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First Internet Bancorp
Form 10-Q
November 12, 2014

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the Quarterly Period September 30, 2014

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 001-35750

First Internet Bancorp
(Exact Name of Registrant as Specified in Its Charter)

Indiana	20-3489991
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)

8888 Keystone Crossing, Suite 1700	46240
Indianapolis, Indiana	
(Address of Principal Executive Offices)	(Zip Code)
(317) 532-7900	
(Registrant's Telephone Number, Including Area Code)	

(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 during the preceding 12 months (or such shorter period that the registrant was required to submit and post such files).

Yes ☐ No ☒

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company (as defined in Rule 12b-2 of the Exchange Act).

Large Accelerated Filer ☐

Accelerated Filer ☐

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Non-accelerated Filer ☐ (Do not check if a smaller reporting company)

Smaller Reporting Company ☒

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

Yes ☐ No ☒

As of November 7, 2014, the registrant had 4,439,575 shares of common stock issued and outstanding.

Cautionary Note Regarding Forward-Looking Statements

This Quarterly Report on Form 10-Q may contain forward-looking statements with respect to the financial condition, results of operations, plans, objectives, future performance, or business of First Internet Bancorp (“we,” “our,” “us” or the “Company”). Forward-looking statements are generally identifiable by the use of words such as “believe,” “expect,” “anticipate,” “plan,” “intend,” “estimate,” “may,” “will,” “would,” “could,” “should,” or other similar expressions. Forward-looking statements are not a guarantee of future performance or results, are based on information available at the time the statements are made, and involve known and unknown risks, uncertainties and other factors that could cause actual results to differ materially from the information in the forward-looking statements. Factors that may cause such differences include: failures of or interruptions in the communications and information systems on which we rely to conduct our business; our plans to grow our commercial real estate and commercial and industrial loan portfolios; competition with national, regional, and community financial institutions; the loss of any key members of senior management; fluctuations in interest rates; general economic conditions and risks relating to the regulation of financial institutions. Additional factors that may affect our results include those discussed in our most recent Annual Report on Form 10-K under the heading “Risk Factors” and in other reports filed with the Securities and Exchange Commission (“SEC”). All statements in this Quarterly Report on Form 10-Q, including forward-looking statements, speak only as of the date they are made, and the Company undertakes no obligation to update any statement in light of new information or future events.

(i)

PART I

ITEM 1. FINANCIAL STATEMENTS

First Internet Bancorp
Condensed Consolidated Balance Sheets
(Amounts in thousands except share data)

	September 30, 2014 (Unaudited)	December 31, 2013
Assets		
Cash and due from banks	\$1,137	\$2,578
Interest-bearing demand deposits	38,470	51,112
Total cash and cash equivalents	39,607	53,690
Interest-bearing time deposits	2,000	2,500
Securities available-for-sale, at fair value (amortized cost of \$129,573 and \$185,091, respectively)	128,203	181,409
Loans held-for-sale (includes \$25,701 and \$24,254 at fair value, respectively)	27,547	28,610
Loans receivable	695,929	501,153
Allowance for loan losses	(5,464)	(5,426)
Net loans receivable	690,465	495,727
Accrued interest receivable	2,803	2,904
Federal Home Loan Bank of Indianapolis stock	2,943	2,943
Cash surrender value of bank-owned life insurance	12,226	11,935
Premises and equipment, net	7,075	7,134
Goodwill	4,687	4,687
Other real estate owned	4,545	4,381
Accrued income and other assets	4,782	6,422
Total assets	\$926,883	\$802,342
Liabilities and Shareholders' Equity		
Liabilities		
Non-interest bearing deposits	\$20,359	\$19,386
Interest-bearing deposits	717,611	653,709
Total deposits	737,970	673,095
Advances from Federal Home Loan Bank	86,871	31,793
Subordinated debt	2,852	2,789
Accrued interest payable	82	102
Accrued expenses and other liabilities	4,334	3,655
Total liabilities	832,109	711,434
Commitments and Contingencies		
Shareholders' Equity		
Preferred stock, no par value; 4,913,779 shares authorized; issued and outstanding - none	—	—
Voting common stock, no par value; 45,000,000 shares authorized; 4,439,575 and 4,448,326 shares issued and outstanding, respectively	71,705	71,378
Nonvoting common stock, no par value; 86,221 shares authorized; issued and outstanding - none	—	—
Retained earnings	23,951	21,902
Accumulated other comprehensive loss	(882)	(2,372)

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Total shareholders' equity	94,774	90,908
Total liabilities and shareholders' equity	\$926,883	\$802,342
See Notes to Condensed Consolidated Financial Statements		

