FIDELITY D & D BANCORP INC
Form 10-Q
August 08, 2017
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE

SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended June 30, 2017

OR

[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE

SECURITIES EXCHANGE ACT OF 1934

For the transition period from ______________to______________________

Commission file number: 333-90273

FIDELITY D & D BANCORP, INC.

STATE OF INCORPORATION:	IRS EMPLOYER IDENTIFICATION NO:
PENNSYLVANIA	23-3017653

Address of principal executive offices:

BLAKELY & DRINKER ST.

DUNMORE, PENNSYLVANIA 18512

TELEPHONE:

570-342-8281

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 subjected to such filing requirements for the past 90 days. [X] YES [ ] NO

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

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

Large accelerated filer [ ]	Accelerated filer [ ]
Non-accelerated filer [ ]	Smaller reporting company [X]
(Do not check if a smaller reporting company)	Emerging growth company [ ]

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

[ ] YES [X] NO

The number of outstanding shares of Common Stock of Fidelity D & D Bancorp, Inc. on July 31, 2017, the latest practicable date, was 2,470,544 shares.

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PART I – Financial Information

Item 1: Financial Statements

Fidelity D & D Bancorp, Inc. and Subsidiary
Consolidated Balance Sheets
(Unaudited)

(dollars in thousands)	June 30, 2017	December 31, 2016
Assets:		
Cash and due from banks	$ 14,858	$ 12,856
Interest-bearing deposits with financial institutions	19	12,987
Total cash and cash equivalents	14,877	25,843
Available-for-sale securities	153,405	130,037
Federal Home Loan Bank stock	4,028	2,606
Loans and leases, net (allowance for loan losses of $9,406 in 2017; $9,364 in 2016)	626,438	588,130
Loans held-for-sale (fair value $1,904 in 2017, $2,907 in 2016)	1,866	2,854
Foreclosed assets held-for-sale	969	1,306
Bank premises and equipment, net	16,833	17,164
Cash surrender value of bank owned life insurance	19,699	11,435
Accrued interest receivable	2,706	2,246
Goodwill	209	-
Other assets	14,438	11,323
Total assets	$ 855,468	$ 792,944
Liabilities:		
Deposits:		
Interest-bearing	$ 532,526	$ 492,306
Non-interest-bearing	174,909	211,153
Total deposits	707,435	703,459
Accrued interest payable and other liabilities	5,738	4,631
Short-term borrowings	34,455	4,223
Long-term debt	23,704	-
Total liabilities	771,332	712,313
Shareholders' equity:		
Preferred stock authorized 5,000,000 shares with no par value; none issued	-	-
Capital stock, no par value (10,000,000 shares authorized; shares issued and outstanding; 2,470,544 in 2017; and 2,453,805 in 2016)	27,565	27,155
Retained earnings	54,719	52,095
Accumulated other comprehensive income	1,852	1,381
Total shareholders' equity	84,136	80,631
Total liabilities and shareholders' equity	$ 855,468	$ 792,944

See notes to unaudited consolidated financial statements

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Fidelity D & D Bancorp, Inc. and Subsidiary
Consolidated Statements of Income

