

MIDDLEFIELD BANC CORP
Form 10-Q
November 14, 2016

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20552

FORM 10 - Q

**QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT
OF 1934**

For the quarterly period ended September 30, 2016

Commission File Number 001-36613

Middlefield Banc Corp.

(Exact name of registrant as specified in its charter)

Ohio **34 - 1585111**
**(State or other jurisdiction of incorporation (IRS Employer Identification No.)
or organization)**

15985 East High Street, Middlefield, Ohio 44062-9263

(Address of principal executive offices)

(440) 632-1666

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d)

of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

YES [] NO []

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (Section 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 or a smaller reporting company. See the definition of "large accelerated filer", "accelerated filer", and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer [] Accelerated filer [] Non-accelerated filer [] Small 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 []

State the number of shares outstanding of each of the issuer's classes of common equity as of the latest practicable date:

Class: Common Stock, without par value

Outstanding at November 10, 2016: 2,250,707

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MIDDLEFIELD BANC CORP.

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MIDDLEFIELD BANC CORP.

CONSOLIDATED BALANCE SHEET

(Dollar amounts in thousands, except share data)

(Unaudited)

	September 30, 2016	December 31, 2015
ASSETS		
Cash and due from banks	\$ 21,976	\$ 22,421
Federal funds sold	1,300	1,329
Cash and cash equivalents	23,276	23,750
Investment securities available for sale, at fair value	123,054	146,520
Loans held for sale	880	1,107
Loans	586,329	533,710
Less allowance for loan and lease losses	6,334	6,385
Net loans	579,995	527,325
Premises and equipment, net	9,921	9,772
Goodwill	4,559	4,559
Core deposit intangibles	46	76
Bank-owned life insurance	13,438	13,141
Other real estate owned	1,205	1,412
Accrued interest and other assets	5,884	7,477
TOTAL ASSETS	762,258	735,139
LIABILITIES		
Deposits:		
Noninterest-bearing demand	\$ 136,320	\$ 116,498
Interest-bearing demand	67,061	57,219
Money market	77,774	78,856
Savings	173,272	180,653
Time	184,915	191,221
Total deposits	639,342	624,447
Short-term borrowings	32,803	35,825
Other borrowings	9,713	9,939
Accrued interest and other liabilities	2,208	2,624
TOTAL LIABILITIES	684,066	672,835
STOCKHOLDERS' EQUITY		
Common stock, no par value; 10,000,000 shares authorized, 2,636,830 and 2,263,403 shares issued; 2,250,665 and 1,877,238 shares outstanding	47,812	36,191

Retained earnings	40,282	37,236
Accumulated other comprehensive income	3,616	2,395
Treasury stock, at cost; 386,165 shares	(13,518)	(13,518)
TOTAL STOCKHOLDERS' EQUITY	78,192	62,304
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	\$ 762,258	\$ 735,139

See accompanying notes to unaudited consolidated financial statements.

MIDDLEFIELD BANC CORP.

CONSOLIDATED STATEMENT OF INCOME

(Dollar amounts in thousands, except per share data)

(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
INTEREST AND DIVIDEND INCOME				
Interest and fees on loans	\$6,459	\$5,971	\$18,949	\$17,656
Interest-bearing deposits in other institutions	15	6	42	26
Federal funds sold	7	4	16	12
Investment securities:				
Taxable interest	235	341	865	1,115
Tax-exempt interest	687	809	2,227	2,373
Dividends on stock	17	20	74	70
Total interest and dividend income	7,420	7,151	22,173	21,252
INTEREST EXPENSE				
Deposits	921	876	2,665	2,581
Short-term borrowings	49	30	288	100
Other borrowings	14	20	47	66
Trust preferred securities	42	33	117	85
Total interest expense	1,026	959	3,117	2,832
NET INTEREST INCOME	6,394	6,192	19,056	18,420
Provision for loan losses	105	105	315	210
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	6,289	6,087	18,741	18,210
NONINTEREST INCOME				
Service charges on deposit accounts	505	471	1,443	1,382
Investment securities gains, net	-	211	303	257
Earnings on bank-owned life insurance	101	101	297	262
Gain on sale of loans	129	113	322	286
Other income	242	212	694	679
Total noninterest income	977	1,108	3,059	2,866
NONINTEREST EXPENSE				
Salaries and employee benefits	2,677	2,285	7,740	7,205