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First Internet Bancorp
Condensed Consolidated Statements of Income – Unaudited
(Amounts in thousands except share and per share data)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
Interest Income				
Loans	\$7,218	\$5,170	\$19,918	\$15,073
Securities – taxable	684	771	2,421	2,063
Securities – non-taxable	—	447	58	1,146
Other earning assets	45	54	195	148
Total interest income	7,947	6,442	22,592	18,430
Interest Expense				
Deposits	1,958	1,758	5,740	5,042
Other borrowed funds	316	329	940	904
Total interest expense	2,274	2,087	6,680	5,946
Net Interest Income	5,673	4,355	15,912	12,484
Provision (Credit) for Loan Losses	(112)	(57)	(38)	101
Net Interest Income After Provision (Credit) for Loan Losses	5,785	4,412	15,950	12,383
Noninterest Income				
Service charges and fees	179	177	533	515
Mortgage banking activities	1,638	1,299	3,767	7,767
Other-than-temporary impairment				
Total loss related to other-than-temporarily impaired securities	—	—	—	(129)
Portion of loss recognized in other comprehensive income	—	—	—	80
Other-than-temporary impairment loss recognized in net income	—	—	—	(49)
Gain (loss) on sale of securities	54	97	538	(69)
Loss on asset disposals	(28)	(34)	(59)	(121)
Other	100	102	297	304
Total noninterest income	1,943	1,641	5,076	8,347
Noninterest Expense				
Salaries and employee benefits	3,346	2,512	9,422	7,737
Marketing, advertising, and promotion	403	562	1,179	1,389
Consulting and professional services	431	577	1,383	1,791
Data processing	246	247	722	693
Loan expenses	208	209	458	574
Premises and equipment	548	534	1,816	1,468
Deposit insurance premium	155	85	437	313
Other	448	414	1,366	1,263
Total noninterest expense	5,785	5,140	16,783	15,228
Income Before Income Taxes	1,943	913	4,243	5,502
Income Tax Provision	661	186	1,384	1,575
Net Income	\$1,282	\$727	\$2,859	\$3,927
Income Per Share of Common Stock				
Basic	\$0.29	\$0.25	\$0.64	\$1.36
Diluted	\$0.28	\$0.25	\$0.63	\$1.36
Weighted-Average Number of Common Shares Outstanding				
Basic	4,497,762	2,890,369	4,496,228	2,888,274
Diluted	4,511,291	2,903,816	4,505,801	2,889,039

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Dividends Declared Per Share	\$0.06	\$0.06	\$0.18	\$0.16
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See Notes to Condensed Consolidated Financial Statements

First Internet Bancorp

Condensed Consolidated Statements of Comprehensive Income – Unaudited

(Dollar amounts in thousands)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
Net income	\$1,282	\$727	\$2,859	\$3,927
Other comprehensive income				
Net unrealized holding gains (losses) on securities available-for-sale	(1,451	) (21	) 2,099	(5,344)
Reclassification adjustment for (gains) losses realized	(54	) (97	) (538	) 69
Net unrealized holding gains (losses) on securities available-for-sale for which an other-than-temporary impairment has been recognized in income	—	—	751	(129)
Reclassification adjustment for other-than-temporary impairment loss recognized in income	—	—	—	49
Other comprehensive income (loss) before income tax	(1,505	) (118	) 2,312	(5,355)
Income tax provision (benefit)	(536	) (41	) 822	(1,874)
Other comprehensive income (loss)	(969	) (77	) 1,490	(3,481)
Comprehensive income	\$313	\$650	\$4,349	\$446

See Notes to Condensed Consolidated Financial Statements

First Internet Bancorp

Condensed Consolidated Statements of Shareholders' Equity - Unaudited

Nine Months Ended September 30, 2014

(Dollar amounts in thousands except per share data)

	Voting and Nonvoting Common Stock	Accumulated Other Comprehensive Loss	Retained Earnings	Total Shareholders' Equity
Balance, January 1, 2014	\$71,378	\$(2,372)	) \$21,902	\$90,908
Net income	—	—	2,859	2,859
Other comprehensive income	—	1,490	—	1,490
Dividends declared (\$0.18 per share)	—	—	(810)	) (810)
Recognition of the fair value of share-based compensation	443	—	—	443
Common stock redeemed for the net settlement of share-based awards	(71)	) —	—	(71)
Other	(45)	) —	—	(45)
Balance, September 30, 2014	\$71,705	\$(882)	) \$23,951	\$94,774

See Notes to Condensed Consolidated Financial Statements

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First Internet Bancorp
Condensed Consolidated Statements of Cash Flows – Unaudited
(Dollar amounts in thousands)