(Unaudited)	Three months ended		Six months ended	
(dollars in thousands except per share data)	June 30, 2017	June 30, 2016	June 30, 2017	June 30, 2016
Interest income:				
Loans and leases:				
Taxable	$ 6,566	$ 5,796	$ 12,726	$ 11,611
Nontaxable	217	193	427	384
Interest-bearing deposits with financial institutions	4	24	10	46
Investment securities:				
U.S. government agency and corporations	658	366	1,277	736
States and political subdivisions (nontaxable)	367	316	713	633
Other securities	42	20	67	41
Total interest income	7,854	6,715	15,220	13,451
Interest expense:				
Deposits	643	567	1,229	1,147
Securities sold under repurchase agreements	5	4	12	12
Other short-term borrowings and other	80	3	137	13
Long-term debt	59	-	97	-
Total interest expense	787	574	1,475	1,172
Net interest income	7,067	6,141	13,745	12,279
Provision for loan losses	225	275	550	425
Net interest income after provision for loan losses	6,842	5,866	13,195	11,854
Other income:				
Service charges on deposit accounts	549	515	1,092	1,003
Interchange fees	425	381	825	737
Fees from trust fiduciary activities	308	193	503	363
Fees from financial services	119	206	265	310
Service charges on loans	176	293	396	471
Fees and other revenue	229	195	439	392
Earnings on bank-owned life insurance	157	88	264	175
Gain on sale or disposal of:				
Loans	168	220	452	327
Investment securities	-	9	-	9
Total other income	2,131	2,100	4,236	3,787
Other expenses:				
Salaries and employee benefits	3,239	2,893	6,324	5,768
Premises and equipment	912	826	1,897	1,744
Advertising and marketing	345	203	580	458
Professional services	528	399	926	788
FDIC assessment	68	112	133	237

Loan collection	47	81	107	125
Other real estate owned	109	67	146	89
Office supplies and postage	107	123	230	242
Automated transaction processing	184	154	358	281
Data processing and communication	280	271	583	459
PA shares tax	47	164	211	306
Other	185	76	353	260
Total other expenses	6,051	5,369	11,848	10,757
Income before income taxes	2,922	2,597	5,583	4,884
Provision for income taxes	739	669	1,420	1,255
Net income	$ 2,183	$ 1,928	$ 4,163	$ 3,629
Per share data:				
Net income - basic	$ 0.89	$ 0.79	$ 1.69	$ 1.48
Net income - diluted	$ 0.88	$ 0.79	$ 1.68	$ 1.48
Dividends	$ 0.31	$ 0.29	$ 0.62	$ 0.56

See notes to unaudited consolidated financial statements

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Fidelity D & D Bancorp, Inc. and Subsidiary

Consolidated Statements of Comprehensive Income (Unaudited) (dollars in thousands)	Three months ended June 30, 2017	2016	Six months ended June 30, 2017	2016
Net income	$ 2,183	$ 1,928	$ 4,163	$ 3,629
Other comprehensive income, before tax:				
Unrealized holding gain on available-for-sale securities	687	1,209	714	2,293
Reclassification adjustment for net gains realized in income	-	(9)	-	(9)
Net unrealized gain	687	1,200	714	2,284
Tax effect	(234)	(408)	(243)	(777)
Unrealized gain, net of tax	453	792	471	1,507
Other comprehensive income, net of tax	453	792	471	1,507
Total comprehensive income, net of tax	$ 2,636	$ 2,720	$ 4,634	$ 5,136

See notes to unaudited consolidated financial statements

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Fidelity D & D Bancorp, Inc. and Subsidiary
Consolidated Statements of Changes in Shareholders' Equity
For the six months ended June 30, 2017 and 2016
(Unaudited)

(dollars in thousands)	Capital stock Shares	Amount	Retained earnings	Accumulated other comprehensive income	Total
Balance, December 31, 2015	2,443,405	$ 26,700	$ 47,463	$ 2,188	$ 76,351
Net income			3,629		3,629
Other comprehensive income				1,507	1,507
Issuance of common stock through Employee Stock Purchase Plan	3,695	111			111
Issuance of common stock from vested restricted share grants through stock compensation plans	6,205				
Issuance of common stock through exercise of stock options	500	14			14
Stock-based compensation expense		167			167
Cash dividends declared			(1,383)		(1,383)
Balance, June 30, 2016	2,453,805	$ 26,992	$ 49,709	$ 3,695	$ 80,396
Balance, December 31, 2016	2,453,805	$ 27,155	$ 52,095	$ 1,381	$ 80,631
Net income			4,163		4,163
Other comprehensive income				471	471
Issuance of common stock through Employee Stock Purchase Plan	4,085	126			126
Issuance of common stock through Dividend Reinvestment Plan	2,478	90			90
Issuance of common stock from vested restricted share grants through stock compensation plans	9,657				
Issuance of common stock through exercise of stock options	519	15			15
Stock-based compensation expense		179			179
Cash dividends declared			(1,539)		(1,539)
Balance, June 30, 2017	2,470,544	$ 27,565	$ 54,719	$ 1,852	$ 84,136

