER SHARE

Earnings per share consisted of the following components for the periods indicated:

	Three Months Ended		Nine Months Ended	
	September 30		September 30	
	2016	2015	2016	2015
	(Dollars in thousands, except share and per share data)			
Net income	$20,484	$ 18,594	$59,469	$ 45,505
Weighted Average Shares				
Basic shares	26,324,316	26,200,621	26,301,340	25,774,571
Effect of dilutive securities	53,072	63,493	48,354	72,921
Diluted shares	26,377,388	26,264,114	26,349,694	25,847,492
Net income per share				
Basic EPS	$0.78	$ 0.71	$2.26	$ 1.77
Effect of dilutive securities	—	—	—	(0.01)
Diluted EPS	$0.78	$ 0.71	$2.26	$ 1.76

The following table illustrates the options to purchase common stock or shares of performance-based restricted stock that were excluded from the calculation of diluted earnings per share because they were anti-dilutive for the periods indicated:

	Three Months Ended		Nine Months Ended	
	September 30		September 30	
	2016	2015	2016	2015
Stock options	4,293	—	1,441	—
Performance-based restricted stock	—	—	—	—

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NOTE 6 - STOCK BASED COMPENSATION

Time Vested Restricted Stock Awards

During the nine months ended September 30, 2016, the Company made the following awards of restricted stock:

Date	Shares Granted	Plan	Grant Date Fair Value Per Share	Vesting Period
2/11/2016	51,475	2005 Employee Stock Plan	$ 41.96	Ratably over 5 years from grant date
3/1/2016	600	2005 Employee Stock Plan	$ 44.37	Ratably over 5 years from grant date
5/24/2016	8,700	2010 NonEmployee Director Stock Plan	$ 48.34	Cliff vest 5 years from grant date
9/19/2016	800	2005 Employee Stock Plan	$ 52.92	Ratably over 5 years from grant date

The fair value of the restricted stock awards is based upon the average of the high and low price at which the Company’s common stock traded on the date of grant. The holders of restricted stock awards participate fully in the rewards of stock ownership of the Company, including voting and dividend rights.

Performance-Based Restricted Stock Awards

On February 11, 2016, the Company granted 20,450 performance-based restricted stock awards to certain executive level employees. These performance-based restricted stock awards were issued from the 2005 Employee Stock Plan and were determined to have a grant date fair value per share of $41.96. The number of shares to be vested will be contingent upon the Company's attainment of certain performance measures outlined in the award agreement and will be measured as of the end of the three year performance period (January 1, 2016 - December 31, 2018). These awards will be accounted for as equity awards due to the nature of these awards and the fact that these shares will not be settled in cash.

The fair value of the performance-based restricted stock awards, assuming achievement at target, is based upon the average of the high and low price at which the Company’s common stock traded on the date of grant. The holders of these awards are not entitled to receive dividends or vote until the shares are vested.

Stock Options

The Company has made the following awards of nonqualified options to purchase shares of common stock during the nine months ended September 30, 2016:

	Nine Months Ended September 30, 2016	
Date of grant	7/14/2016	2/20/2016
Plan	2010	2010
Options granted	5,000	5,000
Vesting period (beginning on grant date)	18 months	22 months
Expiration date	7/14/2026	2/20/2026
Expected volatility	32.28 %	32.44 %
Expected life (years)	5.5	5.5
Expected dividend yield	2.37 %	2.28 %
Risk free interest rate	1.14 %	1.29 %
Fair value per option	$ 11.46	$ 10.59

NOTE 7 - REPURCHASE AGREEMENTS

The Company can raise additional liquidity by entering into repurchase agreements at its discretion. In a security repurchase agreement transaction, the Company will generally sell a security, agreeing to repurchase either the same or substantially identical security on a specified later date, at a greater price than the original sales price. The difference between the sale price and purchase price is the cost of the proceeds, which is recorded as interest expense. The securities underlying the agreements are delivered to counterparties as security for the repurchase obligations.

Since the securities are treated as collateral and the agreement does not

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qualify for a full transfer of effective control, the transactions does not meet the criteria to be classified as a sale, and is therefore considered a secured borrowing transaction for accounting purposes. Payments on such borrowings are interest only until the scheduled repurchase date. In a repurchase agreement the Company is subject to the risk that the purchaser may default at maturity and not return the securities underlying the agreements. In order to minimize this potential risk, the Company either deals with established firms when entering into these transactions or with customers whose agreements stipulate that the securities underlying the agreement are not delivered to the customer and instead are held in segregated safekeeping accounts by the Company's safekeeping agents. The tables below set forth information regarding the Company's repurchase agreements allocated by source of collateral at the dates indicated:

	September 30, 2016				
	Remaining Contractual Maturity of the Agreements				
	Overnight and Continuous	Up to 30 Days	30-90 Days	Greater than 90 Days	Total
	(Dollars in thousands)				
Sources of collateral					
U.S. government agency securities	$15,608	$ —	$ —	$ —	$15,608
Agency mortgage-backed securities	54,535	—	—	—	54,535
Agency collateralized mortgage obligations	70,771	—	—	—	70,771
Total borrowings	$140,914	$ —	$ —	$ —	$140,914

	December 31, 2015				
	Remaining Contractual Maturity of the Agreements				
	Overnight and Continuous	Up to 30 Days	30-90 Days	Greater than 90 Days	Total
	(Dollars in thousands)				
Sources of Collateral					
U.S. government agency securities	$10,157	$ —	$ —	$ —	$10,157
Agency mortgage-backed securities	69,142	—	—	—	69,142
Agency collateralized mortgage obligations	54,659	—	—	—	54,659
Total borrowings	$133,958	$ —	$ —	$ —	$133,958

Certain counterparties monitor collateral, and may request additional collateral to be posted from time to time. For further information regarding the Company's repurchase agreements see Note 9 - Balance Sheet Offsetting.

NOTE 8 - DERIVATIVE AND HEDGING ACTIVITIES

The Company's derivative financial instruments are used to manage differences in the amount, timing, and duration of the Company's known or expected cash receipts and its known or expected cash payments principally to manage the Company's interest rate risk. Additionally, the Company enters into interest rate derivatives and foreign exchange contracts to accommodate the business requirements of its customers ("customer related positions"). The Company minimizes the market and liquidity risks of customer related positions by entering into similar offsetting positions with broker-dealers. Derivative instruments are carried at fair value in the Company's financial statements. The accounting for changes in the fair value of a derivative instrument is dependent upon whether or not it qualifies as a hedge for accounting purposes, and further, by the type of hedging relationship.

The Company does not enter into proprietary trading positions for any derivatives.