	Nine Months Ended September 30,	
	2014	2013
Operating Activities		
Net income	\$2,859	\$3,927
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	1,432	1,774
Increase in cash surrender value of bank-owned life insurance	(291)	(296)
Provision (credit) for loan losses	(38)	101
Share-based compensation expense	443	274
Loss on other-than-temporary impairment of securities	—	49
Loss (gain) from sale of available-for-sale securities	(538)	69
Loans originated for sale	(285,686)	(606,768)
Proceeds from sale of loans	290,454	659,441
Gain on loans sold	(3,278)	(7,208)
Unrealized gain on loans held-for-sale	(427)	(540)
Gain on derivatives	(62)	(19)
Net change in:		
Accrued interest receivable	101	(614)
Accrued income and other assets	530	1,161
Accrued expenses and other liabilities	638	923
Net cash provided by operating activities	6,137	52,274
Investing Activities		
Net change in loans	(88,148)	(29,105)
Proceeds from sale of other real estate owned	235	—
Net change in interest bearing deposits	500	(2,500)
Maturities of securities available-for-sale	14,394	27,319
Proceeds from sale of securities available-for-sale	137,816	41,680
Purchase of securities available-for-sale	(96,803)	(135,627)
Purchase of premises and equipment	(683)	(6,563)
Loans purchased	(106,480)	(53,342)
Net cash used in investing activities	(139,169)	(158,138)
Financing Activities		
Net increase in deposits	64,875	105,962
Cash dividends paid	(794)	(282)
Proceeds from issuance of subordinated debt and related warrants	—	3,000
Proceeds from advances from Federal Home Loan Bank	95,000	13,000
Repayment of advances from Federal Home Loan Bank	(40,000)	(22,000)
Other, net	(132)	—
Net cash provided by financing activities	118,949	99,680
Net Decrease in Cash and Cash Equivalents	(14,083)	(6,184)
Cash and Cash Equivalents, Beginning of Period	53,690	32,513
Cash and Cash Equivalents, End of Period	\$39,607	\$26,329
Supplemental Disclosures of Cash Flows Information		
Cash paid during the period for interest	\$6,700	\$5,985
Cash paid during the period for taxes	1,225	723

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Loans transferred to real estate owned	—	507
Cash dividends declared, not paid	265	169
See Notes to Condensed Consolidated Financial Statements		

First Internet Bancorp

Notes to Condensed Consolidated Financial Statements – Unaudited

(Dollar amounts in thousands except per share data)

Note 1: Basis of Presentation

The accompanying unaudited condensed consolidated financial statements have been prepared in conformity with U.S. generally accepted accounting principles ("GAAP") for interim financial information and pursuant to the rules and regulations of the SEC. Accordingly, they do not include all of the information or footnotes necessary for a complete presentation of financial condition, results of operations, or cash flows in accordance with U.S. GAAP. In our opinion, all adjustments (consisting only of normal recurring adjustments) necessary for a fair presentation have been included. The results of operations for the three and nine months ended September 30, 2014 are not necessarily indicative of the results expected for the year ending December 31, 2014 or any other period. The September 30, 2014 condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes included in the First Internet Bancorp Annual Report on Form 10-K for the year ended December 31, 2013.

The preparation of the condensed consolidated financial statements in conformity with U.S. GAAP requires management to make estimates, judgments, or assumptions that could have a material effect on the carrying value of certain assets and liabilities. These estimates, judgments, and assumptions affect the amounts reported in the condensed consolidated financial statements and the disclosures provided. The determination of the allowance for loan losses, valuations and impairments of investment securities, and the accounting for income tax expense are highly dependent upon management's estimates, judgments, and assumptions where changes in any of these could have a significant impact on the financial statements.

The Company is subject to claims and lawsuits that arise primarily in the ordinary course of business. It is the opinion of management that the disposition or ultimate resolution of such claims and lawsuits will not have a material adverse effect on the consolidated financial position, results of operations, and cash flows of the Company.

The condensed consolidated financial statements include the accounts of First Internet Bancorp (the "Company"), its wholly-owned subsidiary, First Internet Bank of Indiana (the "Bank"), and the Bank's wholly-owned subsidiary, JKH Realty Services, LLC. All significant intercompany accounts and transactions have been eliminated in consolidation.

Certain reclassifications have been made to the 2013 financial statements to conform to the 2014 financial statement presentation. These reclassifications had no effect on net income.

On June 21, 2013, the Company completed a three-for-two (3:2) split of its common stock by the payment of a stock dividend of one-half of one share on each outstanding share of common stock. Except as otherwise indicated, all of the share and per-share information referenced throughout this report has been adjusted to reflect this stock split.

Note 2: Earnings Per Share

Earnings per share of common stock are based on the weighted-average number of basic shares and dilutive shares outstanding during the period.

The following is a reconciliation of the weighted-average common shares for the basic and diluted earnings per share computations for the three and nine months ended September 30, 2014 and 2013:

	Three Months Ended September 30, 2014 2013	
Basic earnings per share		
Net income available to common shareholders	\$ 1,282	\$ 727
Weighted-average common shares	4,497,762	2,890,369
Basic earnings per common share	\$0.29	\$0.25
Diluted earnings per share		
Net income applicable to diluted earnings per share	\$ 1,282	\$ 727
Weighted-average common shares	4,497,762	2,890,369
Dilutive effect of warrants	—	13,447
Dilutive effect of equity compensation	13,529	—
Weighted-average common and incremental shares	4,511,291	2,903,816
Diluted earnings per common share	\$0.28	\$0.25
Number of warrants excluded from the calculation of diluted earnings per share as the exercise prices were greater than the average market price of the Company's common stock during the period	48,750	—
	Nine Months Ended September 30, 2014 2013	
Basic earnings per share		
Net income available to common shareholders	\$ 2,859	\$ 3,927
Weighted-average common shares	4,496,228	2,888,274
Basic earnings per common share	\$0.64	\$ 1.36
Diluted earnings per share		
Net income applicable to diluted earnings per share	\$ 2,859	\$ 3,927
Weighted-average common shares	4,496,228	2,888,274
Dilutive effect of warrants	3,871	765
Dilutive effect of equity compensation	5,702	—
Weighted-average common and incremental shares	4,505,801	2,889,039
Diluted earnings per common share	\$0.63	\$ 1.36
Number of warrants excluded from the calculation of diluted earnings per share as the exercise prices were greater than the average market price of the Company's common stock during the period	—	—