See notes to unaudited consolidated financial statements

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Fidelity D & D Bancorp, Inc. and Subsidiary
Consolidated Statements of Cash Flows

(Unaudited)	Six months ended June 30,	
(dollars in thousands)	2017	2016
Cash flows from operating activities:		
Net income	$ 4,163	$ 3,629
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation, amortization and accretion	1,528	1,765
Provision for loan losses	550	425
Deferred income tax expense	585	1,110
Stock-based compensation expense	288	252
Excess tax benefit from exercise of stock options	1	-
Proceeds from sale of loans held-for-sale	20,700	18,931
Originations of loans held-for-sale	(17,279)	(17,301)
Earnings from bank-owned life insurance	(264)	(175)
Net gain from sales of loans	(452)	(327)
Net gain from sales of investment securities	-	(9)
Net loss from sale and write-down of foreclosed assets held-for-sale	75	24
Change in:		
Accrued interest receivable	(456)	23
Other assets	(3,542)	(2,466)
Accrued interest payable and other liabilities	938	44
Net cash provided by operating activities	6,835	5,925
Cash flows from investing activities:		
Available-for-sale securities:		
Proceeds from sales	-	2,884
Proceeds from maturities, calls and principal pay-downs	8,285	9,301
Purchases	(31,487)	(15,231)
(Increase) decrease in FHLB stock	(1,423)	980
Net increase in loans and leases	(39,785)	(8,241)
Purchase of life insurance policies	(8,000)	-
Acquisition of bank premises and equipment	(472)	(802)
Net cash acquired in acquisition of bank branch	11,817	-
Proceeds from sale of bank premises and equipment	6	-
Proceeds from sale of foreclosed assets held-for-sale	463	338
Net cash used in investing activities	(60,596)	(10,771)
Cash flows from financing activities:		
Net (decrease) increase in deposits	(9,832)	42,626

Net increase (decrease) in short-term borrowings	30,232	(20,946)
Proceeds from issuance of long-term debt advances	23,704	-
Proceeds from employee stock purchase plan participants	126	111
Exercise of stock options	15	14
Dividends paid, net of dividends reinvested	(1,450)	(1,383)
Net cash provided by financing activities	42,795	20,422
Net (decrease) increase in cash and cash equivalents	(10,966)	15,576
Cash and cash equivalents, beginning	25,843	12,277
Cash and cash equivalents, ending	$ 14,877	$ 27,853

See notes to unaudited consolidated financial statements

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Fidelity D & D Bancorp, Inc. and Subsidiary
Consolidated Statements of Cash Flows (continued)

(Unaudited)	Six months ended June 30,	
(dollars in thousands)	2017	2016
Supplemental Disclosures of Cash Flow Information		
Cash payments for:		
Interest	$ 1,319	$ 1,134
Income tax	900	200
Supplemental Disclosures of Non-cash Investing Activities:		
Net change in unrealized gains on available-for-sale securities	714	2,284
Transfers from loans to foreclosed assets held-for-sale	202	843
Transfers from loans to loans held-for-sale	2,318	1,658

Acquisition of West Scranton Branch from Wayne Bank	March 17, 2017
Non-cash assets acquired:	
Loans	$ 1,574
Bank premises and equipment	264
Goodwill	209
Accrued interest receivable and other assets	4
Total non-cash assets acquired	$ 2,051
Liabilities assumed:	
Deposits	$ 13,809
Accrued interest payable and other liabilities	59
Total liabilities assumed	$ 13,868

See notes to unaudited consolidated financial statements

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FIDELITY D & D BANCORP, INC.