Interest Rate Positions

The Company currently utilizes interest rate swap agreements as hedging instruments against interest rate risk associated with the Company's borrowings. An interest rate swap is an agreement whereby one party agrees to pay a floating rate of interest on a notional principal amount in exchange for receiving a fixed rate of interest on the same notional amount, for a predetermined period of time, from a second party. The amounts relating to the notional principal amount are not actually exchanged. The maximum length of time over which the Company is currently hedging its exposure to the variability in future cash flows for forecasted transactions related to the payment of variable interest on existing financial instruments is five years.

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The following table reflects the Company’s derivative positions for the periods indicated below for interest rate swaps which qualify as cash flow hedges for accounting purposes:

September 30, 2016

Notional Amount	Trade Date	Effective Date	Maturity Date		Receive (Variable) Index	Current Rate Received		Pay Fixed Swap Rate		Fair Value	
(Dollars in thousands)											
$25,000	16-Feb-06	28-Dec-06	28-Dec-16		3 Month LIBOR	0.85	%	5.04	%	$ (255	)
25,000	16-Feb-06	28-Dec-06	28-Dec-16		3 Month LIBOR	0.85	%	5.04	%	(255	)
25,000	9-Dec-08	10-Dec-08	10-Dec-18		3 Month LIBOR	0.85	%	2.94	%	(1,068	)
25,000	1-Apr-16	17-Jan-17	15-Dec-21	(1)	3 Month LIBOR	TBD		1.36	%	(208	)
25,000	1-Apr-16	17-Jan-17	15-Dec-21	(1)	3 Month LIBOR	TBD		1.36	%	(207	)
$125,000										$ (1,993	)

December 31, 2015

Notional Amount	Trade Date	Effective Date	Maturity Date	Receive (Variable) Index	Current Rate Received		Pay Fixed Swap Rate		Fair Value	
			(Dollars in thousands)							
$25,000	16-Feb-06	28-Dec-06	28-Dec-16	3 Month LIBOR	0.51	%	5.04	%	$ (1,054	)
25,000	16-Feb-06	28-Dec-06	28-Dec-16	3 Month LIBOR	0.51	%	5.04	%	(1,055	)
25,000	9-Dec-08	10-Dec-08	10-Dec-18	3 Month LIBOR	0.49	%	2.94	%	(1,164	)
$75,000									$ (3,273	)

(1) In April 2016, the Company entered into two forward starting swaps with notional amounts of $25.0 million each, with the intention of hedging $50.0 million of existing junior subordinated debentures, as the current hedges on this borrowing expire in December 2016.

For derivative instruments that are designated and qualify as cash flow hedging instruments, the effective portion of the gains or losses is reported as a component of other comprehensive income ("OCI"), and is subsequently reclassified into earnings in the period that the hedged forecasted transaction affects earnings. The Company expects approximately $914,000 (pre-tax) to be reclassified to interest expense from OCI related to the Company’s cash flow hedges in the next twelve months. This reclassification is due to anticipated payments that will be made and/or received on the swaps based upon the forward curve as of September 30, 2016.

The Company recognized $61,000 and $183,000 of net amortization income that was an offset to interest expense related to previously terminated swaps for the three and nine month periods ended September 30, 2016 and 2015, respectively.

The Company had no fair value hedges as of September 30, 2016 or December 31, 2015.

Customer Related Positions

Loan level derivatives, primarily interest rate swaps, offered to commercial borrowers through the Company’s loan level derivative program do not qualify as hedges for accounting purposes. The Company believes that its exposure to commercial customer derivatives is limited because these contracts are simultaneously matched at inception with an offsetting dealer transaction. The commercial customer derivative program allows the Company to retain variable-rate commercial loans while allowing the customer to synthetically fix the loan rate by entering into a variable-to-fixed interest rate swap.

Foreign exchange contracts offered to commercial borrowers through the Company’s derivative program do not qualify as hedges for accounting purposes. The Company acts as a seller and buyer of foreign exchange contracts to accommodate its customers. To mitigate the market and liquidity risk associated with these derivatives, the Company enters into similar offsetting positions.

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The following table reflects the Company's customer related derivative positions for the periods indicated below for those derivatives not designated as hedging:

	Number of Positions (1)	Notional Amount Maturing Less than 1 year	Less than 2 years	Less than 3 years	Less than 4 years	Thereafter	Total	Fair Value
	September 30, 2016 (Dollars in thousands)							
Loan level swaps								
Receive fixed, pay variable	201	$29,006	$33,125	$79,593	$79,123	$559,208	$780,055	$41,390
Pay fixed, receive variable	186	$29,006	$33,125	$79,593	$79,123	$559,208	$780,055	$(41,357)
Foreign exchange contracts								
Buys foreign currency, sells U.S. currency	24	$48,831	$—	$—	$—	$—	$48,831	$91
Buys U.S. currency, sells foreign currency	24	$48,831	$—	$—	$—	$—	$48,831	$(66)
	December 31, 2015 (Dollars in thousands)							
Loan level swaps								
Receive fixed, pay variable	171	$37,732	$34,424	$29,629	$77,041	$488,110	$666,936	$22,467
Pay fixed, receive variable	165	$37,732	$34,424	$29,629	$77,041	$488,110	$666,936	$(22,462)
Foreign exchange contracts								
Buys foreign currency, sells U.S. currency	21	$38,416	$—	$—	$—	$—	$38,416	$(354)
Buys U.S. currency, sells foreign currency	21	$38,416	$—	$—	$—	$—	$38,416	$382

(1) The Company may enter into one dealer swap agreement which offsets multiple commercial borrower swap agreements.

Mortgage Derivatives

Prior to closing and funding certain 1- 4 family residential mortgage loans, an interest rate lock commitment is generally extended to the borrower. During the period from commitment date to closing date, the Company is subject to the risk that market rates of interest may change. If market rates rise, investors generally will pay less to purchase such loans resulting in a reduction in the gain on sale of the loans or, possibly, a loss. In an effort to mitigate such risk, forward delivery sales commitments are executed, under which the Company agrees to deliver whole mortgage loans to various investors. These forward commitments carry a market price that has a strong inverse relationship to that of mortgage prices. Certain assumptions, including pull through rates and rate lock periods, are used in managing the existing and future hedges. The effectiveness of the economic hedges rely on the accuracy of these assumptions.