Note 3: Securities

Securities at September 30, 2014 and December 31, 2013 are as follows:

	September 30, 2014			Fair Value
	Amortized Cost	Gross Gains	Unrealized Losses	
Securities available-for-sale				
U.S. Government-sponsored enterprises	\$ 16,049	\$ 122	\$(446)	) \$ 15,725
Mortgage-backed and asset-backed securities – government-sponsored enterprises	111,524	50	(1,085)	) 110,489
Other securities	2,000	—	(11)	) 1,989
Total available-for-sale	\$ 129,573	\$ 172	\$(1,542)	) \$ 128,203
	December 31, 2013			Fair Value
	Amortized Cost	Gross Gains	Unrealized Losses	
Securities available-for-sale				
U.S. Government-sponsored enterprises	\$ 57,569	\$ 470	\$(1,762)	) \$ 56,277
Municipal securities	46,126	1,080	(883)	) 46,323
Mortgage-backed and asset-backed securities – government-sponsored enterprises	75,058	696	(1,813)	) 73,941
Mortgage-backed and asset-backed securities – private labeled	1,313	9	(90)	) 1,232
Other securities	5,025	—	(1,389)	) 3,636
Total available-for-sale	\$ 185,091	\$ 2,255	\$(5,937)	) \$ 181,409

The carrying value of securities at September 30, 2014 is shown below by their contractual maturity date. Actual maturities will differ because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Available-for-Sale	
	Amortized Cost	Fair Value
Within one year	\$ 2,000	\$ 1,989
One to five years	—	—
Five to ten years	814	803
After ten years	15,235	14,922
	18,049	17,714
Mortgage-backed and asset-backed securities – government-sponsored enterprises	111,524	110,489
Totals	\$ 129,573	\$ 128,203

Gross gains of \$450 and \$104, and gross losses of \$396 and \$7 resulting from sales of available-for-sale securities were realized for the three months ended September 30, 2014 and 2013, respectively. In the nine months ended September 30, 2014 and 2013, gross gains of \$2,749 and \$278 and gross losses of \$2,211 and \$347 were recognized, respectively.

Certain investments in debt securities are reported in the condensed consolidated financial statements at an amount less than their historical cost. Total fair value of these investments at September 30, 2014 and December 31, 2013 was \$107,243 and \$109,946, which is approximately 84% and 61%, respectively, of the Company's available-for-sale investment portfolio. These declines primarily resulted from fluctuations in market interest rates after purchase.

Except as discussed below, management believes the declines in fair value for these securities are temporary.

Should the impairment of any of these securities become other-than-temporary, the cost basis of the investment will be reduced and the resulting loss recognized in net income in the period in which the other-than-temporary impairment (“OTTI”) is identified.

The following tables show the Company’s investments’ gross unrealized losses and fair value, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position at September 30, 2014 and December 31, 2013:

	September 30, 2014					
	Less Than 12 Months		12 Months or Longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Securities available for sale:						
U.S. Government-sponsored enterprises	\$803	\$(11)	\$8,729	\$(435)	\$9,532	\$(446)
Mortgage-backed and asset-backed securities - government-sponsored enterprises	74,317	(365)	21,405	(720)	95,722	(1,085)
Other securities	1,989	(11)	—	—	1,989	(11)
	\$77,109	\$(387)	\$30,134	\$(1,155)	\$107,243	\$(1,542)
	December 31, 2013					
	Less Than 12 Months		12 Months or Longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Securities available for sale:						
U.S. Government-sponsored enterprises	\$43,085	\$(1,761)	\$14	\$(1)	\$43,099	\$(1,762)
Municipal securities	14,105	(882)	351	(1)	14,456	(883)
Mortgage-backed and asset-backed securities - government-sponsored enterprises	47,875	(1,813)	—	—	47,875	(1,813)
Mortgage-backed and asset-backed securities – private labeled	43	(1)	838	(89)	881	(90)
Other securities	1,962	(38)	1,673	(1,351)	3,635	(1,389)
	\$107,070	\$(4,495)	\$2,876	\$(1,442)	\$109,946	\$(5,937)

U.S. Government Sponsored Enterprise and Municipal Securities

The unrealized losses on the Company’s investments in securities issued by U.S. Government-sponsored enterprises and municipal securities were caused by interest rate changes. The contractual terms of those investments do not permit the issuer to settle the securities at a price less than the amortized cost bases of the investments. Because the Company does not intend to sell the investments at a loss and it is not more likely than not the Company will be required to sell the investments before recovery of their amortized cost bases, which may be maturity, the Company does not consider those investments to be other-than-temporarily impaired at September 30, 2014.

