First Internet Bancorp
Form 10-Q
November 09, 2018

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

FORM 10-Q

(Mark One)
þ QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the Quarterly Period ended September 30, 2018
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.)
11201 USA Parkway Fishers, IN	46037
(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 þ No ¨

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes þ 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 þ
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 Exchange Act).
Yes ¨ No þ

As of November 2, 2018, the registrant had 10,181,675 shares of common stock issued and outstanding.

Cautionary Note Regarding Forward-Looking Statements

This Quarterly Report on Form 10-Q contains “forward-looking statements” within the meaning of the federal securities laws. These statements are not historical facts, but rather statements based on the current expectations of First Internet Bancorp and its consolidated subsidiaries (“we,” “our,” “us” or the “Company”) regarding its business strategies, intended results and future performance. Forward-looking statements are generally preceded by terms such as “anticipate,” “believe,” “can,” “estimate,” “expect,” “intend,” “may,” “plan,” “should” and similar expressions. Such statements are subject risks and uncertainties including: general economic conditions, whether national or regional, and conditions in the lending markets in which we participate that may have an adverse effect on the demand for our loans and other products; our credit quality and related levels of nonperforming assets and loan losses, and the value and salability of the real estate that we own or that is the collateral for our loans; failures or breaches of or interruptions in the communication and information systems on which we rely to conduct our business that could reduce our revenues, increase our costs or lead to disruptions in our business; our plans to grow our commercial real estate, commercial and industrial, public finance and healthcare finance loan portfolios which may carry greater risks of non-payment or other unfavorable consequences; our dependence on capital distributions from First Internet Bank of Indiana (the “Bank”); results of examinations of us by our regulators, including the possibility that our regulators may, among other things, require us to increase our allowance for loan losses or to write-down assets; changing bank regulatory conditions, policies or programs, whether arising as new legislation or regulatory initiatives, that could lead to restrictions on activities of banks generally, or the Bank in particular; more restrictive regulatory capital requirements; increased costs, including deposit insurance premiums; regulation or prohibition of certain income producing activities or changes in the secondary market for loans and other products; changes in market rates and prices that may adversely impact the value of securities, loans, deposits and other financial instruments and the interest rate sensitivity of our balance sheet; our liquidity requirements being adversely affected by changes in our assets and liabilities; the effect of legislative or regulatory developments, including changes in laws concerning taxes, banking, securities, insurance and other aspects of the financial services industry; competitive factors among financial services organizations, including product and pricing pressures and our ability to attract, develop and retain qualified banking professionals; execution of future acquisition, reorganization or disposition transactions including without limitation, the related time and costs of implementing such transactions, integrating operations as part of these transactions and possible failures to achieve expected gains, revenue growth and/or expense savings and other anticipated benefits from such transactions; changes in applicable tax laws; the growth and profitability of noninterest or fee income being less than expected; the loss of any key members of senior management; the effect of changes in accounting policies and practices, as may be adopted by the Financial Accounting Standards Board (the “FASB”), the Securities and Exchange Commission (the “SEC”), the Public Company Accounting Oversight Board (the “PCAOB”) and other regulatory agencies; and the effect of fiscal and governmental policies of the United States federal government. 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 SEC. We caution readers not to place undue reliance on any such forward-looking statements, which speak only as of the date made. The factors listed above could affect our financial performance and could cause our actual results for future periods to differ materially from any opinions or statements expressed with respect to future periods in any current statements.

Except as required by law, we do not undertake, and specifically disclaim any obligation, to publicly release the result of any revisions that may be made to any forward-looking statements to reflect events or circumstances after the date of such statements or to reflect the occurrence of anticipated or unanticipated events.

PART I

ITEM 1. FINANCIAL STATEMENTS

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

	September 30, 2018 (Unaudited)	December 31, 2017
Assets		
Cash and due from banks	$ 3,517	$ 4,539
Interest-bearing deposits	82,273	43,442
Total cash and cash equivalents	85,790	47,981
Securities available-for-sale, at fair value (amortized cost of $491,726 and $481,357 in 2018 and 2017, respectively)	468,997	473,275
Securities held-to-maturity, at amortized cost (fair value of $19,510 and $19,083 in 2018 and 2017, respectively)	20,200	19,209
Loans held-for-sale (includes $23,493 and $23,571 at fair value in 2018 and 2017, respectively)	23,493	51,407
Loans	2,493,622	2,091,193
Allowance for loan losses	(16,704)	(14,970)
Net loans	2,476,918	2,076,223
Accrued interest receivable	14,472	11,944
Federal Home Loan Bank of Indianapolis stock	22,050	19,575
Cash surrender value of bank-owned life insurance	35,819	35,105
Premises and equipment, net	10,041	10,058
Goodwill	4,687	4,687
Other real estate owned	5,041	5,041
Accrued income and other assets	35,410	13,182
Total assets	$ 3,202,918	$ 2,767,687
Liabilities and Shareholders’ Equity		
Liabilities		
Noninterest-bearing deposits	$ 42,750	$ 44,686
Interest-bearing deposits	2,403,814	2,040,255
Total deposits	2,446,564	2,084,941
Advances from Federal Home Loan Bank	425,160	410,176
Subordinated debt, net of unamortized discounts and debt issuance costs of $1,163 and $1,274 in 2018 and 2017, respectively	33,837	36,726
Accrued interest payable	887	311
Accrued expenses and other liabilities	8,730	11,406
Total liabilities	2,915,178	2,543,560
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; 10,181,675 and 8,411,077 shares issued and outstanding in 2018 and 2017, respectively	227,454	172,043
	—	—

Nonvoting common stock, no par value; 86,221 shares authorized; issued and outstanding - none		
Retained earnings	74,733	57,103
Accumulated other comprehensive loss	(14,447)	(5,019)
Total shareholders’ equity	287,740	224,127
Total liabilities and shareholders’ equity	$ 3,202,918	$ 2,767,687

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		Nine Months Ended	
	September 30, 2018	September 30, 2017	September 30, 2018	September 30, 2017
Interest Income				
Loans	$26,019	$ 18,922	$71,833	$ 49,494
Securities – taxable	2,659	2,582	7,703	7,515
Securities – non-taxable	698	697	2,109	2,090
Other earning assets	847	493	1,973	960
Total interest income	30,223	22,694	83,618	60,059
Interest Expense				
Deposits	11,650	6,594	29,146	16,617
Other borrowed funds	2,603	1,909	7,626	4,820
Total interest expense	14,253	8,503	36,772	21,437
Net Interest Income	15,970	14,191	46,846	38,622
Provision for Loan Losses	888	1,336	2,405	3,693
Net Interest Income After Provision for Loan Losses	15,082	12,855	44,441	34,929
Noninterest Income				
Service charges and fees	236	226	697	657
Mortgage banking activities	1,402	2,535	4,577	6,306
Gain on sale of loans	—	—	414	—
Other	356	374	1,025	1,039
Total noninterest income	1,994	3,135	6,713	8,002
Noninterest Expense				
Salaries and employee benefits	5,704	5,197	17,436	15,463
Marketing, advertising and promotion	601	741	1,925	1,803
Consulting and professional services	709	897	2,193	2,474
Data processing	368	247	913	729
Loan expenses	241	262	738	724
Premises and equipment	1,244	1,080	3,689	3,058
Deposit insurance premium	441	375	1,386	990
Other	737	602	2,164	1,781
Total noninterest expense	10,045	9,401	30,444	27,022
Income Before Income Taxes	7,031	6,589	20,710	15,909
Income Tax Provision	743	1,694	2,386	4,181
Net Income	$6,288	$ 4,895	$18,324	$ 11,728
Income Per Share of Common Stock				
Basic	$0.61	$ 0.72	$1.99	$ 1.76
Diluted	$0.61	$ 0.71	$1.98	$ 1.75
Weighted-Average Number of Common Shares Outstanding				
Basic	10,261,967	6,834,011	9,230,149	6,656,160
Diluted	10,273,766	6,854,614	9,250,839	6,683,379
Dividends Declared Per Share	$0.06	$ 0.06	$0.18	$ 0.18