The change in fair value on the interest rate lock commitments and forward delivery sale commitments are recorded in current period earnings as a component of mortgage banking income. In addition, the Company has elected the fair value option to carry loans held for sale at fair value. The change in fair value of loans held for sale is recorded in current period earnings as a component of mortgage banking income in accordance with the Company's fair value election. The change in fair value associated with loans held for sale was an increase of $47,000 and a decrease of $181,000 for the three month periods ended September 30, 2016 and 2015, respectively, and increases of $60,000 and $3,000 for the nine month periods ended September 30, 2016 and 2015, respectively. These amounts were offset in earnings by the change in the fair value of mortgage derivatives. The table below presents the fair value of the Company's derivative financial instruments as well as their classification on the balance sheet at the periods indicated:

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	Asset Derivatives			Liability Derivatives		
	Balance Sheet Location	Fair Value at September 30 2016	Fair Value at December 31 2015	Balance Sheet Location	Fair Value at September 30 2016	Fair Value at December 31 2015
	(Dollars in thousands)					
Derivatives designated as hedges						
Interest rate derivatives	Other assets	$ —	$ —	Other liabilities	$ 1,993	$ 3,273
Derivatives not designated as hedges						
Customer Related Positions						
Loan level derivatives	Other assets	$ 41,411	$ 22,470	Other liabilities	$ 41,378	$ 22,465
Foreign exchange contracts	Other assets	494	602	Other liabilities	469	574
Mortgage Derivatives						
Interest rate lock commitments	Other assets	488	233	Other liabilities	—	—
Forward sales agreements	Other assets	163	—	Other liabilities	—	1
		$ 42,556	$ 23,305		$ 41,847	$ 23,040
Total		$ 42,556	$ 23,305		$ 43,840	$ 26,313

The table below presents the effect of the Company’s derivative financial instruments included in OCI and current earnings for the periods indicated:

	Three Months Ended September 30		Nine Months Ended September 30	
	2016	2015	2016	2015
	(Dollars in thousands)			
Derivatives designated as hedges				
Gain in OCI on derivatives (effective portion), net of tax	$674	$132	$653	$596
Loss reclassified from OCI into interest expense (effective portion)	$(648)	$(715)	$(1,949)	$(2,130)
Loss recognized in income on derivatives (ineffective portion and amount excluded from effectiveness testing)				
Interest expense	$—	$—	$—	$—
Other expense	—	—	—	—
Total	$—	$—	$—	$—
Derivatives not designated as hedges				
Changes in fair value of customer related positions				
Other income	$(42)	$39	$71	$56
Other expense	(12)	—	(46)	(51)
Changes in fair value of mortgage derivatives				
Mortgage banking income	115	174	$419	67
Total	$61	$213	$444	$72

By using derivatives, the Company is exposed to credit risk to the extent that counterparties to the derivative contracts do not perform as required. Should a counterparty fail to perform under the terms of a derivative contract, the Company's credit exposure on interest rate swaps is limited to the net positive fair value and accrued interest of all swaps with each counterparty. The Company seeks to minimize counterparty credit risk through credit approvals, limits, monitoring procedures, and obtaining collateral, where appropriate. Institutional counterparties must have an investment grade credit rating and be approved by the Company's Board of Directors. As such, management believes the risk of incurring credit losses on derivative contracts with those counterparties is remote and losses, if any, would be immaterial. The Company had $10,000 exposure at September 30, 2016 and $2,000 in exposure relating to institutional counterparties at December 31, 2015. The Company's exposure relating to customer

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counterparties was approximately $42.1 million and $23.2 million at September 30, 2016 and December 31, 2015, respectively. Credit exposure may be reduced by the amount of collateral pledged by the counterparty.

NOTE 9 - BALANCE SHEET OFFSETTING

The Company does not offset fair value amounts recognized for derivative instruments or repurchase agreements. The Company does net the amount recognized for the right to reclaim cash collateral against the obligation to return cash collateral arising from derivative instruments executed with the same counterparty under a master netting arrangement. Collateral legally required to be maintained at dealer banks by the Company is monitored and adjusted as necessary. At September 30, 2016, it was determined that no additional collateral would have to be posted to immediately settle these instruments.

The following tables present the Company's asset and liability derivative positions and the potential effect of netting arrangements on its financial position, as of the periods indicated:

				Gross Amounts Not Offset in the Statement of Financial Position		
	Gross Amounts Recognized in the Statement of Financial Position	Gross Amounts Offset in the Statement of Financial Position	Net Amounts Presented in the Statement of Financial Position	Financial Instruments	Collateral Pledged (Received)	Net Amount
	September 30, 2016 (Dollars in thousands)					
Derivative Assets						
Loan level derivatives	$41,411	$ —	$41,411	$10	$—	$41,401
Customer foreign exchange contracts	494	—	494	—	—	494
	$41,905	$ —	$41,905	$10	$—	$41,895
Derivative Liabilities						
Interest rate swaps	$1,993	$ —	$1,993	$—	$1,993	$—
Loan level derivatives	41,378	—	41,378	10	41,358	10
Customer foreign exchange contracts	469	—	469	—	—	469
Repurchase agreements						
Customer repurchase agreements	140,914	—	140,914	—	140,914	—
	$184,754	$ —	$184,754	$10	$184,265	$479

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	Gross Amounts Recognized in the Statement of Financial Position	Gross Amounts Offset in the Statement of Financial Position	Net Amounts Presented in the Statement of Financial Position	Gross Amounts Not Offset in the Statement of Financial Position		Net Amount
				Financial Instruments (1)	Collateral Pledged (Received)	
	December 31, 2015					
	(Dollars in thousands)					
Derivative Assets						
Loan level derivatives	$22,470	$ —	$22,470	$2	$—	$22,468
Customer foreign exchange contracts	602	—	602	—	—	602
	$23,072	$ —	$23,072	$2	$—	$23,070
Derivative Liabilities						
Interest rate swaps	$3,273	$ —	$3,273	$—	$3,273	$—
Loan level derivatives	22,465	—	22,465	2	22,461	2
Customer foreign exchange contracts	574	—	574	—	—	574
Repurchase agreements						
Customer repurchase agreements	133,958	—	133,958	—	133,958	—
	$160,270	$ —	$160,270	$2	$159,692	$576

(1) Reflects offsetting derivative positions with the same counterparty.

The Company has agreements with certain of its derivative counterparties that contain a provision where if the Company fails to maintain its status as a well capitalized institution, then the Company could be required to terminate any outstanding derivatives with the counterparty. All liability position interest rate swap and customer loan level swap counterparties have credit-risk contingent features as of the dates indicated in the table above. In addition, derivative instruments that contain credit-risk related contingent features that are in a net liability position require the Company to assign collateral as noted in the table above.