Mortgage-Backed Securities

The unrealized losses on the Company's investments in mortgage-backed securities were caused by interest rate changes. The Company expects to recover the amortized cost bases over the term of the securities. Because the decline in market value is attributable to changes in interest rates and not credit quality, and because the Company does not intend to sell the investments at a loss and it is not more likely than not the Company will be required to sell the investments before

recovery of their amortized cost bases, which may be maturity, the Company does not consider those investments to be other-than-temporarily impaired at September 30, 2014.

For identified mortgage-backed securities in the investment portfolio, an extensive, quarterly review is conducted to determine if an other-than-temporary impairment has occurred. Various inputs to the economic models are used to determine if an unrealized loss is other-than-temporary. The most significant inputs are voluntary prepayment rates, default rates, liquidation rates, and loss severity.

To determine if the unrealized loss for mortgage-backed securities is other-than-temporary, the Company projects total estimated defaults of the underlying assets (mortgages) and multiplies that calculated amount by an estimate of realizable value upon sale in the marketplace (severity) in order to determine the projected collateral loss. The Company also evaluates the current credit enhancement underlying the security to determine the impact on cash flows. If the Company determines that a given mortgage-backed security position will be subject to a write-down or loss, the Company records the expected credit loss as a charge to earnings.

Other Securities

The Company's unrealized loss on investments in other securities at December 31, 2013 primarily consists of two investments, both of which were sold in the second quarter of 2014.

The first investment was a \$2,000 par investment in I-PreTSL I B-2 pooled trust security. The unrealized loss was primarily caused by a sector downgrade by several industry analysts. The determination of no credit loss was calculated by comparing expected discounted cash flows based on performance indicators of the underlying assets in the security to the carrying value of the investment.

The second investment was a \$2,000 par investment in ALESCO IV Series B2 pooled trust security for which the Company recognized an other-than-temporary impairment loss. The unrealized loss was primarily caused by: (a) a decrease in performance; and (b) a sector downgrade by several industry analysts. The credit loss was calculated by comparing expected discounted cash flows based on performance indicators of the underlying assets in the security to the carrying value of the investment.

The Company did not recognize any credit losses in earnings during the three months ended September 30, 2014 and 2013. The credit losses recognized in earnings during the nine months ended September 30, 2014 and 2013 were as follows:

	Nine Months Ended September 30,	
	2014	2013
Mortgage-backed and asset-backed securities – private labeled	—	49
Total credit losses recognized in earnings	\$—	\$49

Credit Losses Recognized on Investments

Certain debt securities have experienced fair value deterioration due to credit losses, as well as due to other market factors, but are not considered other-than-temporarily impaired.

The following tables provide information about debt securities for which only a credit loss was recognized in income and other losses are recorded in accumulated other comprehensive loss. The Company did not own any OTTI securities during the three months ended September 30, 2014.

	Accumulated Credit Losses
Credit losses on debt securities held	
July 1, 2013	\$1,342
Realized losses related to OTTI	(98)
Recoveries related to OTTI	—
Additions related to OTTI losses not previously recognized	—
Additions related to increases in previously recognized OTTI losses	—
September 30, 2013	\$1,244
	Accumulated Credit Losses
Credit losses on debt securities held	
January 1, 2014	\$1,183
Realized losses related to OTTI	(1,139)
Recoveries related to OTTI	(44)
Additions related to OTTI losses not previously recognized	—
Additions related to increases in previously recognized OTTI losses	—
September 30, 2014	\$—
	Accumulated Credit Losses
Credit losses on debt securities held	
January 1, 2013	\$1,737
Realized losses related to OTTI	(542)
Recoveries related to OTTI	—
Additions related to OTTI losses not previously recognized	31
Additions related to increases in previously recognized OTTI losses	18
September 30, 2013	\$1,244

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Amounts reclassified from accumulated other comprehensive loss and the affected line items in the condensed consolidated statements of income during the three and nine months ended September 30, 2014 and 2013, were as follows:

	Amounts Reclassified from Accumulated Other Comprehensive Loss for the Three Months Ended September 30,		Affected Line Item in the Statements of Income
	2014	2013	
Securities available for sale			
Gain realized in earnings	\$54	\$97	Gain (loss) on sale of securities
OTTI losses recognized in earnings	—	—	Other-than-temporary impairment loss recognized in net income
Total reclassified amount before tax	54	97	Income Before Income Taxes
Tax expense	18	34	Income Tax Provision
Total reclassifications out of accumulated other comprehensive loss	\$36	\$63	Net Income
	Amounts Reclassified from Accumulated Other Comprehensive Loss for the Nine Months Ended September 30,		Affected Line Item in the Statements of Income
	2014	2013	
Securities available for sale			
Gain (loss) realized in earnings	\$538	\$(69)	) Gain (loss) on sale of securities
OTTI losses recognized in earnings	—	(49)	) Other-than-temporary impairment loss recognized in net income
Total reclassified amount before tax	538	(118)	) Income Before Income Taxes
Tax expense (benefit)	183	(41)	) Income Tax Provision
Total reclassifications out of accumulated other comprehensive loss	\$355	\$(77)	) Net Income

Note 4: Loans Receivable

Loans that management intends to hold until maturity are reported at their outstanding principal balance adjusted for unearned income, charge-offs, the allowance for loan losses, any unamortized deferred fees or costs on originated loans, and unamortized premiums or discounts on purchased loans.