See Notes to Condensed Consolidated Financial Statements

First Internet Bancorp
Condensed Consolidated Statements of Comprehensive Income – Unaudited
(Amounts in thousands)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
Net income	$6,288	$4,895	$18,324	$11,728
Other comprehensive income				
Net unrealized holding (losses) gains on securities available-for-sale recorded within other comprehensive income before income tax	(3,063)	1,231	(12,301)	6,287
Reclassification adjustment for losses realized	—	8	—	8
Net unrealized holding gains on cash flow hedging derivatives recorded within other comprehensive income tax	1,366	—	408	—
Other comprehensive (loss) income before income tax	(1,697)	1,239	(11,893)	6,295
Income tax (benefit) provision	(1,328)	483	(3,528)	2,062
Other comprehensive (loss) income	(369)	756	(8,365)	4,233
Comprehensive income	$5,919	$5,651	$9,959	$15,961

See Notes to Condensed Consolidated Financial Statements

First Internet Bancorp
Condensed Consolidated Statement of Shareholders' Equity - Unaudited
Nine Months Ended September 30, 2018
(Amounts in thousands except per share data)

	Voting and Nonvoting Common Stock	Retained Earnings	Accumulated Other Comprehensive Loss	Total Shareholders' Equity
Balance, January 1, 2018	$ 172,043	$ 57,103	$ (5,019)	$ 224,127
Impact of adoption of new accounting standards [1]	—	1,063	(1,063)	—
Net income	—	18,324	—	18,324
Other comprehensive loss	—	—	(8,365)	(8,365)
Dividends declared ($0.18 per share)	—	(1,757)	—	(1,757)
Net cash proceeds from common stock issuance	54,334	—	—	54,334
Recognition of the fair value of share-based compensation	1,257	—	—	1,257
Deferred stock rights and restricted stock units issued in lieu of cash dividends payable on outstanding deferred stock rights and restricted stock units	30	—	—	30
Common stock redeemed for the net settlement of share-based awards	(210)	—	—	(210)
Balance, September 30, 2018	$ 227,454	$ 74,733	$ (14,447)	$ 287,740

(1) Represents the impact of adopting Accounting Standards Update ("ASU") 2018-02 and ASU 2016-01. ASU 2018-02 increased retained earnings and accumulated other comprehensive loss by $1.1 million. ASU 2016-01 decreased retained earnings and accumulated other comprehensive loss by $0.1 million. See Note 12 to the condensed consolidated financial statements for more information.

See Notes to Condensed Consolidated Financial Statements

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

	Nine Months Ended September 30,	
	2018	2017
Operating Activities		
Net income	$18,324	$11,728
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	4,262	3,876
Increase in cash surrender value of bank-owned life insurance	(714)	(661)
Provision for loan losses	2,405	3,693
Share-based compensation expense	1,257	787
Loss (gain) from sale of available-for-sale securities	—	8
Loans originated for sale	(282,527)	(302,887)
Proceeds from sale of loans	287,556	317,170
Gain on loans sold	(5,201)	(5,876)
Gain on sale of other real estate owned	(105)	—
Decrease (increase) in fair value of loans held-for-sale	250	(519)
(Gain) loss on derivatives	(100)	89
Net change in accrued income and other assets	(149)	(2,310)
Net change in accrued expenses and other liabilities	(1,924)	1,530
Net cash provided by operating activities	23,334	26,628
Investing Activities		
Net loan activity, excluding purchases	(274,507)	(629,541)
Proceeds from sale of other real estate owned	332	30
Net change in interest-bearing time deposits	—	250
Maturities and calls of securities available-for-sale	48,938	50,165
Proceeds from sale of securities available-for-sale	—	9,192
Purchase of securities available-for-sale	(65,289)	(90,306)
Purchase of securities held-to-maturity	(1,000)	(2,550)
Purchase of Federal Home Loan Bank of Indianapolis stock	(2,475)	(10,665)
Purchase of bank-owned life insurance	—	(10,000)
Purchase of premises and equipment	(1,161)	(821)
Loans purchased	(132,041)	(42,345)
Net proceeds from sale of portfolio loans	25,717	26,679
Other investing activities	(10,166)	—
Net cash used in investing activities	(411,652)	(699,912)
Financing Activities		
Net increase in deposits	361,623	534,161
Cash dividends paid	(1,620)	(1,283)
Repayment of subordinated debt	(3,000)	—
Proceeds from advances from Federal Home Loan Bank	225,000	447,000
Repayment of advances from Federal Home Loan Bank	(210,000)	(271,805)
Net proceeds from common stock issuance	54,334	51,636
Other, net	(210)	(173)
Net cash provided by financing activities	426,127	759,536
Net Increase in Cash and Cash Equivalents	37,809	86,252
Cash and Cash Equivalents, Beginning of Period	47,981	39,452

Cash and Cash Equivalents, End of Period	$85,790	$125,704
Supplemental Disclosures		
Cash paid during the period for interest	$36,196	$21,312
Cash paid during the period for taxes	360	2,922
Loans transferred to other real estate owned	227	648
Cash dividends declared, paid in subsequent period	611	504
Securities purchased during the period, settled in subsequent period	—	1,158
Transfer of other equity investments from securities available-for-sale to other assets in accordance with adoption of ASU 2016-01	2,932	—

See Notes to Condensed Consolidated Financial Statements

First Internet Bancorp
Notes to Condensed Consolidated Financial Statements – Unaudited
(Table amounts in thousands except share and 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 U.S. Securities and Exchange Commission ("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 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, 2018 are not necessarily indicative of the results expected for the year ending December 31, 2018 or any other period. The September 30, 2018 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, 2017.

The preparation of the condensed consolidated financial statements in conformity with 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 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 three wholly-owned subsidiaries, First Internet Public Finance Corp., JKH Realty Services, LLC and SPF15, Inc. All significant intercompany accounts and transactions have been eliminated in consolidation.

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.

Certain reclassifications have been made to the 2017 financial statements to conform to the presentation of the 2018 financial statements. These reclassifications had no effect on net income.

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, 2018 and 2017.

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
Basic earnings per share				
Net income	$6,288	$ 4,895	$18,324	$ 11,728
Weighted-average common shares	10,261,967	6,834,011	9,230,149	6,656,160
Basic earnings per common share	$0.61	$ 0.72	$1.99	$ 1.76
Diluted earnings per share				
Net income	$6,288	$ 4,895	$18,324	$ 11,728
Weighted-average common shares	10,261,967	6,834,011	9,230,149	6,656,160
Dilutive effect of warrants	—		—	8,094
Dilutive effect of equity compensation	11,799	20,603	20,690	19,125
Weighted-average common and incremental shares	10,273,766	6,854,614	9,250,839	6,683,379
Diluted earnings per common share	$0.61	$ 0.71	$1.98	$ 1.75

Note 3: Securities

The following tables summarize securities available-for-sale and securities held-to-maturity as of September 30, 2018 and December 31, 2017.

	September 30, 2018			
	Amortized	Gross Unrealized		Fair
	Cost	Gains	Losses	Value
Securities available-for-sale				
U.S. Government-sponsored agencies	$115,176	$20	$(2,436)	$112,760
Municipal securities	97,160	39	(6,119)	91,080
Mortgage-backed securities	237,703	33	(12,044)	225,692
Asset-backed securities	5,003	—	(43)	4,960
Corporate securities	36,684	41	(2,220)	34,505
Total available-for-sale	$491,726	$133	$(22,862)	$468,997

	September 30, 2018			
	Amortized	Gross Unrealized		Fair
	Cost	Gains	Losses	Value
Securities held-to-maturity				
Municipal securities	$10,159	$—	$(640)	$9,519
Corporate securities	10,041	24	(74)	9,991
Total held-to-maturity	$20,200	$24	$(714)	$19,510

	December 31, 2017			
	Amortized	Gross Unrealized		Fair
	Cost	Gains	Losses	Value
Securities available-for-sale				
U.S. Government-sponsored agencies	$133,424	$531	$(765)	$133,190
Municipal securities	97,370	366	(1,359)	96,377
Mortgage-backed securities	215,452	15	(5,747)	209,720
Asset-backed securities	5,000	9	—	5,009
Corporate securities	27,111	103	(1,167)	26,047
Other securities	3,000	—	(68)	2,932
Total available-for-sale	$481,357	$1,024	$(9,106)	$473,275

	December 31, 2017			
	Amortized	Gross Unrealized		Fair
	Cost	Gains	Losses	Value
Securities held-to-maturity				
Municipal securities	$10,164	$40	$(357)	$9,847
Corporate securities	9,045	191	—	9,236
Total held-to-maturity	$19,209	$231	$(357)	$19,083

The carrying value of securities at September 30, 2018 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	Fair
	Cost	Value
One to five years	$425	$403
Five to ten years	63,004	61,057
After ten years	185,591	176,885
	249,020	238,345
Mortgage-backed securities	237,703	225,692
Asset-backed securities	5,003	4,960
Total	$491,726	$468,997

	Held-to-Maturity	
	Amortized	Fair
	Cost	Value
Five to ten years	$14,286	$13,956
After ten years	5,914	5,554
Total	$20,200	$19,510

There were no gross gains or losses resulting from sales of available-for-sale securities during the three and nine months ended September 30, 2018 and gross losses of $0.0 million for the three and nine months ended September 30, 2017.

Certain investments in debt securities are reported in the condensed consolidated financial statements at an amount less than their historical cost. The total fair value of these investments at September 30, 2018 and December 31, 2017 was $466.6 million and $354.6 million, which was approximately 96% and 72%, respectively, of the Company's available-for-sale and held-to-maturity securities portfolios. These declines resulted primarily from fluctuations in market interest rates after purchase. 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 with the resulting loss recognized in net income in the period the other-than-temporary impairment (“OTTI”) is identified.

U. S. Government-Sponsored Agencies, Municipal Securities and Corporate Securities

The unrealized losses on the Company's investments in securities issued by U.S. Government-sponsored agencies, municipal organizations and corporate entities 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 and it is not likely that the Company will be required to sell the investments before recovery of their amortized cost bases, which may be upon maturity, the Company does not consider those investments to be other-than-temporarily impaired at September 30, 2018.

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 Company does not intend to sell the investments and it is not likely that the Company will be required to sell the investments before recovery of their amortized cost bases, which may be upon maturity, the Company does not consider those investments to be other-than-temporarily impaired at September 30, 2018.

	September 30, 2018					
	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 agencies	$75,589	$ (1,019)	$31,049	$ (1,417)	$106,638	$ (2,436)
Municipal securities	30,647	(1,292)	56,008	(4,827)	86,655	(6,119)
Mortgage-backed securities	55,063	(1,061)	167,901	(10,983)	222,964	(12,044)
Asset-backed securities	4,960	(43)	—	—	4,960	(43)
Corporate securities	9,548	(33)	19,813	(2,187)	29,361	(2,220)
Total	$175,807	$ (3,448)	$274,771	$ (19,414)	$450,578	$ (22,862)

	September 30, 2018					
	Less Than 12 Months		12 Months or Longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Securities held-to-maturity						
Municipal securities	$9,519	$ (640)	$ —	$ —	$9,519	$ (640)
Corporate securities	6,467	(74)	—	—	6,467	(74)
Total	$15,986	$ (714)	$ —	$ —	$15,986	$ (714)

	December 31, 2017					
	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 agencies	$30,194	$ (256)	$22,824	$ (509)	$53,018	$ (765)
Municipal securities	5,638	(77)	57,128	(1,282)	62,766	(1,359)
Mortgage-backed securities	29,542	(251)	177,266	(5,496)	206,808	(5,747)
Corporate securities	1,852	(148)	18,981	(1,019)	20,833	(1,167)

Other securities	—	—	2,932	(68)	2,932	(68)
Total	$67,226	$ (732)	$279,131	$ (8,374)	$346,357	$ (9,106)

	December 31, 2017					
	Less Than 12 Months		12 Months or Longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Securities held-to-maturity						
Municipal securities	$8,255	$ (357)	$ —	$ —	$8,255	$ (357)
Total	$8,255	$ (357)	$ —	$ —	$8,255	$ (357)

There were no amounts reclassified from accumulated other comprehensive loss to the condensed consolidated statements of income during the three and nine months ended September 30, 2018. 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, 2017 were as follows:

Details About Accumulated Other Comprehensive Loss Components	Amounts Reclassified from Accumulated Other Comprehensive Loss for the Three Months Ended September 30, 2017	Nine Months Ended September 30, 2017	Affected Line Item in the Statements of Income
Realized gains and losses on securities available-for-sale			
Loss realized in earnings	$ (8)	$ (8)	Other
Total reclassified amount before tax	(8)	(8)	Income Before Income Taxes
Tax benefit	(3)	(3)	Income Tax Provision
Total reclassifications out of accumulated other comprehensive loss	$ (5)	$ (5)	Net Income

Note 4: Loans

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, 2018	December 31, 2017
Commercial loans		
Commercial and industrial	$ 105,489	$ 122,940
Owner-occupied commercial real estate	93,568	75,768
Investor commercial real estate	5,595	7,273
Construction	38,228	49,213
Single tenant lease financing	883,372	803,299
Public finance	610,858	438,341
Healthcare finance	89,525	31,573
Total commercial loans	1,826,635	1,528,407
Consumer loans		
Residential mortgage	362,574	299,935
Home equity	28,713	30,554
Other consumer	270,567	227,533
Total consumer loans	661,854	558,022
Total commercial and consumer loans	2,488,489	2,086,429
Deferred loan origination costs and premiums and discounts on purchased loans	5,133	4,764
Total loans	2,493,622	2,091,193
Allowance for loan losses	(16,704)	(14,970)
Net loans	$ 2,476,918	$ 2,076,223

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

Commercial and Industrial: Commercial and industrial loans' sources of repayment 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 and industrial loans are secured by the assets being financed and may incorporate a personal guarantee. This portfolio segment is generally concentrated in Central Indiana and adjacent markets and the greater Phoenix, Arizona market.

Owner-Occupied Commercial Real Estate: The primary source of repayment is the cash flow from the ongoing operations and activities conducted by the borrower, or an affiliate of the borrower, who owns the property. This portfolio segment is generally concentrated in the Central Indiana and adjacent markets and the greater Phoenix, Arizona market and its loans are often secured by manufacturing and service facilities, as well as office buildings.

Investor Commercial Real Estate: These loans are underwritten primarily based on the cash flow expected to be generated from the property and are secondarily supported by the value of the real estate. These loans typically incorporate a personal guarantee. This portfolio segment generally 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. Investor commercial real estate loans may be more adversely affected by conditions in the real estate markets, changing industry dynamics, or the overall health of the general economy. The properties securing the Company's investor commercial real estate portfolio tend to be diverse in terms of property type and are typically located in the state of Indiana and markets adjacent to Indiana. Management monitors and evaluates commercial real estate loans based on property financial performance, collateral value, guarantor strength, 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 mitigate these additional risks.

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Construction: Construction loans are secured by real estate and improvements and are made to assist in the construction of new structures, which may include commercial (retail, industrial, office, multi-family) properties or single family residential properties offered for sale by the builder. These loans generally finance a variety of project costs, including land, site preparation, construction, closing and soft costs and interim financing needs. The cash flows of builders, while initially predictable, may fluctuate with market conditions, and the value of the collateral securing these loans may be subject to fluctuations based on general economic changes. This portfolio segment is generally concentrated in Central Indiana.

Single Tenant Lease Financing: These loans are made to property owners of real estate subject to long-term lease arrangements with single tenant operators. The real estate is typically operated by regionally, nationally or globally branded businesses. The loans are underwritten based on the financial strength of the borrower, characteristics of the real estate, cash flows generated from the lease arrangements and the financial strength of the tenant. Similar to the other loan portfolio segments, management monitors and evaluates these loans based on borrower and tenant financial performance, collateral value, industry trends and other risk grade criteria.

Public Finance: These loans are made to governmental and not-for-profit entities to provide both tax-exempt and taxable loans for a variety of purposes including: short term cash-flow needs; debt refinancing; economic development; quality of life projects; infrastructure improvements; and equipment financing. The primary sources of repayment for public finance loans include pledged revenue sources including but not limited to: general obligations; property taxes; income taxes; tax increment revenue; utility revenue; gaming revenues; sales tax; and pledged general revenue. Certain loans may also include an additional collateral pledge of mortgaged property or a security interest in financed equipment. Public finance loans have been completed primarily in the Midwest, with plans to continue expanding nationwide.

Healthcare Finance: These loans are made to healthcare providers, primarily dentists, for refinancing or acquiring practices, refinancing or acquiring owner-occupied commercial real estate, and equipment purchases. The sources of repayment for these loans are primarily based on the identified cash flows of the borrower (including ongoing operations and activities conducted by the borrower, or an affiliate of the borrower, who owns the property) and secondarily on the underlying collateral provided by the borrower. This portfolio segment is generally concentrated in the Western United States with plans to expand nationwide.

Residential Mortgage: With respect to residential loans that are secured by 1-4 family residences and are generally owner occupied, the Company typically establishes a maximum loan-to-value ratio and requires private mortgage insurance if that ratio is exceeded. Repayment of these loans is primarily dependent on the financial circumstances of the borrowers, which can be impacted by economic conditions in their market areas such as unemployment levels. Repayment can also be impacted by changes in residential property values. 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.

Home Equity: Home equity loans and lines of credit are typically secured by a subordinate interest in 1-4 family residences. The properties securing the Company's home equity portfolio segment are generally geographically diverse as the Company offers these products on a nationwide basis. Repayment of these loans and lines of credit is primarily dependent on the financial circumstances of the borrowers and may be impacted by changes in unemployment levels and property values on residential properties, among other economic conditions in the market.

Other Consumer: These loans primarily consist of consumer loans and credit cards. Consumer loans may be secured by consumer assets such as horse trailers or recreational vehicles. Some consumer loans are unsecured, such as small installment loans, home improvement 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 maintain an adequate allowance for loan losses (“ALLL”). The portfolio is segmented by loan type, and the required ALLL for types of performing homogeneous loans which do not have a specific reserve is determined by applying a factor based on average historical losses, adjusted for current economic factors and portfolio trends. 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, or classified 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 costs 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. 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 less costs to sell and allows existing methods for recognizing interest income.

Provision for Loan Losses

A provision for estimated losses on loans is charged to income based upon management’s evaluation of the potential losses. Such an evaluation, which includes a review of all loans for which full repayment 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 attempts 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.

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 down 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. A home improvement loan generally is charged off no later than when it is 90 days past due as to principal or interest.

The following tables present changes in the balance of the ALLL during the three and nine months ended September 30, 2018 and 2017.

	Three Months Ended September 30, 2018				
Allowance for loan losses:	Balance, Beginning of Period	Provision (Credit) Charged to Expense	Losses Charged Off	Recoveries	Balance, End of Period
Commercial and industrial	$ 1,364	$ (51)	$ (6)	$ —	$ 1,307
Owner-occupied commercial real estate	889	69	—	—	958
Investor commercial real estate	67	(5)	—	—	62
Construction	295	(54)	—	—	241
Single tenant lease financing	8,294	186	—	—	8,480
Public finance	1,372	82	—	—	1,454
Healthcare finance	676	249	—	—	925
Residential mortgage	909	68	—	1	978
Home equity	54	(5)	—	5	54
Other consumer	2,133	349	(330)	93	2,245
Total	$ 16,053	$ 888	$ (336)	$ 99	$ 16,704

	Nine Months Ended September 30, 2018				
Allowance for loan losses:	Balance, Beginning of Period	Provision (Credit) Charged to Expense	Losses Charged Off	Recoveries	Balance, End of Period
Commercial and industrial	$ 1,738	$ (428)	$ (6)	$ 3	$ 1,307
Owner-occupied commercial real estate	803	155	—	—	958
Investor commercial real estate	85	(23)	—	—	62
Construction	423	(182)	—	—	241
Single tenant lease financing	7,872	608	—	—	8,480
Public finance	959	495	—	—	1,454
Healthcare finance	313	612	—	—	925
Residential mortgage	956	27	(9)	4	978
Home equity	70	(28)	—	12	54
Other consumer	1,751	1,169	(881)	206	2,245
Total	$ 14,970	$ 2,405	$ (896)	$ 225	$ 16,704

Allowance for loan losses:	Three Months Ended September 30, 2017 Balance, Beginning of Period	Provision (Credit) Charged to Expense	Losses Charged Off	Recoveries	Balance, End of Period
Commercial and industrial	$ 1,525	$ 361	$ (205)	$ —	$ 1,681
Owner-occupied commercial real estate	716	89	—	—	805
Investor commercial real estate	109	(22)	—	—	87
Construction	395	38	—	—	433
Single tenant lease financing	7,403	281	—	—	7,684
Public finance	362	201	—	—	563
Healthcare finance	28	95	—	—	123
Residential mortgage	991	81	(116)	2	958
Home equity	80	(6)	—	1	75
Other consumer	1,585	218	(211)	86	1,678
Total	$ 13,194	$ 1,336	$ (532)	$ 89	$ 14,087

Allowance for loan losses:	Nine Months Ended September 30, 2017 Balance, Beginning of Period	Provision (Credit) Charged to Expense	Losses Charged Off	Recoveries	Balance, End of Period
Commercial and industrial	$ 1,352	$ 465	$ (205)	$ 69	$ 1,681
Owner-occupied commercial real estate	582	223	—	—	805
Investor commercial real estate	168	(81)	—	—	87
Construction	544	(111)	—	—	433
Single tenant lease financing	6,248	1,436	—	—	7,684
Public finance	—	563	—	—	563
Healthcare finance	—	123	—	—	123
Residential mortgage	754	316	(116)	4	958
Home equity	102	(48)	—	21	75
Other consumer	1,231	807	(604)	244	1,678
Total	$ 10,981	$ 3,693	$ (925)	$ 338	$ 14,087

The following tables present the recorded investment in loans based on portfolio segment and impairment method as of September 30, 2018 and December 31, 2017.

September 30, 2018	Loans Ending Balance: Collectively Evaluated for Impairment	Loans Ending Balance: Individually Evaluated for Impairment	Loans Ending Balance	Allowance for Loan Losses Ending Balance: Collectively Evaluated for Impairment	Allowance for Loan Losses Ending Balance: Individually Evaluated for Impairment	Allowance for Loan Losses Ending Balance
Commercial and industrial	$97,540	$ 7,949	$105,489	$1,307	$ —	$1,307
Owner-occupied commercial real estate	92,089	1,479	93,568	958	—	958
Investor commercial real estate	5,595	—	5,595	62	—	62
Construction	38,228	—	38,228	241	—	241
Single tenant lease financing	883,372	—	883,372	8,480	—	8,480
Public finance	610,858	—	610,858	1,454	—	1,454
Healthcare finance	89,525	—	89,525	925	—	925
Residential mortgage	361,995	579	362,574	978	—	978
Home equity	28,713	—	28,713	54	—	54
Other consumer	270,456	111	270,567	2,245	—	2,245
Total	$2,478,371	$ 10,118	$2,488,489	$16,704	$ —	$16,704

December 31, 2017	Loans Ending Balance: Collectively Evaluated for Impairment	Loans Ending Balance: Individually Evaluated for Impairment	Loans Ending Balance	Allowance for Loan Losses Ending Balance: Collectively Evaluated for Impairment	Allowance for Loan Losses Ending Balance: Individually Evaluated for Impairment	Allowance for Loan Losses Ending Balance
Commercial and industrial	$119,054	$ 3,886	$122,940	$1,738	$ —	$1,738
Owner-occupied commercial real estate	75,761	7	75,768	803	—	803
Investor commercial real estate	7,273	—	7,273	85	—	85
Construction	49,213	—	49,213	423	—	423
Single tenant lease financing	803,299	—	803,299	7,872	—	7,872
Public finance	438,341	—	438,341	959	—	959
Healthcare finance	31,573	—	31,573	313	—	313
Residential mortgage	298,796	1,139	299,935	956	—	956
Home equity	30,471	83	30,554	70	—	70
Other consumer	227,443	90	227,533	1,751	—	1,751
Total	$2,081,224	$ 5,205	$2,086,429	$14,970	$ —	$14,970

The Company utilizes a risk grading matrix to assign a risk grade to each of its commercial loans. A description of the general characteristics of the risk grades is as follows:

- “Pass” - Higher quality loans that do not fit any of the other categories described below.

- “Special Mention” - Loans that possess some credit deficiency or potential weakness, which deserve close attention.

- “Substandard” - 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” - 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 that 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” - 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 for which the full collection of principal and interest may be in doubt will be considered for nonaccrual status. At the time a loan is placed on nonaccrual status, all accrued but unpaid interest will be reversed from interest income. Placing the loan on nonaccrual status does not relieve the borrower of the obligation to repay interest. A loan placed on nonaccrual status 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 commercial and consumer loan portfolios based on rating category and payment activity as of September 30, 2018 and December 31, 2017.

	September 30, 2018			
	Pass	Special Mention	Substandard	Total
Commercial and industrial	$95,573	$ 1,967	$ 7,949	$105,489
Owner-occupied commercial real estate	90,571	1,518	1,479	93,568
Investor commercial real estate	5,595	—	—	5,595
Construction	38,228	—	—	38,228
Single tenant lease financing	877,825	5,547	—	883,372
Public finance	610,858	—	—	610,858
Healthcare finance	89,525	—	—	89,525
Total commercial loans	$1,808,175	$ 9,032	$ 9,428	$1,826,635

	September 30, 2018		
	Performing	Nonaccrual	Total
Residential mortgage	$362,395	$ 179	$362,574
Home equity	28,713	—	28,713
Other consumer	270,506	61	270,567
Total consumer loans	$661,614	$ 240	$661,854

	December 31, 2017			
	Pass	Special Mention	Substandard	Total
Commercial and industrial	$113,840	$5,203	$ 3,897	$122,940
Owner-occupied commercial real estate	72,995	2,766	7	75,768
Investor commercial real estate	7,273	—	—	7,273
Construction	49,213	—	—	49,213
Single tenant lease financing	796,307	6,992	—	803,299
Public finance	438,341	—	—	438,341
Healthcare finance	31,573	—	—	31,573
Total commercial loans	$1,509,542	$14,961	$ 3,904	$1,528,407

	December 31, 2017		
	Performing	Nonaccrual	Total
Residential mortgage	$299,211	$ 724	$299,935
Home equity	30,471	83	30,554
Other consumer	227,501	32	227,533
Total consumer loans	$557,183	$ 839	$558,022

The following tables present the Company's loan portfolio delinquency analysis as of September 30, 2018 and December 31, 2017.

	September 30, 2018							
	30-59 Days Past Due	60-89 Days Past Due	90 Days or More Past Due	Total Past Due	Current	Total Loans	Non-accrual Loans	Total Loans 90 Days or More Past Due and Accruing
Commercial and industrial	$—	$ —	$ —	$ —	$105,489	$105,489	$ —	$ —
Owner-occupied commercial real estate	—	—	—	—	93,568	93,568	—	—
Investor commercial real estate	—	—	—	—	5,595	5,595	—	—
Construction	—	—	—	—	38,228	38,228	—	—
Single tenant lease financing	—	—	—	—	883,372	883,372	—	—
Public finance	—	—	—	—	610,858	610,858	—	—
Healthcare finance	—	—	—	—	89,525	89,525	—	—
Residential mortgage	—	98	—	98	362,476	362,574	179	—
Home equity	—	—	—	—	28,713	28,713	—	—
Other consumer	250	153	44	447	270,120	270,567	61	16
Total	$250	$ 251	$ 44	$ 545	$2,487,944	$2,488,489	$ 240	$ 16

	December 31, 2017							
	30-59 Days Past Due	60-89 Days Past Due	90 Days or More Past Due	Total Past Due	Current	Total Loans	Non-accrual Loans	Total Loans 90 Days or More Past Due and Accruing
Commercial and industrial	$—	$ 10	$ —	$ 10	$122,930	$122,940	$ —	$ —
Owner-occupied commercial real estate	—	—	—	—	75,768	75,768	—	—
Investor commercial real estate	—	—	—	—	7,273	7,273	—	—
Construction	—	—	—	—	49,213	49,213	—	—
Single tenant lease financing	—	—	—	—	803,299	803,299	—	—
Public finance	—	—	—	—	438,341	438,341	—	—
Healthcare finance	—	—	—	—	31,573	31,573	—	—
Residential mortgage	—	23	560	583	299,352	299,935	724	—
Home equity	—	—	83	83	30,471	30,554	83	—
Other consumer	299	110	6	415	227,118	227,533	32	—
Total	$299	$ 143	$ 649	$ 1,091	$2,085,338	$2,086,429	$ 839	$ —

Impaired Loans

A loan is designated as impaired, in accordance with the impairment accounting guidance, 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 loans as well as loans modified in troubled debt restructurings 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.

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, less costs to sell, and allows existing methods for recognizing interest income.

The following table presents the Company's impaired loans as of September 30, 2018 and December 31, 2017.

	September 30, 2018			December 31, 2017		
	Recorded Balance	Unpaid Principal Balance	Specific Allowance	Recorded Balance	Unpaid Principal Balance	Specific Allowance
Loans without a specific valuation allowance						
Commercial and industrial	$7,949	$7,949	$ —	$3,886	$ 3,886	$ —
Owner-occupied commercial real estate	1,479	1,479	—	7	7	—
Residential mortgage	579	579	—	1,139	1,144	—
Home equity	—	—	—	83	83	—
Other consumer	111	160	—	90	143	—
Total impaired loans	$10,118	$10,167	$ —	$5,205	$ 5,263	$ —

The table below presents average balances and interest income recognized for impaired loans during the three and nine months ended September 30, 2018 and 2017.

	Three Months Ended		Nine Months Ended		Three Months Ended		Nine Months Ended	
	September 30, 2018				September 30, 2017			
	Average Balance	Interest Income	Average Balance	Interest Income	Average Balance	Interest Income	Average Balance	Interest Income
Loans without a specific valuation allowance								
Commercial and industrial	$7,233	$ 561	$5,430	$ 723	$3,941	$ 71	$2,157	$ 71
Owner-occupied commercial real estate	1,249	75	553	82	4	—	1	—
Residential mortgage	573	—	768	—	1,690	7	1,673	7
Home equity	62	—	76	—	—	—	—	—
Other consumer	104	1	110	1	93	2	113	2
Total	9,221	637	6,937	806	5,728	80	3,944	80
Loans with a specific valuation allowance								
Commercial and industrial	—	—	—	$ —	50	—	46	—
Total	—	—	—	—	50	—	46	—
Total impaired loans	$9,221	$ 637	$6,937	$ 806	$5,778	$ 80	$3,990	$ 80

The Company had $0.6 million in residential mortgage other real estate owned as of September 30, 2018 and had $0.6 million in residential mortgage other real estate owned as of December 31, 2017. There were no loans in the process of foreclosure at September 30, 2018 and $0.2 million of loans in the process of foreclosure at December 31, 2017.

Troubled Debt Restructurings ("TDRs")

The loan portfolio includes TDRs, which are loans that have been modified to grant economic concessions to borrowers who have experienced financial difficulties. These concessions typically result from loss mitigation efforts and could include reductions in the interest rate, payment extensions, forgiveness of principal, forbearance, or other actions. Certain TDRs are classified as nonperforming at the time of restructuring and typically are returned to performing status after considering the borrower's sustained repayment performance for a reasonable period, generally not less than six consecutive months.

When loans are modified in a TDR, any possible impairment similar to other impaired loans is evaluated based on the present value of expected future cash flows, discounted at the contractual interest rate of the original loan agreement, or using the current fair value of the collateral, less selling costs for collateral dependent loans. If it is determined that the value of the modified loan is less than the recorded balance of the loan, impairment is recognized through a specific allowance or charge-off to the allowance. In periods subsequent to modification, all TDRs, including those that have payment defaults, are evaluated for possible impairment, and impairment is recognized through the allowance.

In the course of working with troubled borrowers, the Company may choose to restructure the contractual terms of certain loans in an effort to work out an alternative payment schedule with the borrower in order to optimize the collectability of the loan. Any loan modification is reviewed by the Company to identify whether a TDR has occurred when the Company grants a concession to the borrower that it would not otherwise consider based on economic or legal reasons related to a borrower's financial difficulties. Terms may be modified to fit the ability of the borrower to repay in line with its current financial status or the loan may be restructured to secure additional collateral and/or guarantees to support the debt, or a combination of the two.

There were no loans classified as new TDRs during the three and nine months ended September 30, 2018. There were no new loans classified as new TDRs during the three months ended September 30, 2017 and two commercial and industrial loans classified as new TDRs during the nine months ended September 30, 2017 with a pre-modification and post-modification outstanding recorded investment of $1.8 million. The Company did not allocate a specific allowance for those loans as of September 30, 2017. The modifications consisted of maturity date amendments and certain other term modifications.

Note 5: Premises and Equipment

The following table summarizes premises and equipment at September 30, 2018 and December 31, 2017.

	September 30, 2018	December 31, 2017
Land	$ 2,500	$ 2,500
Building and improvements	6,175	6,427
Furniture and equipment	9,024	7,610
Less: accumulated depreciation	(7,658)	(6,479)
Total	$ 10,041	$ 10,058

Note 6: Goodwill

As of September 30, 2018 and December 31, 2017, the carrying amount of goodwill was $4.7 million. There have been no changes in the carrying amount of goodwill for the periods ended September 30, 2018 and December 31, 2017. Goodwill is tested for impairment on an annual basis as of August 31, or whenever events or changes in circumstances indicate the carrying amount of goodwill exceeds its implied fair value. No events or changes in circumstances have occurred since the August 31, 2018 annual impairment test that would suggest it was more likely than not goodwill impairment existed.

Note 7: Subordinated Debt

In June 2013, the Company issued a subordinated debenture (the "2021 Debenture") in the principal amount of $3.0 million. The 2021 Debenture bore a fixed interest rate of 8.00% per year, payable quarterly, and was scheduled to mature on June 28, 2021. The 2021 Debenture could be repaid, without penalty, at any time after June 28, 2016. The Company repaid the 2021 Debenture in full in June 2018.

In connection with the 2021 Debenture, the Company also issued a warrant to purchase up to 48,750 shares of common stock at an initial per share exercise price equal to $19.33. The warrant became exercisable on June 28, 2014. On May 4, 2017, the Company issued a net amount of 15,915 shares of common stock pursuant to an exercise by the holder of a warrant to purchase 48,750 shares of common stock at a price of $19.33 per share. The holder satisfied the exercise price by instructing the Company to withhold 32,835 of the shares of common stock in accordance with the warrant's cashless exercise feature.

In October 2015, the Company entered into a term loan in the principal amount of $10.0 million, evidenced by a term note due 2025 (the “2025 Note”). The 2025 Note bears a fixed interest rate of 6.4375% per year, payable quarterly, and is scheduled to mature on October 1, 2025. The 2025 Note is an unsecured subordinated obligation of the Company and may be repaid, without penalty, on any interest payment date on or after October 15, 2020. The 2025 Note is intended to qualify as Tier 2 capital under regulatory guidelines.

In September 2016, the Company issued $25.0 million aggregate principal amount of 6.0% Fixed-to-Floating Rate Subordinated Notes due 2026 (the "2026 Notes") in a public offering. The 2026 Notes initially bear a fixed interest rate of 6.00% per year to, but excluding September 30, 2021, and thereafter a floating rate equal to the then-current three-month LIBOR rate plus 485 basis points. All interest on the 2026 Notes is payable quarterly. The 2026 Notes are scheduled to mature on September 30, 2026. The 2026 Notes are unsecured subordinated obligations of the Company and may be repaid, without penalty, on any interest payment date on or after September 30, 2021. The 2026 Notes are intended to qualify as Tier 2 capital under regulatory guidelines.

The following table presents the principal balance and unamortized discount and debt issuance costs for the 2021 Debenture, the 2025 Note and the 2026 Notes as of September 30, 2018 and December 31, 2017.

	September 30, 2018		December 31, 2017	
	Principal	Unamortized Discount and Debt Issuance Costs	Principal	Unamortized Discount and Debt Issuance Costs
2021 Debenture	$—	$ —	$3,000	$ —
2025 Note	10,000	(168)	10,000	(186)
2026 Notes	25,000	(995)	25,000	(1,088)
Total	$35,000	$ (1,163)	$38,000	$ (1,274)

Note 8: Benefit Plans

Employment Agreement

The Company has entered into an employment agreement with its Chief Executive Officer that provides for the continuation of salary and certain benefits for a specified period of time under certain conditions. Under the terms of the agreement, these payments could occur in the event of a termination of employment by us without "cause", by him for "good reason" or in connection with a "change in control," each as defined in the agreement, along with other specific conditions.

2013 Equity Incentive Plan

The 2013 Equity Incentive Plan (the "2013 Plan") authorizes the issuance of 750,000 shares of the Company's common stock in the form of equity-based awards to employees, directors, and other eligible persons. Under the terms of the 2013 Plan, the pool of shares available for issuance may be used for available types of equity awards under the 2013 Plan, which includes stock options, stock appreciation rights, restricted stock awards, stock unit awards, and other share-based awards. All employees, consultants, and advisors of the Company or any subsidiary, as well as all non-employee directors of the Company, are eligible to receive awards under the 2013 Plan.

The Company recorded $0.3 million and $1.3 million of share-based compensation expense for the three and nine months ended September 30, 2018, respectively, related to awards made under the 2013 Plan. The Company recorded $0.3 million and $0.8 million of share-based compensation expense for the three and nine months ended September 30, 2017, respectively, related to awards made under the 2013 Plan.

The following table summarizes the status of the 2013 Plan awards as of September 30, 2018, and activity for the nine months ended September 30, 2018.

	Restricted Stock	Weighted-Average Grant Date Fair	Restricted Stock	Weighted-Average Grant Date Fair	Deferred Stock	Weighted-Average Grant Date Fair

	Units	Value Per Share	Awards	Value Per Share	Units	Value Per Share
Nonvested at December 31, 2017	72,765	$ 27.91	3,333	$ 24.44	—	$ —
Granted	41,334	40.69	11,294	38.75	4	37.23
Vested	(34,241)	26.06	(11,395)	37.21	(4)	37.23
Forfeited	(4,477)	34.57	—	—	—	—
Nonvested at September 30, 2018	75,381	$ 35.36	3,232	$ 31.37	—	$ —

At September 30, 2018, the total unrecognized compensation cost related to nonvested awards was $2.1 million with a weighted-average expense recognition period of 2.0 years.

Directors Deferred Stock Plan

Until January 1, 2014, the Company had a practice granting awards under a stock compensation plan for members of the Board of Directors ("Directors Deferred Stock Plan"). The Company reserved 180,000 shares of common stock that could have been issued pursuant to the Directors Deferred Stock Plan. The Directors Deferred Stock Plan provided directors the option to elect to receive up to 100% of their annual retainer in either common stock or deferred stock rights. Deferred stock rights were to be settled in common stock following the end of the deferral period payable on the basis of one share of common stock for each deferred stock right.

The following table summarizes the status of deferred stock rights related to the Directors Deferred Stock Plan for the nine months ended September 30, 2018.

	Deferred Stock Rights
Outstanding, beginning of period	82,995
Granted	394
Exercised	—
Outstanding, end of period	83,389

All deferred stock rights granted during the 2018 period were additional rights issued in lieu of cash dividends payable on outstanding deferred stock rights.

Note 9: Fair Value of Financial Instruments

ASC Topic 820, Fair Value Measurement, defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. ASC Topic 820 also specifies a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The standard describes three levels of inputs that may be used to measure fair value:

Level 1 Quoted prices in active markets for identical assets or liabilities

Level 2 Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities

Level 3 Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities

Following is a description of the valuation methodologies and inputs used for assets measured at fair value on a recurring basis and recognized in the accompanying condensed consolidated balance sheets, as well as the general classification of such assets pursuant to the valuation hierarchy.

Available-for-Sale Securities

Where quoted market prices are available in an active market, securities are classified within Level 1 of the valuation hierarchy. Level 1 securities include highly liquid mutual funds. If quoted market prices are not available, then fair values are estimated by using pricing models, quoted prices of securities with similar characteristics or discounted cash flows.

Level 2 securities include U.S. Government-sponsored agencies, municipal securities, mortgage and asset-backed securities and certain corporate securities. Matrix pricing is a mathematical technique widely used in the banking industry to value investment securities without relying exclusively on quoted prices for specific investment securities but also on the investment securities' relationship to other benchmark quoted investment securities.

In certain cases where Level 1 or Level 2 inputs are not available, securities are classified within Level 3 of the hierarchy. Fair values are calculated using discounted cash flows. Discounted cash flows are calculated based off of the anticipated future cash flows updated to incorporate loss severities. Rating agency and industry research reports as well as default and deferral activity are reviewed and incorporated into the calculation. The Company did not own any securities classified within Level 3 of the hierarchy as of September 30, 2018 or December 31, 2017.

Loans Held-for-Sale (mandatory pricing agreements)

The fair value of loans held-for-sale is determined using quoted prices for similar assets, adjusted for specific attributes of that loan (Level 2).

Forward Contracts

The fair values of forward contracts on to-be-announced securities are determined using quoted prices in active markets, or benchmarked thereto (Level 1).

Interest Rate Lock Commitments

The fair values of interest rate lock commitments (“IRLCs”) are determined using the projected sale price of individual loans based on changes in market interest rates, projected pull-through rates (the probability that an IRLC will ultimately result in an originated loan), the reduction in the value of the applicant’s option due to the passage of time, and the remaining origination costs to be incurred based on management’s estimate of market costs (Level 3).

The following tables present the fair value measurements of assets and liabilities recognized in the accompanying condensed consolidated balance sheets measured at fair value on a recurring basis and the level within the fair value hierarchy in which the fair value measurements fall at September 30, 2018 and December 31, 2017.

		September 30, 2018 Fair Value Measurements Using		
	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
U.S. Government-sponsored agencies	$112,760	$ —	$ 112,760	$ —
Municipal securities	91,080	—	91,080	—
Mortgage-backed securities	225,692	—	225,692	—
Asset-backed securities	4,960	—	4,960	—
Corporate securities	34,505	—	34,505	—
Total available-for-sale securities	468,997	—	468,997	—
Loans held-for-sale (mandatory pricing agreements)	23,493	—	23,493	—
Interest rate swap assets	8,032	—	8,032	—
Interest rate swap liabilities	(72)	—	(72)	—
Forward contracts	127	127	—	—
IRLCs	383	—	—	383

		December 31, 2017 Fair Value Measurements Using		
	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
U.S. Government-sponsored agencies	$133,190	$ —	$ 133,190	$ —
Municipal securities	96,377	—	96,377	—
Mortgage-backed securities	209,720	—	209,720	—
Asset-backed securities	5,009	—	5,009	—
Corporate securities	26,047	—	26,047	—
Other securities	2,932	2,932	—	—
Total available-for-sale securities	473,275	2,932	470,343	—
Loans held-for-sale (mandatory pricing agreements)	23,571	—	23,571	—
Interest rate swaps	(271)	—	(271)	—
Forward contracts	(80)	(80)	—	—
IRLCs	551	—	—	551

The following tables reconcile the beginning and ending balances of recurring fair value measurements recognized in the accompanying condensed consolidated balance sheets using significant unobservable (Level 3) inputs for the three and nine months ended September 30, 2018 and 2017.

	Three Months Ended Interest Rate Lock Commitments
Balance, July 1, 2018	$ 724
Total realized losses	
Included in net income	(341)
Balance, September 30, 2018	$ 383
Balance, July 1, 2017	$ 652
Total realized gains	
Included in net income	135
Balance, September 30, 2017	$ 787

	Nine Months Ended Interest Rate Lock Commitments
Balance, January 1, 2018	$ 551
Total realized losses	
Included in net income	(168)
Balance, September 30, 2018	$ 383
Balance, January 1, 2017	$ 610
Total realized gains	
Included in net income	177
Balance, September 30, 2017	$ 787

Significant Unobservable (Level 3) Inputs

The following tables present quantitative information about significant unobservable inputs used in recurring and Level 3 fair value measurements other than goodwill.

	Fair Value at September 30, 2018	Valuation Technique	Significant Unobservable Inputs	Range
IRLCs	$ 383	Discounted cash flow	Loan closing rates	38% - 100%

	Fair Value at December 31, 2017	Valuation Technique	Significant Unobservable Inputs	Range
IRLCs	$ 551	Discounted cash flow	Loan closing rates	39% - 100%

The following methods were used to estimate the fair value of all other financial instruments recognized in the accompanying condensed consolidated balance sheets at amounts other than fair value.

Cash and Cash Equivalents

For these instruments, the carrying amount is a reasonable estimate of fair value.

Interest-Bearing Time Deposits

The fair value of these financial instruments approximates carrying value.

Securities Held-to-Maturity

Fair values are determined by using models that are based on security-specific details, as well as relevant industry and economic factors. The most significant of these inputs are quoted market prices, and interest rate spreads on relevant benchmark securities.

Loans Held-for-Sale (best efforts pricing agreements)

The fair value of these loans approximates carrying value.

Loans

The fair value of loans as of September 30, 2018 was impacted by the adoption of Accounting Standards Update 2016-01, which is discussed further in Note 12 of the consolidated financial statements. In accordance with Accounting Standards Update 2016-01, the fair value of loans are estimated on an exit price basis incorporating discounts for credit, liquidity and marketability factors. This is not comparable with the fair values disclosed for December 31, 2017, which were based on an entrance price basis. For that date, fair values of variable rate loans that reprice frequently and with no significant change in credit risk were based on carrying values. The fair value of other loans as of that date were estimated by discounted cash flow analysis, which used interest rates then being offered for loans with similar terms to borrowers of similar credit quality.

Accrued Interest Receivable

The fair value of these financial instruments approximates carrying value.

Federal Home Loan Bank of Indianapolis Stock

The fair value approximates carrying value.

Deposits

The fair value of noninterest-bearing and interest-bearing demand deposits, savings and money market accounts approximates carrying value. The fair value of fixed maturity certificates of deposit and brokered deposits are estimated using rates currently offered for deposits of similar remaining maturities.

Advances from Federal Home Loan Bank

The fair value of fixed rate advances is estimated using rates currently available for advances with similar remaining maturities. The carrying value of variable rate advances approximates fair value.

Subordinated Debt

The fair value of the Company’s publicly traded subordinated debt is obtained from quoted market prices. The fair value of the Company’s remaining subordinated debt is estimated using discounted cash flow analysis, based on current borrowing rates for similar types of debt instruments.

Accrued Interest Payable

The fair value of these financial instruments approximates carrying value.

Commitments

The fair value of commitments to extend credit are based on fees currently charged to enter into similar agreements with similar maturities and interest rates. The Company determined that the fair value of commitments was zero based on the contractual value of outstanding commitments at each of September 30, 2018 and December 31, 2017.

The following tables present the carrying value and estimated fair value of all financial assets and liabilities at September 30, 2018 and December 31, 2017.

	September 30, 2018				
			Fair Value Measurements Using		
	Carrying Amount	Fair Value	Quoted Prices In Active Market for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Cash and cash equivalents	$ 85,790	$ 85,790	$ 85,790	$ —	$ —
Securities held-to-maturity	20,200	19,510	—	19,510	—
Net loans	2,476,918	2,347,403	—	—	2,347,403
Accrued interest receivable	14,472	14,472	14,472	—	—
Federal Home Loan Bank of Indianapolis stock	22,050	22,050	—	22,050	—
Deposits	2,446,564	2,423,037	663,012	—	1,760,025
Advances from Federal Home Loan Bank	425,160	414,668	—	414,668	—
Subordinated debt	33,837	35,877	25,630	10,247	—
Accrued interest payable	887	887	887	—	—

	December 31, 2017				
			Fair Value Measurements Using		
	Carrying Amount	Fair Value	Quoted Prices In Active Market for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Cash and cash equivalents	$ 47,981	$ 47,981	$ 47,981	$ —	$ —
Securities held-to-maturity	19,209	19,083	—	19,083	—
Loans held-for-sale (best efforts pricing agreements)	27,836	27,836	—	27,836	—
Net loans	2,076,223	2,036,575	—	—	2,036,575
Accrued interest receivable	11,944	11,944	11,944	—	—
Federal Home Loan Bank of Indianapolis stock	19,575	19,575	—	19,575	—
Deposits	2,084,941	2,057,708	688,800	—	1,368,908
Advances from Federal Home Loan Bank	410,176	397,950	—	397,950	—
Subordinated debt	36,726	39,972	26,520	13,452	—
Accrued interest payable	311	311	311	—	—

Note 10: Mortgage Banking Activities

The Company's residential real estate lending business originates mortgage loans for customers and typically sells a majority of the originated loans into the secondary market. For most of the mortgages it sells in the secondary market, the Company hedges its mortgage banking pipeline by entering into forward contracts for the future delivery of mortgage loans to third party investors and entering into IRLCs with potential borrowers to fund specific mortgage loans that will be sold into the secondary market. To facilitate the hedging of the loans, the Company has elected the fair value option for loans originated and intended for sale in the secondary market under mandatory pricing agreements. Changes in the fair value of loans held-for-sale, IRLCs and forward contracts are recorded in the mortgage banking activities line item within noninterest income. Refer to Note 11 for further information on derivative financial instruments.

During the three months ended September 30, 2018 and 2017, the Company originated mortgage loans held-for-sale of $104.1 million and $107.8 million, respectively, and sold $102.8 million and $118.3 million of mortgage loans, respectively, into the secondary market. During the nine months ended September 30, 2018 and 2017, the Company originated mortgage loans held-for-sale of $282.5 million and $302.9 million, respectively, and sold $287.6 million and $317.2 million of mortgage loans, respectively, into the secondary market. Additionally, during the nine months ended September 30, 2018, the Company sold $25.2 million of portfolio mortgage loans to an investor, resulting in a gain of $0.4 million.

The following table presents the components of income from mortgage banking activities for the three and nine months ended September 30, 2018 and 2017.

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
Gain on loans sold	$1,622	$2,453	$4,787	$5,876
(Loss) gain resulting from the change in fair value of loans held-for-sale	(168)	(6)	(250)	519
(Loss) gain resulting from the change in fair value of derivatives	(52)	88	40	(89)
Net revenue from mortgage banking activities	$1,402	$2,535	$4,577	$6,306

Fluctuations in interest rates and changes in IRLC and loan volume within the mortgage banking pipeline may cause volatility in the fair value of loans held-for-sale and the fair value of derivatives used to hedge the mortgage banking pipeline.

Note 11: Derivative Financial Instruments

The Company uses derivative financial instruments to help manage exposure to interest rate risk and the effects that changes in interest rates may have on net income and the fair value of assets and liabilities. The Company enters into interest rate swap agreements as part of its asset/liability management strategy to help manage its interest rate risk position. Additionally, the Company enters into forward contracts for the future delivery of mortgage loans to third party investors and enters into IRLCs with potential borrowers to fund specific mortgage loans that will be sold into the secondary market. The forward contracts are entered into in order to economically hedge the effect of changes in interest rates resulting from the Company’s commitment to fund the loans.

The Company entered into various interest rate swap agreements designated and qualifying as accounting hedges during the reported periods. Designating an interest rate swap as an accounting hedge allows the Company to recognize gains and losses, less any ineffectiveness, in the income statement within the same period that the hedged item affects earnings. The Company includes the gain or loss on the hedged items in the same line item as the offsetting loss or gain on the related interest rate swaps. For derivative instruments that are designated and qualify as cash flow hedges, any gains or losses related to changes in fair value are recorded in accumulated other comprehensive loss, net of tax. The fair value of interest rate swaps with a positive fair value are reported in accrued income and other assets in the condensed consolidated balance sheets while interest rate swaps with a negative fair value are reported in accrued expenses and other liabilities in the condensed consolidated balance sheets.

The IRLCs and forward contracts are not designated as accounting hedges, and are recorded at fair value with changes in fair value reflected in noninterest income on the condensed consolidated statements of income. The fair value of derivative instruments with a positive fair value are reported in accrued income and other assets in the condensed consolidated balance sheets while derivative instruments with a negative fair value are reported in accrued expenses and other liabilities in the condensed consolidated balance sheets.

The following table presents amounts that were recorded on the condensed consolidated balance sheets related to cumulative basis adjustments for interest rate swap derivatives designated as fair value accounting hedges as of September 30, 2018 and December 31, 2017.

Line item in the condensed consolidated balance sheets in which the hedged item is included	Carrying amount of the hedged asset		Cumulative amount of fair value hedging adjustment included in the carrying amount of the hedged assets	
	September 30, 2018	December 31, 2017	September 30, 2018	December 31, 2017
Loans	$366,948	$91,653		