FRANKLIN FINANCIAL SERVICES CORP /PA/
Form 10-Q
November 06, 2017
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, 2017

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

For the transition period from__________ to___________

Commission file number 0-12126

FRANKLIN FINANCIAL SERVICES CORPORATION

(Exact name of registrant as specified in its charter)

PENNSYLVANIA	25-1440803
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

20 South Main Street, Chambersburg	PA 17201-0819
(Address of principal executive offices)	(Zip Code)

(717) 264-6116

(Registrant's telephone number, including area code)

Not Applicable

(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the 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 No

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

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

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company Emerging growth company

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

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

There were 4,347,855 outstanding shares of the Registrant's common stock as of October 31, 2017.

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Part I FINANCIAL INFORMATION

Item 1 Financial Statements

Consolidated Balance Sheets

(Dollars in thousands, except share and per share data)(unaudited)	September 30, 2017	December 31, 2016
Assets		
Cash and due from banks	$ 16,678	$ 16,888
Interest-bearing deposits in other banks	54,683	19,777
Total cash and cash equivalents	71,361	36,665
Investment securities available for sale, at fair value	132,322	143,875
Restricted stock	456	1,767
Loans held for sale	452	540
Loans	911,503	893,873
Allowance for loan losses	(11,543)	(11,075)
Net Loans	899,960	882,798
Premises and equipment, net	13,807	14,058
Bank owned life insurance	22,850	22,459
Goodwill	9,016	9,016
Other real estate owned	2,629	4,915
Deferred tax asset, net	6,146	5,844
Other assets	6,550	5,506
Total assets	$ 1,165,549	$ 1,127,443
Liabilities		
Deposits		
Non-interest bearing checking	$ 183,297	$ 170,345
Money management, savings and interest checking	774,513	737,140
Time	75,338	74,635
Total deposits	1,033,148	982,120
Short-term borrowings	—	24,270
Other liabilities	7,821	4,560
Total liabilities	1,040,969	1,010,950
Shareholders' equity		
Common stock, $1 par value per share,15,000,000 shares authorized with 4,688,349 shares issued and 4,346,394 shares outstanding at September 30, 2017 and 4,688,349 shares issued and 4,316,836 shares outstanding at December 31, 2016	4,688	4,688
Capital stock without par value, 5,000,000 shares authorized with no shares issued and outstanding	—	—
Additional paid-in capital	40,238	39,752
Retained earnings	89,532	83,081
Accumulated other comprehensive loss	(3,607)	(4,215)

Treasury stock, 341,955 shares at September 30, 2017 and 371,513 shares at December 31, 2016, at cost	(6,271)	(6,813)
Total shareholders' equity	124,580	116,493
Total liabilities and shareholders' equity	$ 1,165,549	$ 1,127,443

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

Consolidated Statements of Income

(Dollars in thousands, except per share data) (unaudited)	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2017	2016	2017	2016
Interest income				
Loans, including fees	$ 9,130	$ 8,343	$ 26,808	$ 24,394
Interest and dividends on investments:				
Taxable interest	509	569	1,558	1,729
Tax exempt interest	275	355	861	1,079
Dividend income	2	2	23	12
Deposits and obligations of other banks	147	79	297	220
Total interest income	10,063	9,348	29,547	27,434
Interest expense				
Deposits	629	559	1,785	1,650
Short-term borrowings	—	4	15	6
Total interest expense	629	563	1,800	1,656
Net interest income	9,434	8,785	27,747	25,778
Provision for loan losses	250	1,150	420	3,325
Net interest income after provision for loan losses	9,184	7,635	27,327	22,453
Noninterest income				
Investment and trust services fees	1,353	1,211	3,991	3,683
Loan service charges	201	102	657	518
Deposit service charges and fees	611	635	1,789	1,815
Other service charges and fees	340	325	996	941
Debit card income	325	373	1,062	1,095
Increase in cash surrender value of life insurance	130	131	391	399
Net loss on sale of other real estate owned	(23)	(20)	(23)	(31)
OTTI losses on debt securities	—	(10)	—	(30)
Securities gains, net	1	—	3	4
Other	33	56	186	219
Total noninterest income	2,971	2,803	9,052	8,613
Noninterest Expense				
Salaries and employee benefits	4,694	4,566	14,190	13,282
Occupancy, furniture and equipment, net	809	777	2,386	2,363
Advertising	332	296	873	839
Legal and professional	502	423	1,173	1,114
Data processing	567	539	1,643	1,540
Pennsylvania bank shares tax	243	203	728	699
FDIC Insurance	82	188	281	514
ATM/debit card processing	190	214	630	642
Foreclosed real estate	24	18	95	93
Telecommunications	106	91	308	300
Other	756	665	2,116	2,119
Total noninterest expense	8,305	7,980	24,423	23,505
Income before federal income taxes	3,850	2,458	11,956	7,561