For loans recorded at cost, interest income is accrued based on the unpaid principal balance. Loan origination fees, net of certain direct origination costs, as well as premiums and discounts, are deferred and amortized as a level yield adjustment over the respective term of the loan.

Categories of loans include:

	September 30, 2014	December 31, 2013
Real estate loans		
Residential	\$282,298	\$191,007
Commercial	235,878	142,429
Total real estate loans	518,176	333,436
Commercial loans	72,099	55,168
Consumer loans	100,074	107,562
Total loans	690,349	496,166
Deferred loan origination costs and premiums and discounts on purchased loans	5,580	4,987
Allowance for loan losses	(5,464)	(5,426)
Net loans receivable	\$690,465	\$495,727

The risk characteristics of each loan portfolio segment are as follows:

Commercial Real Estate: These loans are viewed primarily as cash flow loans and secondarily as loans secured by real estate. These loans may also incorporate a personal guarantee. Commercial real estate lending typically involves higher loan principal amounts, and the repayment of these loans is generally dependent on the successful operation of the property securing the loan or the business conducted on the property securing the loan. Commercial real estate loans may be more adversely affected by conditions in the real estate markets or in the general economy. The properties securing the Company's commercial real estate portfolio are diverse in terms of property type and geographic location. Management monitors and evaluates commercial real estate loans based on property financial performance, collateral value, and other risk grade criteria. As a general rule, the Company avoids financing special use projects or properties outside of its designated market areas unless other underwriting factors are present to help mitigate risk. In addition, management tracks the level of owner-occupied commercial real estate loans versus non-owner-occupied loans.

Commercial: Commercial loans are primarily based on the identified cash flows of the borrower and secondarily on the underlying collateral provided by the borrower. The cash flows of borrowers, however, may not be as expected, and the collateral securing these loans may fluctuate in value. Loans are made for working capital, equipment purchases, or other purposes. Most commercial loans are secured by the assets being financed and may incorporate a personal guarantee; however, some short-term loans may be made on an unsecured basis.

Residential and Consumer: With respect to residential loans that are secured by 1-4 family residences and are generally owner occupied, the Company generally establishes a maximum loan-to-value ratio and requires private mortgage insurance if that ratio is exceeded. Home equity loans are typically secured by a subordinate interest in 1-4 family residences. The properties securing the Company's residential loan portfolio are generally geographically diverse as the Company offers these loans on a nationwide basis. Repayment on residential loans can be impacted by changes in property values on residential properties. Consumer loans are secured by consumer assets such as horse trailers, recreational vehicles, or automobiles. Some consumer loans are unsecured, such as small installment loans and certain lines of credit. Repayment of consumer loans is primarily dependent upon the personal income of the borrowers, which can be impacted by economic conditions in their market areas such as unemployment levels. Risk is mitigated by the fact that the loans are of smaller individual amounts and spread over a large number of borrowers in geographically diverse locations throughout the country.

Allowance for Loan Losses Methodology

Company policy is designed to ensure that an adequate allowance for loan losses (“ALLL”) is maintained. The portfolio is segmented by loan type. The required ALLL for types of performing homogeneous loans which do not have a specific reserve is determined by applying a factor based on historical losses averaged over the past twelve months. Management believes the historical loss experience methodology is appropriate in the current economic environment, as it captures loss rates that are comparable to the current period being analyzed. Management adds qualitative factors for observable trends, changes in internal practices, changes in delinquencies and impairments, and external factors. Observable factors include changes in the composition and size of portfolios, as well as loan terms or concentration levels. The Company evaluates the impact of internal changes such as management and staff experience levels or modification to loan underwriting processes. Delinquency trends are scrutinized for both volume and severity of past due, nonaccrual, classified, or graded loans as well as any changes in the value of underlying collateral. Finally, the Company considers the effect of other external factors such as national, regional, and local economic and business conditions, as well as competitive, legal, and regulatory requirements. Loans that are considered to be impaired are evaluated to determine the need for a specific allowance by applying at least one of three methodologies: present value of future cash flows; fair value of collateral less cost to sell; or the loan’s observable market price. All troubled debt restructurings (“TDR”) are considered impaired loans. Loans evaluated for impairment are removed from other pools to prevent double-counting.

Provision (Credit) for Loan Losses

A provision for estimated losses on loans is charged to operations based upon management’s evaluation of the potential losses. Such an evaluation, which includes a review of all loans for which full collectability may not be reasonably assured considers, among other matters, the estimated net realizable value of the underlying collateral, as applicable, economic conditions, loan loss experience, and other factors that are particularly susceptible to changes that could result in a material adjustment in the near term. While management endeavors to use the best information available in making its evaluations, future allowance adjustments may be necessary if economic conditions change substantially from the assumptions used in making the evaluations.