NOTE 10 - FAIR VALUE MEASUREMENTS

Fair value is a market-based measure considered from the perspective of a market participant rather than an entity-specific measure. Therefore, even when market assumptions are not readily available, the Company's own assumptions are set to reflect those that market participants would use in pricing the asset or liability at the measurement date. If there has been a significant decrease in the volume and level of activity for the asset or liability, regardless of the valuation technique(s) used, the objective of a fair value measurement remains the same. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction (that is, not a forced liquidation or distressed sale) between market participants at the measurement date under current market conditions. The Company uses prices and inputs that are current as of the measurement date. In periods of market dislocation, the observability of prices and inputs may be reduced for many instruments. This condition could cause an instrument to be reclassified from one level to another.

The Fair Value Measurements and Disclosures Topic of the FASB ASC defines fair value and establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy under the Fair Value Measurements and Disclosures Topic of the FASB ASC are described below:

Level 1 – Inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that the reporting entity has the ability to access at the measurement date.

Level 2 – Valuations based on quoted prices in markets that are not active or for which all significant inputs are observable, either directly or indirectly.

Level 3 – Prices or valuations that require inputs that are both significant to the fair value measurement and unobservable.

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To the extent that valuation is based on models or inputs that are less observable or unobservable in the market, the determination of fair value requires more judgment. Accordingly, the degree of judgment exercised by the Company in determining fair value is greatest for instruments categorized in Level 3. A financial instrument’s level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement.

Valuation Techniques

There have been no changes in the valuation techniques used during the current period.

Securities:

Trading Securities

These equity securities are valued based on market quoted prices. These securities are categorized in Level 1 as they are actively traded and no valuation adjustments have been applied.

U.S. Government Agency Securities

Fair value is estimated using either multi-dimensional spread tables or benchmarks. The inputs used include benchmark yields, reported trades, and broker/dealer quotes. These securities are classified as Level 2.

Agency Mortgage-Backed Securities

Fair value is estimated using either a matrix or benchmarks. The inputs used include benchmark yields, reported trades, broker/dealer quotes, and issuer spreads. These securities are categorized as Level 2.

Agency Collateralized Mortgage Obligations and Small Business Administration Pooled Securities

The valuation model for these securities is volatility-driven and ratings based, and uses multi-dimensional spread tables. The inputs used include benchmark yields, reported trades, new issue data, broker dealer quotes, and collateral performance. If there is at least one significant model assumption or input that is not observable, these securities are categorized as Level 3 within the fair value hierarchy; otherwise, they are classified as Level 2.

State, County, and Municipal Securities

The fair value is estimated using a valuation matrix with inputs including bond interest rate tables, recent transaction, and yield relationships. These securities are categorized as Level 2.

Single and Pooled Issuer Trust Preferred Securities

The fair value of trust preferred securities, including pooled and single issuer preferred securities, is estimated using external pricing models, discounted cash flow methodologies or similar techniques. The inputs used in these valuations include benchmark yields, reported trades, new issue data, broker dealer quotes, and collateral performance. If there is at least one significant model assumption or input that is not observable, these securities are classified as Level 3 within the fair value hierarchy; otherwise, they are classified as Level 2.

Equity Securities

These equity securities are valued based on market quoted prices. These securities are classified as Level 1 as they are actively traded and no valuation adjustments have been applied.

Loans Held for Sale

The Company has elected the fair value option to account for originated closed loans intended for sale. The fair value is measured on an individual loan basis using quoted market prices and when not available, comparable market value or discounted cash flow analysis may be utilized. These assets are typically classified as Level 2.

Derivative Instruments

Derivatives

The valuation of these instruments is determined using widely accepted valuation techniques including discounted cash flow analysis on the expected cash flows of each derivative. This analysis reflects the contractual terms of the derivatives, including the period to maturity, and uses observable market-based inputs, including interest rate curves and implied volatilities. The Company incorporates credit valuation adjustments to appropriately reflect nonperformance risk in the fair value measurements. In adjusting the fair value of its derivative contracts for the effect of nonperformance risk, the Company has considered the impact of netting and any applicable credit enhancements, such as collateral postings. Additionally, in conjunction with fair value measurement guidance, the Company has made an accounting policy election to measure the credit risk of its derivative financial

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instruments that are subject to master netting agreements on a net basis by counterparty portfolio. Although the Company has determined that the majority of the inputs used to value its interest rate derivatives fall within Level 2 of the fair value hierarchy, the credit valuation adjustments associated with its derivatives utilize Level 3 inputs, such as estimates of current credit spreads to evaluate the likelihood of default by the Company and its counterparties. However, as of September 30, 2016 and December 31, 2015, the Company has assessed the significance of the impact of the credit valuation adjustments on the overall valuation of its derivative positions and has determined that the credit valuation adjustments are not significant to the overall valuation of its derivatives. As a result, the Company has determined that its derivative valuations in their entirety are classified as Level 2.

Mortgage Derivatives

The fair value of mortgage derivatives is determined based on current market prices for similar assets in the secondary market and, therefore, classified as Level 2 within the fair value hierarchy.

Impaired Loans

Collateral dependent loans that are deemed to be impaired are valued based upon the lower of cost or fair value of the underlying collateral less costs to sell. The inputs used in the appraisals of the collateral are not always observable, and therefore the loans may be classified as Level 3 within the fair value hierarchy; otherwise, they are classified as Level 2.

Other Real Estate Owned and Other Foreclosed Assets

The fair values are generally estimated based upon recent appraisal values of the property less costs to sell the property, as Other Real Estate Owned ("OREO") and Other Foreclosed Assets are valued at the lower of cost or fair value of the property, less estimated costs to sell. Certain inputs used in appraisals are not always observable, and therefore OREO and Other Foreclosed Assets may be classified as Level 3 within the fair value hierarchy.

Goodwill and Other Intangible Assets

Goodwill and other intangible assets are subject to impairment testing. The Company conducts an annual impairment test of goodwill in the third quarter of each year, or more frequently if necessary, and other intangible assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of the assets may not be recoverable. To estimate the fair value of goodwill and, if necessary, other intangible assets, the Company utilizes both a comparable analysis of relevant price multiples in recent market transactions and discounted cash flow analysis. Both valuation models require a significant degree of management judgment. In the event the fair value as determined by the valuation model is less than the carrying value, the intangibles may be impaired. If the impairment testing resulted in impairment, the Company would classify the impaired goodwill and other intangible assets subjected to nonrecurring fair value adjustments as Level 3.