Federal income tax expense	774	383	2,517	1,198
Net income	$ 3,076	$ 2,075	$ 9,439	$ 6,363
Per share				
Basic earnings per share	$ 0.71	$ 0.48	$ 2.18	$ 1.48
Diluted earnings per share	$ 0.70	$ 0.48	$ 2.17	$ 1.48
Cash dividends declared	$ 0.24	$ 0.21	$ 0.69	$ 0.61

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

Consolidated Statements of Comprehensive Income

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
(Dollars in thousands) (unaudited)	2017	2016	2017	2016
Net Income	$ 3,076	$ 2,075	$ 9,439	$ 6,363
Securities:				
Unrealized gains arising during the period	(97)	(524)	924	1,528
Reclassification adjustment for net (gains) losses and OTTI included in net income (1)	(1)	10	(3)	26
Net unrealized gains	(98)	(514)	921	1,554
Tax effect	33	174	(313)	(528)
Net of tax amount	(65)	(340)	608	1,026
Pension:				
Change in plan assets and benefit obligations	—	—	—	—
Reclassification adjustment for losses included in net income (2)	—	225	—	225
Net unrealized losses	—	225	—	225
Tax effect	—	(76)	—	(76)
Net of tax amount	—	149	—	149
Total other comprehensive (loss) income	(65)	(191)	608	1,175
Total Comprehensive Income	$ 3,011	$ 1,884	$ 10,047	$ 7,538

Reclassification adjustment / Statement line item	Tax expense (benefit)			
(1) Securities / securities (gains) losses and OTTI losses, net	$ —	$ (3)	$ 1	$ (9)
(2) Pension / Salary & Benefits	—	(77)	—	(77)

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

Consolidated Statements of Changes in Shareholders' Equity

For the Nine Months ended September 30, 2017 and 2016

(Dollars in thousands, except per share data) (unaudited)	Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Treasury Stock	Total
Balance at December 31, 2015	$ 4,659	$ 38,778	$ 78,517	$ (3,722)	$ (6,856)	$ 111,376
Net income	—	—	6,363	—	—	6,363
Other comprehensive income	—	—	—	1,175	—	1,175
Cash dividends declared, $.61 per share	—	—	(2,618)	—	—	(2,618)
Acquisition of 30,196 shares of treasury stock	—	—	—	—	(700)	(700)
Treasury shares issued under employer stock purchase plan, 539 shares	—	2	—	—	10	12
Treasury shares issued under dividend reinvestment plan, 24,171 shares	—	134	—	—	438	572
Common stock issued under dividend reinvestment plan, 25,230 shares	25	527	—	—	—	552
Common stock issued under incentive stock option plan, 3,600 shares	4	55	—	—	—	59
Stock option compensation expense	—	88	—	—	—	88
Balance at September 30, 2016	$ 4,688	$ 39,584	$ 82,262	$ (2,547)	$ (7,108)	$ 116,879
Balance at December 31, 2016	$ 4,688	$ 39,752	$ 83,081	$ (4,215)	$ (6,813)	$ 116,493
Net income	—	—	9,439	—	—	9,439
Other comprehensive income	—	—	—	608	—	608
Cash dividends declared, $.69 per share	—	—	(2,988)	—	—	(2,988)
Treasury shares issued under employee stock purchase plan, 6,568 shares	—	29	—	—	120	149
Treasury shares issued under dividend reinvestment plan, 22,990 shares	—	296	—	—	422	718
Stock option compensation expense	—	161	—	—	—	161
Balance at September 30, 2017	$ 4,688	$ 40,238	$ 89,532	$ (3,607)	$ (6,271)	$ 124,580