Notes to Consolidated Financial Statements

(Unaudited)

1. Nature of operations and critical accounting policies

Nature of operations

Fidelity Deposit and Discount Bank (the Bank) is a commercial bank chartered under the law of the Commonwealth of Pennsylvania and a wholly-owned subsidiary of Fidelity D & D Bancorp, Inc. (collectively, the Company). Having commenced operations in 1903, the Bank is committed to provide superior customer service, while offering a full range of banking products and financial and trust services to both our consumer and commercial customers from our main office located in Dunmore and other branches located throughout Lackawanna and Luzerne Counties.

Principles of consolidation

The accompanying unaudited consolidated financial statements of the Company and the Bank 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 this Form 10-Q and Rule 8-03 of Regulation S-X. Accordingly, they do not include all of the information and footnote disclosures required by GAAP for complete financial statements. In the opinion of management, all normal recurring adjustments necessary for a fair presentation of the financial condition and results of operations for the periods have been included. All significant inter-company balances and transactions have been eliminated in consolidation.

For additional information and disclosures required under GAAP, refer to the Company’s Annual Report on Form 10-K for the year ended December 31, 2016.

Management is responsible for the fairness, integrity and objectivity of the unaudited financial statements included in this report. Management prepared the unaudited financial statements in accordance with GAAP. In meeting its responsibility for the financial statements, management depends on the Company's accounting systems and related internal controls. These systems and controls are designed to provide reasonable but not absolute assurance that the financial records accurately reflect the transactions of the Company, the Company’s assets are safeguarded and that the financial statements present fairly the financial condition and results of operations of the Company.

In the opinion of management, the consolidated balance sheets as of June 30, 2017 and December 31, 2016 and the related consolidated statements of income and consolidated statements of comprehensive income for the three and six months ended June 30, 2017 and 2016, and consolidated statements of changes in shareholders’ equity and consolidated statements of cash flows for the six months ended June 30, 2017 and 2016 present fairly the financial condition and results of operations of the Company. All material adjustments required for a fair presentation have been made. These adjustments are of a normal recurring nature. Certain reclassifications have been made to the 2016 financial statements to conform to the 2017 presentation.

In preparing these consolidated financial statements, the Company evaluated the events and transactions that occurred after June 30, 2017 through the date these consolidated financial statements were issued.

This Quarterly Report on Form 10-Q should be read in conjunction with the Company's audited financial statements for the year ended December 31, 2016, and the notes included therein, included within the Company's Annual Report filed on Form 10-K.

Critical accounting policies

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

A material estimate that is particularly susceptible to significant change relates to the determination of the allowance for loan losses. Management believes that the allowance for loan losses at June 30, 2017 is adequate and reasonable. Given the subjective nature of identifying and estimating loan losses, it is likely that well-informed individuals could make different assumptions and could, therefore, calculate a materially different allowance amount. While management uses available information to recognize losses on loans, changes in economic conditions may necessitate revisions in the future. In addition, various regulatory agencies, as an integral part of their examination process, periodically review the Company's allowance for loan losses. Such agencies may require the Company to recognize adjustments to the allowance based on their judgment of information available to them at the time of their examination.

Another material estimate is the calculation of fair values of the Company's investment securities. Fair values of investment securities are determined by pricing provided by a third-party vendor, who is a provider of financial market data, analytics and related services to financial institutions. Based on experience, management is aware that estimated fair values of investment securities tend to vary among valuation services. Accordingly, when selling investment securities, price quotes may be obtained from more than one source. All of the Company's investment securities are classified as available-for-sale (AFS). AFS securities are carried at fair value on the

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consolidated balance sheets, with unrealized gains and losses, net of income tax, reported separately within shareholders' equity as a component of accumulated other comprehensive income (AOCI).