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Occupancy expense	306	305	933	945
Equipment expense	221	249	700	706
Data processing costs	334	287	928	798
Ohio state franchise tax	186	75	448	225
Federal deposit insurance expense	132	120	396	352
Professional fees	547	229	1,057	825
Loss (gain) on other real estate owned	(49)	24	(52)	72
Advertising expense	206	195	604	586
Other real estate expense	97	116	299	449
Directors fees	102	98	330	343
Core deposit intangible amortization	10	10	30	30
Appraiser fees	114	97	334	327
ATM fees	102	89	296	295
Other expense	677	490	1,872	1,539
Total noninterest expense	5,662	4,669	15,915	14,697
Income before income taxes	1,604	2,526	5,885	6,379
Income taxes	261	544	1,129	1,264
NET INCOME	\$1,343	\$1,982	\$4,756	\$5,115
EARNINGS PER SHARE				
Basic	\$0.60	\$0.96	\$2.31	\$2.49
Diluted	0.60	0.96	2.30	2.47
DIVIDENDS DECLARED PER SHARE	\$0.27	\$0.27	\$0.81	\$0.80

See accompanying notes to unaudited consolidated financial statements.

MIDDLEFIELD BANC CORP.

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

(Dollar amounts in thousands)

(Unaudited)

	Three Months Ended September 30, 2016		Nine Months Ended September 30, 2016		
	2015	2016	2015	2016	
Net income		\$1,343	\$1,982	\$4,756	\$5,115
Other comprehensive income (loss):					
Net unrealized holding gain (loss) on available-for-sale securities		(400)	1,416	2,153	(699)
Tax effect		137	(481)	(732)	238
Reclassification adjustment for investment securities gains included in net income		-	(211)	(303)	(257)
Tax effect		-	71	103	87
Total other comprehensive income (loss)		(263)	795	1,221	(631)
Comprehensive income		\$1,080	\$2,777	\$5,977	\$4,484

See accompanying notes to unaudited consolidated financial statements.

MIDDLEFIELD BANC CORP.

CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS EQUITY

(Dollar amounts in thousands, except share data)

(Unaudited)

	Common Stock	Retained Earnings	Accumulated Other Comprehensive Income	Treasury Stock	Total Stockholders' Equity
Balance, December 31, 2015	\$ 36,191	\$ 37,236	\$ 2,395	\$(13,518)	\$ 62,304
Net income		4,756			4,756
Other comprehensive income			1,221		1,221
Common stock issuance, net of offering cost (360,815 shares)	11,239				11,239
Dividend reinvestment and purchase plan (11,712 shares)	382				382
Cash dividends (\$0.81 per share)		(1,710)			(1,710)
Balance, September 30, 2016	\$ 47,812	\$ 40,282	\$ 3,616	\$(13,518)	\$ 78,192

See accompanying notes to unaudited consolidated financial statements.

MIDDLEFIELD BANC CORP.

CONSOLIDATED STATEMENT OF CASH FLOWS

(Dollar amounts in thousands)

(Unaudited)

	Nine Months Ended September 30,	
	2016	2015
OPERATING ACTIVITIES		
Net income	\$4,756	\$5,115
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	315	210
Investment securities gain, net	(303)	(257)
Depreciation and amortization	774	763
Amortization of premium and discount on investment securities	352	553
Accretion of deferred loan fees, net	(150)	(468)
Origination of loans held for sale	(15,497)	(14,740)
Proceeds from sale of loans	16,046	14,844
Gain on sale of loans	(322)	(286)
Earnings on bank-owned life insurance	(297)	(262)
Deferred income tax	224	397
Loss (gain) on sale of other real estate owned	(52)	72
Other real estate owned writedowns	73	56
Increase in accrued interest receivable	(139)	(481)
(Decrease) increase in accrued interest payable	(4)	58
Other, net	253	(158)
Net cash provided by operating activities	6,029	5,416
INVESTING ACTIVITIES		
Investment securities available for sale:		
Proceeds from repayments and maturities	17,896	7,530
Proceeds from sale of securities	9,115	15,284
Purchases	(1,744)	(14,876)
Increase in loans, net	(53,430)	(40,554)
Proceeds from the sale of other real estate owned	781	1,094
Purchase of bank-owned life insurance	-	(4,000)
Purchase of premises and equipment	(679)	(454)
Net cash used for investing activities	(28,061)	(35,976)
FINANCING ACTIVITIES		
Net increase in deposits	14,895	40,436
Decrease in short-term borrowings, net	(3,022)	(10,761)
Repayment of other borrowings	(226)	(324)