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

Consolidated Statements of Cash Flows

	Nine Months Ended September 30,	
	2017	2016
(Dollars in thousands) (unaudited)		
Cash flows from operating activities		
Net income	$ 9,439	$ 6,363
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	973	1,002
Net amortization of loans and investment securities	1,269	1,218
Amortization and net change in mortgage servicing rights valuation	41	41
Provision for loan losses	420	3,325
Gain on sales of securities	(3)	(4)
Impairment write-down on securities recognized in earnings	—	30
Loans originated for sale	(6,773)	(6,598)
Proceeds from sale of loans	6,861	6,692
Write-down of other real estate owned	60	46
Write-down on premises and equipment available for sale	45	—
Net loss on sale or disposal of other real estate/other repossessed assets	23	31
Increase in cash surrender value of life insurance	(391)	(399)
Stock option compensation	161	88
Decrease in other assets	(1,242)	154
Increase (decrease) in other liabilities	2,753	(2,247)
Net cash provided by operating activities	13,636	9,742
Cash flows from investing activities		
Proceeds from sales and calls of investment securities available for sale	875	1,925
Proceeds from maturities and pay-downs of securities available for sale	16,875	18,984
Purchase of investment securities available for sale	(6,533)	(16,605)
Net decrease in restricted stock	1,311	(336)
Net increase in loans	(17,643)	(79,275)
Capital expenditures	(871)	(515)
Proceeds from surrender of life insurance policy	—	436
Proceeds from sale of other assets	154	—
Proceeds from sale of other real estate	2,255	625
Net cash used in investing activities	(3,577)	(74,761)
Cash flows from financing activities		
Net increase in demand deposits, interest-bearing checking, and savings accounts	50,325	68,454
Net increase (decrease) in time deposits	703	(8,414)
Net decrease (increase) in short-term borrowings	(24,270)	8,530
Dividends paid	(2,988)	(2,618)
Treasury shares issued under employee stock purchase plan	149	—
Treasury shares issued under dividend reinvestment plan	718	—
Common stock issued under stock option plans	—	71
Common stock issued under dividend reinvestment plan	—	1,124
Purchase of Treasury shares	—	(700)
Net cash provided by financing activities	24,637	66,447

Increase in cash and cash equivalents	34,696	1,428
Cash and cash equivalents as of January 1	36,665	39,166
Cash and cash equivalents as of September 30	$ 71,361	$ 40,594
Supplemental Disclosures of Cash Flow Information		
Cash paid during the year for:		
Interest on deposits and other borrowed funds	$ 1,786	$ 1,643
Income taxes	$ 3,405	$ 2,100
Noncash Activities:		
Loans transferred to Other Real Estate	$ 52	$ 123

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

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FRANKLIN FINANCIAL SERVICES CORPORATION and SUBSIDIARIES

UNAUDITED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 1 - Basis of Presentation

The consolidated financial statements include the accounts of Franklin Financial Services Corporation (the Corporation), and its wholly-owned subsidiaries, Farmers and Merchants Trust Company of Chambersburg (the Bank) and Franklin Future Fund Inc. Farmers and Merchants Trust Company of Chambersburg is a commercial bank that has one wholly-owned subsidiary, Franklin Financial Properties Corp. Franklin Financial Properties Corp. holds real estate assets that are leased by the Bank. Franklin Future Fund Inc. is a non-bank investment company. The activities of non-bank entities are not significant to the consolidated totals. All significant intercompany transactions and account balances have been eliminated.

In the opinion of management, all adjustments (which include only normal recurring adjustments) necessary to present fairly the consolidated financial position, results of operations, and cash flows as of September 30, 2017, and for all other periods presented have been made.

Certain information and footnote disclosures normally included in consolidated financial statements prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”) have been condensed or omitted. It is suggested that these consolidated financial statements be read in conjunction with the audited consolidated financial statements and notes thereto included in the Corporation’s 2016 Annual Report on Form 10-K. The consolidated results of operations for the three and nine month periods ended September 30, 2017 are not necessarily indicative of the operating results for the full year. Management has evaluated subsequent events for potential recognition and/or disclosure through the date these consolidated financial statements were issued.

The consolidated balance sheet at December 31, 2016 has been derived from the audited consolidated financial statements at that date, but does not include all of the information and footnotes required by GAAP for complete consolidated financial statements.