The fair value of residential mortgage loans, classified as held-for-sale (HFS), is obtained from the Federal National Mortgage Association (FNMA) or the Federal Home Loan Bank (FHLB). Generally, the market to which the Company sells residential mortgages it originates for sale is restricted and price quotes from other sources are not typically obtained. On occasion, the Company may transfer loans from the loan portfolio to loans HFS. Under these circumstances, pricing may be obtained from other entities and the residential mortgage loans are transferred at the lower of cost or market value and simultaneously sold. For other loans transferred to HFS, pricing may be obtained from other entities or modeled and the other loans are transferred at the lower of cost or market value and then sold. As of June 30, 2017 and December 31, 2016, loans classified as HFS consisted of residential mortgage loans.

Financing of automobiles, provided to customers under lease arrangements of varying terms, are accounted for as direct finance leases. Interest income on automobile direct finance leasing is determined using the interest method to arrive at a level effective yield over the life of the lease.

Foreclosed assets held-for-sale includes other real estate acquired through foreclosure (ORE) and may, from time-to-time, include repossessed assets such as automobiles. ORE is carried at the lower of cost (principal balance at date of foreclosure) or fair value less estimated cost to sell. Any write-downs at the date of foreclosure are charged to the allowance for loan losses. Expenses incurred to maintain ORE properties, subsequent write downs to the asset's fair value, any rental income received and gains or losses on disposal are included as components of other real estate owned expense in the consolidated statements of income.

Goodwill is recorded on the consolidated balance sheets as the excess of liabilities assumed over identifiable assets acquired on the acquisition date. Goodwill is recorded at its net carrying value which represents estimated fair value. The goodwill is deductible for tax purposes over a 15 year period.

The Company maintains bank owned life insurance policies (BOLI) for a selected group of employees, namely its officers where the Company is the owner and sole beneficiary of the policies. The earnings from the BOLI are recognized as a component of other income in the consolidated statements of income. The BOLI is an asset that can be liquidated, if necessary, with tax consequences. However, the Company intends to hold these policies and accordingly, the Company has not provided for deferred taxes on the earnings from the increase in the cash surrender value.

The Company holds separate supplemental executive retirement (SERP) agreements for certain officers and an amount is credited to each participant's SERP account monthly while they are actively employed by the bank until retirement. A deferred tax asset is provided for the non-deductible SERP expense. The Company also entered into separate split dollar life insurance arrangements with three executives providing post-retirement benefits and accrues monthly expense for this benefit. Monthly expenses for the SERP and post-retirement split dollar life benefit are recorded as components of salaries and employee benefit expense on the consolidated statements of income.

For purposes of the consolidated statements of cash flows, cash and cash equivalents includes cash on hand, amounts due from banks and interest-bearing deposits with financial institutions. Expenditures for construction in process, a component of other assets in the consolidated balance sheets, are included in acquisition of premises and equipment.

2. New accounting pronouncements

In June 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standard Update (ASU) 2016-13, Financial Instruments – Credit Losses (Topic 326) Measurement of Credit Losses on Financial Instruments. The amendments in this update require financial assets measured at amortized cost basis to be presented at the net amount expected to be collected, through an allowance for credit losses that is deducted from the amortized cost basis. Previously, when credit losses were measured under GAAP, an entity only considered past events and current conditions when measuring the incurred loss. The amendments in this update broaden the information that an entity must consider in developing its expected credit loss estimate for assets measured either collectively or individually. The measurement of expected credit losses is based on relevant information about past events, including historical experience, current conditions, and reasonable and supportable forecasts that affect the collectability of the reported amount. An entity must use judgement in determining the relevant information and estimation methods that are appropriate under the circumstances. The amendments in this update also require that credit losses on available-for-sale debt securities be presented as an allowance for credit losses rather than a writedown. The amendments in this update are effective for fiscal years, including interim periods within those fiscal years, beginning after December 15, 2019 for public companies. Early adoption is permitted beginning after December 15, 2018, including interim periods within those fiscal years. An entity will apply the amendments in this update through a cumulative-effect adjustment to retained earnings as of the beginning of the period of adoption (modified-retrospective approach). Upon adoption, the change in this accounting guidance could result in an increase in the Company's allowance for loan losses and require the Company to record loan losses more rapidly. The Company is currently evaluating the impact of ASU 2016-13 on its consolidated financial statements.