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Assets and liabilities measured at fair value at the periods indicated were as follows:

	Balance	Fair Value Measurements at Reporting Date Using Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
	September 30, 2016 (Dollars in thousands)			
Recurring fair value measurements				
Assets				
Trading securities	$809	$809	$—	$ —
Securities available for sale				
U.S. Government agency securities	25,306	—	25,306	$ —
Agency mortgage-backed securities	185,573	—	185,573	—
Agency collateralized mortgage obligations	108,596	—	108,596	—
State, county, and municipal securities	4,360	—	4,360	—
Single issuer trust preferred securities issued by banks and insurers	2,297	—	2,297	—
Pooled trust preferred securities issued by banks and insurers	1,538	—	—	1,538
Small business administration pooled securities	39,880	—	39,880	—
Equity securities	19,458	19,458	—	—
Loans held for sale	13,334	—	13,334	—
Derivative instruments	42,556	—	42,556	—
Liabilities				
Derivative instruments	43,840	—	43,840	—
Total recurring fair value measurements	$399,867	$20,267	$ 378,062	$ 1,538
Nonrecurring fair value measurements				
Assets				
Collateral dependent impaired loans	$3,056	$—	$—	$ 3,056
Other real estate owned and other foreclosed assets	1,798	—	—	1,798
Total nonrecurring fair value measurements	$4,854	$—	$—	$ 4,854

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	Balance	Fair Value Measurements at Reporting Date Using Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
	December 31, 2015 (Dollars in thousands)			
Recurring fair value measurements				
Assets				
Trading securities	$356	$356	$—	$ —
Securities available for sale				
U.S. Government agency securities	$30,215	$—	$ 30,215	$ —
Agency mortgage-backed securities	210,937	—	210,937	—
Agency collateralized mortgage obligations	63,584	—	63,584	—
State, county, and municipal securities	4,659	—	4,659	—
Single issuer trust preferred securities issued by banks and insurers	2,792	—	2,792	—
Pooled trust preferred securities issued by banks and insurers	1,572	—	—	1,572
Small business administration pooled securities	40,449	—	40,449	—
Equity securities	13,041	13,041	—	—
Loans held for sale	5,990	—	5,990	—
Derivative instruments	23,305	—	23,305	—
Liabilities				
Derivative instruments	26,313	—	26,313	—
Total recurring fair value measurements	$370,587	$13,397	$ 355,618	$ 1,572
Nonrecurring fair value measurements:				
Assets				
Collateral dependent impaired loans	$4,598	$—	$—	$ 4,598
Other real estate owned and other foreclosed assets	2,159	—	—	2,159
Total nonrecurring fair value measurements	$6,757	$—	$—	$ 6,757

The table below presents a reconciliation for all assets and liabilities measured at fair value on a recurring basis using significant unobservable inputs (Level 3), which were valued using pricing models and discounted cash flow methodologies, as of the dates indicated:

	Three Months Ended September 30	
	2016	2015
	(Dollars in thousands)	
Pooled Trust Preferred Securities		
Beginning balance	$1,506	$1,595
Gains and (losses) (realized/unrealized)		
Included in other comprehensive income	41	12

Settlements	(9)	(21)
Ending balance	$1,538	$1,586

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	Nine Months Ended September 30	
	2016	2015
	(Dollars in thousands)	
Pooled Trust Preferred Securities		
Beginning balance	$1,572	$6,321
Gains and (losses) (realized/unrealized)		
Included in other comprehensive income	(17)	20
Sales	—	(4,679)
Settlements	(17)	(76)
Ending balance	$1,538	$1,586

It is the Company's policy to recognize the transfers between levels of the fair value hierarchy as of the end of the reporting period. There were no transfers between the levels of the fair value hierarchy for any assets or liabilities measured at fair value on a recurring basis during the nine month periods ended September 30, 2016 or 2015.

The following table sets forth certain unobservable inputs regarding the Company's investment in securities that are classified as Level 3 for the periods indicated:

	September 30 2016	December 31 2015		September 30 2016	December 31 2015	September 30 2016	December 31 2015
Valuation Technique	Fair Value		Unobservable Inputs	Range		Weighted Average	
	(Dollars in thousands)						
Discounted cash flow methodology							
Pooled trust preferred securities	$1,538	$ 1,572	Cumulative prepayment	0% - 63%	0% - 64%	2.6%	2.7%
			Cumulative default	5% - 100%	5% - 100%	12.9%	15.1%
			Loss given default	85% - 100%	85% - 100%	94.2%	94.2%
			Cure given default	0% - 75%	0% - 75%	60.9%	62.3%
Appraisals of collateral (1)							
Impaired loans	$3,056	$ 4,598					
Other real estate owned and foreclosed assets	$1,798	$ 2,159					

(1) Fair value is generally determined through independent appraisals of the underlying collateral, which generally include various Level 3 inputs which are not identifiable. Appraisals may be adjusted by management for qualitative factors such as economic factors and estimated liquidation expenses. The range of these possible adjustments may vary.

For the fair value measurements in the table above, which are classified as Level 3 within the fair value hierarchy, the Company's Treasury and Finance groups determine the valuation policies and procedures. For the pricing of the securities, the Company uses third-party pricing information, without adjustment. Depending on the type of the security, management employs various techniques to analyze the pricing it receives from third parties, such as analyzing changes in market yields and in certain instances reviewing the underlying collateral of the security. Management reviews changes in fair value from period to period and performs testing to ensure that prices received from the third parties are consistent with their expectation of the market. For the securities whose market is deemed to be inactive and which are categorized as Level 3, the fair value models are calibrated and significant inputs are back tested on a quarterly basis, to the extent possible. This testing is done by the third party service provider, who performs this testing by comparing anticipated inputs to actual results. Significant changes in fair value from period to period are closely scrutinized to ensure fair value models are not flawed. The driver(s) of the respective change in fair value and the method for forecasting the driver(s) is closely considered by management.

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The significant unobservable inputs used in the fair value measurement of the Company’s pooled trust preferred securities are cumulative prepayment rates, cumulative default rates, loss given default rates and cure given default rates. Significant increases (decreases) in deferrals or defaults, in isolation, would result in a significantly lower (higher) fair value measurement. Alternatively, significant increases (decreases) in cure rates, in isolation, would result in a significantly higher (lower) fair value measurement.

Additionally, the Company has certain assets which are marked to fair value on a nonrecurring basis which are categorized within Level 3. These assets include collateral dependent impaired loans and OREO. The determination of the fair value amount is derived from the use of independent third party appraisals and evaluations, prepared by firms from a predetermined list of qualified and approved appraisers or evaluators. Upon receipt of an appraisal or evaluation, the Company's Commercial Real Estate Appraisal Department will review the report for compliance with regulatory and Company standards, as well as reasonableness and acceptance of the value conclusions. Any issues or concerns regarding compliance or value conclusions will be addressed with the engaged firm and the report may be adjusted or revised. If a disagreement cannot be resolved, the Commercial Real Estate Appraisal Department will either address the key issues and modify the report for acceptance or reject the report and re-order a new report. Ultimately, the Company’s Commercial Real Estate Appraisal Department will confirm the collateral value as part of its review process.