For purposes of reporting cash flows, cash and cash equivalents include cash and due from banks, interest-bearing deposits in other banks and federal funds sold. Generally, federal funds are purchased and sold for one-day periods.

Earnings per share are computed based on the weighted average number of shares outstanding during each period end. A reconciliation of the weighted average shares outstanding used to calculate basic earnings per share and diluted earnings per share follows:

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
(Dollars and shares in thousands, except per share data)	2017	2016	2017	2016
Weighted average shares outstanding (basic)	4,343	4,307	4,332	4,295
Impact of common stock equivalents	21	7	21	3
Weighted average shares outstanding (diluted)	4,364	4,314	4,353	4,298

Anti-dilutive options excluded from calculation	—	9	—	37
Net income	$ 3,076	$ 2,075	$ 9,439	$ 6,363
Basic earnings per share	$ 0.71	$ 0.48	$ 2.18	$ 1.48
Diluted earnings per share	$ 0.70	$ 0.48	$ 2.17	$ 1.48

Note 2. Recent Accounting Pronouncements

Standard	Description	Effective Date	Effect on the financial statements or other significant matters
ASU 2016-09, Stock Compensation (Topic 718): Improvements to Employee Share-based Payment Accounting	The standard requires entities to recognize the income tax effects of share-based awards in the income statement when the awards vest or are settled (i.e. the additional paid-in capital pools will be eliminated). The guidance on employers' accounting for an employee's use of shares to satisfy the employer's statutory income tax withholding obligation and for forfeitures is changing. The standard also provides an entity the option to make an entity-wide accounting policy election to either estimate the number of awards that are expected to vest or account for forfeitures when they occur.	January 1, 2017	We adopted the standard during the first quarter of 2017. Due to the type of stock compensation plans used by the Corporation, there was no effect on the Corporation's consolidated financial statements.
ASU 2017-09, Premium Amortization on Purchased Callable Debt Securities	The standard shortens the amortization period for premiums on purchased callable debt securities to the earliest call date, rather than amortizing over the full contractual term. The standard does change the standard for securities held at a discount. The amendments require companies to reset the effective yield using the payment terms of the debt security if the call option is not exercised on the earliest call date. If the security has additional future called dates, any excess of the amortized cost basis over the amount repayable by the issuer at the next call date should be amortized to the next call date.	January 1, 2017	We adopted the standard during the first quarter of 2017, and there was no effect on the Corporation's consolidated financial statements.
ASU 2016-15, Statements of Cash Flow (Topic 320): Classification of Certain Cash Receipts and Cash Payments	The standard clarifies how certain cash receipts and cash payments are presented and classified in the statement of cash flows. The amendments are intended to reduce diversity in practice. The standard contains additional guidance clarifying when an entity should separate cash receipts and cash payments and classifies them into more than one class of cash flows (including when reasonable judgement is required to estimate and allocate cash flows) versus when an entity should classify the aggregate amount into one class of cash flows on the basis of predominance.	January 1, 2018	We do not expect this guidance will have an effect on the Corporation's consolidated financial statements.

ASU 2017-07, Employee Benefits Plan (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost	This standard requires an employer to report the service cost component in the same line item or items as other compensation costs arising from services rendered by the pertinent employees during the period. The other components of net benefit cost are required to be presented in the income statement separately from the service cost component and outside a subtotal of income from operations. The amendments in this update also allow only the service cost component to be eligible for capitalization when applicable.	January 1, 2018	We do not expect this standard will have an effect on the Corporation's consolidated financial statements.
ASU 2014-09, Revenue from Contracts with Customers (Topic 606)	The amendments in this Update (ASU 2014-09) establish a comprehensive revenue recognition standard. The revenue standard's core principle is built on the contract between a vendor and a customer for the provision of goods and services. It attempts to depict the exchange of rights and obligations between the parties in the pattern of revenue recognition based on the consideration to which the vendor is entitled. To accomplish this objective, the standard requires five basic steps: (i) identify the contract with the customer, (ii) identify the performance obligations in the contract, (iii) determine the transaction price, (iv) allocate the transaction price to the performance obligations in the contract, and (v) recognize revenue when (or as) the entity satisfies a performance obligation. Three basic transition methods are available – full retrospective, retrospective with certain practical expedients, and a cumulative effect approach.	January 1, 2018	The majority of our revenue comes from net interest income, and is explicitly out of scope of the guidance. The contracts in noninterest income that are in scope of the guidance are primarily related to service charges and fees on deposit accounts, investment and trust income and other service charges and fees. We have completed the analysis of the contracts in scope and have determined only estate settlement fees will require a change in the method of revenue recognition. The effect of this change has not been determined but it is not expected to be material to the Corporation's consolidated financial statements.