In March 2016, the FASB issued ASU 2016-09, Compensation – Stock Compensation (Topic 718) Improvements to Employee Share-Based Payment Accounting. The areas for simplification in the update involve several aspects of accounting for share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities, and classification on the

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statement of cash flows. The amendments in this update are effective for annual reporting periods, including interim periods within those annual periods, beginning after December 15, 2016. Early adoption is permitted. Amendments should be applied using either a modified retrospective transition method by means of a cumulative-effect adjustment to equity as of the beginning of the period in which the guidance is adopted, retrospectively, prospectively, or using either a prospective transition method or a retrospective transition method. The Company adopted this accounting standard during the first quarter of 2017 and does not expect this amendment to have a material impact on its consolidated financial statements.

In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers, which supersedes nearly all existing revenue recognition guidance under U.S. GAAP. The core principle of ASU 2014-09 is to recognize revenues when promised goods or services are transferred to customers in an amount that reflects the consideration to which an entity expects to be entitled for those goods or services. ASU 2014-09 defines a five step process to achieve this core principle and, in doing so, more judgment and estimates may be required within the revenue recognition process than are required under existing U.S. GAAP: identify the contract(s) with a customer; identify the performance obligations in the contract; determine the transaction price; allocate the transaction price to the performance obligations in the contract; recognize revenue when (or as) the entity satisfies a performance obligation. The standard is effective for annual periods beginning after December 15, 2017, and interim periods therein, using either of the following transition methods: a full retrospective approach reflecting the application of the standard in each prior reporting period with the option to elect certain practical expedients, or a retrospective approach with the cumulative effect of initially adopting ASU 2014-09 recognized at the date of adoption (which includes additional footnote disclosures).

Subsequently, the FASB issued additional guidance to clarify certain implementation issues. Specifically, the FASB issued Principal versus Agent Considerations, Identifying Performance Obligations and Licensing, Narrow-Scope Improvements and Practical Expedients and Technical Corrections and Improvements in March, April, May and December 2016, respectively. These amendments do not change the core principle in Revenue from Contracts with Customers (Topic 606) and the effective date and transition requirements are consistent with those in Topic 606. The Company is in the process of determining the revenue streams that are in the scope of ASU 2014-09 and has not yet determined the method by which it will adopt the standard effective on January 1, 2018. The Company expects that this guidance will change how certain non-interest income is recognized but does not expect the new standard, or any of its amendments, to have a material effect on its consolidated financial statements. The Company does expect the guidance will require some additional footnote disclosures.

In January 2016, the FASB issued ASU 2016-01 related to Financial Instruments - Overall (Subtopic 825-10) Recognition and Measurement of Financial Assets and Financial Liabilities. The update applies to all entities that hold financial assets or owe financial liabilities. The amendments in this update make targeted improvements to U.S. GAAP as follows:

- Require equity investments to be measured at fair value with changes in fair value recognized in net income;
- Simplify the impairment assessment of equity investments without readily determinable fair values by requiring a qualitative assessment to identify impairment;
- Require public business entities to use the exit price notion when measuring fair value of financial instruments for disclosure purposes;
- Require separate presentation of financial assets and financial liabilities by measurement category and form of financial asset;
- Clarify that an entity should evaluate the need for a valuation allowance on a deferred tax asset related to available-for-sale securities.

The amendments are effective for public business entities for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. The Company is evaluating the impact of the adoption of ASU 2016-01 on its consolidated financial statements, but does not expect it to have a significant impact.

In February 2016, the FASB issued ASU 2016-02, Leases (Topic 842) to increase transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet and disclosing key information about leasing arrangements. ASU 2016-02 requires the recognition of a right-of-use asset and related lease liability by lessees for leases classified as operating leases under GAAP. The Company is expected to make an election to exclude leases less than 12 months from the provisions of this ASU. The amendments in this update are effective for the Company for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. Early adoption of the amendments in this update are permitted. A modified retroactive approach must be applied for leases existing at, or entered into after, the beginning of the earliest comparative period. Upon adoption, this change in accounting guidance could have a significant impact on the consolidated balance sheets and could potentially impact debt covenant agreements with our customers. The Company is currently evaluating the amount of the impact of ASU 2016-02 on its consolidated financial statements.