The estimated fair values and related carrying amounts for assets and liabilities for which fair value is only disclosed are shown below as of the periods indicated:

			Fair Value Measurements at Reporting Date Using		
	Carrying Value	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
	September 30, 2016 (Dollars in thousands)				
Financial assets					
Securities held to maturity(a)					
U.S. Treasury securities	$1,008	$1,089	$ —	$ 1,089	$ —
Agency mortgage-backed securities	148,822	155,131	—	155,131	—
Agency collateralized mortgage obligations	246,744	250,260	—	250,260	—
Single issuer trust preferred securities issued by banks	1,500	1,547	—	1,547	—
Small business administration pooled securities	32,689	33,807	—	33,807	—
Loans, net of allowance for loan losses(b)	5,684,872	5,622,922	—	—	5,622,922
Financial liabilities					
Time certificates of deposits(c)	$629,071	$631,043	$ —	$ 631,043	$ —
Federal Home Loan Bank borrowings(c)	50,826	51,172	—	51,172	—
Customer repurchase agreements and other short-term borrowings(c)	140,914	140,914	—	—	140,914
Junior subordinated debentures(d)	73,157	75,993	—	75,993	—
Subordinated debentures(c)	34,624	35,222	—	—	35,222

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	Carrying Value	Fair Value	Fair Value Measurements at Reporting Date Using: Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
	December 31, 2015 (Dollars in thousands)				
Financial assets					
Securities held to maturity(a)					
U.S. Treasury securities	$1,009	$1,064	$ —	$ 1,064	$ —
Agency mortgage-backed securities	167,134	170,375	—	170,375	—
Agency collateralized mortgage obligations	267,348	264,891	—	264,891	—
State, county, and municipal securities	225	227	—	227	—
Single issuer trust preferred securities issued by banks	1,500	1,522	—	1,522	—
Small business administration pooled securities	35,291	35,664	—	35,664	—
Corporate debt securities	5,000	5,006	—	5,006	—
Loans, net of allowance for loan losses(b)	5,487,298	5,417,425	—	—	5,417,425
Financial liabilities					
Time certificates of deposits(c)	$684,830	$684,370	$ —	$ 684,370	$ —
Federal Home Loan Bank borrowings(c)	102,080	102,396	—	102,396	—
Customer repurchase agreements and other short-term borrowings(c)	133,958	133,958	—	—	133,958
Junior subordinated debentures(d)	73,306	73,871	—	73,871	—
Subordinated debentures(c)	34,589	34,370	—	—	34,370

(a) The fair values presented are based on quoted market prices, where available. If quoted market prices are not available, fair values are based on quoted market prices of comparable instruments and/or discounted cash flow analyses.

(b) Fair value is estimated by discounting the future cash flows using the current rates at which similar loans would be made to borrowers with similar credit ratings and for the same remaining maturities or cash flows.

(c) Fair value was determined by discounting anticipated future cash payments using rates currently available for instruments with similar remaining maturities.

(d) Fair value was determined based upon market prices of securities with similar terms and maturities.

This summary excludes financial assets and liabilities for which the carrying value approximates fair value. For financial assets, these include cash and due from banks, federal funds sold, short-term investments, FHLB stock, and cash surrender value of life insurance policies. For financial liabilities, these include demand, savings, money market deposits, and federal funds purchased. These instruments would all be considered to be classified as Level 1 within the fair value hierarchy. Also excluded from the summary are financial instruments measured at fair value on a recurring and nonrecurring basis, as previously described.

The Company considers its financial instruments' current use to be the highest and best use of the instruments.

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NOTE 11 - COMPREHENSIVE INCOME (LOSS)

The following table presents a reconciliation of the changes in the components of other comprehensive income (loss) for the dates indicated, including the amount of income tax (expense) benefit allocated to each component of other comprehensive income (loss):

	Three Months Ended September 30, 2016			Nine Months Ended September 30, 2016		
	Pre Tax Amount	Tax (Expense) Benefit	After Tax Amount	Pre Tax Amount	Tax (Expense) Benefit	After Tax Amount
	(Dollars in thousands)					
Change in fair value of securities available for sale	$(1,315)	$ 499	$(816)	$8,351	$ (3,248)	$5,103
Less: net security losses reclassified into other noninterest income	—	—	—	(27)	11	(16)
Net change in fair value of securities available for sale	(1,315)	499	(816)	8,378	(3,259)	5,119
Change in fair value of cash flow hedges	486	(196)	290	(852)	352	(500)
Less: net cash flow hedge gains reclassified into interest on borrowings expense (1)	(648)	264	(384)	(1,949)	796	(1,153)
Net change in fair value of cash flow hedges	1,134	(460)	674	1,097	(444)	653
Net unamortized loss related to defined benefit pension and other postretirement adjustments arising during the period	(28)	11	(17)	(84)	33	(51)
Amortization of net actuarial losses	61	(25)	36	183	(75)	108
Amortization of net prior service costs	69	(29)	40	207	(84)	123
Net change in other comprehensive income for defined benefit postretirement plans (2)	102	(43)	59	306	(126)	180
Total other comprehensive income (loss)	$(79)	$ (4)	$(83)	$9,781	$ (3,829)	$5,952

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	Three Months Ended September 30, 2015			Nine Months Ended September 30, 2015		
	Pre Tax Amount	Tax (Expense) Benefit	After Tax Amount	Pre Tax Amount	Tax (Expense) Benefit	After Tax Amount
	(Dollars in thousands)					
Change in fair value of securities available for sale	$1,966	$ (755)	$1,211	$597	$ (239)	$358
Less: net security losses reclassified into other noninterest income	—	—	—	(315)	129	(186)
Net change in fair value of securities available for sale	1,966	(755)	1,211	912	(368)	544
Change in fair value of cash flow hedges	(493)	201	(292)	(1,096)	429	(667)
Less: net cash flow hedge losses reclassified into interest on borrowings expense (1)	715	(291)	424	2,130	(867)	1,263
Net change in fair value of cash flow hedges	222	(90)	132	1,034	(438)	596
Net unamortized gain related to defined benefit pension and other postretirement adjustments arising during the period	50	(21)	29	137	(71)	66
Amortization of net actuarial losses	61	(25)	36	182	(74)	108
Amortization of net prior service costs	75	(30)	45	227	(92)	135
Net change in other comprehensive income for defined benefit postretirement plans (2)	186	(76)	110	546	(237)	309
Total other comprehensive income	$2,374	$ (921)	$1,453	$2,492	$ (1,043)	$1,449

(1) Includes the amortization of the remaining balance of a realized but unrecognized gain, net of tax, from the termination of interest rate swaps in June 2009. The original gain of $1.4 million, net of tax, is being recognized in earnings through December 2018, the original maturity date of the swap. The balance of this gain has amortized to $317,000 and $463,000 at September 30, 2016 and 2015, respectively.