ASU 2016-01, Financial Instruments - Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities	The standard amends the guidance on the classification and measurement of financial instruments. Some of the amendments include the following: 1) requires equity investments to be measured at fair value with changes in fair value recognized in net income; 2) simplifies the impairment assessment of equity investments without readily determinable fair values by requiring a qualitative assessment to identify impairment; 3) requires public business entities to use the exit price notion when measuring the fair value of financial instruments for disclosure purposes; and 4) requires an entity to present separately in other comprehensive income the portion of the total change in the fair value of a liability resulting from a change in the instrument-specific credit risk when the entity has elected to measure the liability at fair value; among others.	January 1, 2018	We do not expect this guidance will have a material effect on the Corporation's consolidated financial statements. We do not have a significant number of AFS equity securities. Additionally we do not have financial liabilities accounted for under the fair value option. The adoption of this guidance is not expected to be material.
ASU 2016-02, Leases (Topic 842)	From the lessee’s perspective, the new standard established a right-of-use (ROU) model that requires a lessee to record a ROU asset and a lease liability on the balance sheet for all leases with terms longer than 12 months. Leases will be classified as either finance or operating, with classification affecting the pattern of expense recognition in the income statement for a lessees. From the lessor’s perspective, the new standard requires a lessor to classify leases as either sales-type, finance or operating. A lease will be treated as a sale if it transfers all of the risks and rewards, as well as control of the underlying asset, to the lessee. If risks and rewards are conveyed without the transfer of control, the lease is treated as financing. If the lessor doesn’t convey risks and rewards or control, an operating lease results.	January 1, 2019	The Corporation currently has real estate and equipment leases that it classifies as operating leases that are not recognized on the balance sheet. Under the new standard, these leases will move onto the balance sheet. The Corporation has identified a lease accounting model it expects to use to implement the standard. It is expected the model will be functional during the fourth quarter of 2017, but the Corporation does not plan to early adopt the standard. The Corporation believes the new standard will not have a material effect on its consolidated financial statements.
ASU 2017-04, Goodwill (Topic 350)	This guidance, among other things, removes step 2 of the goodwill impairment test thus eliminating the need to determine the fair value of individual assets and liabilities of the reporting unit. Upon adoption of this standard, goodwill impairment will be the amount by which a reporting unit's carrying value exceeds its fair value, not to exceed the carrying amount of goodwill. This may result in more or less impairment being recognized than under the current guidance.	January 1, 2020	We do not currently expect this guidance to have a material effect on the Corporation's consolidated financial statements based upon the most recent goodwill impairment analysis.

ASU 2016-13, Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments	This standard requires credit losses on most financial assets measured at amortized cost and certain other instruments to be measured using an expected credit loss model (referred to as the current expected credit loss (CECL) model). Under this model, entities will estimate credit losses over the entire contractual term of the instrument (considering estimated prepayments, but not expected extensions or modifications unless reasonable expectation of a troubled debt restructuring exists) from the date of initial recognition of that instrument. The ASU replaces the current accounting model for purchased credit impaired loans and debt securities. The allowance for credit losses for purchased financial assets with a more-than insignificant amount of credit deterioration since origination (“PCD assets”), should be determined in a similar manner to other financial assets measured on an amortized cost basis. However, upon initial recognition, the allowance for credit losses is added to the purchase price (“gross up approach”) to determine the initial amortized cost basis. The subsequent account for PCD financial assets is the same expected loss model described above.	January 1, 2020	We have formed an implementation team led by the Corporation's Risk Management function. The team is reviewing the requirements of the ASU and evaluating methods and models for implementation. The Corporation preliminarily believes the new standard will result in earlier recognition of additions to the allowance for loan losses and possibly a larger allowance for loan loss balance with a corresponding increase in the provision for loan losses in results of operations; however, the Corporation is continuing to evaluate the impact of the pending adoption of the new standard on its consolidated financial statements.