Accounting Standards Codification (“ASC”) Topic 310, Receivables, requires that impaired loans be measured based on the present value of expected future cash flows discounted at the loans’ effective interest rates or the fair value of the underlying collateral and allows existing methods for recognizing interest income.

Policy for Charging Off Loans

The Company’s policy is to charge off a loan at any point in time when it no longer can be considered a bankable asset, meaning collectible within the parameters of policy. A secured loan is generally charged off to the estimated fair value of the collateral, less costs to sell, no later than when it is 120 days past due as to principal or interest. An unsecured loan generally is charged off no later than when it is 180 days past due as to principal or interest.

The following tables present changes in the balance of the ALLL during the three and nine month periods ended September 30, 2014 and 2013:

	Three Months Ended September 30, 2014				
	Residential Real Estate	Commercial Real Estate	Commercial	Consumer	Total
Allowance for loan losses:					
Balance, beginning of period	\$1,203	\$2,395	\$735	\$807	\$5,140
Provision (credit) charged to expense	53	(248	) 188	(105	) (112
Losses charged off	(5	) —	(14	) (92	) (111

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Recoveries	7	459	—	81	547
Balance, end of period	\$1,258	\$2,606	\$909	\$691	\$5,464

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	Nine Months Ended September 30, 2014				
	Residential Real Estate	Commercial Real Estate	Commercial	Consumer	Total
Allowance for loan losses:					
Balance, beginning of period	\$1,219	\$2,517	\$819	\$871	\$5,426
Provision (credit) charged to expense	224	(370)	) 104	4	(38)
Losses charged off	(216)	) —	(14)	) (427)	) (657)
Recoveries	31	459	—	243	733
Balance, end of period	\$1,258	\$2,606	\$909	\$691	\$5,464

	Three Months Ended September 30, 2013				
	Residential Real Estate	Commercial Real Estate	Commercial	Consumer	Total
Allowance for loan losses:					
Balance, beginning of period	\$984	\$2,918	\$547	\$1,078	\$5,527
Provision (credit) charged to expense	33	(36)	) 168	(222)	) (57)
Losses charged off	(18)	) —	—	(175)	) (193)
Recoveries	73	—	—	109	182
Balance, end of period	\$1,072	\$2,882	\$715	\$790	\$5,459

	Nine Months Ended September 30, 2013				
	Residential Real Estate	Commercial Real Estate	Commercial	Consumer	Total
Allowance for loan losses:					
Balance, beginning of period	\$1,149	\$3,107	\$371	\$1,206	\$5,833
Provision (credit) charged to expense	(97)	) 13	274	(89)	) 101
Losses charged off	(72)	) (238)	) —	(573)	) (883)
Recoveries	92	—	70	246	408
Balance, end of period	\$1,072	\$2,882	\$715	\$790	\$5,459

The following tables present the recorded investment in loans based on portfolio segment and impairment method as of September 30, 2014, and December 31, 2013:

	September 30, 2014				
	Residential Real Estate	Commercial Real Estate	Commercial	Consumer	Total
Loans:					
Ending balance	\$282,298	\$235,878	\$72,099	\$100,074	\$690,349
Ending balance: individually evaluated for impairment	1,080	89	—	283	1,452
Ending balance: collectively evaluated for impairment	\$281,218	\$235,789	\$72,099	\$99,791	\$688,897
Allowance for loan losses:					
Ending balance	\$1,258	\$2,606	\$909	\$691	\$5,464
Ending balance: individually evaluated for impairment	7	—	—	22	29
Ending balance: collectively evaluated for impairment	\$1,251	\$2,606	\$909	\$669	\$5,435

	December 31, 2013				
	Residential Real Estate	Commercial Real Estate	Commercial	Consumer	Total
Loans:					
Ending balance	\$ 191,007	\$ 142,429	\$ 55,168	\$ 107,562	\$ 496,166
Ending balance: individually evaluated for impairment	1,684	1,054	—	339	3,077
Ending balance: collectively evaluated for impairment	\$ 189,323	\$ 141,375	\$ 55,168	\$ 107,223	\$ 493,089
Allowance for loan losses:					
Ending balance	\$ 1,219	\$ 2,517	\$ 819	\$ 871	\$ 5,426
Ending balance: individually evaluated for impairment	116	98	—	28	242
Ending balance: collectively evaluated for impairment	\$ 1,103	\$ 2,419	\$ 819	\$ 843	\$ 5,184

The Company utilizes a risk grading matrix to assign a risk grade to each of its commercial loans. Loans are graded on a scale of 1 to 9. A description of the general characteristics of the nine risk grades is as follows:

•“Pass” (Grades 1-5) - Higher quality loans that do not fit any of the other categories described below.

•“Special Mention” (Grade 6) - Loans that possess some credit deficiency or potential weakness which deserve close attention.

•“Substandard” (Grade 7) - Loans that possess a defined weakness or weaknesses that jeopardize the liquidation of the debt. Loans characterized by the distinct possibility that the institution will sustain some loss if the deficiencies are not corrected. Loans that are inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any.

•“Doubtful” (Grade 8) - Such loans have been placed on nonaccrual status and may be heavily dependent upon collateral possessing a value that is difficult to determine or based upon some near-term event which lacks clear certainty. These loans have all of the weaknesses of those classified as Substandard; however, based on existing conditions, these weaknesses make full collection of the principal balance highly improbable.

•“Loss” (Grade 9) - Loans that are considered uncollectible and of such little value that continuing to carry them as assets is not warranted.

Nonaccrual Loans

Any loan which becomes 90 days delinquent or has the full collection of principal and interest in doubt will be considered for nonaccrual status. At the time a loan is placed on nonaccrual, all accrued but unpaid interest will be reversed from interest income. Placing the loan on nonaccrual does not relieve the borrower of the obligation to repay interest. A loan placed on nonaccrual may be restored to accrual status when all delinquent principal and interest has been brought current, and the Company expects full payment of the remaining contractual principal and interest.

The following tables present the credit risk profile of the Company’s loan portfolio based on rating category and payment activity as of September 30, 2014 and December 31, 2013:

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	September 30, 2014	
	Commercial Real Estate	Commercial
Rating:		
1-5 Pass	\$233,437	\$69,649
6 Special Mention	815	—
7 Substandard	1,626	2,450
8 Doubtful	—	—
Total	\$235,878	\$72,099

	September 30, 2014	
	Residential Real Estate	Consumer
Performing	\$282,241	\$99,921
Nonaccrual	57	153
Total	\$282,298	\$100,074

	December 31, 2013	
	Commercial Real Estate	Commercial
Rating:		
1-5 Pass	\$139,052	\$54,035
6 Special Mention	2,323	1,133
7 Substandard	1,054	—
8 Doubtful	—	—
Total	\$142,429	\$55,168

	December 31, 2013	
	Residential Real Estate	Consumer
Performing	\$190,377	\$107,412
Nonaccrual	630	150
Total	\$191,007	\$107,562

The following tables present the Company's loan portfolio delinquency analysis as of September 30, 2014 and December 31, 2013:

	September 30, 2014							
	30-59 Days Past Due	60-89 Days Past Due	90 Days or More Past Due	Total Past Due	Current	Total Loans Receivable	Non-accrual Loans	Total Loans 90 Days or More Past Due and Accruing
Residential real estate	\$48	\$160	\$96	\$304	\$281,994	\$282,298	\$57	\$96
Commercial real estate	—	—	—	—	235,878	235,878	89	—
Commercial	—	—	—	—	72,099	72,099	—	—
Consumer	296	93	55	444	99,630	100,074	153	5
Total	\$344	\$253	\$151	\$748	\$689,601	\$690,349	\$299	\$101

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December 31, 2013

	30-59 Days Past Due	60-89 Days Past Due	90 Days or More Past Due	Total Past Due	Current	Total Loans Receivable	Non- accrual Loans	Total Loans 90 Days or More Past Due and Accruing
Residential real estate	\$ 122	\$—	\$ 603	\$ 725	\$ 190,282	\$ 191,007	\$ 630	\$—
Commercial real estate	—	—	955	955	141,474	142,429	1,054	—
Commercial	—	—	—	—	55,168	55,168	—	—
Consumer	484	45	84	613	106,949	107,562	150	18
Total	\$ 606	\$ 45	\$ 1,642	\$ 2,293	\$ 493,873	\$ 496,166	\$ 1,834	\$ 18

Impaired Loans

A loan is designated as impaired, in accordance with the impairment accounting guidance (ASC 310-10-35-16) when, based on current information or events, it is probable that the Company will be unable to collect all amounts due (principal and interest) according to the contractual terms of the loan agreement. Payments with delays generally not exceeding 90 days outstanding are not considered impaired. Certain nonaccrual and substantially all delinquent loans more than 90 days past due may be considered to be impaired. Generally, loans are placed on nonaccrual status at 90 days past due and accrued interest is reversed against earnings, unless the loan is well-secured and in the process of collection. The accrual of interest on impaired and nonaccrual loans is discontinued when, in management's opinion, the borrower may be unable to meet payments as they become due.

Impaired loans include nonperforming commercial loans but also include loans modified in TDRs where concessions have been granted to borrowers experiencing financial difficulties. These concessions could include a reduction in the interest rate on the loan, payment extensions, forgiveness of principal, forbearance, or other actions intended to maximize collection.

The following table presents the Company's impaired loans as of September 30, 2014 and December 31, 2013:

	September 30, 2014			December 31, 2013		
	Recorded Balance	Unpaid Principal Balance	Specific Allowance	Recorded Balance	Unpaid Principal Balance	Specific Allowance
Loans without a specific valuation allowance						
Residential real estate loans	\$ 1,048	\$ 1,057	\$—	\$ 1,551	\$ 1,842	\$—
Commercial real estate loans	89	89	—	956	2,310	—
Commercial loans	—	—	—	—	—	—
Consumer loans	222	368	—	271	326	—
Total	1,359	1,514	—	2,778	4,478	—
Loans with a specific valuation allowance						
Residential real estate loans	32	32	7	133	141	116
Commercial real estate loans	—	—	—	98	—	—