(2) The amortization of prior service costs is included in the computation of net periodic pension cost as disclosed in the Employee Benefit Plans footnote in the Company's Annual Report on Form 10-K for the year ended December 31, 2015, filed with the Securities and Exchange Commission.

Information on the Company’s accumulated other comprehensive income (loss), net of tax, is comprised of the following components as of the periods indicated:

	Unrealized Gain on Securities	Unrealized Loss on Cash Flow Hedge	Deferred Gain on Hedge Transactions	Defined Benefit Postretirement Plans	Accumulated Other Comprehensive Income (Loss)
	(Dollars in thousands)				
	2016				
Beginning balance: January 1, 2016	$1,306	$ (1,955)	$ 427	$ (2,230)	$ (2,452)
Net change in other comprehensive income (loss)	5,119	763	(110)	180	5,952
Ending balance: September 30, 2016	$6,425	$ (1,192)	$ 317	$ (2,050)	$ 3,500
	2015				
Beginning balance: January 1, 2015	$3,389	$ (3,298)	$ 571	$ (2,794)	$ (2,132)
Net change in other comprehensive income (loss)	544	704	(108)	309	1,449
Ending balance: September 30, 2015	$3,933	$ (2,594)	$ 463	$ (2,485)	$ (683)

NOTE 12 - COMMITMENTS AND CONTINGENCIES

Financial Instruments with Off-Balance Sheet Risk

In the normal course of business, the Company enters into various transactions to meet the financing needs of its customers, which, in accordance with GAAP, are not included in its consolidated balance sheets. These transactions include commitments

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to extend credit and standby letters of credit, which involve, to varying degrees, elements of credit risk and interest rate risk in excess of the amounts recognized in the consolidated balance sheets. The Company minimizes its exposure to loss under these commitments by subjecting them to credit approval and monitoring procedures.

The Company enters into contractual commitments to extend credit, normally with fixed expiration dates or termination clauses, at specified rates and for specific purposes. Substantially all of these commitments to extend credit are contingent upon customers maintaining specific credit standards at the time of loan funding.

Standby letters of credit are written conditional commitments issued to guarantee the performance of a customer to a third party. In the event the customer does not perform in accordance with the terms of the agreement with the third party, the Company would be required to fund the commitment. The maximum potential amount of future payments the Company could be required to make is represented by the contractual amount of the commitment. If the commitment were funded, the Company would be entitled to seek recovery from the customer. The Company’s policies generally require that standby letter of credit arrangements contain security and debt covenants similar to those contained in loan agreements.

The fees collected in connection with the issuance of standby letters of credit are representative of the fair value of its obligation undertaken in issuing the guarantee. In accordance with applicable accounting standards related to guarantees, fees collected in connection with the issuance of standby letters of credit are deferred. The fees are then recognized in income proportionately over the life of the standby letter of credit agreement. The deferred standby letter of credit fees represent the fair value of the Company's potential obligations under the standby letter of credit guarantees.

The following table summarizes the above financial instruments at the dates indicated:

	September 30, 2016	December 31, 2015
	(Dollars in thousands)	
Commitments to extend credit	$2,189,953	$ 2,091,170
Standby letters of credit	17,798	17,962
Deferred standby letter of credit fees	112	72

Lease Commitments

The Company leases office space, space for ATM locations, and certain branch locations under noncancelable operating leases.

Rent expense incurred under operating leases was approximately $2.1 million for both the three months ended September 30, 2016 and 2015, respectively, and $6.4 million and $6.1 million for the nine months ending, September 30, 2016 and 2015, respectively. Renewal options ranging from 1-10 years exist for several of these leases.

There has been no significant change in the future minimum lease payments payable by the Company since December 31, 2015. See the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2015 for information regarding our leases and other commitments.

Other Contingencies

At September 30, 2016, Rockland Trust was involved in pending lawsuits that arose in the ordinary course of business. Management has reviewed these pending lawsuits with legal counsel and has taken into consideration the view of counsel as to their outcome. In the opinion of management, the final disposition of pending lawsuits is not expected to have a material adverse effect on the Company’s financial position or results of operations.

The Bank is required to maintain certain reserve requirements of vault cash and/or deposits with the Federal Reserve Bank of Boston. There was no reserve requirement at September 30, 2016 and $21.7 million at December 31, 2015.

NOTE 13 - LOW INCOME HOUSING PROJECT INVESTMENTS

The Company has invested in low income housing projects that generate Low Income Housing Tax Credits (“LIHTC”) which provide the Company with tax credits and operating loss tax benefits over a period of approximately 15 years. None of the original investment is expected to be repaid. The investment in LIHTC projects is being accounted for using the proportional amortization method, under which the Company amortizes the initial cost of the investment in proportion to the amount of the tax credits and other tax benefits received and recognizes the net investment benefit in the income statement as a component of income tax expense (benefit).

The following table presents the Company's investments in low income housing projects as of the dates indicated:

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	September 30, 2016	December 31, 2015
	(Dollars in thousands)	
Original investment value	$42,362	$ 42,199
Current recorded investment	35,566	38,151
Unfunded liability obligation	9,297	14,607
Tax credits and benefits (1)	5,311	3,632
Amortization of investments (2)	3,669	2,450
Net income tax benefit (3)	1,642	1,182

(1) This amount reflects anticipated tax credits and tax benefits for the full year ended December 31, 2016.
(2) The amortization amount reduces the tax credits and benefits anticipated for the full year ended December 31, 2016.
(3) This amount represents the net tax benefit expected to be realized for the full year ended December 31, 2016 in determining the Company's effective tax rate.

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NOTE 14 - SUBSEQUENT EVENT

On October 20, 2016, the Company announced the signing of a definitive agreement under which the Company will acquire Island Bancorp, Inc. ("Island Bancorp") and Rockland Trust Company will acquire The Edgartown National Bank.

Under the merger agreement each share of Island Bancorp stock will be exchanged for either 9.525 shares of the Company's common stock or $500 in cash, subject to customary pro-ration procedures which will result in an aggregate stock/cash consideration mix of 80% stock/20% cash. The transaction is intended to qualify as a tax-free reorganization for federal income tax purposes and to provide a tax-free exchange for Island Bancorp shareholders to the extent they receive Independent common stock as consideration.

Independent anticipates issuing approximately 369,311 shares of its common stock in the merger. Based upon the Company's $53.25 per share closing price on October 19, 2016 the transaction is valued at approximately $24.5 million.

The boards of directors of each company have unanimously approved the transaction. The transaction is subject to certain conditions, including the receipt of required regulatory approvals, approval by Island Bancorp shareholders, and other standard conditions. The Company shareholders do not need to approve the merger. Island Bancorp directors who currently own, in the aggregate, about 33% of Island Bancorp’s outstanding shares have signed voting agreements pursuant to which they have agreed to vote their shares in favor of the merger.

Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations

The following discussion should be read in conjunction with the consolidated financial statements, notes and tables included in the Company’s Annual Report on Form 10-K for the fiscal year ended December 31, 2015, filed with the Securities and Exchange Commission.

Cautionary Statement Regarding Forward-Looking Statements

This Quarterly Report on Form 10-Q, both in the Management's Discussion and Analysis of Financial Condition and Results of Operations and elsewhere, contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Such statements are not historical facts and include expressions about management’s confidence and strategies and management’s expectations about new and existing programs and products, acquisitions, relationships, opportunities, taxation, technology, market conditions and economic expectations. These statements may be identified by forward-looking terminology such as “should,” “expect,” “believe,” “view,” “opportunity,” “allow,” “continues,” “reflects,” “typically,” “usually,” “anticipate,” or similar statements or variations of such terms. Such forward-looking statements involve certain risks and uncertainties and our actual results may differ materially from such forward-looking statements. Factors that may cause actual results to differ materially from those contemplated by such forward-looking statements, in addition to those risk factors listed under the “Risk Factors” section of the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2015, include, but are not limited to:

- a weakening in the United States economy in general and the regional and local economies within the New England region and the Company’s market area;
- adverse changes in the local real estate market;
- adverse changes in asset quality including an unanticipated credit deterioration in our loan portfolio;
- acquisitions may not produce results at levels or within time frames originally anticipated and may result in unforeseen integration issues or impairment of goodwill and/or other intangibles;
- changes in trade, monetary and fiscal policies and laws, including interest rate policies of the Board of Governors of the Federal Reserve System;
- higher than expected tax expense, resulting from failure to comply with general tax laws, changes in tax laws, or failure to comply with requirements of the federal New Markets Tax Credit program;
- unexpected changes in market interest rates for interest earning assets and/or interest bearing liabilities;

- unexpected increased competition in the Company's market area;
- unanticipated loan delinquencies, loss of collateral, decreased service revenues, and other potential negative effects on our business caused by severe weather or other external events;
- a deterioration in the conditions of the securities markets;
- a deterioration of the credit rating for U.S. long-term sovereign debt;
- our inability to adapt to changes in information technology;
- electronic fraudulent activity within the financial services industry, especially in the commercial banking sector;
- adverse changes in consumer spending and savings habits;

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- failure to consummate or delay in consummating the acquisition of Island Bancorp, which is subject to certain standard conditions, including approval of the transaction by Island Bancorp shareholders and receipt of required regulatory approvals;
- the inability to realize expected revenue synergies from merger transactions in the amounts or in the timeframe anticipated;
- inability to retain customers and employees, including those of previous mergers;
- the effect of laws and regulations regarding the financial services industry including, but not limited to, the Dodd-Frank Wall Street Reform and Consumer Protection Act;
- changes in laws and regulations (including laws and regulations concerning taxes, banking, securities and insurance) generally applicable to the Company's business;
- changes in accounting policies, practices and standards, as may be adopted by the regulatory agencies as well as the Public Company Accounting Oversight Board, the Financial Accounting Standards Board, and other accounting standard setters;
- cyber security attacks or intrusions that could adversely impact our businesses; and
- other unexpected material adverse changes in our operations or earnings.

Except as required by law, the Company disclaims any intent or obligation to update publicly any such forward-looking statements, whether in response to new information, future events or otherwise. Any public statements or disclosures by the Company following this Quarterly Report on Form 10-Q which modify or impact any of the forward-looking statements contained in this Quarterly Report on Form 10-Q will be deemed to modify or supersede such statements in this Quarterly Report on Form 10-Q.

Selected Quarterly Financial Data

The selected consolidated financial and other data of the Company set forth below does not purport to be complete and should be read in conjunction with, and is qualified in its entirety by, the more detailed information, including the Consolidated Financial Statements and related notes, appearing elsewhere in this Quarterly Report on Form 10-Q.

	Three Months Ended				
	September 30, 2016	June 30, 2016	March 31, 2016	December 31, 2015	September 30, 2015
	(Dollars in thousands, except per share data)				
Financial condition data					
Securities available for sale	$387,008	$389,824	$378,227	$ 367,249	$ 365,792
Securities held to maturity	430,763	438,656	457,641	477,507	448,139
Loans	5,746,133	5,674,253	5,589,231	5,547,721	5,498,121
Allowance for loan losses	(58,205)	(57,727)	(56,432)	(55,825)	(55,205)
Goodwill and other intangible assets	210,834	211,526	212,218	212,909	213,612
Total assets	7,502,009	7,418,866	7,189,268	7,209,469	7,134,903
Total deposits	6,269,460	6,197,892	5,995,247	5,990,703	5,914,863
Total borrowings	299,521	298,368	293,265	343,933	350,516
Stockholders' equity	818,242	803,897	788,147	771,463	759,203
Nonperforming loans	24,793	25,628	25,499	27,690	29,567
Nonperforming assets	26,591	27,473	27,219	29,849	32,099
Income statement					
Interest income	$62,308	$61,160	$59,741	$ 59,870	$ 60,228
Interest expense	4,640	4,627	4,850	4,985	5,183
Net interest income	57,668	56,533	54,891	54,885	55,045
Provision for loan losses	950	600	525	500	800
Noninterest income	20,416	21,095	19,155	19,824	19,247

Noninterest expenses	46,857	47,146	46,482	46,486	47,031
Net income	20,484	20,374	18,611	19,455	18,594
Per share data	—				

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Net income—basic	$0.78	$0.77	$0.71	$0.74	$0.71
Net income—diluted	0.78	0.77	0.71	0.74	0.71
Cash dividends declared	0.29	0.29	0.29	0.26	0.26
Book value per share	31.09	30.55	29.97	29.40	28.96
Tangible book value per share (1)	23.08	22.52	21.90	21.29	20.81
Performance ratios	—				
Return on average assets	1.09 %	1.13 %	1.04 %	1.07 %	1.03 %
Return on average common equity	9.98 %	10.24 %	9.52 %	10.03 %	9.75 %
Net interest margin (on a fully tax equivalent basis)	3.40 %	3.47 %	3.39 %	3.34 %	3.39 %
Equity to assets	10.91 %	10.84 %	10.96 %	10.70 %	10.64 %
Dividend payout ratio	37.25 %	37.43 %	36.66 %	35.03 %	36.58 %