Note 3. Accumulated Other Comprehensive Loss

The components of accumulated other comprehensive losses included in shareholders' equity are as follows:

(Dollars in thousands)	September 30, 2017	December 31, 2016
Net unrealized gains (losses) on securities	$ 901	$ (20)
Tax effect	(306)	7
Net of tax amount	595	(13)
Accumulated pension adjustment	(6,366)	(6,366)
Tax effect	2,164	2,164
Net of tax amount	(4,202)	(4,202)
Total accumulated other comprehensive loss	$ (3,607)	$ (4,215)

Note 4. Investments

The amortized cost and estimated fair value of investment securities available for sale as of September 30, 2017 and December 31, 2016 are as follows:

(Dollars in thousands) September 30, 2017	Amortized cost	Gross unrealized gains	Gross unrealized losses	Fair value
Equity securities	$ 164	$ 183	$ —	$ 347
U.S. Government and Agency securities	11,591	123	(32)	11,682
Municipal securities	59,920	971	(193)	60,698
Trust preferred securities	5,994	4	(187)	5,811
Agency mortgage-backed securities	52,818	359	(402)	52,775
Private-label mortgage-backed securities	905	81	(5)	981
Asset-backed securities	29	—	(1)	28
	$ 131,421	$ 1,721	$ (820)	$ 132,322

(Dollars in thousands) December 31, 2016	Amortized cost	Gross unrealized gains	Gross unrealized losses	Fair value
Equity securities	$ 164	$ 126	$ —	$ 290
U.S. Government and Agency securities	12,598	148	(26)	12,720
Municipal securities	62,763	793	(571)	62,985
Trust preferred securities	5,979	—	(518)	5,461
Agency mortgage-backed securities	61,305	431	(452)	61,284
Private-label mortgage-backed securities	1,053	56	(5)	1,104
Asset-backed securities	33	—	(2)	31
	$ 143,895	$ 1,554	$ (1,574)	$ 143,875

At September 30, 2017 and December 31, 2016, the fair value of investment securities pledged to secure public funds, trust balances, deposit and other obligations totaled $92.5 million and $79.1 million, respectively.

The amortized cost and estimated fair value of debt securities at September 30, 2017, by contractual maturity are shown below. Actual maturities may differ from contractual maturities because of prepayment or call options embedded in the securities.

(Dollars in thousands)	Amortized cost	Fair value
Due in one year or less	$ 951	$ 953
Due after one year through five years	14,110	14,354
Due after five years through ten years	33,407	33,683
Due after ten years	29,066	29,229
	77,534	78,219
Mortgage-backed securities	53,723	53,756
	$ 131,257	$ 131,975

The composition of the net realized securities gains for the three and nine months ended are as follows:

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
(Dollars in thousands)	2017	2016	2017	2016
Gross gains realized	$ 1	$ —	$ 3	$ 4
Gross losses realized	—	—	—	—
Net gains realized	$ 1	$ —	$ 3	$ 4

The following table provides additional detail about trust preferred securities as of September 30, 2017:

Trust Preferred Securities

(Dollars in thousands)

Deal Name	Maturity	Single Issuer or Pooled	Class	Amortized Cost	Fair Value	Gross Unrealized Gain (Loss)	Lowest Credit Rating Assigned
BankAmerica Cap III	1/15/2027	Single	Preferred Stock	$ 969	$ 945	$ (24)	BB+
Wachovia Cap Trust II	1/15/2027	Single	Preferred Stock	280	282	2	BBB
Huntington Cap Trust	2/1/2027	Single	Preferred Stock	949	903	(46)	BB
Corestates Captl Tr II	2/15/2027	Single	Preferred Stock	946	948	2	BBB
Huntington Cap Trust II	6/15/2028	Single	Preferred Stock	905	852	(53)	BB
Chase Cap VI JPM	8/1/2028	Single	Preferred Stock	967	934	(33)	BBB-
Fleet Cap Tr V	12/18/2028	Single	Preferred Stock	978	947	(31)	BB+

$ 5,994	$ 5,811	$ (183)