In August 2016, the FASB released ASU 2016-15, Statement of Cash Flows (Topic 230) to clarify the presentation of certain cash receipts and payments on the statement of cash flows. The update addressed eight specific cash flow issues with the objective of reducing the existing diversity in practice. The amendments in this update are effective for public business entities for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years. Early adoption is permitted, including adoption in an interim period. The amendments in this update should be applied using a retrospective transition method to each period presented. The Company is currently evaluating the impact of the adoption of ASU 2016-15 on its consolidated financial statements, but does not expect it to have a significant impact.

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In January 2017, the FASB issued ASU 2017-04, Intangibles-Goodwill and Other (Topic 350) to simplify the test for goodwill impairment. To simplify the subsequent measurement of goodwill, the Board eliminated Step 2 from the goodwill impairment test. Under the amendments in this update, an entity should perform its annual goodwill impairment test by comparing the fair value of a reporting unit with its carrying amount. An entity should recognize an impairment charge for the amount by which the carrying amount exceeds the reporting units fair value; however, the loss recognized should not exceed the total amount of goodwill allocated to that reporting unit. An entity should apply the amendments in his update on a prospective basis. The amendments in this update are effective for the Company for its annual goodwill impairment tests in fiscal years beginning after December 15, 2019. Early adoption is permitted for interim or annual goodwill impairment tests performed on testing dates after January 1, 2017. The Company will early adopt this standard and it will not have an impact on its consolidated financial statements.

In March 2017, the FASB issued ASU 2017-08, Receivables-Nonrefundable Fees and Other Costs (Subtopic 310-20) Premium Amortization on Purchased Callable Debt Securities to amend the amortization period for certain purchased callable debt securities held at a premium. The amendments in this update shorten the amortization period for the premium to the earliest call date. The amendments in this update are effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018. Early adoption is permitted, including adoption in an interim period. An entity should apply the amendments in this update on a modified retrospective basis through a cumulative effect adjustment directly to retained earnings as of the beginning of the period of adoption. The Company has adopted this standard and it will not have an effect on its consolidated financial statements.

3. Accumulated other comprehensive income

The following tables illustrate the changes in accumulated other comprehensive income by component and the details about the components of accumulated other comprehensive income as of and for the periods indicated:

As of and for the six months ended June 30, 2017

(dollars in thousands)	Unrealized gains (losses) on available-for-sale securities	Total
Beginning balance	$ 1,381	$ 1,381
Other comprehensive income before reclassifications, net of tax	471	471
Amounts reclassified from accumulated other comprehensive income, net of tax	-	-
Net current-period other comprehensive income	471	471
Ending balance	$ 1,852	$ 1,852

As of and for the three months ended June 30, 2017

(dollars in thousands)	Unrealized gains (losses) on available-for-sale securities	Total
Beginning balance	$ 1,399	$ 1,399

Other comprehensive income before reclassifications, net of tax	453	453
Amounts reclassified from accumulated other comprehensive income, net of tax	-	-
Net current-period other comprehensive income	453	453
Ending balance	$ 1,852	$ 1,852

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As of and for the six months ended June 30, 2016

(dollars in thousands)	Unrealized gains (losses) on available-for-sale securities	Total
Beginning balance	$ 2,188	$ 2,188
Other comprehensive income before reclassifications, net of tax	1,513	1,513
Amounts reclassified from accumulated other comprehensive income, net of tax	(6)	(6)
Net current-period other comprehensive income	1,507	1,507
Ending balance	$ 3,695	$ 3,695