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Common stock issued	11,239	-
Stock options exercised	-	6
Proceeds from dividend reinvestment and purchase plan	382	504
Cash dividends	(1,710)	(1,645)
Net cash provided by financing activities	21,558	28,216
Decrease in cash and cash equivalents	(474)	(2,344)
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	23,750	25,639
CASH AND CASH EQUIVALENTS AT END OF PERIOD	\$23,276	\$23,295
SUPPLEMENTAL INFORMATION		
Cash paid during the year for:		
Interest on deposits and borrowings	\$3,121	\$2,774
Income taxes	475	350
Noncash investing transactions:		
Transfers from loans to other real estate owned	\$595	\$638

See accompanying notes to unaudited consolidated financial statements.

MIDDLEFIELD BANC CORP.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 - BASIS OF PRESENTATION

The consolidated financial statements of Middlefield Banc Corp. ("Company") include its bank subsidiary, The Middlefield Banking Company ("MB"), and a nonbank asset resolution subsidiary EMORECO, Inc. All significant inter-company items have been eliminated.

The accompanying unaudited financial statements have been prepared in accordance with U.S. generally accepted accounting principles and the instructions for Form 10-Q and Article 10 of Regulation S-X. In management's opinion, the financial statements include all adjustments, consisting of normal recurring adjustments, that the Company considers necessary to fairly state the Company's financial position and the results of operations and cash flows. The consolidated balance sheet at December 31, 2015, has been derived from the audited financial statements at that date but does not include all of the necessary informational disclosures and footnotes as required by U.S. generally accepted accounting principles. The accompanying financial statements should be read in conjunction with the financial statements and notes thereto included with the Company's Form 10-K for the year ended December 31, 2015. The results of the Company's operations for any interim period are not necessarily indicative of the results of the Company's operations for any other interim period or for a full fiscal year.

Recent Accounting Pronouncements –

In May 2014, the FASB issued ASU 2014-09, *Revenue from Contracts with Customers* (a new revenue recognition standard). The Update's core principle is that a company will recognize revenue to depict the transfer of goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. In addition, this Update specifies the accounting for certain costs to obtain or fulfill a contract with a customer and expands disclosure requirements for revenue recognition. This Update is effective for annual reporting periods beginning after December 15, 2016, including interim periods within that reporting period. The Company is currently evaluating the impact the adoption of the standard will have on the Company's financial position or results of operations.

In June 2014, the FASB issued ASU 2014-12, *Compensation – Stock Compensation (Topic 718): Accounting for Share-Based Payments when the Terms of an Award Provide that a Performance Target Could Be Achieved After the*

Requisite Service Period. The amendments require that a performance target that affects vesting and that could be achieved after the requisite service period be treated as a performance condition. The amendments in this Update are effective for annual periods and interim periods within those annual periods beginning after December 15, 2015. Earlier adoption is permitted. Entities may apply the amendments in this Update either (a) prospectively to all awards granted or modified after the effective date or (b) retrospectively to all awards with performance targets that are outstanding as of the beginning of the earliest annual period presented in the financial statements and to all new or modified awards thereafter. If retrospective transition is adopted, the cumulative effect of applying this Update as of the beginning of the earliest annual period presented in the financial statements should be recognized as an adjustment to the opening retained earnings balance at that date. Additionally, if retrospective transition is adopted, an entity may use hindsight in measuring and recognizing the compensation cost. This Update is not expected to have a significant impact on the Company's financial statements, or the Company is currently evaluating the impact the adoption of the standard will have on the Company's financial position or results of operations.

In August 2015, the FASB issued ASU 2015-14, *Revenue from Contracts with Customers (Topic 606)*. The amendments in this Update defer the effective date of ASU 2014-09 for all entities by one year. Public business entities, certain not-for-profit entities, and certain employee benefit plans should apply the guidance in ASU 2014-09 to annual reporting periods beginning after December 15, 2017, including interim reporting periods within that reporting period. All other entities should apply the guidance in ASU 2014-09 to annual reporting periods beginning after December 15, 2018, and interim reporting periods within annual reporting periods beginning after December 15, 2019. The Company is evaluating the effect of adopting this new accounting Update.

In January 2016, the FASB issued ASU 2016-01, *Financial Instruments – Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities*. This Update applies to all entities that hold financial assets or owe financial liabilities and is intended to provide more useful information on the recognition, measurement, presentation, and disclosure of financial instruments. Among other things, this Update (a) requires equity investments (except those accounted for under the equity method of accounting or those that result in consolidation of the investee) to be measured at fair value with changes in fair value recognized in net income; (b) simplifies the impairment assessment of equity investments without readily determinable fair values by requiring a qualitative assessment to identify impairment; (c) eliminates the requirement to disclose the fair value of financial instruments measured at amortized cost for entities that are not public business entities; (d) eliminates the requirement for public business entities to disclose the method(s) and significant assumptions used to estimate the fair value that is required to be disclosed for financial instruments measured at amortized cost on the balance sheet; (e) requires public business entities to use the exit price notion when measuring the fair value of financial instruments for disclosure purposes; (f) requires 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 in accordance with the fair value option for financial instruments; (g) requires separate presentation of financial assets and financial liabilities by measurement category and form of financial asset (that is, securities or loans and receivables) on the balance sheet or the accompanying notes to the financial statements; and (h) clarifies that an entity should evaluate the need for a valuation allowance on a deferred tax asset related to available-for-sale securities in combination with the entity's other deferred tax assets. For public business entities, the amendments in this Update are effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. For all other entities, including not-for-profit entities and employee benefit plans within the scope of Topics 960 through 965 on plan accounting, the amendments in this Update are effective for fiscal years beginning after December 15, 2018, and interim periods within fiscal years beginning after December 15, 2019. All entities that are not public business entities may adopt the amendments in this Update earlier as of the fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. The Company is currently evaluating the impact the adoption of the standard will have on the Company's financial position or results of operations.

In February 2016, the FASB issued ASU 2016-02, *Leases (Topic 842)*. The standard requires lessees to recognize the assets and liabilities that arise from leases on the balance sheet. A lessee should recognize in the statement of financial position a liability to make lease payments (the lease liability) and a right-of-use asset representing its right to use the underlying asset for the lease term. A short-term lease is defined as one in which (a) the lease term is 12 months or less and (b) there is not an option to purchase the underlying asset that the lessee is reasonably certain to exercise. For short-term leases, lessees may elect to recognize lease payments over the lease term on a straight-line basis. For public business entities, the amendments in this Update are effective for fiscal years beginning after December 15, 2018, and interim periods within those years. For all other entities, the amendments in this Update are effective for fiscal years beginning after December 15, 2019, and for interim periods within fiscal years beginning after December 15, 2020. The amendments should be applied at the beginning of the earliest period presented using a modified retrospective approach with earlier application permitted as of the beginning of an interim or annual reporting period. This Update is not expected to have a significant impact on the Company's financial statements.

In March 2016, the FASB issued ASU 2016-04, *Liabilities – Extinguishments of Liabilities (Subtopic 405-20)*. The standard provides that liabilities related to the sale of prepaid stored-value products within the scope of this Update are financial liabilities. The amendments in the Update provide a narrow-scope exception to the guidance in Subtopic

405-20 to require that breakage for those liabilities be accounted for consistent with the breakage guidance in Topic 606. The amendments in this Update are effective for public business entities, certain not-for-profit entities, and certain employee benefit plans for financial statements issued for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years. For all other entities, the amendments are effective for financial statements issued for fiscal years beginning after December 15, 2018, and interim periods within fiscal years beginning after December 15, 2019. Earlier application is permitted, including adoption in an interim period. This Update is not expected to have a significant impact on the Company's financial statements.

In March 2016, the FASB issued ASU 2016-05, *Derivatives and Hedging (Topic 815)*. The amendments in this Update apply to all reporting entities for which there is a change in the counterparty to a derivative instrument that has been designated as a hedging instrument under Topic 815. The standards in this Update clarify that a change in the counterparty to a derivative instrument that has been designated as the hedging instrument under Topic 815 does not, in and of itself, require designation of that hedging relationship provided that all other hedge accounting criteria continue to be met. For public business entities, the amendments in this Update are effective for financial statements issued for fiscal years beginning after December 15, 2016, and interim periods within those fiscal years. For all other entities, the amendments in this Update are effective for financial statements issued for fiscal years beginning after December 15, 2017, and interim periods within fiscal years beginning after December 15, 2018. An entity has an option to apply the amendments in this Update on either a prospective basis or a modified retrospective basis. Early adoption is permitted, including adoption in an interim period. This Update is not expected to have a significant impact on the Company's financial statements.

In March 2016, the FASB issued ASU 2016-06, *Derivatives and Hedging (Topic 815)*. The amendments apply to all entities that are issuers of or investors in debt instruments (or hybrid financial instruments that are determined to have a debt host) with embedded call (put) options. The amendments in this Update clarify the requirements for assessing whether contingent call (put) options that can accelerate the payment of principal on debt instruments are clearly and closely related to their debt host. An entity performing the assessment under the amendments in this Update is required to assess the embedded call (put) options solely in accordance with the four-step decision sequence. For public business entities, the amendments in this Update are effective for financial statements issued for fiscal years beginning after December 15, 2016, and interim periods within those fiscal years. For entities other than public business entities, the amendments in this Update are effective for financial statements issued for fiscal years beginning after December 15, 2017, and interim periods within fiscal years beginning after December 15, 2018. Early adoption is permitted, including adoption in an interim period. This Update is not expected to have a significant impact on the Company's financial statements.

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

In March 2016, the FASB issued ASU 2016-08, *Revenue from Contracts with Customers (Topic 606)*. The amendments in this Update affect entities with transactions included within the scope of Topic 606, which includes entities that enter into contracts with customers to transfer goods or services (that are an output of the entity's ordinary activities) in exchange for consideration. The amendments in this Update do not change the core principle of the guidance in Topic 606; they simply clarify the implementation guidance on principal versus agent considerations. The amendments in this Update are intended to improve the operability and understandability of the implementation guidance on principal versus agent considerations. The amendments in this Update affect the guidance in ASU 2014-09, *Revenue from Contracts with Customers (Topic 606)*, which is not yet effective. The effective date and transition requirements for the amendments in this Update are the same as the effective date and transition requirements of Update 2014-09. ASU No. 2015-14, *Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date*, defers the effective date of Update 2014-09 by one year. The Company is currently evaluating the impact the adoption of the standard will have on the Company's financial position or results of operations.

In March 2016, the FASB issued ASU 2016-09, *Compensation – Stock Compensation (Topic 718)*. The amendments in this Update affect all entities that issue share-based payment awards to their employees. The standards in this Update provide simplification for several aspects of the accounting for share-based payment transactions, including the income tax consequences, classification of awards as with equity or liabilities, and classification on the statement of cash flows. Some of the areas for simplification apply only to nonpublic entities. In addition to those simplifications, the amendments eliminate the guidance in Topic 718 that was indefinitely deferred shortly after the issuance of FASB Statement No. 123 (revised 2004), *Share-Based Payment*. This should not result in a change in practice because the guidance that is being superseded was never effective. For public business entities, the amendments in this Update are effective for annual periods beginning after December 15, 2016, and interim periods within those annual periods. For all other entities, the amendments are effective for annual periods beginning after December 15, 2017, and interim periods within annual periods beginning after December 15, 2018. Early adoption is permitted for any entity in any interim or annual period. This Update is not expected to have a significant impact on the Company's financial statements.

In April 2016, the FASB issued ASU 2016-10, *Revenue from Contracts with Customers (Topic 606)*. The amendments in this Update affect entities with transactions included within the scope of Topic 606, which includes entities that enter into contracts with customers to transfer goods or services in exchange for consideration. The amendments in this Update do not change the core principle for revenue recognition in Topic 606. Instead, the amendments provide (1) more detailed guidance in a few areas and (2) additional implementation guidance and examples based on feedback the FASB received from its stakeholders. The amendments are expected to reduce the degree of judgment necessary to comply with Topic 606, which the FASB expects will reduce the potential for diversity arising in practice and reduce the cost and complexity of applying the guidance. The amendments in this Update affect the guidance in ASU 2014-09, *Revenue from Contracts with Customers (Topic 606)*, which is not yet effective. The effective date and transition requirements for the amendments in this Update are the same as the effective date and transition requirements in Topic 606 (and any other Topic amended by Update 2014-09). ASU 2015-14, *Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date*, defers the effective date of Update 2014-09 by one year. The Company is currently evaluating the impact the adoption of the standard will have on the Company's financial position or results of operations.

In May 2016, the FASB issued ASU 2016-11, *Revenue Recognition (Topic 605) and Derivative and Hedging (Topic 815)*, which rescinds SEC paragraphs pursuant to two SEC Staff Announcements at the March 3, 2016, Emerging Issues Task Force meeting. This Update did not have a significant impact on the Company's financial statements.

In May 2016, the FASB issued ASU 2016-12, *Revenue from Contracts with Customers (Topic 606)*, which among other things clarifies the objective of the collectability criterion in Topic 606, as well as certain narrow aspects of Topic 606. The amendments in this Update affect the guidance in ASU 2014-09, *Revenue from Contracts with Customers (Topic 606)*, which is not yet effective. The effective date and transition requirements for the amendments in this Update are the same as the effective date and transition requirements for Topic 606 (and any other Topic amended by Update 2014-09). ASU 2015-14, *Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date*, defers the effective date of Update 2014-09 by one year. This Update is not expected to have a significant impact on the Company's financial statements.

In June 2016, the FASB issued ASU 2016-13, *Financial Instruments - Credit Losses: Measurement of Credit Losses on Financial Instruments ("ASU 2016-13")*, which changes the impairment model for most financial assets. This Update is intended to improve financial reporting by requiring timelier recording of credit losses on loans and other financial instruments held by financial institutions and other organizations. The underlying premise of the Update is that financial assets measured at amortized cost should be presented at the net amount expected to be collected, through an allowance for credit losses that is deducted from the amortized cost basis. The allowance for credit losses should reflect management's current estimate of credit losses that are expected to occur over the remaining life of a financial asset. The income statement will be effected for the measurement of credit losses for newly recognized financial assets, as well as the expected increases or decreases of expected credit losses that have taken place during the period. ASU 2016-13 is effective for annual and interim periods beginning after December 15, 2019, and early adoption is permitted for annual and interim periods beginning after December 15, 2018. With certain exceptions, transition to the new requirements will be through a cumulative effect adjustment to opening retained earnings as of the beginning of the first reporting period in which the guidance is adopted. The Company is currently evaluating the impact the adoption of the standard will have on the Company's financial position or results of operations.

In August 2016, the FASB issued ASU 2016-15, Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments (“ASU 2016-15”), which addresses eight specific cash flow issues with the objective of reducing diversity in practice. Among these include recognizing cash payments for debt prepayment or debt extinguishment as cash outflows for financing activities; cash proceeds received from the settlement of insurance claims should be classified on the basis of the related insurance coverage; and cash proceeds received from the settlement of bank-owned life insurance policies should be classified as cash inflows from investing activities while the cash payments for premiums on bank-owned policies may be classified as cash outflows for investing activities, operating activities, or a combination of investing and operating activities. 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. For all other entities, the amendments are effective for fiscal years beginning after December 15, 2018, and interim periods within fiscal years beginning after December 15, 2019. Early adoption is permitted, including adoption in an interim period. If an entity early adopts the amendments in an interim period, any adjustments should be reflected as of the beginning of the fiscal year that includes that interim period. An entity that elects early adoption must adopt all of the amendments in the same period. The amendments in this Update should be applied using a retrospective transition method to each period presented. If it is impracticable to apply the amendments retrospectively for some of the issues, the amendments for those issues would be applied prospectively as of the earliest date practicable. The Company is currently evaluating the impact the adoption of the standard will have on the Company’s statement of cash flows.

NOTE 2 - STOCK-BASED COMPENSATION

The Company had no unvested stock options outstanding or unrecognized stock-based compensation costs outstanding as of September 30, 2016 and 2015.

Stock option activity during the nine months ended September 30 is as follows:

	2016	Weighted- average Exercise Price	2015	Weighted- average Exercise Price
Outstanding, January 1	31,949	\$ 25.03	46,451	\$ 27.90
Expired	-	-	(3,639)	37.33
Exercised	-	-	(1,025)	20.21
Outstanding, September 30	31,949	\$ 25.03	41,787	\$ 27.27
Exercisable, September 30	31,949	\$ 25.03	41,787	\$ 27.27

NOTE 3 - EARNINGS PER SHARE

The Company provides dual presentation of basic and diluted earnings per share. Basic earnings per share is calculated by dividing net income by the average shares outstanding. Diluted earnings per share adds the dilutive effects of stock options to average shares outstanding.

The following table sets forth the composition of the weighted-average common shares (denominator) used in the basic and diluted earnings per share computation.

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2016	2015	2016	2015
Weighted-average common shares outstanding	2,633,752	2,253,584	2,445,821	2,248,468
Average treasury stock shares	(386,165)	(189,530)	(386,165)	(189,530)
Weighted-average common shares and common stock equivalents used to calculate basic earnings per share	2,247,587	2,064,054	2,059,656	2,058,938
Additional common stock equivalents (stock options) used to calculate diluted earnings per share	8,643	8,585	8,876	9,254
Weighted-average common shares and common stock equivalents used to calculate diluted earnings per share	2,256,230	2,072,639	2,068,532	2,068,192

Options to purchase 31,949 shares of common stock, at prices ranging from \$17.55 to \$40.24, were outstanding during the three and nine months ended September 30, 2016. Of those options, 24,700 were considered dilutive for the three and nine month periods based on the market price exceeding the strike price.

Options to purchase 41,787 shares of common stock, at prices ranging from \$17.55 to \$37.48, were outstanding during the three and nine months ended September 30, 2015. Of those options, 27,000 were considered dilutive for the three month period based on the market price exceeding the strike price. For the nine months ended September 30, 2015, 27,250 options were considered dilutive.

NOTE 4 - FAIR VALUE MEASUREMENTS

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in the principal or most advantageous market for an asset or liability in an orderly transaction between market participants at the measurement date. GAAP established a fair value hierarchy that prioritizes the use of inputs used in valuation methodologies into the following levels:

Level I: Quoted prices are available in active markets for identical assets or liabilities as of the reported date.

Level II: Pricing inputs are other than the quoted prices in active markets, which are either directly or indirectly observable as of the reported date. The nature of these assets and liabilities includes items for which quoted prices are available but traded less frequently and items that are fair valued using other financial instruments, the parameters of which can be directly observed.

Level III: Assets and liabilities that have little to no pricing observability as of the reported date. These items do not have two-way markets and are measured using management's best estimate of fair value, where the inputs into the determination of fair value require significant management judgment or estimation.

The following tables present the assets measured on a recurring basis on the Consolidated Balance Sheet at their fair value by level within the fair value hierarchy. Financial assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement.

(Dollar amounts in thousands)	September 30, 2016			Total
	Level I	Level II	Level III	
Assets measured on a recurring basis:				
U.S. government agency securities	\$ -	\$ 10,863	\$ -	\$ 10,863
Obligations of states and political subdivisions	-	87,525	-	87,525
Mortgage-backed securities in government- sponsored entities	-	21,380	-	21,380
Private-label mortgage-backed securities	-	2,068	-	2,068
Total debt securities	-	121,836	-	121,836
Equity securities in financial institutions	5	1,213	-	1,218
Total	\$ 5	\$ 123,049	\$ -	\$ 123,054

(Dollar amounts in thousands)	December 31, 2015			Total
	Level I	Level II	Level III	
Assets measured on a recurring basis:				
U.S. government agency securities	\$ -	\$ 21,629	\$ -	\$ 21,629
Obligations of states and political subdivisions	-	97,290	-	97,290
Mortgage-backed securities in government- sponsored entities	-	24,524	-	