The following table provides additional detail about private label mortgage-backed securities as of September 30, 2017:

Private Label Mortgage Backed Securities

(Dollars in thousands) Description	Origination Date	Amortized Cost	Fair Value	Gross Unrealized Gain (Loss)	Collateral Type	Lowest Credit Rating Assigned	Credit Support %	Cumulative OTTI Charges
MALT 2004-6 7A1	6/1/2004	$ 250	$ 245	$ (5)	ALT A	CCC	16.60	$ —
RALI 2005-QS2 A1	2/1/2005	113	127	14	ALT A	CC	0.44	15
RALI 2006-QS4 A2	4/1/2006	343	369	26	ALT A	Caa3	—	323
GSR 2006-5F 2A1	5/1/2006	30	39	9	Prime	D	—	15
RALI 2006-QS8 A1	7/28/2006	169	201	32	ALT A	Ca	—	242
		$ 905	$ 981	$ 76				$ 595

Impairment:

The investment portfolio contained ninety-three securities with $51.1 million of temporarily impaired fair value and $820 thousand in unrealized losses at September 30, 2017. The total unrealized loss position has improved from a $1.6 million unrealized loss at year-end 2016.

For securities with an unrealized loss, Management applies a systematic methodology in order to perform an assessment of the potential for other-than-temporary impairment. In the case of debt securities, investments considered for other-than-temporary impairment: (1) had a specified maturity or repricing date; (2) were generally expected to be redeemed at par, and (3) were expected to achieve a recovery in market value within a reasonable period of time. In addition, the Bank considers whether it intends to sell these securities or whether it will be forced to sell these securities before the earlier of amortized cost recovery or maturity. Equity securities are assessed for other-than-temporary impairment based on the length of time of impairment, dollar amount of the impairment and general market and financial conditions relating to specific issues. The impairment identified on debt and equity securities and subject to assessment at September 30, 2017, was deemed to be temporary and required no further adjustments to the financial statements, unless otherwise noted.

The following table reflects temporary impairment in the investment portfolio (excluding restricted stock), aggregated by investment category, length of time that individual securities have been in a continuous unrealized loss position and the number of securities in each category as of September 30, 2017 and December 31, 2016:

	September 30, 2017								
	Less than 12 months			12 months or more			Total		
(Dollars in thousands)	Fair Value	Unrealized Losses	Count	Fair Value	Unrealized Losses	Count	Fair Value	Unrealized Losses	Count
U.S. Government and Agency securities	$ 1,690	$ (3)	4	$ 3,628	$ (29)	10	$ 5,318	$ (32)	14
Municipal securities	4,823	(34)	8	6,561	(159)	12	11,384	(193)	20
Trust preferred securities	—	—	—	4,581	(187)	5	4,581	(187)	5
Agency mortgage-backed securities	14,801	(115)	27	14,760	(287)	25	29,561	(402)	52
Private-label mortgage-backed securities	245	(5)	1	—	—	—	245	(5)	1
Asset-backed securities	—	—	—	4	(1)	1	4	(1)	1
Total temporarily impaired securities	$ 21,559	$ (157)	40	$ 29,534	$ (663)	53	$ 51,093	$ (820)	93

	December 31, 2016								
	Less than 12 months			12 months or more			Total		
(Dollars in thousands)	Fair Value	Unrealized Losses	Count	Fair Value	Unrealized Losses	Count	Fair Value	Unrealized Losses	Count
U.S. Government and Agency securities	$ 789	$ (9)	1	$ 3,413	$ (17)	10	$ 4,202	$ (26)	11
Municipal securities	23,407	(417)	43	1,598	(154)	2	25,005	(571)	45
Trust preferred securities	—	—	—	5,461	(518)	7	5,461	(518)	7
Agency mortgage-backed securities	26,995	(359)	39	4,656	(93)	11	31,651	(452)	50
Private-label mortgage-backed securities	281	(5)	1	—	—	—	281	(5)	1
Asset-backed securities	—	—	—	4	(2)	1	4	(2)	1
Total temporarily impaired securities	$ 51,472	$ (790)	84	$ 15,132	$ (784)	31	$ 66,604	$ (1,574)	115

The unrealized loss in the municipal bond portfolio decreased to $193 thousand from $571 thousand at December 31, 2016 as market prices improved during the quarter. There are twenty securities in this portfolio with an unrealized loss and the loss in this portfolio is deemed to be non-credit related and no other-than-temporary impairment charges have been recorded.

The trust preferred portfolio contains five securities with a fair value of $4.6 million and an unrealized loss of $187 thousand. The trust-preferred securities held by the Bank are single entity issues, not pooled trust preferred securities. Therefore, the impairment review of these securities is based only on the issuer and the security cannot be impaired by the performance of other issuers as if it was a pooled trust-preferred bond. All of the Bank's trust preferred securities are single issue, variable rate notes with long maturities (2027 – 2028). None of these bonds have suspended or missed a dividend payment. At September 30, 2017, the Bank believes it will be able to collect all interest and principal due on these bonds and no other-than-temporary-impairment charges were recorded.

The PLMBS sector is showing an unrealized gain of $76 thousand at quarter end. This is primarily a result of the cumulative OTTI charges recorded on this portfolio. Due to the nature of these bonds, they are evaluated closely. These bonds were all rated AAA at time of purchase, but have since experienced rating declines. Some have experienced increased delinquencies and defaults, while others have seen the credit support increase as the bonds paid-down. The Bank monitors the performance of the PLMBS investments on a regular basis and reviews delinquencies, default rates, credit support levels and various cash flow stress test scenarios. In determining the credit related loss, Management considers all principal past due 60 days or more as a loss. If additional principal moves beyond 60 days past due, it will also be considered a loss. The Bank has recorded $595 thousand of cumulative impairment charges on this portfolio. Management continues to monitor these securities and it is possible that additional write-downs may occur if current loss trends continue.

The following table represents the cumulative credit losses on debt securities recognized in earnings for:

(Dollars in thousands)	Nine Months Ended September 30, 2017	2016
Balance of cumulative credit-related OTTI at January 1	$ 595	$ 555
Additions for credit-related OTTI not previously recognized	—	30
Additional increases for credit-related OTTI previously recognized when there is no intent to sell and no requirement to sell before recovery of amortized cost basis	—	—
Decreases for previously recognized credit-related OTTI because there was an intent to sell	—	—
Reduction for increases in cash flows expected to be collected	—	—
Balance of credit-related OTTI at September 30	$ 595	$ 585

The Bank held $456 thousand of restricted stock at September 30, 2017. Except for $30 thousand, this investment represents stock in FHLB Pittsburgh. The Bank is required to hold this stock to be a member of FHLB and it is carried at cost of $100 per share. The level of FHLB stock held is determined by FHLB and is comprised of a minimum membership amount plus a variable activity amount. FHLB stock is evaluated for impairment primarily based on an assessment of the ultimate recoverability of its cost. As a government sponsored entity, FHLB has the ability to raise funding through the U.S. Treasury that can be used to support its operations. There is not a public market for FHLB stock and the benefits of FHLB membership (e.g., liquidity and low cost funding) add value to the stock beyond purely financial measures. Management intends to remain a member of the FHLB and believes that it will be able to fully recover the cost basis of this investment.

Note 5. Loans

The Bank reports its loan portfolio based on the primary collateral of the loan. It further classifies these loans by the primary purpose, either consumer or commercial. The Bank's residential real estate loans include long-term loans to individuals and businesses secured by mortgages on the borrower's real property and include home equity loans. Construction loans are made to finance the purchase of land and the construction of residential and commercial buildings thereon, and are secured by mortgages on real estate. Commercial real estate loans include construction, owner and non-owner occupied properties and farm real estate. Commercial loans are made to businesses of various sizes for a variety of purposes including property, plant and equipment, working capital and loans to government municipalities. Commercial lending is concentrated in the Bank's primary market, but also includes purchased loan participations. Consumer loans are comprised of installment loans and unsecured personal lines of credit.

A summary of loans outstanding, by class, at the end of the reporting periods is as follows:

(Dollars in thousands)	September 30, 2017	December 31, 2016
Residential Real Estate 1-4 Family		
Consumer first liens	$ 98,905	$ 103,125
Commercial first lien	62,075	65,445
Total first liens	160,980	168,570
Consumer junior liens and lines of credit	44,789	44,817
Commercial junior liens and lines of credit	5,352	5,396
Total junior liens and lines of credit		