As of and for the three months ended June 30, 2016

(dollars in thousands)	Unrealized gains (losses) on available-for-sale securities	Total
Beginning balance	$ 2,903	$ 2,903
Other comprehensive income before reclassifications, net of tax	798	798
Amounts reclassified from accumulated other comprehensive income, net of tax	(6)	(6)
Net current-period other comprehensive income	792	792
Ending balance	$ 3,695	$ 3,695

Details about accumulated other comprehensive income components (dollars in thousands)	Amount reclassified from accumulated other comprehensive income				Affected line item in the statement where net income is presented
	Three months ended June 30,		Six months ended June 30,		
	2017	2016	2017	2016	
Unrealized gains on AFS securities	$ -	$ 9	$ -	$ 9	Gain on sale of investment securities
	-	(3)	-	(3)	Provision for income taxes

Total reclassifications for the period	$ -	$ 6	$ -	$ 6	Net income

4. Investment securities

Agency – Government-sponsored enterprise (GSE) and MBS - GSE residential

Agency – GSE and MBS – GSE residential securities consist of short- to long-term notes issued by Federal Home Loan Mortgage Corporation (FHLMC), Federal National Mortgage Association (FNMA), Federal Home Loan Bank (FHLB) and Government National Mortgage Association (GNMA). These securities have interest rates that are fixed and adjustable, have varying short- to long-term maturity dates and have contractual cash flows guaranteed by the U.S. government or agencies of the U.S. government.

Obligations of states and political subdivisions

The municipal securities are bank qualified or bank eligible, general obligation and revenue bonds rated as investment grade by various credit rating agencies and have fixed rates of interest with mid- to long-term maturities. Fair values of these securities are highly driven by interest rates. Management performs ongoing credit quality reviews on these issues.

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The amortized cost and fair value of investment securities at June 30, 2017 and December 31, 2016 are summarized as follows:

(dollars in thousands)	Amortized cost	Gross unrealized gains	Gross unrealized losses	Fair value
June 30, 2017				
Available-for-sale securities:				
Agency - GSE	$ 18,301	$ 30	$ (81)	$ 18,250
Obligations of states and political subdivisions	42,099	2,081	(93)	44,087
MBS - GSE residential	89,903	820	(374)	90,349
Total debt securities	150,303	2,931	(548)	152,686
Equity securities - financial services	294	425	-	719
Total available-for-sale securities	$ 150,597	$ 3,356	$ (548)	$ 153,405

(dollars in thousands)	Amortized cost	Gross unrealized gains	Gross unrealized losses	Fair value
December 31, 2016				
Available-for-sale securities:				
Agency - GSE	$ 18,362	$ 58	$ (144)	$ 18,276
Obligations of states and political subdivisions	38,648	1,803	(260)	40,191
MBS - GSE residential	70,639	851	(553)	70,937
Total debt securities	127,649	2,712	(957)	129,404
Equity securities - financial services	294	339	-	633
Total available-for-sale securities	$ 127,943	$ 3,051	$ (957)	$ 130,037

The amortized cost and fair value of debt securities at June 30, 2017 by contractual maturity are summarized below:

(dollars in thousands)	Amortized cost	Fair value
Available-for-sale securities:		
Debt securities:		

Due in one year or less	$ 5,004	$ 5,005
Due after one year through five years	14,107	14,153
Due after five years through ten years	1,914	1,996
Due after ten years	39,375	41,183
Total debt securities	60,400	62,337
MBS - GSE residential	89,903	90,349
Total available-for-sale debt securities	$ 150,303	$ 152,686

Actual maturities will differ from contractual maturities because issuers and borrowers may have the right to call or repay obligations with or without call or prepayment penalty. Agency – GSE and municipal securities are included based on their original stated maturity. MBS – GSE residential, which are based on weighted-average lives and subject to monthly principal pay-downs, are listed in total. Most of the securities have fixed rates or have predetermined scheduled rate changes and many have call features that allow the issuer to call the security at par before its stated maturity without penalty.

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The following table presents the fair value and gross unrealized losses of investment securities aggregated by investment type, the length of time and the number of securities that have been in a continuous unrealized loss position as of June 30, 2017 and December 31, 2016: