SANDY SPRING BANCORP INC
Form 10-Q
August 04, 2017

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

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

For the Quarterly Period Ended June 30, 2017

OR

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

For the transition period from ____________ to ____________

Commission File Number: 0-19065

SANDY SPRING BANCORP, INC.

(Exact name of registrant as specified in its charter)

Maryland	**52-1532952**
(State of incorporation)	(I.R.S. Employer Identification Number)

17801 Georgia Avenue, Olney, Maryland	**20832**
(Address of principal executive office)	(Zip Code)

301-774-6400

(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 filing requirements for the past 90 days.

Yes X No __

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes X 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 X 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 X

The number of outstanding shares of common stock outstanding as of August 1, 2017

Common stock, $1.00 par value – 23,987,383 shares

SANDY SPRING BANCORP, INC.

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Forward-Looking Statements

This Quarterly Report on Form 10-Q, as well as other periodic reports filed with the Securities and Exchange Commission, and written or oral communications made from time to time by or on behalf of Sandy Spring Bancorp and its subsidiaries (the “Company”), may contain statements relating to future events or future results of the Company that are considered “forward-looking statements” under the Private Securities Litigation Reform Act of 1995. These forward-looking statements may be identified by the use of words such as “believe,” “expect,” “anticipate,” “plan,” “estimate,” “intend” and “potential,” or words of similar meaning, or future or conditional verbs such as “should,” “could,” or “may.” Forward-looking statements include statements of our goals, intentions and expectations; statements regarding our business plans, prospects, growth and operating strategies; statements regarding the quality of our loan and investment portfolios; and estimates of our risks and future costs and benefits.

Forward-looking statements reflect our expectation or prediction of future conditions, events or results based on information currently available. These forward-looking statements are subject to significant risks and uncertainties that may cause actual results to differ materially from those in such statements. These risks and uncertainties include, but are not limited to, the risks identified in Item 1A of the Company’s 2016 Annual Report on Form 10-K, Item 1A of Part II of this report and the following:

- general business and economic conditions nationally or in the markets that the Company serves could adversely affect, among other things, real estate prices, unemployment levels, and consumer and business confidence, which could lead to decreases in the demand for loans, deposits and other financial services that we provide and increases in loan delinquencies and defaults;

- changes or volatility in the capital markets and interest rates may adversely impact the value of securities, loans, deposits and other financial instruments and the interest rate sensitivity of our balance sheet as well as our liquidity;

- our liquidity requirements could be adversely affected by changes in our assets and liabilities;

- our investment securities portfolio is subject to credit risk, market risk, and liquidity risk as well as changes in the estimates we use to value certain of the securities in our portfolio;

- 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 companies, including product and pricing pressures and our ability to attract, develop and retain qualified banking professionals;

- the effect of changes in accounting policies and practices, as may be adopted by the Financial Accounting Standards Board, the Securities and Exchange Commission, the Public Company Accounting Oversight Board and other regulatory agencies; and

- the effect of fiscal and governmental policies of the United States federal government.

Forward-looking statements speak only as of the date of this report. The Company does not undertake to update forward-looking statements to reflect circumstances or events that occur after the date of this report or to reflect the occurrence of unanticipated events except as required by federal securities laws.

Part I
Item 1. FINANCIAL STATEMENTS
Sandy Spring Bancorp, Inc. and Subsidiaries
CONDENSED CONSOLIDATED STATEMENTS OF CONDITION - UNAUDITED

(Dollars in thousands)	**June 30, 2017**	December 31, 2016
Assets		
Cash and due from banks	**$ 48,637**	$ 53,190
Federal funds sold	**2,831**	1,953
Interest-bearing deposits with banks	**25,468**	78,982
Cash and cash equivalents	**76,936**	134,125
Residential mortgage loans held for sale (at fair value)	**5,743**	13,222
Investments available-for-sale (at fair value)	**780,078**	733,554
Other equity securities	**41,413**	46,094
Total loans	**4,133,171**	3,927,808
Less: allowance for loan losses	**(45,079)**	(44,067)
Net loans	**4,088,092**	3,883,741
Premises and equipment, net	**53,235**	53,562
Other real estate owned	**1,460**	1,911
Accrued interest receivable	**14,910**	14,589
Goodwill	**85,768**	85,768
Other intangible assets, net	**629**	680
Other assets	**122,257**	124,137
Total assets	**$ 5,270,521**	$ 5,091,383
Liabilities		
Noninterest-bearing deposits	**$ 1,302,536**	$ 1,138,139
Interest-bearing deposits	**2,582,909**	2,439,405
Total deposits	**3,885,445**	3,577,544
Securities sold under retail repurchase agreements and federal funds purchased	**127,312**	125,119
Advances from FHLB	**670,000**	790,000
Subordinated debentures	**-**	30,000
Accrued interest payable and other liabilities	**33,081**	35,148
Total liabilities	**4,715,838**	4,557,811
Stockholders' Equity		
Common stock -- par value $1.00; shares authorized 50,000,000; shares issued and outstanding 23,983,997 and 23,901,084 at June 30, 2017 and December 31, 2016, respectively	**23,984**	23,901
Additional paid in capital	**166,705**	165,871
Retained earnings	**367,706**	350,414
Accumulated other comprehensive loss	**(3,712)**	(6,614)
Total stockholders' equity	**554,683**	533,572
Total liabilities and stockholders' equity	**$ 5,270,521**	$ 5,091,383

The accompanying notes are an integral part of these statements

SANDY SPRING BANCORP, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF INCOME - UNAUDITED

	Three Months Ended June 30,		Six Months Ended June 30,	
(Dollars in thousands, except per share data)	**2017**	2016	**2017**	2016
Interest income:				
Interest and fees on loans and leases	**$ 42,747**	$ 36,928	**$ 82,970**	$ 73,134
Interest on loans held for sale	**72**	64	**154**	198
Interest on deposits with banks	**91**	54	**181**	107
Interest and dividends on investment securities:				
Taxable	**3,554**	2,840	**7,162**	6,126
Exempt from federal income taxes	**2,106**	1,916	**4,057**	3,889
Interest on federal funds sold	**6**	1	**10**	2
Total interest income	**48,576**	41,803	**94,534**	83,456
Interest expense:				
Interest on deposits	**3,023**	2,041	**5,511**	3,878
Interest on retail repurchase agreements and federal funds purchased	**79**	72	**155**	138
Interest on advances from FHLB	**3,148**	2,739	**6,277**	6,113
Interest on subordinated debt	**-**	219	**12**	473
Total interest expense	**6,250**	5,071	**11,955**	10,602
Net interest income	**42,326**	36,732	**82,579**	72,854
Provision for loan losses	**1,322**	2,957	**1,516**	4,193
Net interest income after provision for loan losses	**41,004**	33,775	**81,063**	68,661
Non-interest income:				
Investment securities gains	**1,273**	150	**1,275**	1,919
Service charges on deposit accounts	**2,017**	1,956	**3,981**	3,859
Mortgage banking activities	**840**	1,106	**1,448**	1,641
Wealth management income	**4,744**	4,448	**9,228**	8,853
Insurance agency commissions	**1,222**	949	**2,974**	2,394
Income from bank owned life insurance	**605**	615	**1,199**	1,230
Bank card fees	**1,253**	1,220	**2,398**	2,309
Other income	**1,617**	2,307	**3,700**	3,909
Total non-interest income	**13,571**	12,751	**26,203**	26,114
Non-interest expense:				
Salaries and employee benefits	**18,282**	17,221	**36,083**	35,451
Occupancy expense of premises	**3,211**	3,162	**6,613**	6,635
Equipment expense	**1,767**	1,693	**3,491**	3,357
Marketing	**776**	662	**1,439**	1,343
Outside data services	**1,367**	1,355	**2,759**	2,718
FDIC insurance	**823**	649	**1,628**	1,286
Amortization of intangible assets	**25**	28	**51**	60
Merger expenses	**987**	-	**987**	-
Other expense	**5,630**	6,101	**9,798**	12,338
Total non-interest expense	**32,868**	30,871	**62,849**	63,188
Income before income taxes	**21,707**	15,655	**44,417**	31,587
Income tax expense	**6,966**	5,008	**14,564**	10,127
Net income	**$ 14,741**	$ 10,647	**$ 29,853**	$ 21,460

Per share information:								
Basic net income per share	**$**	**0.61**	$	0.45	**$**	**1.24**	$	0.90
Diluted net income per share	**$**	**0.61**	$	0.44	**$**	**1.23**	$	0.89
Dividends declared per common share	**$**	**0.26**	$	0.24	**$**	**0.52**	$	0.48

The accompanying notes are an integral part of these statements

SANDY SPRING BANCORP, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME - UNAUDITED

	Three Months Ended June 30,		Six Months Ended June 30,	
(In thousands)	**2017**	2016	**2017**	2016
Net income	**$ 14,741**	$ 10,647	**$ 29,853**	$ 21,460
Other comprehensive income:				
Investments available-for-sale:				
Net change in unrealized gains on investments available-for-sale	**4,003**	2,598	**5,505**	13,253
Related income tax expense	**(1,593)**	(1,031)	**(2,191)**	(5,263)
Net investment gains reclassified into earnings	**(1,273)**	(150)	**(1,275)**	(1,919)
Related income tax expense	**508**	60	**508**	765
Net effect on other comprehensive income for the period	**1,645**	1,477	**2,547**	6,836
Defined benefit pension plan:				
Recognition of unrealized loss	**295**	291	**590**	575
Related income tax benefit	**(118)**	(115)	**(235)**	(228)
Net effect on other comprehensive income for the period	**177**	176	**355**	347
Total other comprehensive income	**1,822**	1,653	**2,902**	7,183
Comprehensive income	**$ 16,563**	$ 12,300	**$ 32,755**	$ 28,643

The accompanying notes are an integral part of these statements

SANDY SPRING BANCORP, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS - UNAUDITED

	Six Months Ended June 30,	
(Dollars in thousands)	**2017**	2016
Operating activities:		
Net income	**$ 29,853**	$ 21,460
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	**3,967**	3,897
Provision for loan losses	**1,516**	4,193
Share based compensation expense	**1,052**	992
Tax benefits associated with share based compensation	**692**	267
Deferred income tax expense/(benefit)	**(540)**	60
Origination of loans held for sale	**(70,736)**	(72,226)
Proceeds from sales of loans held for sale	**79,489**	94,282
Gains on sales of loans held for sale	**(1,443)**	(1,517)
(Gains) losses on sales of other real estate owned	**(17)**	52
Investment securities gains	**(1,275)**	(1,919)
Net (increase) decrease in accrued interest receivable	**(321)**	44
Net decrease in other assets	**(1,506)**	(2,526)
Net increase (decrease) in accrued expenses and other liabilities	**(4,069)**	(3,880)
Other – net	**3,605**	650
Net cash provided by operating activities	**40,267**	43,829
Investing activities:		
Proceeds of other equity securities	**4,681**	6,994
Purchases of investments available-for-sale	**(115,028)**	(113,273)
Proceeds from sales of investment available-for-sale	**2,251**	40,863
Proceeds from maturities, calls and principal payments of investments held-to-maturity	**-**	5,004
Proceeds from maturities, calls and principal payments of investments available-for-sale	**70,361**	179,038
Net increase in loans	**(223,705)**	(195,826)
Proceeds from the sales of other real estate owned	**759**	1,352
Proceeds from sales of loans previously held for investment	**18,222**	-
Expenditures for premises and equipment	**(2,395)**	(2,594)
Net cash provided (used) in investing activities	**(244,854)**	(78,442)
Financing activities:		
Net increase in deposits	**307,901**	246,411
Net increase in retail repurchase agreements and federal funds purchased	**2,193**	8,742
Proceeds from advances from FHLB	**2,220,000**	1,290,000
Repayment of advances from FHLB	**(2,340,000)**	(1,460,000)
Retirement of subordinated debt	**(30,000)**	(5,000)
Proceeds from issuance of common stock	**817**	728
Stock tendered for payment of withholding taxes	**(952)**	(683)
Repurchase of common stock	**-**	(13,273)
Dividends paid	**(12,561)**	(11,622)
Net cash provided by financing activities	**147,398**	55,303

Net increase (decrease) in cash and cash equivalents		**(57,189)**		20,690
Cash and cash equivalents at beginning of period		**134,125**		72,882
Cash and cash equivalents at end of period	**$**	**76,936**	$	93,572
Supplemental disclosures:				
Interest payments	**$**	**12,391**	$	11,114
Income tax payments		**16,287**		12,984
Transfer of investments held-to-maturity to available-for-sale		**-**		203,118
Transfer from loans to residential mortgage loans held for sale		**18,053**		18,752
Transfer from loans to other real estate owned		**288**		-

The accompanying notes are an integral part of these statements

SANDY SPRING BANCORP, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY - UNAUDITED

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(Dollars in thousands, except per share data)	Common Stock	Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Stockholders' Equity
Balances at January 1, 2017	**$ 23,901**	**$ 165,871**	**$ 350,414**	**$ (6,614)**	**$ 533,572**
Net income	**-**	**-**	**29,853**	**-**	**29,853**
Other comprehensive income, net of tax	**-**	**-**	**-**	**2,902**	**2,902**
Common stock dividends - $0.52 per share	**-**	**-**	**(12,561)**	**-**	**(12,561)**
Stock compensation expense	**-**	**1,052**	**-**	**-**	**1,052**
Common stock issued pursuant to:					
Stock option plan - 27,284 shares	**27**	**491**	**-**	**-**	**518**
Employee stock purchase plan - 8,565 shares	**9**	**290**	**-**	**-**	**299**
Restricted stock - 47,064 shares	**47**	**(999)**	**-**	**-**	**(952)**
Balances at June 30, 2017	**$ 23,984**	**$ 166,705**	**$ 367,706**	**$ (3,712)**	**$ 554,683**
Balance at January 1, 2016	$ 24,296	$ 175,588	$ 325,840	$ (1,297)	$ 524,427
Net income	-	-	21,460	-	21,460
Other comprehensive income, net of tax	-	-	-	7,183	7,183
Common stock dividends - $0.48 per share	-	-	(11,622)	-	(11,622)
Stock compensation expense	-	992	-	-	992
Common stock issued pursuant to:					
Stock option plan - 28,941 shares	29	393	-	-	422
Employee stock purchase plan - 12,471 shares	12	279	-	-	291
Director's stock purchase plan - 258 shares	1	15	-	-	16
Restricted stock - 49,648 shares	49	(466)	-	-	(417)
Purchase of treasury shares - 512,459 shares	(512)	(12,761)	-	-	(13,273)
Balances at June 30, 2016	$ 23,875	$ 164,040	$ 335,678	$ 5,886	$ 529,479

The accompanying notes are an integral part of these statements

Sandy Spring Bancorp, Inc. and Subsidiaries

Notes to the CONDENSED Consolidated Financial Statements - UNAUDITED

Note 1 – Significant Accounting Policies

Nature of Operations

Sandy Spring Bancorp (the "Company"), a Maryland corporation, is the bank holding company for Sandy Spring Bank (the "Bank"). The Bank offers a broad range of commercial banking, retail banking, mortgage and trust services throughout central Maryland, Northern Virginia and the greater Washington D.C. market through its operation of 44 community offices and six financial centers across the region. The Bank also offers a comprehensive menu of insurance and wealth management services through its subsidiaries, Sandy Spring Insurance Corporation and West Financial Services, Inc.

Basis of Presentation

The accounting and reporting policies of the Company conform to accounting principles generally accepted in the United States of America ("GAAP") and prevailing practices within the financial services industry for interim financial information and Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and notes required for complete financial statements and prevailing practices within the banking industry. The following summary of significant accounting policies of the Company is presented to assist the reader in understanding the financial and other data presented in this report. Operating results for the three and six months ended June 30, 2017 are not necessarily indicative of the results that may be expected for any future periods or for the year ending December 31, 2017. In the opinion of management, all adjustments (comprising only normal recurring accruals) necessary for a fair presentation of the results of the interim periods have been included. Certain reclassifications have been made to prior period amounts, as necessary, to conform to the current period presentation. The Company has evaluated subsequent events through the date of the issuance of its financial statements.

These statements should be read in conjunction with the financial statements and accompanying notes included in the Company's 2016 Annual Report on Form 10-K as filed with the Securities and Exchange Commission ("SEC") on March 3, 2017. There have been no significant changes to the Company's accounting policies as disclosed in the 2016 Annual Report on Form 10-K.

Principles of Consolidation

The unaudited condensed consolidated financial statements include the accounts of the Company and its wholly owned subsidiary, Sandy Spring Bank and its subsidiaries, Sandy Spring Insurance Corporation and West Financial Services, Inc. Consolidation has resulted in the elimination of all intercompany accounts and transactions.

Use of Estimates

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the date of the financial statements, and affect the reported amounts of revenues earned and expenses incurred during the reporting period. Actual results could differ from those estimates. Estimates that could change significantly relate to the provision for loan losses and the related allowance, determination of impaired loans and the related measurement of impairment, potential impairment of goodwill or other intangible assets, valuation of investment securities and the determination of whether impaired securities are other-than-temporarily impaired, valuation of other real estate owned, prepayment rates, valuation of share-based compensation, the assessment that a liability should be recognized with respect to any matters under litigation, the calculation of current and deferred income taxes and the actuarial projections related to pension expense and the related liability.

Cash Flows

For purposes of reporting cash flows, cash and cash equivalents include cash and due from banks, federal funds sold and interest-bearing deposits with banks (items with stated original maturity of three months or less).

Pending Accounting Pronouncements

The FASB issued Update No. 2017-08, *Receivables-Nonrefundable Fees and Other Costs (Subtopic 310-20): Premium Amortization on Purchased Callable Debt Securities*, in March 2017. This guidance is intended to eliminate the current diversity in practice with respect to the amortization period for certain purchased callable debt securities held at a premium. Under current generally accepted accounting principles (GAAP), entities generally amortize the premium as an adjustment of yield over the contractual life. As a result, upon the exercise of a call on a callable debt security held at a premium, the unamortized premium is recorded as a loss in earnings. The amendments in this update shorten the amortization period for such callable debt securities held at a premium requiring the premium to be amortized to the earliest call date. This guidance is effective for a public business entity that is a U.S. Securities and Exchange Commission (SEC) filer for its fiscal years, and interim periods within those fiscal years, beginning after December 15, 2019. The adoption of this standard is not expected to have a material impact on the Company's financial position, results of operations or cash flows.

The FASB issued Update No. 2017-04, *Intangibles-Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment*, in January 2017. The objective of this guidance is to simplify an entity's required test for impairment of goodwill by eliminating Step 2 from the goodwill impairment test. In Step 2 an entity measured a goodwill impairment loss by comparing the implied fair value of a reporting unit's goodwill with the carrying amount of that goodwill. In computing the implied fair value of goodwill, an entity had to determine the fair value at the impairment date of its assets and liabilities, including any unrecognized assets and liabilities, following a procedure that would be required in determining the fair value of assets acquired and liabilities assumed in a business combination. Under this Update, an entity should perform its annual or quarterly goodwill impairment test by comparing the fair value of the reporting unit with its carrying amount and record an impairment charge for the excess of the carrying amount over the reporting unit's fair value. The loss recognized should not exceed the total amount of goodwill allocated to the reporting unit and the entity must consider the income tax effects from any tax deductible goodwill on the carrying amount of the reporting unit when measuring the goodwill impairment loss, if applicable. This guidance is effective for a public business entity that is an SEC filer for its annual or any interim goodwill impairment tests in fiscal years beginning after December 15, 2019. The adoption of this standard is not expected to have a material impact on the Company's financial position, results of operations or cash flows.

The FASB issued Update 2017-1, *Business Combinations (Topic 805): Clarifying the Definition of a Business*, in January 2017. The objective of this guidance is to clarify the definition of a business to provide entities with assistance in evaluating whether transactions should be accounted for as acquisitions (or disposals) of assets or businesses. The update provides a screen to determine when an integrated set of assets and activities (a "set") is not a business. The screen requires that when substantially all of the fair value of the gross assets acquired (or disposed of) is concentrated in a single identifiable assets or a group of similar identifiable assets, the set is not a business. The screen thus reduces the number of transactions that need to be further evaluated. If the screen is not met, the amendments in this Update (1) require that to be considered a business, as set must include, at a minimum, an input and substantive process that together significantly contribute to the ability to create output and (2) remove the evaluation of whether a market participant could replace missing elements. The amendments provide a framework to assist entities in evaluating whether both an input and a substantive process are present. The framework includes two sets of criteria to consider that depend on whether a set has outputs. Although outputs are not required for an asset to be a business, outputs generally are a key element of a business; therefore, the Board has developed more stringent criteria for sets without outputs. This guidance is effective for public business entities for annual periods beginning after December 15, 2017, including interim periods within those periods. The adoption of this standard is not expected to have a material impact on the Company's financial position, results of operations or cash flows.

The FASB issued Update No. 2016-15, *Statement of Cash Flow (Topic 230): Classification of Certain Cash Receipts and Cash Payments*, in August 2016. This guidance is intended to reduce the diversity in practice with respect to the presentation and classification of items in the statement of cash flows. This guidance is effective for public business entities for the first interim or annual period beginning after December 15, 2017. The standard's provisions will be applied using a retrospective transition method to each period presented. An entity may elect early adoption but must adopt all of the amendments in the same period. The adoption of this standard is not expected to have a material impact on the Company's financial position, results of operations or cash flows.

The FASB issued Update No. 2016-13, *Current Expected Credit Losses (CECL)*, in June 2016. This guidance changes the impairment model for most financial assets measured at amortized cost and certain other instruments. Entities will be required to use an expected loss model, replacing the incurred loss model that is currently in use. Under the new guidance, an entity will measure all expected credit losses for financial instruments held at the reporting date based on historical experience, current condition and reasonable and supportable forecasts. This will result in earlier recognition of loss allowances in most instances. Credit losses related to available-for-sale debt securities (regardless of whether the impairment is considered to be other-than-temporary) will be measured in a manner similar to the present, except that such losses will be recorded as allowances rather than as reductions in the amortized cost of the related securities. With respect to trade and other receivables, loans, held-to-maturity debt securities, net investments in leases and off-balance-sheet credit exposures, the guidance requires that an entity estimate its lifetime expected credit loss and record an allowance resulting in the net amount expected to be collected to be reflected as the financial asset. Entities are also required to provide significantly more disclosures, including information used to track credit quality by year of origination for most financing receivables. This guidance is effective for public business entities for the first interim or annual period beginning after December 15, 2019. The standard’s provisions will be applied as a cumulative-effect adjustment to retained earnings as of the beginning of the first reporting period in which the guidance is effective. Early adoption by public business entities is permitted for the first interim or annual period beginning after December 15, 2018. The Company is assessing this guidance to determine its impact on the Company’s financial position, results of operations and cash flows.

The FASB issued Update No. 2016-08, *Revenue from Contracts with Customers (Topic 606): Principal versus Agent Considerations (Reporting Revenue Gross versus Net),* in March 2016. This guidance is intended to clarify a potential implementation issue with respect to determining whether an entity is a principal or an agent in an arrangement. The guidance provides indicators to assist in this evaluation when another party is involved in the arrangement to identify which party is the principal and which party is the agent. The effective date for this guidance is the same as the effective date of Update 2014-09, Revenue from Contracts with Customers. The adoption of this standard is not expected to have a material impact on the Company’s financial position, results of operations or cash flows.

The FASB issued Update No. 2016-02, *Leases*, in February 2016. From the lessee’s perspective, the new standard establishes a right-of-use (ROU) model that requires a lessee to record a ROU asset and a lease liability on the balance sheet for all leases with terms longer than 12 months. Leases will be classified as either finance or operating, with classification affecting the pattern of expense recognition in the income statement for lessees. The guidance also eliminates the current real estate-specific provision and changes the guidance on sale-leaseback transactions, initial direct costs and lease executory costs. With respect to lessors, the guidance modifies the classification criteria and the accounting for sales-type and direct financing leases. All entities will classify leases to determine how to recognize lease-related revenue and expense. In applying this guidance entities will also need to determine whether an arrangement contains a lease or service agreement. Disclosures are required by lessees and lessors to meet the objective of enabling users of financials statements to assess the amount, timing, and uncertainty of cash flows arising from leases. For public entities, this guidance is effective for the first interim or annual period beginning after December 15, 2018. Early adoption is permitted. Entities are required to use a modified retrospective approach for leases that exist or are entered into after the beginning of the earliest comparative period in the financial statements. The Company is assessing this guidance to determine its impact on the Company’s financial position, results of operations and cash flows.

The FASB issued Update No. 2016-01, *Financial Instruments - Overall*, in January 2016. This guidance requires entities to measure equity investments at fair value and recognize changes on fair value in net income. The guidance also provides a new measurement alternative for equity investments that do not have readily determinable fair values and don’t qualify for the net asset value practical expedient. Entities will have to record changes in instrument –specific credit risk for financial liabilities measured under the fair value option in other comprehensive income, except for certain financial liabilities of consolidated collateralized financing entities. Entities will also have to reassess the realizability of a deferred tax asset related to an available-for-sale debt security in combination with their other deferred tax assets. This simplifies the impairment assessment of equity investments without readily determinable fair values by requiring a qualitative assessment to identify impairment. For public entities, the guidance in this update is effective for the first interim or annual period beginning after December 15, 2017. Early adoption by public entities is permitted as of the beginning of the year of adoption for selected amendments by a cumulative effect adjustment to the balance sheet. The adoption of this standard is not expected to have a material impact on the Company’s financial position, results of operations or cash flows.

The FASB issued Update No. 2014-09, *Revenue from Contracts with Customers (Topic 606)*, in May 2014 that provides accounting guidance for all revenue arising from contracts with customers and affects all entities that enter into contracts to provide goods or services to customers. The guidance also provides for a model for the measurement and recognition of gains and losses on the sale of certain nonfinancial assets, such as property and equipment, including real estate. This standard may affect an entity's financial statements, business processes and internal control over financial reporting. The guidance is effective for the first interim or annual period beginning after December 15, 2017. The guidance must be adopted using either a full retrospective approach for all periods presented in the period of adoption or a modified retrospective approach. The Company's revenue is comprised of net interest income and noninterest income. As ASU 2014-09 does not apply to revenue associated with financial instruments, net interest income, mortgage origination and servicing activities, and gains and losses from securities are not impacted by the standard. For other revenue streams such as: 1) wealth management income; 2) insurance agency commissions; 3) bank card fees; and 4) service charges on deposit accounts, the Company does not expect this standard to have a material impact on the timing of revenue recognition. The Company is currently evaluating the disclosure requirements of the standard. The adoption of this standard is not expected to have a material impact on the Company's financial position, results of operations and cash flows.

Note 2 – Investments

Investments available-for-sale

The amortized cost and estimated fair values of investments available-for-sale at the dates indicated are presented in the following table:

	June 30, 2017				December 31, 2016			
(In thousands)	**Amortized Cost**	**Gross Unrealized Gains**	**Gross Unrealized Losses**	**Estimated Fair Value**	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
U.S. government agencies	**$114,346**	**$ -**	**$(1,985)**	**$112,361**	$124,314	$ 32	$(2,556)	$121,790
State and municipal	**315,972**	**9,039**	**(78)**	**324,933**	281,090	7,180	(586)	287,684
Mortgage-backed	**332,578**	**2,762**	**(3,065)**	**332,275**	314,029	2,851	(4,169)	312,711
Corporate debt	**9,100**	**289**	**-**	**9,389**	9,100	34	-	9,134
Trust preferred	**931**	**-**	**(23)**	**908**	1,089	-	(77)	1,012
Total debt securities	**772,927**	**12,090**	**(5,151)**	**779,866**	729,622	10,097	(7,388)	732,331
Marketable equity securities	**212**	**-**	**-**	**212**	1,223	-	-	1,223
Total investments available-for-sale	**$773,139**	**$ 12,090**	**$(5,151)**	**$780,078**	$730,845	$10,097	$(7,388)	$733,554

Any unrealized losses in the U.S. government agencies, state and municipal, mortgage-backed or corporate debt investment securities at June 30, 2017 are not the result of credit related events but due to changes in interest rates. These declines in fair market value are considered temporary in nature and are expected to recover over time as these securities approach maturity.

The mortgage-backed securities portfolio at June 30, 2017 is composed entirely of either the most senior tranches of GNMA, FNMA or FHLMC collateralized mortgage obligations ($114.2 million), or GNMA, FNMA or FHLMC mortgage-backed securities ($218.1 million). The Company does not intend to sell these securities and has sufficient liquidity to hold these securities for an adequate period of time to allow for any anticipated recovery in fair value.

At June 30, 2017 the trust preferred portfolio consisted of one pooled trust preferred security. The pooled trust preferred security, which is backed by debt issued by banks and thrifts, totaled $0.9 million with a fair value of the same amount. The fair value of this security was determined by management through the use of a third party valuation specialist due to the limited trading activity for this security.

As a result of this evaluation, it was determined that the pooled trust preferred security had not incurred any credit-related other-than-temporary impairment (“OTTI”) for the quarter ended June 30, 2017. The security had an insignificant unrealized loss at June 30, 2017 recognized in other comprehensive income (“OCI”). The security is not expected to be sold and the Company has the ability to hold it until maturity.

The following table provides the activity of OTTI on investment securities due to credit losses recognized in earnings for the period indicated:

(In thousands)		OTTI Losses
Cumulative credit losses on investment securities, through December 31, 2016	$	531
Additions for credit losses not previously recognized		-
Cumulative credit losses on investment securities through June 30, 2017	$	531

Gross unrealized losses and fair value by length of time that the individual available-for-sale securities have been in an unrealized loss position at the dates indicated are presented in the following table:

			June 30, 2017 Continuous Unrealized Losses Existing for:		
(Dollars in thousands)	**Number of Securities**	**Fair Value**	**Less than 12 months**	**More than 12 months**	**Total Unrealized Losses**
U.S. government agencies	**11**	**$ 92,362**	**$ 1,985**	**$ -**	**$ 1,985**
State and municipal	**15**	**12,760**	**38**	**40**	**78**
Mortgage-backed	**36**	**186,396**	**2,900**	**165**	**3,065**
Trust preferred	**1**	**908**	**23**	**-**	**23**
Total	**63**	**$ 292,426**	**$ 4,946**	**$ 205**	**$ 5,151**

			December 31, 2016 Continuous Unrealized Losses Existing for:		
(Dollars in thousands)	Number of Securities	Fair Value	Less than 12 months	More than 12 months	Total Unrealized Losses
U.S. government agencies	12	$ 96,788	$ 2,556	$ -	$ 2,556
State and municipal	53	48,010	516	70	586
Mortgage-backed	37	212,844	3,971	198	4,169
Trust preferred	1	1,012	-	77	77
Total	103	$ 358,654	$ 7,043	$ 345	$ 7,388

The amortized cost and estimated fair values of debt securities available-for-sale by contractual maturity at the dates indicated are provided in the following table. The Company has allocated mortgage-backed securities into the four maturity groupings reflected in the following table using the expected average life of the individual securities based on statistics provided by independent third party industry sources. Expected maturities will differ from contractual maturities as borrowers may have the right to prepay obligations with or without prepayment penalties.

	June 30, 2017		December 31, 2016	
(In thousands)	**Amortized Cost**	**Estimated Fair Value**	Amortized Cost	Estimated Fair Value
Due in one year or less	**$ 9,400**	**$ 9,503**	$ 7,493	$ 7,541
Due after one year through five years	**156,757**	**162,574**	156,953	162,233
Due after five years through ten years	**267,567**	**269,361**	282,468	282,713
Due after ten years	**339,203**	**338,428**	282,708	279,844
Total debt securities available for sale	**$ 772,927**	**$ 779,866**	$ 729,622	$ 732,331

At June 30, 2017 and December 31, 2016, investments available-for-sale with a book value of $428.2 million and $453.0 million, respectively, were pledged as collateral for certain government deposits and for other purposes as required or permitted by law. The outstanding balance of no single issuer, except for U.S. Agencies securities, exceeded ten percent of stockholders' equity at June 30, 2017 and December 31, 2016.

Equity securities

Other equity securities at the dates indicated are presented in the following table:

(In thousands)	**June 30, 2017**	December 31, 2016
Federal Reserve Bank stock	**$ 8,366**	$ 8,334
Federal Home Loan Bank of Atlanta stock	**33,047**	37,760
Total equity securities	**$ 41,413**	$ 46,094

Note 3 – LOANS

Outstanding loan balances at June 30, 2017 and December 31, 2016 are net of unearned income including net deferred loan costs of $2.1 million and $1.4 million, respectively. The loan portfolio segment balances at the dates indicated are presented in the following table:

(In thousands)	**June 30, 2017**	December 31, 2016
Residential real estate:		
Residential mortgage	**$ 871,766**	$ 841,692
Residential construction	**169,901**	150,229
Commercial real estate:		
Commercial owner occupied real estate	**797,629**	775,552
Commercial investor real estate	**1,069,988**	928,113
Commercial acquisition, development and construction	**314,259**	308,279
Commercial business	**451,570**	467,286
Consumer	**458,058**	456,657
Total loans	**$ 4,133,171**	$ 3,927,808

Note 4 – CREDIT QUALITY ASSESSMENT

Allowance for Loan Losses

Summary information on the allowance for loan loss activity for the period indicated is provided in the following table:

	Six Months Ended June 30,	
(In thousands)	**2017**	2016
Balance at beginning of year	**$ 44,067**	$ 40,895
Provision for loan losses	**1,516**	4,193
Loan charge-offs	**(824)**	(2,272)
Loan recoveries	**320**	568
Net charge-offs	**(504)**	(1,704)
Balance at period end	**$ 45,079**	$ 43,384

The following tables provide information on the activity in the allowance for loan losses by the respective loan portfolio segment for the period indicated:

For the Six Months Ended June 30, 2017

		Commercial Real Estate				Residential Real Estate		
(Dollars in thousands)	**Commercial Business**	**Commercial AD&C**	**Commercial Investor R/E**	**Commercial Owner Occupied R/E**	**Consumer**	**Residential Mortgage**	**Residential Construction**	**Total**
Balance at beginning of year	**$ 7,539**	**$ 4,652**	**$ 12,939**	**$ 7,885**	**$ 2,828**	**$ 7,261**	**$ 963**	**$ 44,067**
Provision (credit)	**1,877**	**(630)**	**150**	**(1,204)**	**464**	**725**	**134**	**1,516**
Charge-offs	**(411)**	**-**	**-**	**-**	**(404)**	**(9)**	**-**	**(824)**
Recoveries	**44**	**103**	**83**	**-**	**48**	**28**	**14**	**320**
Net recoveries (charge-offs)	**(367)**	**103**	**83**	**-**	**(356)**	**19**	**14**	**(504)**
Balance at end of period	**$ 9,049**	**$ 4,125**	**$ 13,172**	**$ 6,681**	**$ 2,936**	**$ 8,005**	**$ 1,111**	**$ 45,079**
Total loans and leases	**$451,570**	**$314,259**	**$1,069,988**	**$797,629**	**$458,058**	**$871,766**	**$169,901**	**$4,133,171**
Allowance for loans losses to total loans ratio	**2.00%**	**1.31%**	**1.23%**	**0.84%**	**0.64%**	**0.92%**	**0.65%**	**1.09%**
Balance of loans specifically evaluated for impairment	**$ 8,977**	**$ 137**	**$ 6,934**	**$ 5,667**	**$ na.**	**$ 2,888**	**$ -**	**$ 24,603**
Allowance for loans specifically evaluated for impairment	**$ 4,740**	**$ -**	**$ 736**	**$ 296**	**$ na.**	**$ -**	**$ -**	**$ 5,772**
Specific allowance to specific loans ratio	**52.80%**	**-**	**10.61%**	**5.22%**	**na.**	**-**	**-**	**23.46%**
Balance of loans collectively evaluated	**$442,593**	**$314,122**	**$1,063,054**	**$791,962**	**$458,058**	**$868,878**	**$169,901**	**$4,108,568**
Allowance for loans collectively evaluated	**$ 4,309**	**$ 4,125**	**$ 12,436**	**$ 6,385**	**$ 2,936**	**$ 8,005**	**$ 1,111**	**$ 39,307**
Collective allowance to collective loans ratio	**0.97%**	**1.31%**	**1.17%**	**0.81%**	**0.64%**	**0.92%**	**0.65%**	**0.96%**

For the Year Ended December 31,2016

		Commercial Real Estate				Residential Real Estate		
(Dollars in thousands)	Commercial Business	Commercial AD&C	Commercial Investor R/E	Commercial Owner Occupied R/E	Consumer	Residential Mortgage	Residential Construction	Total
Balance at beginning of year	$ 6,529	$ 4,691	$ 10,440	$ 7,984	$ 3,456	$ 6,901	$ 894	$ 40,895
Provision (credit)	1,563	(31)	2,563	(104)	112	1,406	37	5,546
Charge-offs	(597)	(48)	(197)	-	(888)	(1,404)	-	(3,134)

Recoveries	44	40	133	5	148	358	32	760
Net recoveries (charge-offs)	(553)	(8)	(64)	5	(740)	(1,046)	32	(2,374)
Balance at end of period	$ 7,539	$ 4,652	$ 12,939	$ 7,885	$ 2,828	$ 7,261	$ 963	$ 44,067
Total loans and leases	$467,286	$308,279	$928,113	$775,552	$456,657	$841,692	$150,229	$3,927,808
Allowance for loan losses to total loans ratio	1.61%	1.51%	1.39%	1.02%	0.62%	0.86%	0.64%	1.12%
Balance of loans specifically evaluated for impairment	$ 7,018	$ 137	$ 8,107	$ 5,567	$ na.	$ 3,263	$ -	$ 24,092
Allowance for loans specifically evaluated for impairment	$ 2,604	$ -	$ 1,736	$ 485	$ na.	$ -	$ -	$ 4,825
Specific allowance to specific loans ratio	37.10%	-	21.41%	8.71%	na.	-	-	20.03%
Balance of loans collectively evaluated	$460,268	$308,142	$920,006	$769,985	$456,657	$838,429	$150,229	$3,903,716
Allowance for loans collectively evaluated	$ 4,935	$ 4,652	$ 11,203	$ 7,400	$ 2,828	$ 7,261	$ 963	$ 39,242
Collective allowance to collective loans ratio	1.07%	1.51%	1.22%	0.96%	0.62%	0.87%	0.64%	1.01%

The following table provides summary information regarding impaired loans at the dates indicated and for the periods then ended:

(In thousands)	**June 30, 2017**		December 31, 2016	
Impaired loans with a specific allowance	**$**	**14,193**	$	13,563
Impaired loans without a specific allowance		**10,410**		10,529
Total impaired loans	**$**	**24,603**	$	24,092
Allowance for loan losses related to impaired loans	**$**	**5,772**	$	4,825
Allowance for loan losses related to loans collectively evaluated		**39,307**		39,242
Total allowance for loan losses	**$**	**45,079**	$	44,067
Average impaired loans for the period	**$**	**24,190**	$	26,382
Contractual interest income due on impaired loans during the period	**$**	**1,281**	$	2,082
Interest income on impaired loans recognized on a cash basis	**$**	**415**	$	511
Interest income on impaired loans recognized on an accrual basis	**$**	**134**	$	186

The following tables present the recorded investment with respect to impaired loans, the associated allowance by the applicable portfolio segment and the principal balance of the impaired loans prior to amounts charged-off at the dates indicated:

	June 30, 2017					
		Commercial Real Estate				**Total Recorded Investment in Impaired**
(In thousands)	**Commercial**	**Commercial AD&C**	**Commercial Investor R/E**	**Commercial Owner Occupied R/E**	**All Other Loans**	**Loans**
Impaired loans with a specific allowance						
Accruing	**$ 896**	**$ -**	**$ -**	**$ -**	**$ -**	**$ 896**
Non-accruing	**4,405**	**-**	**6,029**	**1,224**	**-**	**11,658**
Restructured accruing	**992**	**-**	**-**	**-**	**-**	**992**
Restructured non-accruing	**8**	**-**	**-**	**639**	**-**	**647**
Balance	**$ 6,301**	**$ -**	**$ 6,029**	**$ 1,863**	**$ -**	**$ 14,193**
Allowance	**$ 4,740**	**$ -**	**$ 736**	**$ 296**	**$ -**	**$ 5,772**
Impaired loans without a specific allowance						
Non-accruing	**$ 1,597**	**$ -**	**$ 426**	**$ 1,907**	**$ -**	**$ 3,930**
Restructured accruing	**282**	**-**	**-**	**741**	**554**	**1,577**
Restructured non-accruing	**797**	**137**	**479**	**1,156**	**2,334**	**4,903**
Balance	**$ 2,676**	**$ 137**	**$ 905**	**$ 3,804**	**$ 2,888**	**$ 10,410**
Total impaired loans						

Accruing	**$ 896**	**$ -**	**$ -**	**$ -**	**$ -**	**$ 896**
Non-accruing	**6,002**	**-**	**6,455**	**3,131**	**-**	**15,588**
Restructured accruing	**1,274**	**-**	**-**	**741**	**554**	**2,569**
Restructured non-accruing	**805**	**137**	**479**	**1,795**	**2,334**	**5,550**
Balance	**$ 8,977**	**$ 137**	**$ 6,934**	**$ 5,667**	**$ 2,888**	**$ 24,603**
Unpaid principal balance in total impaired loans	**$ 10,926**	**$ 4,398**	**$ 11,514**	**$ 7,822**	**$ 3,710**	**$ 38,370**

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	June 30, 2017					
		Commercial Real Estate				
(In thousands)	**Commercial**	**Commercial AD&C**	**Commercial Investor R/E**	**Commercial Owner Occupied R/E**	**All Other Loans**	**Total Recorded Investment in Impaired Loans**
Average impaired loans for the period	**$ 7,669**	**$ 137**	**$ 7,670**	**$ 5,694**	**$ 3,020**	**$ 24,190**
Contractual interest income due on impaired loans during the period	**$ 436**	**$ 160**	**$ 350**	**$ 265**	**$ 70**	
Interest income on impaired loans recognized on a cash basis	**$ 189**	**$ -**	**$ 14**	**$ 96**	**$ 116**	
Interest income on impaired loans recognized on an accrual basis	**$ 97**	**$ -**	**$ -**	**$ 18**	**$ 19**	

	December 31, 2016					
		Commercial Real Estate				
(In thousands)	Commercial	Commercial AD&C	Commercial Investor R/E	Commercial Owner Occupied R/E	All Other Loans	Total Recorded Investment in Impaired Loans
Impaired loans with a specific allowance						
Non-accruing	$ 2,807	$ -	$ 7,029	$ 1,884	$ -	$ 11,720
Restructured accruing	1,140	-	-	-	-	1,140
Restructured non-accruing	64	-	-	639	-	703
Balance	$ 4,011	$ -	$ 7,029	$ 2,523	$ -	$ 13,563
Allowance	$ 2,604	$ -	$ 1,736	$ 485	$ -	$ 4,825
Impaired loans without a specific allowance						
Non-accruing	$ 1,562	$ -	$ 562	$ 1,083	$ -	$ 3,207
Restructured accruing	45	-	-	744	560	1,349
Restructured non-accruing	1,400	137	516	1,217	2,703	5,973
Balance	$ 3,007	$ 137	$ 1,078	$ 3,044	$ 3,263	$ 10,529
Total impaired loans						
Non-accruing	$ 4,369	$ -	$ 7,591	$ 2,967	$ -	$ 14,927
Restructured accruing	1,185	-	-	744	560	2,489
Restructured non-accruing	1,464	137	516	1,856	2,703	6,676
Balance	$ 7,018	$ 137	$ 8,107	$ 5,567	$ 3,263	$ 24,092
Unpaid principal balance in total impaired loans	$ 10,082	$ 4,398	$ 12,805	$ 7,760	$ 3,971	$ 39,016

December 31, 2016

(In thousands)	Commercial	Commercial AD&C	Commercial Real Estate: Commercial Investor R/E	Commercial Real Estate: Commercial Owner Occupied R/E	All Other Loans	Total Recorded Investment in Impaired Loans
Average impaired loans for the period	$ 5,646	$ 150	$ 9,480	$ 6,561	$ 4,545	$ 26,382
Contractual interest income due on impaired loans during the period	$ 570	$ 294	$ 718	$ 310	$ 190	
Interest income on impaired loans recognized on a cash basis	$ 153	$ -	$ 43	$ 266	$ 49	
Interest income on impaired loans recognized on an accrual basis	$ 107	$ -	$ -	$ 37	$ 42	

Credit Quality

The following tables provide information on the credit quality of the loan portfolio by segment at the dates indicated:

	June 30, 2017							
		Commercial Real Estate				Residential Real Estate		
(In thousands)	Commercial	Commercial AD&C	Commercial Investor R/E	Commercial Owner Occupied R/E	Consumer	Residential Mortgage	Residential Construction	Total
Non-performing loans and assets:								
Non-accrual loans	$ 6,807	$ 137	$ 6,934	$ 4,926	$ 3,111	$ 7,101	$ 187	$ 29,203
Loans 90 days past due	-	-	-	424	4	-	-	428
Restructured loans	1,274	-	-	741	-	554	-	2,569
Total non-performing loans	8,081	137	6,934	6,091	3,115	7,655	187	32,200
Other real estate owned	39	365	395	-	-	661	-	1,460
Total non-performing assets	$ 8,120	$ 502	$ 7,329	$ 6,091	$ 3,115	$ 8,316	$ 187	$ 33,660

	December 31, 2016							
		Commercial Real Estate				Residential Real Estate		
(In thousands)	Commercial	Commercial AD&C	Commercial Investor R/E	Commercial Owner Occupied R/E	Consumer	Residential Mortgage	Residential Construction	Total
Non-performing loans and assets:								
Non-accrual loans	$ 5,833	$ 137	$ 8,107	$ 4,823	$ 2,859	$ 7,257	$ 195	$ 29,211
Loans 90 days past due	-	-	-	-	-	232	-	232
Restructured loans	1,185	-	-	744	-	560	-	2,489
Total non-performing loans	7,018	137	8,107	5,567	2,859	8,049	195	31,932
Other real estate owned	39	365	395	637	-	475	-	1,911
Total non-performing assets	$ 7,057	$ 502	$ 8,502	$ 6,204	$ 2,859	$ 8,524	$ 195	$ 33,843

	June 30, 2017							
		Commercial Real Estate				Residential Real Estate		
(In thousands)	Commercial	Commercial AD&C	Commercial Investor R/E	Commercial Owner Occupied R/E	Consumer	Residential Mortgage	Residential Construction	Total
Past due loans								
31-60 days	$ 4,980	$ -	$ 219	$ 580	$ 1,071	$ 8,645	$ -	$ 15,495

61-90 days	**191**	**-**	**181**	**304**	**141**	**2,623**	**-**	**3,440**
> 90 days	**-**	**-**	**-**	**424**	**4**	**-**	**-**	**428**
Total past due	**5,171**	**-**	**400**	**1,308**	**1,216**	**11,268**	**-**	**19,363**
Non-accrual loans	**6,807**	**137**	**6,934**	**4,926**	**3,111**	**7,101**	**187**	**29,203**
Current loans	**439,592**	**314,122**	**1,062,654**	**791,395**	**453,731**	**853,397**	**169,714**	**4,084,605**
Total loans	**$451,570**	**$314,259**	**$1,069,988**	**$797,629**	**$458,058**	**$871,766**	**$169,901**	**$4,133,171**

	December 31, 2016							
		Commercial Real Estate				Residential Real Estate		
(In thousands)	Commercial	Commercial AD&C	Commercial Investor R/E	Commercial Owner Occupied R/E	Consumer	Residential Mortgage	Residential Construction	Total
Past due loans								
31-60 days	$ 663	$ 896	$ 850	$ 1,479	$ 808	$ 3,969	$ -	$ 8,665
61-90 days	672	-	1,206	744	1,104	2,139	-	5,865
> 90 days	-	-	-	-	-	232	-	232
Total past due	1,335	896	2,056	2,223	1,912	6,340	-	14,762
Non-accrual loans	5,833	137	8,107	4,823	2,859	7,257	195	29,211
Current loans	460,118	307,246	917,950	768,506	451,886	828,095	150,034	3,883,835
Total loans	$467,286	$308,279	$928,113	$775,552	$456,657	$841,692	$150,229	$3,927,808

The following tables provide information by credit risk rating indicators for each segment of the commercial loan portfolio at the dates indicated:

		June 30, 2017 Commercial Real Estate			
(In thousands)	Commercial	Commercial AD&C	Commercial Investor R/E	Commercial Owner Occupied R/E	Total
Pass	$ 432,870	$ 314,122	$ 1,060,362	$ 783,831	$ 2,591,185
Special Mention	2,848	-	2,357	5,645	10,850
Substandard	15,852	137	7,269	8,153	31,411
Doubtful	-	-	-	-	-
Total	$ 451,570	$ 314,259	$ 1,069,988	$ 797,629	$ 2,633,446

		December 31, 2016 Commercial Real Estate			
(In thousands)	Commercial	Commercial AD&C	Commercial Investor R/E	Commercial Owner Occupied R/E	Total
Pass	$ 442,725	$ 308,142	$ 917,255	$ 758,651	$ 2,426,773
Special Mention	10,010	-	2,395	9,255	21,660
Substandard	14,551	137	8,463	7,646	30,797
Doubtful	-	-	-	-	-
Total	$ 467,286	$ 308,279	$ 928,113	$ 775,552	$ 2,479,230

Homogeneous loan pools do not have individual loans subjected to internal risk ratings therefore, the credit indicator applied to these pools is based on their delinquency status. The following tables provide information by credit risk rating indicators for those remaining segments of the loan portfolio at the dates indicated:

		June 30, 2017 Residential Real Estate		
(In thousands)	Consumer	Residential Mortgage	Residential Construction	Total
Performing	$ 454,943	$ 864,111	$ 169,714	$ 1,488,768
Non-performing:				
90 days past due	4	-	-	4
Non-accruing	3,111	7,101	187	10,399
Restructured loans	-	554	-	554
Total	$ 458,058	$ 871,766	$ 169,901	$ 1,499,725

		December 31, 2016 Residential Real Estate		
(In thousands)	Consumer	Residential Mortgage	Residential Construction	Total

Performing	$ 453,798	$ 833,643	$ 150,034	$ 1,437,475
Non-performing:				
90 days past due	-	232	-	232
Non-accruing	2,859	7,257	195	10,311
Restructured loans	-	560	-	560
Total	$ 456,657	$ 841,692	$ 150,229	$ 1,448,578

During the six months ended June 30, 2017, the Company restructured $0.2 million in loans. No modifications resulted in the reduction of the principal in the associated loan balances. Restructured loans are subject to periodic credit reviews to determine the necessity and adequacy of a specific loan loss allowance based on the collectability of the recorded investment in the restructured loan. Loans restructured during 2017 did not have any specific reserves. For the year ended December 31, 2016, the Company restructured $0.6 million in loans. Modifications consisted principally of interest rate concessions and no modifications resulted in the reduction of the recorded investment in the associated loan balances. Loans restructured during 2016 did not have significant specific reserves at December 31, 2016. The commitments to lend additional funds on loans that have been restructured at June 30, 2017 and December 31, 2016 were not significant.

The following table provides the amounts of the restructured loans at the date of restructuring for specific segments of the loan portfolio during the period indicated:

	For the Six Months Ended June 30, 2017					
		Commercial Real Estate				
(In thousands)	**Commercial**	**Commercial AD&C**	**Commercial Investor R/E**	**Commercial Owner Occupied R/E**	**All Other Loans**	**Total**
Troubled debt restructurings						
Restructured accruing	**$ 244**	**$ -**	**$ -**	**$ -**	**$ -**	**$ 244**
Restructured non-accruing	**-**	**-**	**-**	**-**	**-**	**-**
Balance	**$ 244**	**$ -**	**$ -**	**$ -**	**$ -**	**$ 244**
Specific allowance	**$ -**	**$ -**	**$ -**	**$ -**	**$ -**	**$ -**
Restructured and subsequently defaulted	**$ -**	**$ -**	**$ -**	**$ -**	**$ -**	**$ -**

	For the Year Ended December 31, 2016					
		Commercial Real Estate				
(In thousands)	Commercial	Commercial AD&C	Commercial Investor R/E	Commercial Owner Occupied R/E	All Other Loans	Total
Troubled debt restructurings						
Restructured accruing	$ 42	$ -	$ -	$ 508	$ -	$ 550
Restructured non-accruing	-	-	-	-	-	-
Balance	$ 42	$ -	$ -	$ 508	$ -	$ 550
Specific allowance	$ 39	$ -	$ -	$ -	$ -	$ 39
Restructured and subsequently defaulted	$ -	$ -	$ 479	$ -	$ -	$ 479

Other Real Estate Owned

Other real estate owned totaled $1.5 million and $1.9 million at June 30, 2017 and December 31, 2016, respectively.

Note 5 – Goodwill and Other Intangible Assets

The gross carrying amounts and accumulated amortization of intangible assets and goodwill are presented at the dates indicated in the following table:

	June 30, 2017			**Weighted**	December 31, 2016			Weighted
(Dollars in thousands)	**Gross Carrying Amount**	**Accumulated Amortization**	**Net Carrying Amount**	**Average Remaining Life**	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Average Remaining Life
Amortizing intangible assets:								
Other identifiable intangibles	**$ 786**	**$ (157)**	**$ 629**	**13.4 years**	$ 786	$ (106)	$ 680	13.8 years
Total amortizing intangible assets	**$ 786**	**$ (157)**	**$ 629**		$ 786	$ (106)	$ 680	
Goodwill	**$ 85,768**		**$ 85,768**		$ 85,768		$ 85,768	

The following table presents the estimated future amortization expense for amortizing intangible assets within the years ending December 31:

(In thousands)	Amount
2017	$ 49
2018	95
2019	83
2020	66
Thereafter	336
Total amortizing intangible assets	$ 629

Note 6 – Deposits

The following table presents the composition of deposits at the dates indicated:

(In thousands)	**June 30, 2017**	December 31, 2016
Noninterest-bearing deposits	**$ 1,302,536**	$ 1,138,139
Interest-bearing deposits:		
Demand	**605,976**	615,058
Money market savings	**991,503**	927,837
Regular savings	**329,165**	310,471
Time deposits of less than $100,000	**282,234**	258,621
Time deposits of $100,000 or more	**374,031**	327,418
Total interest-bearing deposits	**2,582,909**	2,439,405
Total deposits	**$ 3,885,445**	$ 3,577,544

Note 7 – Stockholders' Equity

The Company re-approved a stock repurchase program in August 2015 that permits the repurchase of up to 5% of the Company's outstanding shares of common stock or approximately 1.2 million shares. Repurchases, which will be conducted through open market purchases or privately negotiated transactions, will be made depending on market conditions and other factors. The Company did not repurchase any shares during the first six months of 2017.

Note 8 – Share Based Compensation

At June 30, 2017, the Company had two share based compensation plans in existence, the 2005 Omnibus Stock Plan ("Omnibus Stock Plan") and the 2015 Omnibus Incentive Plan ("Omnibus Incentive Plan"). The Omnibus Stock Plan expired during the second quarter of 2015 but has outstanding options that may still be exercised. The Omnibus Incentive Plan is described in the following paragraph.

The Company’s Omnibus Incentive Plan was approved on May 6, 2015 and provides for the granting of incentive stock options, non-qualifying stock options, stock appreciation rights, restricted stock grants, restricted stock units and performance awards to selected employees on a periodic basis at the discretion of the board. The Omnibus Incentive Plan authorizes the issuance of up to 1,500,000 shares of common stock, of which 1,339,989 are available for issuance at June 30, 2017, has a term of ten years, and is administered by a committee of at least three directors appointed by the board of directors. Options granted under the plan have an exercise price which may not be less than 100% of the fair market value of the common stock on the date of the grant and must be exercised within seven to ten years from the date of grant. The exercise price of stock options must be paid for in full in cash or shares of common stock, or a combination of both. The board committee has the discretion when making a grant of stock options to impose restrictions on the shares to be purchased upon the exercise of such options. The Company generally issues authorized but previously unissued shares to satisfy option exercises.

The fair values of all of the options granted for the periods indicated have been estimated using a binomial option-pricing model. The weighted-average assumptions for the periods shown are presented in the following table:

	Six Months Ended June 30,	
	2017	2016
Dividend yield	**2.45%**	3.48%
Weighted average expected volatility	**40.27%**	41.54%
Weighted average risk-free interest rate	**2.14%**	1.42%
Weighted average expected lives (in years)	**5.67**	5.71
Weighted average grant-date fair value	**$13.42**	$7.75

The dividend yield is based on estimated future dividend yields. The risk-free rate for periods within the contractual term of the share option is based on the U.S. Treasury yield curve in effect at the time of the grant. Expected volatilities are generally based on historical volatilities. The expected term of share options granted is generally derived from historical experience.

Compensation expense is recognized on a straight-line basis over the vesting period of the respective stock option or restricted stock grant. The Company recognized compensation expense of $0.5 million and $0.5 million for the three months ended June 30, 2017 and 2016, respectively, related to the awards of stock options and restricted stock grants. Compensation expense of $1.0 million and $0.9 million was recognized for the six months ended June 30, 2017 and 2016, respectively. The intrinsic value of stock options exercised in the six months ended June 30, 2017 and 2016 was $0.6 million and $0.4 million, respectively. The total of unrecognized compensation cost related to stock options was approximately $0.3 million as of June 30, 2017. That cost is expected to be recognized over a weighted average period of approximately 2.2 years. The total of unrecognized compensation cost related to restricted stock was approximately $5.3 million as of June 30, 2017. That cost is expected to be recognized over a weighted average period of approximately 3.4 years. The fair value of the options vested during the six months ended June 30, 2017 and 2016, was not significant.

In the first quarter of 2017, 12,941 stock options were granted, subject to a three year vesting schedule with one third of the options vesting on April 1st of each year. The Company granted 55,211 shares of restricted stock in the first quarter of 2017, 6,479 shares are subject to a three year vesting schedule with one third of the shares vesting each year and 41,859 shares are subject to a five year vesting schedule with one fifth of the shares vesting each year. All of these restricted shares will vest on April 1st of each year. An additional 6,873 shares of performance based restricted stock grants were also approved as part of the restricted shares granted in the first quarter. The performance shares are subject to cliff vesting after three years based on the relative performance of the Company's stock price in comparison to a selected peer group. Vesting can vary from 0-150% of the initial grant based on the results of the Company's stock performance.

A summary of share option activity for the period indicated is reflected in the following table:

	Number of Common Shares	Weighted Average Exercise Share Price	Weighted Average Contractual Remaining Life (Years)	Aggregate Intrinsic Value (in thousands)

Balance at January 1, 2017	108,503	$ 22.46		$ 1,902
Granted	12,941	$ 42.48		
Exercised	(27,284)	$ 19.00		$ 609
Forfeited or expired	(3,577)	$ 30.07		
Balance at June 30, 2017	90,583	$ 26.08	4.0	$ 1,347
Exercisable at June 30, 2017	60,098	$ 22.43	3.0	$ 1,097
Weighted average fair value of options granted during the year		$ 13.42		

A summary of the activity for the Company’s restricted stock for the period indicated is presented in the following table:

(In dollars, except share data):	Number of Common Shares	Weighted Average Grant-Date Fair Value
Restricted stock at January 1, 2017	212,646	$ 25.19
Granted	55,211	$ 42.48
Vested	(70,382)	$ 23.82
Forfeited	(7,800)	$ 27.21
Restricted stock at June 30, 2017	189,675	$ 30.67

Note 9 – Pension, Profit Sharing, and Other Employee Benefit Plans

Defined Benefit Pension Plan

The Company has a qualified, noncontributory, defined benefit pension plan (the "Plan"). Benefits after January 1, 2005, are based on the benefit earned as of December 31, 2004, plus benefits earned in future years of service based on the employee's compensation during each such year. All benefit accruals for employees were frozen as of December 31, 2007 based on past service and thus salary increases and additional years of service after such date no longer affect the defined benefit provided by the plan although additional vesting may continue to occur.

The Company's funding policy is to contribute amounts to the plan sufficient to meet the minimum funding requirements of the Employee Retirement Income Security Act of 1974 ("ERISA"), as amended. In addition, the Company contributes additional amounts as it deems appropriate based on benefits attributed to service prior to the date of the plan freeze. The Plan invests primarily in a diversified portfolio of managed fixed income and equity funds.

The components of net periodic benefit cost for the periods indicated are presented in the following table:

	Three Months Ended June 30,		Six Months Ended June 30,	
(In thousands)	**2017**	2016	**2017**	2016
Interest cost on projected benefit obligation	**$ 410**	$ 415	**$ 820**	$ 826
Expected return on plan assets	**(496)**	(375)	**(992)**	(747)
Recognized net actuarial loss	**295**	291	**590**	575
Net periodic benefit cost	**$ 209**	$ 331	**$ 418**	$ 654

Contributions

The decision as to whether or not to make a plan contribution and the amount of any such contribution is dependent on a number of factors. Such factors include the investment performance of the plan assets in the current economy and, since the plan is currently frozen, the remaining investment horizon of the plan. After consideration of these factors, the Company did not make a contribution to the plan during the first quarter of 2017 Management continues to monitor the funding level of the pension plan and may make contributions as necessary during 2017.

Note 10 – Net Income per Common Share

The calculation of net income per common share for the periods indicated is presented in the following table:

(Dollars and amounts in thousands, except per share data)	Three Months Ended June 30, **2017**	2016	Six Months Ended June 30, **2017**	2016
Net income	**$ 14,741**	$ 10,647	**$ 29,853**	$ 21,460
Basic:				
Basic weighted average EPS shares	**24,198**	23,865	**24,164**	23,920
Basic net income per share	**$ 0.61**	$ 0.45	**$ 1.24**	$ 0.90
Diluted:				
Basic weighted average EPS shares	**24,198**	23,865	**24,164**	23,920
Dilutive common stock equivalents	**65**	244	**95**	246
Dilutive EPS shares	**24,263**	24,109	**24,259**	24,166
Diluted net income per share	**$ 0.61**	$ 0.44	**$ 1.23**	$ 0.89
Anti-dilutive shares	**5**	7	**3**	6

NOTE 11 – ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS)

Comprehensive income is defined as net income plus transactions and other occurrences that are the result of non-owner changes in equity. For condensed financial statements presented for the Company, non-owner changes in equity are comprised of unrealized gains or losses on available-for-sale debt securities and any minimum pension liability adjustments. The following table presents the activity in net accumulated other comprehensive income (loss) and the components of the activity for the periods indicated:

(In thousands)	**Unrealized Gains (Losses) on Investments Available-for-Sale**	**Defined Benefit Pension Plan**	**Total**
Balance at January 1, 2017	**$ 1,642**	**$ (8,256)**	**$ (6,614)**
Other comprehensive income before reclassification, net of tax	**3,314**	**-**	**3,314**
Reclassifications from accumulated other comprehensive income, net of tax	**(767)**	**355**	**(412)**
Current period change in other comprehensive income, net of tax	**2,547**	**355**	**2,902**
Balance at June 30, 2017	**$ 4,189**	**$ (7,901)**	**$ (3,712)**

Unrealized
Gains

(In thousands)	(Losses) on Investments Available-for-Sale	Defined Benefit Pension Plan	Total
Balance at January 1, 2016	$ 6,566	$ (7,863)	$ (1,297)
Other comprehensive income before reclassification, net of tax	7,990	-	7,990
Reclassifications from accumulated other comprehensive income, net of tax	(1,154)	347	(807)
Current period change in other comprehensive income, net of tax	6,836	347	7,183
Balance at June 30, 2016	$ 13,402	$ (7,516)	$ 5,886

The following table provides the information on the reclassification adjustments out of accumulated other comprehensive income for the periods indicated:

(In thousands)	Six Months Ended June 30, 2017	2016
Unrealized gains/(losses) on investments available-for-sale		
Affected line item in the Statements of Income:		
Investment securities gains	**$ 1,275**	$ 1,919
Income before taxes	**1,275**	1,919
Tax expense	**(508)**	(765)
Net income	**$ 767**	$ 1,154
Amortization of defined benefit pension plan items		
Affected line item in the Statements of Income:		
Recognized actuarial loss[1]	**$ (590)**	$ (575)
Income before taxes	**(590)**	(575)
Tax benefit	**235**	228
Net income/(loss)	**$ (355)**	$ (347)

(1) This amount is included in the computation of net periodic benefit cost, see Note 9

Note 12 – Financial Instruments with Off-balance Sheet Risk and Derivatives

The Company has entered into interest rate swaps ("swaps") to facilitate customer transactions and meet their financing needs. These swaps qualify as derivatives, but are not designated as hedging instruments. Interest rate swap contracts involve the risk of dealing with counterparties and their ability to meet contractual terms. When the fair value of a derivative instrument contract is positive, this generally indicates that the counterparty or customer owes the Company, and results in credit risk to the Company. When the fair value of a derivative instrument contract is negative, the Company owes the customer or counterparty and therefore, has no credit risk. The notional value of commercial loan swaps outstanding was $18.3 million with a fair value of $0.9 million as of June 30, 2017 compared to $18.9 million with a fair value of $1.0 million as of December 31, 2016. The swap positions are offset to minimize the potential impact on the Company's financial statements. Fair values of the swaps are carried as both gross assets and gross liabilities in the condensed consolidated statements of condition. The associated net gains and losses on the swaps are recorded in other non-interest income.

Note 13 – Litigation

The Company and its subsidiaries are subject in the ordinary course of business to various pending or threatened legal proceedings in which claims for monetary damages are asserted. After consultation with legal counsel, management does not anticipate that the ultimate liability, if any, arising out of these legal matters will have a material adverse effect on the Company's financial condition, operating results or liquidity.

Note 14 – Fair Value

Generally accepted accounting principles provide entities the option to measure eligible financial assets, financial liabilities and commitments at fair value (i.e. the fair value option), on an instrument-by-instrument basis, that are otherwise not permitted to be accounted for at fair value under other accounting standards. The election to use the fair value option is available when an entity first recognizes a financial asset or financial liability or upon entering into a commitment. Subsequent changes in fair value must be recorded in earnings. The Company applies the fair value option on residential mortgage loans held for sale. The fair value option on residential mortgage loans allows the recognition of gains on sale of mortgage loans to more accurately reflect the timing and economics of the transaction.

The standard for fair value measurement establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy are described below.

Basis of Fair Value Measurement:

Level 1- Unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities;

Level 2- Quoted prices in markets that are not active, or inputs that are observable, either directly or indirectly, for substantially the full term of the asset or liability;

Level 3- Prices or valuation techniques that require inputs that are both significant to the fair value measurement and unobservable (i.e. supported by little or no market activity).

A financial instrument's level within the fair value hierarchy is based on the lowest level of input that is significant to the fair value measurement.

Changes to interest rates may result in changes in the cash flows due to prepayments or extinguishments. Accordingly, this could result in higher or lower measurements of the fair values.

Assets and Liabilities

Mortgage loans held for sale

Mortgage loans held for sale are valued based on quotations from the secondary market for similar instruments and are classified as Level 2 of the fair value hierarchy.

Investments available-for-sale

<u>U.S. government agencies and mortgage-backed securities</u>

Valuations are based on active market data and use of evaluated broker pricing models that vary based by asset class and includes available trade, bid, and other market information. Generally, the methodology includes broker quotes, proprietary models, descriptive terms and conditions databases coupled with extensive quality control programs. Multiple quality control evaluation processes review available market, credit and deal level information to support the evaluation of the security. If there is a lack of objectively verifiable information available to support the valuation, the evaluation of the security is discontinued. Additionally, proprietary models and pricing systems, mathematical tools, actual transacted prices, integration of market developments and experienced evaluators are used to determine the value of a security based on a hierarchy of market information regarding a security or securities with similar characteristics. The Company does not adjust the quoted price for such securities. Such instruments are generally classified within Level 2 of the fair value hierarchy.

<u>State and municipal securities</u>

Proprietary valuation matrices are used for valuing all tax-exempt municipals that can incorporate changes in the municipal market as they occur. Market evaluation models include the ability to value bank qualified municipals and general market municipals that can be broken down further according to insurer, credit support, state of issuance and rating to incorporate additional spreads and municipal curves. Taxable municipals are valued using a third party model that incorporates a methodology that captures the trading nuances associated with these bonds. Such instruments are generally classified within Level 2 of the fair value hierarchy.

Trust preferred securities and corporate debt

In active markets, these types of instruments are valued based on quoted market prices that are readily accessible at the measurement date and are classified within Level 1 of the fair value hierarchy. Positions that are not traded in active markets or are subject to transfer restrictions are valued or adjusted to reflect illiquidity and/or non-transferability, and such adjustments are generally based on available market evidence. In the absence of such evidence, management uses a process that employs certain assumptions to determine the present value. Positions that are not traded in active markets or are subject to transfer restrictions are classified within Level 3 of the fair value hierarchy.

Interest rate swap agreements

Interest rate swap agreements are measured by alternative pricing sources with reasonable levels of price transparency in markets that are not active. Based on the complex nature of interest rate swap agreements, the markets these instruments trade in are not as efficient and are less liquid than that of the more mature Level 1 markets. These markets do however have comparable, observable inputs in which an alternative pricing source values these assets in order to arrive at a fair market value. These characteristics classify interest rate swap agreements as Level 2.

Assets Measured at Fair Value on a Recurring Basis

The following tables set forth the Company's financial assets and liabilities at the dates indicated that were accounted for or disclosed at fair value. Assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement:

	June 30, 2017			
(In thousands)	**Quoted Prices in Active Markets for Identical Assets (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**	**Total**
Assets				
Residential mortgage loans held for sale	**$ -**	**$ 5,743**	**$ -**	**$ 5,743**
Investments available-for-sale:				
U.S. government agencies	**-**	**112,361**	**-**	**112,361**
State and municipal	**-**	**324,933**	**-**	**324,933**
Mortgage-backed	**-**	**332,275**	**-**	**332,275**
Corporate debt	**-**	**-**	**9,389**	**9,389**
Trust preferred	**-**	**-**	**908**	**908**
Marketable equity securities	**-**	**212**	**-**	**212**
Interest rate swap agreements	**-**	**886**	**-**	**886**
Liabilities				
Interest rate swap agreements	**$ -**	**$ (886)**	**$ -**	**$ (886)**

	December 31, 2016			
(In thousands)	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
Assets				
Residential mortgage loans held for sale	$ -	$ 13,222	$ -	$ 13,222
Investments available-for-sale:				
U.S. government agencies	-	121,790	-	121,790
State and municipal	-	287,684	-	287,684
Mortgage-backed	-	312,711	-	312,711
Corporate debt	-	-	9,134	9,134
Trust preferred	-	-	1,012	1,012
Marketable equity securities	-	1,223	-	1,223

Interest rate swap agreements		-		1,010		-		1,010
Liabilities								
Interest rate swap agreements	$	-	$	(1,010)	$	-	$	(1,010)

The following table provides unrealized losses included in assets measured in the Condensed Consolidated Statements of Condition at fair value on a recurring basis for the period indicated:

(In thousands)	Significant Unobservable Inputs (Level 3)
Investments available-for-sale:	
Balance at January 1, 2017	$ 10,146
Principal redemption	(158)
Total unrealized gains included in other comprehensive loss	309
Balance at June 30, 2017	$ 10,297

Assets Measured at Fair Value on a Nonrecurring Basis

The following table sets forth the Company's financial assets subject to fair value adjustments (impairment) on a nonrecurring basis at the date indicated that are valued at the lower of cost or market. Assets are classified in their entirety based on the lowest level of input that is significant to the fair value measurement:

	June 30, 2017				
(In thousands)	**Quoted Prices in Active Markets for Identical Assets (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**	**Total**	**Total Losses**
Impaired loans	**$ -**	**$ -**	**$ 8,395**	**$ 8,395**	**$ (10,879)**
Other real estate owned	**-**	**-**	**1,460**	**1,460**	**(116)**
Total	**$ -**	**$ -**	**$ 9,855**	**$ 9,855**	**$ (10,995)**

	December 31, 2016				
(In thousands)	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total	Total Losses
Impaired loans	$ -	$ -	$ 8,981	$ 8,981	$ (10,600)
Other real estate owned	-	-	1,911	1,911	(107)
Total	$ -	$ -	$ 10,892	$ 10,892	$ (10,707)

At June 30, 2017, impaired loans totaling $24.6 million were written down to fair value of $18.8 million as a result of specific loan loss allowances of $5.8 million associated with the impaired loans which was included in the allowance for loan losses. Impaired loans totaling $24.1 million were written down to fair value of $19.3 million at December 31, 2016 as a result of specific loan loss allowances of $4.8 million associated with the impaired loans.

Loan impairment is measured using the present value of expected cash flows, the loan’s observable market price or the fair value of the collateral (less selling costs) if the loans are collateral dependent. Collateral may be real estate and/or business assets including equipment, inventory and/or accounts receivable. The value of business equipment, inventory and accounts receivable collateral is based on net book value on the business’ financial statements and, if necessary, discounted based on management’s review and analysis. Appraised and reported values may be discounted based on management’s historical knowledge, changes in market conditions from the time of valuation, and/or management’s expertise and knowledge of the client and client’s business. Impaired loans are reviewed and evaluated on at least a quarterly basis for additional impairment and adjusted accordingly, based on the factors identified above. Valuation techniques are consistent with those techniques applied in prior periods.

Other real estate owned ("OREO") is adjusted to fair value upon transfer of the loans to OREO. Subsequently, OREO is carried at the lower of carrying value or fair value. The estimated fair value for other real estate owned included in Level 3 is determined by independent market based appraisals and other available market information, less cost to sell, that may be reduced further based on market expectations or an executed sales agreement. If the fair value of the collateral deteriorates subsequent to initial recognition, the Company records the OREO as a non-recurring Level 3 adjustment. Valuation techniques are consistent with those techniques applied in prior periods.

Fair Value of Financial Instruments

The Company discloses fair value information about financial instruments for which it is practicable to estimate the value, whether or not such financial instruments are recognized on the balance sheet. Fair value is the amount at which a financial instrument could be exchanged in a current transaction between willing parties, other than in a forced sale or liquidation, and is best evidenced by a quoted market price, if one exists.

Quoted market prices, where available, are shown as estimates of fair market values. Because no quoted market prices are available for a significant portion of the Company's financial instruments, the fair value of such instruments has been derived based on the amount and timing of future cash flows and estimated discount rates based on observable inputs ("Level 2") or unobservable inputs ("Level 3").

Present value techniques used in estimating the fair value of many of the Company's financial instruments are significantly affected by the assumptions used. In that regard, the derived fair value estimates cannot be substantiated by comparison to independent markets and, in many cases, could not be realized in immediate cash settlement of the instrument. Additionally, the accompanying estimates of fair values are only representative of the fair values of the individual financial assets and liabilities, and should not be considered an indication of the fair value of the Company.

The carrying amounts and fair values of the Company's financial instruments at the dates indicated are presented in the following table:

	June 30, 2017		Fair Value Measurements		
(In thousands)	**Carrying Amount**	**Estimated Fair Value**	**Quoted Prices in Active Markets for Identical Assets (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**
Financial Assets					
Other equity securities	**$ 41,413**	**$ 41,413**	**$ -**	**$ 41,413**	**$ -**
Loans, net of allowance	**4,088,092**	**4,139,371**	**-**	**-**	**4,139,371**
Other assets	**94,526**	**94,526**	**-**	**94,526**	**-**
Financial Liabilities					
Time deposits	**$ 656,265**	**$ 654,677**	**$ -**	**$ 654,677**	**$ -**
Securities sold under retail repurchase agreements and federal funds purchased	**127,312**	**127,312**	**-**	**127,312**	**-**
Advances from FHLB	**670,000**	**677,244**	**-**	**677,244**	**-**

	December 31, 2016		Fair Value Measurements		
(In thousands)	Carrying Amount	Estimated Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Financial Assets					
Other equity securities	$ 46,094	$ 46,094	$ -	$ 46,094	$ -
Loans, net of allowance	3,883,741	3,933,700	-	-	3,933,700
Other assets	93,328	93,328	-	93,328	-
Financial Liabilities					
Time deposits	$ 586,039	$ 584,868	$ -	$ 584,868	$ -
Securities sold under retail repurchase agreements and federal funds purchased	125,119	125,119	-	125,119	-
Advances from FHLB	790,000	800,756	-	800,756	-

Subordinated debentures	30,000	29,985	-	-	29,985

The following methods and assumptions were used to estimate the fair value of each category of financial instruments for which it is practicable to estimate that value:

Cash and Temporary Investments: The carrying amounts of cash and cash equivalents approximate their fair value and have been excluded from the table above.

Investments: The fair value of marketable securities is based on quoted market prices, prices quoted for similar instruments, and prices obtained from independent pricing services.

Loans: For certain categories of loans, such as mortgage, installment and commercial loans, the fair value is estimated by discounting the expected future cash flows using the current rates at which similar loans would be made to borrowers with similar credit ratings and similar remaining maturities. Expected cash flows were projected based on contractual cash flows, adjusted for estimated prepayments.

Accrued interest receivable: The carrying value of accrued interest receivable approximates fair value due to the short-term duration and has been excluded from the table above.

Other assets: The investment in bank-owned life insurance represents the cash surrender value of the policies at June 30, 2017 and December 31, 2016 as determined by each insurance carrier.

Deposits: The fair value of demand, money market savings and regular savings deposits, which have no stated maturity, were considered equal to their carrying amount, representing the amount payable on demand. While management believes that the Bank's core deposit relationships provide a relatively stable, low-cost funding source that has a substantial intangible value separate from the value of the deposit balances, these estimated fair values do not include the intangible value of core deposit relationships, which comprise a significant portion of the Bank's deposit base.

Short-term borrowings: The carrying values of short-term borrowings, including overnight, securities sold under agreements to repurchase and federal funds purchased approximates the fair values due to the short maturities of those instruments.

Long-term borrowings: The fair value of the Federal Home Loan Bank of Atlanta ("FHLB") advances and subordinated debentures was estimated by computing the discounted value of contractual cash flows payable at current interest rates for obligations with similar remaining terms. The Company's credit risk is not material to calculation of fair value because the FHLB borrowings are collateralized. The Company classifies advances from the Federal Home Loan Bank of Atlanta within Level 2 of the fair value hierarchy since the fair value of such borrowings is based on rates currently available for borrowings with similar terms and remaining maturities. Subordinated debentures are classified as Level 3 in the fair value hierarchy due to the lack of market activity of such instruments.

Accrued interest payable: The carrying value of accrued interest payable approximates fair value due to the short-term duration and has been excluded from the previous table.

Note 15 - Segment Reporting

Currently, the Company conducts business in three operating segments—Community Banking, Insurance and Investment Management. Each of the operating segments is a strategic business unit that offers different products and services. The Insurance and Investment Management segments were businesses that were acquired in separate transactions where management of the acquired business was retained. The accounting policies of the segments are the same as those of the Company. However, the segment data reflect inter-segment transactions and balances.

The Community Banking segment is conducted through Sandy Spring Bank and involves delivering a broad range of financial products and services, including various loan and deposit products to both individuals and businesses. Parent company income is included in the Community Banking segment, as the majority of effort of these functions is related to this segment. Major revenue sources include net interest income, gains on sales of mortgage loans, trust income fees and service charges on deposit accounts. Expenses include personnel, occupancy, marketing, equipment and other expenses. Non-cash charges associated with amortization of intangibles was not significant for the three and six months ended June 30, 2017 and 2016, respectively.

The Insurance segment is conducted through Sandy Spring Insurance Corporation, a subsidiary of the Bank, and offers annuities as an alternative to traditional deposit accounts. Sandy Spring Insurance Corporation operates Sandy Spring Insurance, a general insurance agency located in Annapolis, Maryland, and Neff and Associates, located in Ocean City, Maryland. Major sources of revenue are insurance commissions from commercial lines, personal lines, and medical liability lines. Expenses include personnel and support charges. Non-cash charges associated with amortization of intangibles was not significant for the three and six months ended June 30, 2017 and 2016, respectively.

The Investment Management segment is conducted through West Financial Services, Inc., a subsidiary of the Bank. This asset management and financial planning firm, located in McLean, Virginia, provides comprehensive investment management and financial planning to individuals, families, small businesses and associations including cash flow analysis, investment review, tax planning, retirement planning, insurance analysis and estate planning. West Financial currently has approximately $1.3 billion in assets under management. Major revenue sources include non-interest income earned on the above services. Expenses include personnel and support charges. Non-cash charges associated with amortization of intangibles was not significant for the three and six months ended June 30, 2017 and 2016, respectively.

Information for the operating segments and reconciliation of the information to the condensed consolidated financial statements for the periods indicated is presented in the following tables:

	Three Months Ended June 30, 2017				
(In thousands)	**Community Banking**	**Insurance**	**Investment Mgmt.**	**Inter-Segment Elimination**	**Total**
Interest income	**$ 48,576**	**$ -**	**$ 2**	**$ (2)**	**$ 48,576**
Interest expense	**6,252**	**-**	**-**	**(2)**	**6,250**
Provision for loan losses	**1,322**	**-**	**-**	**-**	**1,322**
Noninterest income	**10,544**	**1,223**	**2,014**	**(210)**	**13,571**
Noninterest expense	**30,602**	**1,324**	**1,152**	**(210)**	**32,868**
Income before income taxes	**20,944**	**(101)**	**864**	**-**	**21,707**
Income tax expense	**6,669**	**(40)**	**337**	**-**	**6,966**
Net income	**$ 14,275**	**$ (61)**	**$ 527**	**$ -**	**$ 14,741**
Assets	**$ 5,273,823**	**$ 8,046**	**$ 13,676**	**$ (25,024)**	**$ 5,270,521**

	Three Months Ended June 30, 2016				
(In thousands)	Community Banking	Insurance	Investment Mgmt.	Inter-Segment Elimination	Total
Interest income	$ 41,804	$ -	$ 1	$ (2)	$ 41,803
Interest expense	5,073	-	-	(2)	5,071
Provision for loan losses	2,957	-	-	-	2,957
Non-interest income	10,136	950	1,843	(178)	12,751
Non-interest expense	28,999	1,030	1,020	(178)	30,871
Income before income taxes	14,911	(80)	824	-	15,655
Income tax expense	4,718	(31)	321	-	5,008
Net income	$ 10,193	$ (49)	$ 503	$ -	$ 10,647
Assets	$ 4,742,368	$ 5,754	$ 11,601	$ (20,274)	$ 4,739,449

	Six Months Ended June 30, 2017				
(In thousands)	**Community Banking**	**Insurance**	**Investment Mgmt.**	**Inter-Segment Elimination**	**Total**
Interest income	**$ 94,533**	**$ 1**	**$ 4**	**$ (4)**	**$ 94,534**
Interest expense	**11,959**	**-**	**-**	**(4)**	**11,955**
Provision for loan losses	**1,516**	**-**	**-**	**-**	**1,516**
Noninterest income	**19,630**	**2,975**	**4,017**	**(419)**	**26,203**
Noninterest expense	**58,401**	**2,679**	**2,188**	**(419)**	**62,849**
Income before income taxes	**42,287**	**297**	**1,833**	**-**	**44,417**
Income tax expense	**13,729**	**121**	**714**	**-**	**14,564**

Net income	**$ 28,558**	**$ 176**	**$ 1,119**	**$ -**	**$ 29,853**
Assets	**$ 5,273,823**	**$ 8,046**	**$ 13,676**	**$ (25,024)**	**$ 5,270,521**

	Six Months Ended June 30, 2016				
(In thousands)	Community Banking	Insurance	Investment Mgmt.	Inter-Segment Elimination	Total
Interest income	$ 83,457	$ 1	$ 2	$ (4)	$ 83,456
Interest expense	10,606	-	-	(4)	10,602
Provision for loan losses	4,193	-	-	-	4,193
Non-interest income	20,355	2,403	3,712	(356)	26,114
Non-interest expense	59,379	2,201	1,964	(356)	63,188
Income before income taxes	29,634	203	1,750	-	31,587
Income tax expense	9,362	83	682	-	10,127
Net income	$ 20,272	$ 120	$ 1,068	$ -	$ 21,460
Assets	$ 4,742,368	$ 5,754	$ 11,601	$ (20,274)	$ 4,739,449

Note 16 – PENDING AQUISITION

On May 15, 2017, the Company and WashingtonFirst Bankshares, Inc., a Virginia corporation (“WashingtonFirst”) and parent company for WashingtonFirst Bank, entered into a definitive agreement and plan of merger that provides for WashingtonFirst to merge with and into the Company (the “Merger”). At the effective time of the Merger, the combined entity shall exist as a Maryland corporation.

Subsequent to the effective date of the Merger, WashingtonFirst Bank, a Virginia state-chartered bank and a wholly-owned subsidiary of WashingtonFirst, will merge with and into the Bank (the “Bank Merger”). The Bank will survive the Bank Merger and continue to exist as a Maryland banking corporation.

Under the terms of the agreement, WashingtonFirst shareholders are expected to receive 0.8713 shares of Company common stock for each share owned of WashingtonFirst common stock, subject to adjustment if the Company’s average stock price during a specified measurement period prior to closing is more than $50.15 or less than $37.07 per share. The transaction, which is expected to close in the fourth quarter of 2017, has a value of approximately $498 million in the aggregate, based on the Company’s closing price of $42.72 on May 15, 2017. Upon closing, Sandy Spring shareholders will own approximately 67.8% of the combined company and WashingtonFirst’s shareholders will own approximately 32.2% of the combined company.

As of March 31, 2017, WashingtonFirst had $2.1 billion in assets with 19 full-service community banking offices throughout the Washington D.C. Metropolitan region. In addition, WashingtonFirst also provides wealth management services through its subsidiary, 1st Portfolio Wealth Advisors, and mortgage banking services through its subsidiary, WashingtonFirst Mortgage Corporation.

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Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

The Company

Sandy Spring Bancorp, Inc. (the "Company") is the bank holding company for Sandy Spring Bank (the "Bank"). The Company is registered as a bank holding company pursuant to the Bank Holding Company Act of 1956, as amended (the "Holding Company Act"). As such, the Company is subject to supervision and regulation by the Board of Governors of the Federal Reserve System (the "Federal Reserve"). The Company began operating in 1988. The Bank traces its origin to 1868, making it among the oldest institutions in the region. The Bank is an independent, community oriented commercial banking business that conducts full-service banking through 44 community offices located in Central Maryland, Northern Virginia and Washington D.C. The Bank is a state chartered bank subject to supervision and regulation by the Federal Reserve and the State of Maryland. The Bank's deposit accounts are insured by the Deposit Insurance Fund administered by the Federal Deposit Insurance Corporation (the "FDIC") to the maximum permitted by law. The Bank is a member of the Federal Reserve System and is an Equal Housing Lender. The Company, the Bank, and its other subsidiaries are Affirmative Action/Equal Opportunity Employers.

The Company is a $5.3 billion community banking organization that focuses its lending and other services on businesses and consumers in the local market area. Through its subsidiaries, Sandy Spring Insurance Corporation and West Financial Services, Inc., Sandy Spring Bank offers a comprehensive menu of insurance and investment management services.

On May 16, 2017, the Company announced it had entered into a definitive agreement and plan of merger pursuant to which WashingtonFirst Bankshares, Inc., the parent company for WashingtonFirst Bank, will merge with and into the Company in a transaction valued at approximately $498 million. WashingtonFirst, headquartered in Reston, Virginia, has 19 community banking offices and more than $2.1 billion in assets (as of March 31, 2017).

Overview

Net income for the Company for the second quarter of 2017 totaled $14.7 million ($0.61 per diluted share) as compared to net income of $10.6 million ($0.44 per diluted share) for the second quarter of 2016. These results reflect the following events:

- Average total loans for the second quarter of 2017 increased 13% compared to the second quarter of 2016 due primarily to organic growth of 16% in the commercial loan portfolio. Overall, the entire portfolio grew $461 million over the prior year period.

- Average total deposits grew 11% to $3.9 billion for the second quarter of 2017 as compared to $3.5 billion for the second quarter of 2016.

- The net interest margin was 3.60% for the second quarter of 2017, compared to 3.51% for the second quarter of 2016 and 3.51% for the first quarter of 2017.

- The return on average equity for the second quarter of 2017 increased 32% to 10.80% as compared to 8.21% from the prior year.

- The Non-GAAP efficiency ratio was 54.10% for the current quarter as compared to 59.12% for the second quarter of 2016 and 54.78% for the first quarter of 2017.

The local economy continues to display certain positive economic trends such as lower unemployment and increased housing starts; however, these trends have been tempered by other concerns such as the lack of wage growth and the strength of the dollar. These factors in concert have acted to restrict the pace of economic expansion. Volatility in global economic markets and geo-political unrest has continued to cause uncertainty in the financial markets. Furthermore, concern over rising interest rates has acted to restrain confidence among individual consumers and small and mid-sized businesses. In light of this mixed economic environment, management is optimistic that the regional economy will continue to improve and present further growth opportunities for the Company.

Total assets at June 30, 2017 increased 4% compared to December 31, 2016 driven by loan balances that increased 5% compared to the prior year end due to growth in commercial loans. Customer funding sources, which include deposits plus other short-term borrowings from core customers, increased 8% compared to balances at December 31, 2016. The increase in customer funding sources was driven primarily by increases of 9% in noninterest-bearing and interest-bearing transaction accounts and 7% in money market savings accounts. Additionally, certificates of deposit increased 12% compared to the balances at December 31, 2016 as the Company increased rates to fund loan growth. Liquidity remained strong due to the borrowing lines with the Federal Home Loan Bank of Atlanta and the Federal Reserve and the size and composition of the investment portfolio. During the first six months of 2017, stockholders' equity increased $21 million to $555 million due to the increase in retained earnings during the period.

Non-performing loans represented 0.78% of total assets at June 30, 2017 compared to 0.85% at June 30, 2016 due to asset growth. The Company's non-performing assets were $32.2 million at June 30, 2017 compared to $31.4 million at June 30, 2016. The ratio of net charge-offs to average loans was 0.01% for the second quarter of 2017 compared to 0.15% for the prior year quarter.

The net interest margin was 3.60% for the second quarter of 2017, compared to 3.51% for the second quarter of 2016. The quarter's margin included the effect of the receipt of $0.7 million from the full payoff of a previously acquired credit-impaired loan. Exclusive of this non-core item, the margin would have been 3.54%. The Company continued to manage its net interest margin through the prepayment of higher rate FHLB advances, sales of selected investment securities and the extinguishment of $30 million of subordinated debentures in the first quarter of 2017. These transactions have contributed to an improving net interest margin in the second quarter of 2017 compared to the second quarter of 2016.

The provision for loan losses was $1.3 million for the second quarter of 2017 compared to $3.0 million for the second quarter of 2016. The decrease in the current quarter's charge versus the prior year's quarter reflected improved loan portfolio credit quality that partially offset the effects of loan growth on the provision over the past year.

Non-interest income increased to $13.6 million for the second quarter of 2017 compared to $12.8 million for the second quarter of 2016. The second quarter of 2017 included gains of $1.3 million on sales of investment securities. The second quarter of 2016 included a $1.2 million gain on the extinguishment of subordinated debentures and $0.2 million in gains on the sales of investment securities. Excluding these gains, non-interest income increased 8% compared to the prior year quarter.

Non-interest expenses increased 6% to $32.9 million for the second quarter of 2017 compared to $30.9 million in the second quarter of 2016. The second quarter of 2017 included $1.3 million in penalties on the early payoff of high-rate FHLB advances and $1.0 million in merger expenses. The comparable period for 2016 included $1.4 million in prepayment penalties. Excluding these transactions, non-interest expenses increased 4% compared to the second quarter of 2016 due to merit increases, performance incentives and volume driven compensation costs. The non-GAAP efficiency ratio was 54.10% for the second quarter of 2017 compared to 59.12% for the second quarter of

2016 as a result of the growth in net interest income.

Sandy Spring Bancorp, Inc. and Subsidiaries
CONSOLIDATED AVERAGE BALANCES, YIELDS AND RATES

	Six Months Ended June 30,					
	2017			2016		
(Dollars in thousands and tax-equivalent)	**Average Balances**	**(1) Interest**	**Annualized Average Yield/Rate**	Average Balances	(1) Interest	An A Yi
Assets						
Residential mortgage loans	**$ 854,022**	**$14,879**	**3.48%**	$ 809,574	$13,802	
Residential construction loans	**163,174**	**3,015**	**3.73**	138,781	2,463	
Total mortgage loans	**1,017,196**	**17,894**	**3.52**	948,355	16,265	
Commercial AD&C loans	**306,604**	**7,421**	**4.88**	266,888	6,113	
Commercial investor real estate loans	**977,915**	**21,699**	**4.47**	769,803	17,600	
Commercial owner occupied real estate loans	**775,625**	**19,009**	**4.94**	681,347	16,365	
Commercial business loans	**458,563**	**10,069**	**4.43**	457,181	9,956	
Total commercial loans	**2,518,707**	**58,198**	**4.66**	2,175,219	50,034	
Consumer loans	**459,927**	**8,101**	**3.58**	450,335	7,774	
Total loans (2)	**3,995,830**	**84,193**	**4.24**	3,573,909	74,073	
Loans held for sale	**7,238**	**154**	**4.27**	11,181	198	
Taxable securities	**534,306**	**7,413**	**2.78**	490,338	6,356	
Tax-exempt securities (3)	**296,323**	**6,280**	**4.24**	284,524	6,024	
Total investment securities	**830,629**	**13,693**	**3.30**	774,862	12,380	
Interest-bearing deposits with banks	**40,038**	**181**	**0.91**	42,777	107	
Federal funds sold	**2,320**	**10**	**0.84**	608	2	
Total interest-earning assets	**4,876,055**	**98,231**	**4.05**	4,403,337	86,760	
Less: allowance for loan losses	**(43,703)**			**(41,567)**		
Cash and due from banks	**48,165**			**46,783**		
Premises and equipment, net	**53,548**			**53,396**		
Other assets	**223,228**			**212,915**		
Total assets	**$5,157,293**			$**4,674,864**		
Liabilities and Stockholders' Equity						
Interest-bearing demand deposits	**$ 612,608**	**237**	**0.08%**	$ 577,771	223	
Regular savings deposits	**320,577**	**106**	**0.07**	294,339	89	
Money market savings deposits	**986,625**	**1,854**	**0.38**	902,352	932	
Time deposits	**616,713**	**3,314**	**1.08**	538,435	2,634	
Total interest-bearing deposits	**2,536,523**	**5,511**	**0.44**	2,312,897	3,878	
Other borrowings	**130,531**	**155**	**0.24**	116,792	138	
Advances from FHLB	**699,641**	**6,277**	**1.81**	599,423	6,113	
Subordinated debentures	**829**	**12**	**2.91**	32,995	473	
Total interest-bearing liabilities	**3,367,524**	**11,955**	**0.72**	3,062,107	10,602	
Noninterest-bearing demand deposits	**1,205,809**			1,052,116		
Other liabilities	**42,659**			37,793		
Stockholders' equity	**541,301**			522,848		
Total liabilities and stockholders' equity	**$5,157,293**			$4,674,864		

Net interest income and spread	**86,276**	**3.33%**	76,158
Less: tax-equivalent adjustment	**3,697**		3,304
Net interest income	**$82,579**		$72,854
Interest income/earning assets		**4.05%**	
Interest expense/earning assets		**0.49**	
Net interest margin		**3.56%**	

(1) Tax-equivalent income has been adjusted using the combined marginal federal and state rate of 39.88% for 2017 and 2016. annualized taxable-equivalent
adjustments utilized in the above table to compute yields aggregated to $3.7 million and $3.3 million in 2017 and 2016, res
(2) Non-accrual loans are included in the average balances.
(3) Includes only investments that are exempt from federal taxes.

Results of Operations

For the Six Months Ended June 30, 2017 Compared to the Six Months Ended June 30, 2016

Net income for the Company for the first six months of 2017 totaled $29.9 million ($1.23 per diluted share) compared to net income of $21.5 million ($0.89 per diluted share) for the first six months of 2016.

Net Interest Income

The largest source of the Company's operating revenue is net interest income, which is the difference between the interest earned on interest-earning assets and the interest paid on interest-bearing liabilities. For purposes of this discussion and analysis, the interest earned on tax-exempt investment securities has been adjusted to an amount comparable to interest subject to normal income taxes. The result is referred to as tax-equivalent interest income and tax-equivalent net interest income. The following discussion of net interest income should be considered in conjunction with the review of the information provided in the preceding table.

Net interest income for the first six months of 2017 was $82.6 million compared to $72.9 million for the first six months of 2016. On a tax-equivalent basis, net interest income for the first six months of 2017 was $86.3 million compared to $76.2 million for the first six months of 2016, an increase of 13%. The preceding table provides an analysis of net interest income performance that reflects a net interest margin that has increased to 3.56% for the first six months of 2017 compared to 3.47% for the first six months of 2016. The first six months of 2017 net interest income included $0.7 million from the full payoff of a previously acquired credit impaired loan. Exclusive of this recovered interest income, the net interest margin would have been 3.54%.

The higher net interest margin was driven by an increase in the yield on interest-earning assets as a result of loan growth and the migration of assets from lower-yielding investment securities into higher-yielding loans. Average interest-earning assets increased by 11% while average interest-bearing liabilities increased 10% in the first six months of 2017 compared to the first six months of 2016. Average noninterest-bearing deposits increased 15% in the first six months of 2017. As the percentage of average noninterest-bearing deposits to total deposits rose slightly to 32% in the first six months of 2017 compared to 31% in the first six months of 2016.

Interest Income

The Company's total tax-equivalent interest income increased 13% for the first six months of 2017 compared to the prior year period. The previous and following table reflect that the increase in interest income has been driven almost entirely by loan growth.

The average balance of the loan portfolio increased 12% for the first six months of 2017 compared to the first six months of 2016. This growth occurred in all segments of the loan portfolio with the most significant growth in the commercial portfolio. The increases were driven by organic loan growth as the regional economy improved. Excluding the interest recovery, the yield on average loans increased by 5 basis points from the prior year. The rise in the portfolio yield was driven primarily by an increase the yields in all major segments of the loan portfolio as loan volumes had a greater impact than their associated rates on the increase in the overall yield.

The average yield on total investment securities increased 10 basis points as the average balance of the portfolio increased 7% for the first six months of 2017 compared to the first six months of 2016. The increase in the yield on investments was due primarily to securities purchased in early 2017 at favorable yields in addition to the decline in the size of the lower-yielding mortgage-backed securities portfolio due sales of such securities that occurred in early 2016. The effect of these transactions was to increase the relative size of the higher yielding state and municipal portfolio as part of the total investment securities portfolio.

Interest Expense

Interest expense increased 13% in the first six months of 2017 compared to the first six months of 2016. The cost of interest-bearing deposits increased as the Company increased rates to maintain deposit relationships and to provide funding for loan growth. The average rate paid on Federal Home Loan Bank advances decreased due to the prepayments of high rate advances over the past year. Average deposits increased 11% in the first six months of 2017 compared to the first six months of 2016. This increase was primarily due to increases of $189 million or 12% in average noninterest-bearing and interest-bearing checking accounts together with increases of $78 million or 15% in certificates of deposit and $84 million or 9% in money market accounts as the Company increased rates on the deposit products.

Effect of Volume and Rate Changes on Net Interest Income

The following table analyzes the reasons for the changes from year-to-year in the principal elements that comprise net interest income:

	2017 vs. 2016			2016 vs. 2015		
	Increase			Increase		
	Or	**Due to Change In Average:***		Or	Due to Change In Average:*	
(Dollars in thousands and tax equivalent)	**(Decrease)**	**Volume**	**Rate**	(Decrease)	Volume	Rate
Interest income from earning assets:						
Residential mortgage loans	**$ 1,077**	**$ 784**	**$ 293**	$ 1,523	$ 1,375	$ 148
Residential construction loans	**552**	**440**	**112**	(26)	74	(100)
Commercial AD&C loans	**1,308**	**939**	**369**	1,251	1,262	(11)
Commercial investor real estate loans	**4,099**	**4,610**	**(511)**	2,250	2,613	(363)
Commercial owner occupied real estate loans	**2,644**	**2,270**	**374**	1,165	1,564	(399)
Commercial business loans	**113**	**24**	**89**	1,449	1,468	(19)
Leasing	**-**	**-**	**-**	(1)	1	-
Consumer loans	**327**	**157**	**170**	668	357	311
Loans held for sale	**(44)**	**(79)**	**35**	(10)	11	(21)
Taxable securities	**1,057**	**582**	**475**	(1,366)	(1,634)	268
Tax exempt securities	**256**	**242**	**14**	(281)	(196)	(85)
Interest-bearing deposits with banks	**74**	**(7)**	**81**	63	11	52
Federal funds sold	**8**	**6**	**2**	1	1	-
Total interest income	**11,471**	**9,968**	**1,503**	6,686	6,907	(219)
Interest expense on funding of earning assets:						
Interest-bearing demand deposits	**14**	**14**	**-**	16	22	(6)
Regular savings deposits	**17**	**6**	**11**	18	6	12
Money market savings deposits	**922**	**95**	**827**	342	49	293
Time deposits	**680**	**400**	**280**	941	352	589
Other borrowings	**17**	**17**	**-**	28	23	5
Advances from FHLB	**164**	**936**	**(772)**	(389)	(152)	(237)
Subordinated debentures	**(461)**	**(466)**	**5**	31	(26)	57
Total interest expense	**1,353**	**1,002**	**351**	987	274	713
Net interest income	**$ 10,118**	**$ 8,966**	**$ 1,152**	$ 5,699	$ 6,633	$ (932)

* Variances that are the combined effect of volume and rate, but cannot be separately identified, are allocated to the volume and rate variances based on their respective relative amounts.

Non-interest Income

Non-interest income amounts and trends are presented in the following table for the periods indicated:

(Dollars in thousands)	Six Months Ended June 30, **2017**	2016	2017/2016 $ Change	2017/2016 % Change
Securities gains	**$ 1,275**	$ 1,919	$ (644)	(33.6)%
Service charges on deposit accounts	**3,981**	3,859	122	3.2
Mortgage banking activities	**1,448**	1,641	(193)	(11.8)
Wealth management income	**9,228**	8,853	375	4.2
Insurance agency commissions	**2,974**	2,394	580	24.2
Income from bank owned life insurance	**1,199**	1,230	(31)	(2.5)
Bank card fees	**2,398**	2,309	89	3.9
Other income	**3,700**	3,909	(209)	(5.3)
Total non-interest income	**$ 26,203**	$ 26,114	$ 89	0.3

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Total non-interest income was $26.2 million for the first six months of 2017 compared to $26.1 million for the first six months of 2016. The first six months of 2017 includes $1.3 million in gains on sales of investment securities. The prior year period included a $1.2 million gain on the extinguishment of subordinated debentures and $1.9 million in gains on the sales of investment securities. Excluding these gains, non-interest income increased 8% compared to the prior year period. Further detail by type of non-interest income follows:

- Gains on the sales of investment securities declined to $1.3 million for the first six months of 2017 compared to $1.9 million for the first six months of 2016. During the first six months of 2017 the Company sold specific equity securities for gains that were applied to offset the impact of prepayment penalties incurred on FHLB advances during the current quarter. A similar strategy was executed for the same period of the prior year.

- Income from mortgage banking activities decreased in the first six months of 2017 compared to the first six months of 2016 due primarily due to lower volumes of bulk loan sales compared to the prior year period.

- Wealth management income is comprised of income from trust and estate services and investment management fees earned by the Company’s investment management subsidiary. Overall, wealth management income increased 4% for the first six months of 2017 compared to the same period of the prior year. The prior year’s wealth management income included $0.4 million in fees on sales of investment products. The portfolio responsible for these fees was sold in early 2016. Excluding these fees from the prior year period, wealth management income grew 9% from prior year levels. Trust services fees increased 8% for the first six months of 2017 compared to the prior year period. Investment management fees increased 10% for the first six months of 2017 compared to the same period of 2016, due to an increase in assets under management. Overall total assets under management increased to $2.6 billion at June 30, 2017 compared to $2.3 billion at June 30, 2016 primarily as a result of positive trends occurring in the financial markets and increased sales efforts.

- Insurance agency commissions increased for the first six months of 2017 compared to the same period of 2016 primarily due to the increased commission income resulting from the agency acquisition that occurred in the third quarter of the prior year.

- Other non-interest income decreased mainly due to a $1.2 million gain realized on the extinguishment of subordinated debentures in the first six months of 2016. Excluding this gain, other non-interest income increased 37% for the first six months of 2017 as compared to the first six months of 2016 due to prepayment fees, commissions and incentives.

Non-interest Expense

Non-interest expense amounts and trends are presented in the following table for the periods indicated:

	Six Months Ended June 30,		2017/2016	2017/2016
(Dollars in thousands)	**2017**	2016	$ Change	% Change
Salaries and employee benefits	**$ 36,083**	$ 35,451	$ 632	1.8 %

Occupancy expense of premises		**6,613**		6,635	(22)	(0.3)
Equipment expenses		**3,491**		3,357	134	4.0
Marketing		**1,439**		1,343	96	7.1
Outside data services		**2,759**		2,718	41	1.5
FDIC insurance		**1,628**		1,286	342	26.6
Amortization of intangible assets		**51**		60	(9)	(15.0)
Merger expenses		**987**		-	987	100.0
Professional fees		**2,000**		2,585	(585)	(22.6)
Other real estate owned		**(1)**		12	(13)	(108.3)
Other expense		**7,799**		9,741	(1,942)	(19.9)
Total non-interest expense	**$**	**62,849**	$	63,188 $	(339)	(0.5)

Non-interest expenses totaled $62.8 million in the first six months of 2017 compared to $63.2 million in the first six months of 2016, a 1% decrease. The non-interest expenses for six months ended June 30, 2017, included $1.3 million in prepayment penalties for the early payoff of high-rate FHLB advances as compared to $3.2 million in prepayment penalties included for the six months ended June 30, 2016. The current period also included $1.0 million in merger expenses. Excluding the impact of prepayment penalties and merger expenses, non-interest expenses increased 1% over the prior year period. Further detail by category of non-interest expense follows:

- Salaries and employee benefits, the largest component of non-interest expenses, increased in the first six months of 2017 due to higher compensation expense as a result of merit increases, performance incentives and volume based compensation costs. The increased compensation costs were partially offset by a decrease in healthcare expense. The average number of full-time equivalent employees was 733 in the first six months of 2017 compared to 725 in the first six months of 2016.

- Equipment expenses increased in 2017 compared to 2016 due primarily to higher software amortization expense.

- Marketing expense increased 7% as a result of focused marketing initiatives.

- FDIC insurance experienced a 26% increase directly associated with the asset growth of the Company over the past twelve months.

- Merger expense is the direct result of costs associated with the prospective WashingtonFirst acquisition.

- Occupancy, outside data services and intangible amortization expense levels remained comparable to the prior year period.

- Other non-interest expenses decreased in the first six months of 2017 compared to the prior year period. The current year included $1.3 million in penalties related to the prepayment of FHLB advances as compared to the previous year which included $3.2 million in prepayment penalties. Excluding these expenses, other non-interest expenses declined 7% for the first six months compared to the prior year period.

Operating Expense Performance

Management views the GAAP efficiency ratio as an important financial measure of expense performance and cost management. The ratio expresses the level of non-interest expenses as a percentage of total revenue (net interest income plus total non-interest income). Lower ratios indicate improved productivity.

Non-GAAP Financial Measures

The Company also uses a traditional efficiency ratio that is a non-GAAP financial measure of operating expense control and efficiency of operations. Management believes that its traditional ratio better focuses attention on the operating performance of the Company over time than does a GAAP ratio, and is highly useful in comparing period-to-period operating performance of the Company's core business operations. It is used by management as part of its assessment of its performance in managing non-interest expenses. However, this measure is supplemental, and is not a substitute for an analysis of performance based on GAAP measures. The reader is cautioned that the non-GAAP efficiency ratio used by the Company may not be comparable to GAAP or non-GAAP efficiency ratios reported by other financial institutions.

In general, the efficiency ratio is non-interest expenses as a percentage of net interest income plus non-interest income. Non-interest expenses used in the calculation of the non-GAAP efficiency ratio exclude goodwill impairment losses, the amortization of intangibles, and non-recurring expenses. Income for the non-GAAP ratio includes the favorable effect of tax-exempt income, and excludes securities gains and losses, which vary widely from period to period without appreciably affecting operating expenses, and non-recurring gains. The measure is different from the GAAP efficiency ratio, which also is presented in this report. The GAAP measure is calculated using non-interest expense and income amounts as shown on the face of the Condensed Consolidated Statements of Income. The GAAP and non-GAAP efficiency ratios are reconciled and provided in the following table. The GAAP efficiency ratio improved in the first six months of 2017 compared to the first six months of 2016 due primarily to the increase in net interest income discussed previously and expense control discipline.

In addition, the Company uses pre-tax, pre-provision income as a measure of the level of recurring income before taxes. Management believes this provides financial statement users with a useful metric of the run-rate of revenues and expenses which is readily comparable to other financial institutions. This measure is calculated by adding (subtracting) the provision (credit) for loan and lease losses, and the provision for income taxes back to net income. This metric increased in the first six months of 2017 compared to the first six months of 2016 due primarily to the increase in net interest income.

	Three Months Ended June 30,		Six Months Ended June 30,	
(Dollars in thousands)	**2017**	2016	**2017**	2016
Pre-tax pre-provision income:				
Net income	**$ 14,741**	$ 10,647	**$ 29,853**	$ 21,460
Plus non-GAAP adjustment:				
Merger expenses	**987**	-	**987**	-
Income taxes	**6,966**	5,008	**14,564**	10,127
Provision for loan losses	**1,322**	2,957	**1,516**	4,193
Pre-tax pre-provision income	**$ 24,016**	$ 18,612	**$ 46,920**	$ 35,780
Efficiency ratio - GAAP basis:				
Non-interest expense	**$ 32,868**	$ 30,871	**$ 62,849**	$ 63,188
Net interest income plus non-interest income	**$ 55,897**	$ 49,483	**$ 108,782**	$ 98,968
Efficiency ratio - GAAP basis	**58.80%**	62.39%	**57.78%**	63.85%
Efficiency ratio - Non-GAAP basis:				
Non-interest expense	**$ 32,868**	$ 30,871	**$ 62,849**	$ 63,188
Less non-GAAP adjustment:				
Amortization of intangible assets	**25**	28	**51**	60
Loss on FHLB redemption	**1,275**	1,416	**1,275**	3,167
Merger expenses	**987**	-	**987**	-
Non-interest expenses - as adjusted	**$ 30,581**	$ 29,427	**$ 60,536**	$ 59,961
Net interest income plus non-interest income	**$ 55,897**	$ 49,483	**$ 108,782**	$ 98,968
Plus non-GAAP adjustment:				
Tax-equivalent income	**1,901**	1,640	**3,697**	3,304
Less non-GAAP adjustments:				
Securities gains	**1,273**	150	**1,275**	1,919
Gain on redemption of subordinated debentures	**-**	1,200	**-**	1,200
Net interest income plus non-interest income - as adjusted	**$ 56,525**	$ 49,773	**$ 111,204**	$ 99,153
Efficiency ratio - Non-GAAP basis	**54.10%**	59.12%	**54.44%**	60.47%

Income Taxes

The Company had income tax expense of $14.6 million in the first six months of 2017, compared to income tax expense of $10.1 million in the first six months of 2016. The resulting effective tax rates were 33% for the first six months of 2017 and 32% for the first six months of 2016. This rate increase was due to the decline in tax-advantaged interest income in proportion to total interest income.

Results of Operations

For the Three Months Ended June 30, 2017 Compared to the Three Months Ended June 30, 2016

Net income for the Company for the second quarter of 2017 totaled $14.7 million ($0.61 per diluted share) compared to net income of $10.6 million ($0.44 per diluted share) for the second quarter of 2016.

Net Interest Income

Net interest income for the second quarter of 2017 was $42.3 million compared to $36.7 million for the second quarter of 2016. On a tax-equivalent basis, net interest income for the second quarter of 2017 was $44.2 million compared to $38.4 million for the second quarter of 2016, an increase of 15%. The following table provides an analysis of net interest income performance that reflects a net interest margin that has increased to 3.60% for the second quarter of 2017 compared to 3.51% for the second quarter of 2016. Net interest income for the second quarter of 2017 included $0.7 million from the full payoff during the quarter of a previously acquired credit impaired loan. Exclusive of the recovered interest income, the net interest margin would have been 3.54%.

Average interest-earning assets increased by 12% while average interest-bearing liabilities increased 11% in the second quarter of 2017 compared to the second quarter of 2016. Average noninterest-bearing deposits increased 16% in the second quarter of 2017 while the percentage of average noninterest-bearing deposits to total deposits increased to 33% in the current quarter compared to 32% in the second quarter of 2016. During the quarter the net interest margin was driven by an increase in the yield on interest-earning assets, loan and investment portfolio growth, and a reduced borrowing costs resulting from the prepayment of FHLB advances over the previous twelve months and the extinguishment of subordinated debentures early in the first quarter of 2017. The impact of these factors were partially offset by an increase in the cost of deposits as the Company increased rates to maintain deposit relationships and fund loan growth.

Sandy Spring Bancorp, Inc. and Subsidiaries
CONSOLIDATED AVERAGE BALANCES, YIELDS AND RATES

	Three Months Ended June 30,					
		2017			2016	
			Annualized			An
	Average	**(1)**	**Average**	Average	(1)	A
(Dollars in thousands and tax-equivalent)	**Balances**	**Interest**	**Yield/Rate**	Balances	Interest	Yi
Assets						
Residential mortgage loans	**$ 860,081**	**$ 7,531**	**3.50%**	$ 811,705	$ 6,934	
Residential construction loans	**169,130**	**1,579**	**3.74**	142,854	1,268	
Total mortgage loans	**1,029,211**	**9,110**	**3.54**	954,559	8,202	
Commercial AD&C loans	**302,924**	**3,767**	**4.99**	272,090	3,115	
Commercial investor real estate loans	**1,010,389**	**11,280**	**4.48**	788,785	8,988	
Commercial owner occupied real estate loans	**776,279**	**9,981**	**5.16**	684,907	8,280	
Commercial business loans	**454,724**	**5,062**	**4.46**	453,459	4,943	
Total commercial loans	**2,544,316**	**30,090**	**4.74**	2,199,241	25,326	
Consumer loans	**461,672**	**4,171**	**3.66**	449,594	3,885	
Total loans (2)	**4,035,199**	**43,371**	**4.31**	3,603,394	37,413	
Loans held for sale	**7,077**	**72**	**4.09**	8,326	64	
Taxable securities	**535,028**	**3,678**	**2.75**	456,803	2,943	
Tax-exempt securities (3)	**307,809**	**3,259**	**4.23**	282,329	2,968	
Total investment securities	**842,837**	**6,937**	**3.29**	739,132	5,911	
Interest-bearing deposits with banks	**34,738**	**91**	**1.06**	43,300	54	
Federal funds sold	**2,538**	**6**	**0.96**	727	1	
Total interest-earning assets	**4,922,389**	**50,477**	**4.11**	4,394,879	43,443	
Less: allowance for loan losses	**(43,679)**			(42,064)		
Cash and due from banks	**47,517**			46,527		
Premises and equipment, net	**53,449**			53,218		
Other assets	**222,722**			211,783		
Total assets	**$5,202,398**			$4,664,343		
Liabilities and Stockholders' Equity						
Interest-bearing demand deposits	**$ 615,141**	**123**	**0.08%**	$ 586,323	115	
Regular savings deposits	**325,634**	**57**	**0.07**	298,435	47	
Money market savings deposits	**983,185**	**1,076**	**0.44**	907,670	495	
Time deposits	**634,824**	**1,767**	**1.12**	554,707	1,384	
Total interest-bearing deposits	**2,558,784**	**3,023**	**0.47**	2,347,135	2,041	
Other borrowings	**132,553**	**79**	**0.24**	122,601	72	
Advances from FHLB	**668,791**	**3,148**	**1.89**	519,780	2,739	
Subordinated debentures	**-**	**-**	**-**	30,989	219	
Total interest-bearing liabilities	**3,360,128**	**6,250**	**0.75**	3,020,505	5,071	
Noninterest-bearing demand deposits	**1,251,396**			1,082,762		
Other liabilities	**43,645**			39,689		
Stockholders' equity	**547,229**			521,387		
Total liabilities and stockholders' equity	**$5,202,398**			$4,664,343		

Net interest income and spread	**44,227**	**3.36%**	38,372
Less: tax-equivalent adjustment	**1,901**		1,640
Net interest income	**$42,326**		$36,732
Interest income/earning assets		**4.11%**	
Interest expense/earning assets		**0.51**	
Net interest margin		**3.60%**	

(1) Tax-equivalent income has been adjusted using the combined marginal federal and state rate of 39.88% for 2017 and 2016. annualized taxable-equivalent
adjustments utilized in the above table to compute yields aggregated to $1.9 million and $1.6 million in 2017 and 2016, res
(2) Non-accrual loans are included in the average balances.
(3) Includes only investments that are exempt from federal taxes.

Interest Income

The Company's total tax-equivalent interest income increased 16% for the second quarter of 2017 compared to the prior year quarter. The previous table shows that this increase was driven by loan growth during the previous twelve months.

The average balance of the loan portfolio increased 12% for the second quarter of 2017 compared to the prior year period. The increase has been driven by organic loan growth due to the strength of the regional economy. The majority of growth was concentrated in the commercial real estate loan portfolios. The yield on average loans increased by l4 basis points compared to the prior year quarter. Exclusive of the previously mentioned recovered interest income, the yield on average loans would have increased by 7 basis points to 4.24%.

The average yield on total investment securities increased 9 basis points while the average balance of the portfolio increased 14% for the second quarter of 2017 compared to the second quarter of 2016. The increase in the yield on investments was due to the addition of relatively higher-yielding tax-exempt municipal securities that occurred in early 2017.

Average deposits increased 11% in the second quarter of 2017 compared to the second quarter of 2016. This increase was primarily due to increases of $197 million or 12% in average noninterest-bearing and interest-bearing checking accounts together with increases of $80 million or 14% in certificates of deposit and $76 million or 8% in money market accounts as the Company increased rates on these products. The cost of interest-bearing deposits increased as the Company increased rates to maintain deposit relationships and fund loan growth. This increase was somewhat offset by the lower average rates paid on FHLB advances due in part to the prepayment of such advances during the current quarter.

Non-interest Income

Non-interest income amounts and trends are presented in the following table for the periods indicated:

	Three Months Ended June 30,		2017/2016	2017/2016
(Dollars in thousands)	**2017**	2016	$ Change	% Change
Securities gains	**$ 1,273**	$ 150	$ 1,123	N/M %
Service charges on deposit accounts	**2,017**	1,956	61	3.1
Mortgage banking activities	**840**	1,106	(266)	(24.1)
Wealth management income	**4,744**	4,448	296	6.7

Insurance agency commissions	**1,222**	949	273	28.8
Income from bank owned life insurance	**605**	615	(10)	(1.6)
Bank card fees	**1,253**	1,220	33	2.7
Other income	**1,617**	2,307	(690)	(29.9)
Total non-interest income	**$ 13,571**	$ 12,751	$ 820	6.4

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Total non-interest income was $13.6 million for the second quarter of 2017 compared to $12.8 million for the second quarter of 2016, an increase of 6%. The second quarter of 2017 included gains of $1.3 million on sales of investment securities. The second quarter of 2016 included a $1.2 million gain on the extinguishment of subordinated debentures and $0.2 million in gains on the sales of investment securities. Excluding these gains, non-interest income increased 8% compared to the prior year quarter due to increases in insurance agency commissions, wealth management fees and other non-interest income. These increases were partially offset by a decrease in mortgage banking income due to reduced volumes combined with a recent rise in interest rates late in the second quarter of 2017. Further detail by type of non-interest income follows:

- Gains on the sales of investment securities increased to $1.3 million for the quarter ended June 30, 2017 compared to $0.2 million for the same quarter of 2016. During the second quarter of 2017 the Company sold specific equity securities for gains that were applied to offset the impact of prepayment penalties incurred on FHLB advances during the current quarter.

- Income from mortgage banking activities decreased in the second quarter of 2017 compared to the second quarter of 2016 due to reduced lending volumes and the impact of the rise in interest rates late in the second quarter.

- Wealth management income is comprised of income from trust and estate services and investment management fees earned by the Company's investment management subsidiary. Overall, wealth management income increased 7% for the quarter ended June 30, 2017 compared to the same quarter of the prior year. Trust services fees increased 5% for the second quarter of 2017 compared to the prior year period. Investment management fees increased 9% for the second quarter of 2017 compared to the same period of 2016, due to an increase in assets under management. Overall total assets under management increased to $2.6 billion at June 30, 2017 compared to $2.3 billion at June 30, 2016.

- Insurance agency commissions increased 29% during the second quarter of 2017 compared to the second quarter of 2016 due to the commission income from the agency acquisition in the third quarter of the prior year.

- Other non-interest income for the three months ended June 30, 2017 compared to the same period of 2016 decreased 30% as the second quarter of 2016 included a $1.2 million gain on the extinguishment of subordinated debentures. Excluding the extinguishment gain, other non-interest income increased 46% during the second quarter of 2017 compared to the second quarter of 2016 due to prepayment fees, commissions and incentives.

Non-interest Expense

Non-interest expense amounts and trends are presented in the following table for the periods indicated:

	Three Months Ended June 30,		2017/2016	2017/2016
(Dollars in thousands)	**2017**	2016	$ Change	% Change
Salaries and employee benefits	**$ 18,282**	$ 17,221	$ 1,061	6.2 %

Occupancy expense of premises	**3,211**	3,162	49	1.5
Equipment expenses	**1,767**	1,693	74	4.4
Marketing	**776**	662	114	17.2
Outside data services	**1,367**	1,355	12	0.9
FDIC insurance	**823**	649	174	26.8
Amortization of intangible assets	**25**	28	(3)	(10.7)
Merger expenses	**987**	-	987	100.0
Professional fees	**1,045**	1,447	(402)	(27.8)
Other real estate owned	**(6)**	(5)	(1)	20.0
Other expense	**4,591**	4,659	(68)	(1.5)
Total non-interest expense	**$ 32,868**	$ 30,871	$ 1,997	6.5

Non-interest expenses totaled $32.9 million in the second quarter of 2017 compared to $30.9 million in the second quarter of 2016 and increase of 6%. The second quarter of 2017 included $1.3 million in penalties on the early payoff of high-rate FHLB advances and $1.0 million in merger expenses. The comparable period for 2016 included $1.4 million in prepayment penalties. Excluding these transactions, non-interest expenses increased 4% compared to the second quarter of 2016 due to higher compensation costs. Further detail by category of non-interest expense follows:

- Salaries and employee benefits, the largest component of non-interest expenses, increased in the second quarter of 2017 due primarily to an increase in compensation expenses as a result of merit increases, performance incentives and volume driven compensation costs. The average number of full-time equivalent employees was 735 in the second quarter of 2017 compared to 728 in the second quarter of 2016.

- Marketing expense increased 7% from the prior year due to an increase in focused ad campaigns.
- FDIC insurance expense increased due to asset growth.
- Merger expense is the direct result of costs associated with the prospective Washington First acquisition.
- Professional fees decreased in the second quarter of 2017 due to decreases in various professional fees.
- Other non-interest expenses for the second quarter of 2017 remain relatively flat compared to the prior year quarter after excluding $1.3 million in penalties from the early payoff of high-rate FHLB advances incurred in the second quarter of 2017 and $1.4 million for the comparable period for 2016.

Income Taxes

The Company had income tax expense of $7.0 million in the second quarter of 2017, compared to income tax expense of $5.0 million in the second quarter of 2016. The resulting effective tax rate was 32% for both the second quarter of 2017 and the second quarter of 2016. The effective tax rate for the current quarter remained comparable to the prior year quarter as the decline in tax-advantaged interest income in proportion to total interest income was offset by the impact of tax benefits associated with stock-based compensation which positively affected income tax expense. The treatment of these tax benefits was the result of recently adopted authoritative guidance. Prior to the issuance of this guidance, the tax benefits associated with stock-based compensation directly affected capital.

FINANCIAL CONDITION

The Company's total assets were $5.3 billion at June 30, 2017, an increase of $179 million or 4% compared to December 31, 2016. The increase was primarily due to the growth in total loans, which increased 5% compared to the previous year end.

Analysis of Loans and Leases

A comparison of the loan portfolio at the dates indicated is presented in the following table:

	June 30, 2017		December 31, 2016		Period-to-Period Change	
(Dollars in thousands)	**Amount**	**%**	Amount	%	$	%
Residential real estate:						
Residential mortgage	**$ 871,766**	**21.1%**	$ 841,692	21.4%	$ 30,074	3.6%
Residential construction	**169,901**	**4.1**	150,229	3.8	19,672	13.1
Commercial real estate:						
Commercial owner occupied real estate	**797,629**	**19.3**	775,552	19.8	22,077	2.8
Commercial investor real estate	**1,069,988**	**25.9**	928,113	23.6	141,875	15.3
Commercial AD&C	**314,259**	**7.6**	308,279	7.9	5,980	1.9
Commercial business	**451,570**	**10.9**	467,286	11.9	(15,716)	(3.4)
Consumer	**458,058**	**11.1**	456,657	11.6	1,401	0.3
Total loans	**$4,133,171**	**100.0%**	$3,927,808	100.0%	$ 205,363	5.2

Total loans, excluding loans held for sale, increased 5% at June 30, 2017 compared to December 31, 2016. The commercial loan portfolio increased 6% at June 30, 2017 driven by an increase of 15% in investor real estate loans. The owner occupied real estate portfolio increased 3% offset by a 3% decrease in the commercial business loans portfolio. The residential real estate portfolio, which is comprised of residential construction and permanent residential mortgage loans, increased 5% at June 30, 2017 compared to December 31, 2016. This increase was driven by a 13% increase in residential construction loans during the second quarter. The consumer loan portfolio remained level at June 30, 2017 compared to December 31, 2016.

Analysis of Investment Securities

The composition of investment securities at the periods indicated is presented in the following table:

	June 30, 2017		December 31, 2016		Period-to-Period Change	
(Dollars in thousands)	**Amount**	**%**	Amount	%	$	%
Investments available-for-sale:						
U.S. government agencies and corporations	**$ 112,361**	**13.7%**	$ 121,790	15.6%	$ (9,429)	(7.7)%
State and municipal	**324,933**	**39.6**	287,684	36.9	37,249	12.9
Mortgage-backed	**332,275**	**40.5**	312,711	40.1	19,564	6.3
Corporate debt	**9,389**	**1.1**	9,134	1.2	255	2.8
Trust preferred	**908**	**0.1**	1,012	0.1	(104)	(10.3)
Marketable equity securities	**212**	**-**	1,223	0.2	(1,011)	(82.7)

Total available-for-sale securities	**780,078**	**95.0**	733,554	94.1	46,524	6.3
Investments held-to-maturity and other equity:						
Other equity securities	**41,413**	**5.0**	46,094	5.9	(4,681)	(10.2)
Total held-to-maturity and other equity	**41,413**	**5.0**	46,094	5.9	(4,681)	(10.2)
Total securities	**$ 821,491**	**100.0%**	$ 779,648	100.0%	$ 41,843	5.4

The investment portfolio increased 5% at June 30, 2017 compared to December 31, 2016. as funds from increased deposits were invested at favorable rates.

The investment portfolio consists primarily of U.S. Agency securities, U.S. Agency mortgage-backed securities, U.S. Agency collateralized mortgage obligations and state and municipal securities. The duration of the portfolio was 3.4 years at June 30, 2017 and 3.3 years at December 31, 2016. The Company considers the duration of the portfolio to be adequate for liquidity purposes. This investment strategy has resulted in a portfolio with low credit risk that would provide the liquidity necessary to meet loan demand. The portfolio is monitored on a continuing basis with consideration given to interest rate trends and the structure of the yield curve and with constant assessment of economic projections and analysis.

Other Earning Assets

Residential mortgage loans held for sale were $6 million at June 30, 2017 compared to $13 million at December 31, 2016 due to the effect of the timing of loan sales on the amounts held for sale at quarter end. The aggregate of federal funds sold and interest-bearing deposits with banks decreased by $53 million to $28 million at June 30, 2017 compared to December 31, 2016 due to the timing of cash flows.

Deposits

The composition of deposits at the periods indicated is presented in the following table:

	June 30, 2017		December 31, 2016		Period-to-Period Change	
(Dollars in thousands)	**Amount**	**%**	Amount	%	$	%
Noninterest-bearing deposits	**$ 1,302,536**	**33.5%**	$ 1,138,139	31.8%	$ 164,397	14.4%
Interest-bearing deposits:						
Demand	**605,976**	**15.6**	615,058	17.2	(9,082)	(1.5)
Money market savings	**991,503**	**25.5**	927,837	25.9	63,666	6.9
Regular savings	**329,165**	**8.5**	310,471	8.7	18,694	6.0
Time deposits of less than $100,000	**282,234**	**7.3**	258,621	7.2	23,613	9.1
Time deposits of $100,000 or more	**374,031**	**9.6**	327,418	9.2	46,613	14.2
Total interest-bearing deposits	**2,582,909**	**66.5**	2,439,405	68.2	143,504	5.9
Total deposits	**$ 3,885,445**	**100.0%**	$ 3,577,544	100.0%	$ 307,901	8.6

Deposits and Borrowings

Total deposits increased $308 million or 9% at June 30, 2017 compared to December 31, 2016. This increase was due primarily to increases of 14% in noninterest-bearing checking accounts and 7% in money market savings accounts. In addition, regular savings accounts increased 6% and certificates of deposit increased 12% compared to December 31, 2016. The increase in interest-bearing products occurred as the Company raised rates to maintain client relationships and to fund loan growth. Total borrowings decreased 16% at June 30, 2017 compared to December 31, 2016 due to the reduced dependence on borrowings as a result of the growth in deposits and the extinguishment of $30 million in subordinated debentures during the first three months of 2017.

Capital Management

Management monitors historical and projected earnings, dividends and asset growth, as well as risks associated with the various types of on and off-balance sheet assets and liabilities, in order to determine appropriate capital levels. Total stockholders' equity was $555 million at June 30, 2017 compared to $534 million at December 31, 2016 as net income during the period exceeded the payment of dividends. The ratio of average equity to average assets was 10.50% for the six months ended June 30, 2017, as compared to 11.18% for the first six months of 2016 as the ratio was affected by the growth of average assets.

Bank holding companies and banks are required to maintain capital ratios in accordance with guidelines adopted by the federal bank regulators. These guidelines are commonly known as Risk-Based Capital guidelines. The actual regulatory ratios and required ratios for capital adequacy, in addition to the ratios required to be categorized as "well capitalized", are summarized for the Company in the following table.

Risk-Based Capital Ratios

	Ratios at		Minimum Regulatory Requirements
	June 30, 2017	December 31, 2016	
Total capital to risk-weighted assets	**12.00%**	12.80%	8.00%
Tier 1 capital to risk-weighted assets	**10.96%**	11.74%	6.00%
Common equity tier 1 capital	**10.96%**	11.01%	4.50%
Tier 1 leverage	**9.26%**	10.14%	4.00%

As of June 30, 2017, the most recent notification from the Bank's primary regulator categorized the Bank as a "well-capitalized" institution under the prompt corrective action rules of the Federal Deposit Insurance Act. Designation as a well-capitalized institution under these regulations is not a recommendation or endorsement of the Company or the Bank by federal bank regulators.

In July 2013, the Federal Reserve Board approved revisions to its capital adequacy guidelines and prompt corrective action rules that implement the revised standards of the Basel Committee on Banking Supervision, commonly called Basel III, and address relevant provisions of the Dodd-Frank Act. The rules include new risk-based capital and leverage ratios, which were effective January 1, 2015, and revise the definition of what constitutes "capital" for calculating those ratios. The minimum capital level requirements applicable to the Company and the Bank are: (1) a common equity Tier 1 capital ratio of 4.5%; (2) a Tier 1 capital ratio of 6%; (3) a total capital ratio of 8%; and (4) a Tier 1 leverage ratio of 4%. The rules eliminate the inclusion of certain instruments, such as trust preferred securities, from Tier 1 capital. Instruments issued prior to May 19, 2010 have been grandfathered for companies with consolidated assets of $15 billion or less. The rules also establish a "capital conservation buffer" of 2.5% above the new regulatory minimum capital requirements, which must consist entirely of common equity Tier 1 capital. The new capital conservation buffer requirement began to phase in beginning in January 2016 at 0.625% of risk-weighted assets and will increase by that amount each year until fully implemented in January 2019. An institution would be subject to limitations on paying dividends, engaging in share repurchases, and paying discretionary bonuses to executive officers if its capital level falls below the buffer amount. These limitations establish a maximum percentage of eligible retained income that could be utilized for such actions.

Tangible Common Equity

Tangible equity, tangible assets and tangible book value per share are non-GAAP financial measures calculated using GAAP amounts. Tangible common equity and tangible assets exclude the balances of goodwill and other intangible assets from stockholder's equity and total assets, respectively. Management believes that this non-GAAP financial measure provides information to investors that may be useful in understanding our financial condition. Because not all companies use the same calculation of tangible equity and tangible assets, this presentation may not be comparable to other similarly titled measures calculated by other companies. A reconciliation of the non-GAAP ratio of tangible equity to tangible assets and tangible book value per share are provided in the following table.

Tangible Common Equity Ratio – Non-GAAP

(Dollars in thousands, except per share data)	**June 30, 2017**	December 31, 2016
Tangible common equity ratio:		
Total stockholders' equity	**$ 554,683**	$ 533,572
Accumulated other comprehensive loss	**3,712**	6,614
Goodwill	**(85,768)**	(85,768)
Other intangible assets, net	**(629)**	(680)
Tangible common equity	**$ 471,998**	$ 453,738
Total assets	**$ 5,270,521**	$ 5,091,383
Goodwill	**(85,768)**	(85,768)
Other intangible assets, net	**(629)**	(680)
Tangible assets	**$ 5,184,124**	$ 5,004,935
Tangible common equity ratio	**9.10%**	9.07%
Tangible book value per share	**$ 19.68**	$ 18.98

Credit Risk

The fundamental lending business of the Company is based on understanding, measuring and controlling the credit risk inherent in the loan portfolio. The Company's loan portfolio is subject to varying degrees of credit risk. Credit risk entails both general risks, which are inherent in the process of lending, and risk specific to individual borrowers. The Company's credit risk is mitigated through portfolio diversification, which limits exposure to any single customer, industry or collateral type. Typically, each consumer and residential lending product has a generally predictable level of credit losses based on historical loss experience. Residential mortgage and home equity loans and lines generally have the lowest credit loss experience. Loans secured by personal property, such as auto loans, generally experience medium credit losses. Unsecured loan products, such as personal revolving credit, have the highest credit loss experience and for that reason, the Company has chosen not to engage in a significant amount of this type of lending. Credit risk in commercial lending can vary significantly, as losses as a percentage of outstanding loans can shift widely during economic cycles and are particularly sensitive to changing economic conditions. Generally, improving economic conditions result in improved operating results on the part of commercial customers, enhancing their ability to meet their particular debt service requirements. Improvements, if any, in operating cash flows can be offset by the impact of rising interest rates that may occur during improved economic times. Inconsistent economic conditions may have an adverse effect on the operating results of commercial customers, reducing their ability to meet debt service obligations.

Total non-performing loans increased 1% to $32.2 million at June 30, 2017 compared to the balance at December 31, 2016. While the diversification of the lending portfolio among different commercial, residential and consumer product lines along with different market conditions of the D.C. suburbs, Northern Virginia and Baltimore metropolitan area has mitigated some of the risks in the portfolio, local economic conditions and levels of non-performing loans may continue to be influenced by the conditions being experienced in various business sectors of the economy on both a regional and national level.

To control and manage credit risk, management has a credit process in place to reasonably ensure that credit standards are maintained along with an in-house loan administration accompanied by oversight and review procedures. The primary purpose of loan underwriting is the evaluation of specific lending risks and involves the analysis of the borrower's ability to service the debt as well as the assessment of the value of the underlying collateral. Oversight and review procedures include the monitoring of portfolio credit quality, early identification of potential problem credits and the aggressive management of problem credits. As part of the oversight and review process, the Company maintains an allowance for loan losses (the "allowance").

The allowance represents an estimation of the losses that are inherent in the loan portfolio. The adequacy of the allowance is determined through the ongoing evaluation of the credit portfolio, and involves consideration of a number of factors, as outlined below, to establish an adequate allowance for loan losses. Determination of the allowance is inherently subjective and requires significant estimates, including estimated losses on pools of homogeneous loans based on historical loss experience and consideration of current economic trends, which may be susceptible to significant change. Loans deemed uncollectible are charged against the allowance, while recoveries are credited to the allowance. Management adjusts the level of the allowance through the provision for loan losses, which is recorded as a current period operating expense.

The methodology for assessing the appropriateness of the allowance includes: (1) a general allowance that reflects historical losses, as adjusted, by credit category, and (2) a specific allowance for impaired credits on an individual or portfolio basis. This methodology is further described in “Note 1 – Significant Accounting Policies” of the Notes to the Consolidated Financial Statements. The amount of the allowance is reviewed and approved quarterly by the Risk Committee of the board of directors.

The Company recognizes a collateral dependent lending relationship as non-performing when either the loan becomes 90 days delinquent or as a result of factors (such as bankruptcy, interruption of cash flows, etc.) considered at the monthly credit committee meeting. When a commercial loan is placed on non-accrual status, it is considered to be impaired and all accrued but unpaid interest is reversed. Classification as an impaired loan is based on a determination that the Company may not collect all principal and interest payments according to contractual terms. Impaired loans exclude large groups of smaller-balance homogeneous loans that are collectively evaluated for impairment such as residential real estate and consumer loans. Typically, all payments received on non-accrual loans are first applied to the remaining principal balance of the loans. Any additional recoveries are credited to the allowance. Integral to the assessment of the allowance process is an evaluation that is performed to determine whether a specific allowance on an impaired loan is warranted and, when losses are confirmed, a charge-off is taken to reduce the loan to its net realizable value. Any further collateral deterioration results in either further specific allowances being established or additional charge-offs. At such time an action plan is agreed upon for the particular loan and an appraisal will be ordered depending on the time elapsed since the prior appraisal, the loan balance and/or the result of the internal evaluation. A current appraisal on large loans is usually obtained if the appraisal on file is more than 12 months old and there has been a material change in market conditions, zoning, physical use or the adequacy of the collateral based on an internal evaluation. The Company’s policy is to strictly adhere to regulatory appraisal standards. If an appraisal is ordered, no more than a 30 day turnaround is requested from the appraiser, who is selected by Credit Administration from an approved appraiser list. After receipt of the updated appraisal, the assigned credit officer will recommend to the Chief Credit Officer whether a specific allowance or a charge-off should be taken. The Chief Credit Officer has the authority to approve a specific allowance or charge-off between monthly credit committee meetings to ensure that there are no significant time lapses during this process.

The Company’s methodology for evaluating whether a loan is impaired begins with risk-rating credits on an individual basis and includes consideration of the borrower’s overall financial condition, payment record and available cash resources that may include the sufficiency of collateral value and, in a select few cases, verifiable support from financial guarantors. In measuring impairment, the Company looks primarily to the discounted cash flows of the project itself or to the value of the collateral as the primary sources of repayment of the loan. The Company may consider the existence of guarantees and the financial strength and wherewithal of the guarantors involved in any loan relationship. Guarantees may be considered as a source of repayment based on the guarantor's financial condition and respective payment capacity. Accordingly, absent a verifiable payment capacity, a guarantee alone would not be sufficient to avoid classifying the loan as impaired.

Management has established a credit process that dictates that structured procedures be performed to monitor these loans between the receipt of an original appraisal and the updated appraisal. These procedures include the following:

- An internal evaluation is updated quarterly to include borrower financial statements and/or cash flow projections.

- The borrower may be contacted for a meeting to discuss an updated or revised action plan which may include a request for additional collateral.

- Re-verification of the documentation supporting the Company's position with respect to the collateral securing the loan.

- At the monthly credit committee meeting the loan may be downgraded and a specific allowance may be decided upon in advance of the receipt of the appraisal.

- Upon receipt of the updated appraisal (or based on an updated internal financial evaluation) the loan balance is compared to the appraisal and a specific allowance is decided upon for the particular loan, typically for the amount of the difference between the appraisal and the loan balance.

- The Company will specifically reserve for or charge-off the excess of the loan amount over the amount of the appraisal net of closing costs.

If an updated appraisal is received subsequent to the preliminary determination of a specific allowance or partial charge-off, and it is less than the initial appraisal used in the initial assessment, an additional specific allowance or charge-off is taken on the related credit. Partially charged-off loans are not written back up based on updated appraisals and always remain on non-accrual with any and all subsequent payments first applied to the remaining balance of the loan as principal reductions. No interest income is recognized on loans that have been partially charged-off.

Loans that have their terms restructured (e.g., interest rates, loan maturity date, payment and amortization period, etc.) in circumstances that provide payment relief or other concessions, to a borrower experiencing financial difficulty are considered troubled debt restructured loans (TDR's). All restructurings that constitute concessions to a borrower experiencing financial difficulties are considered impaired loans and may either be in accruing status or non-accruing status. Non-accruing restructured loans may return to accruing status provided there is a sufficient period of payment performance in accordance with the restructure terms. Loans may be removed from disclosure as a troubled debt restructuring if their revised loans terms are considered to be consistent with terms that can be obtained in the credit market for loans with comparable risk.

The Company may extend the maturity of a performing or current loan that may have some inherent weakness associated with the loan. However, the Company generally follows a policy of not extending maturities on non-performing loans under existing terms. Maturity date extensions only occur under revised terms that clearly place the Company in a position to increase the likelihood of or assure full collection of the loan under the contractual terms and /or terms at the time of the extension that may eliminate or mitigate the inherent weakness in the loan. These terms may incorporate, but are not limited to additional assignment of collateral, significant balance curtailments/liquidations and assignments of additional project cash flows. Guarantees may be a consideration in the extension of loan maturities. As a general matter, the Company does not view extension of a loan to be a satisfactory approach to resolving non-performing credits. On an exception basis, certain performing loans that have displayed some inherent weakness in the underlying collateral values, an inability to comply with certain loan covenants which are not affecting the performance of the credit or other identified weakness may be extended.

Collateral values or estimates of discounted cash flows (inclusive of any potential cash flow from guarantees) are evaluated to estimate the probability and severity of potential losses. The actual occurrence and severity of losses involving impaired credits can differ substantially from estimates.

The determination of the allowance requires significant judgment, and estimates of probable losses in the loan portfolio can vary significantly from the amounts actually observed. While management uses available information to recognize probable losses, future additions to the allowance may be necessary based on changes in the credits comprising the portfolio and changes in the financial condition of borrowers, such as may result from changes in economic conditions. In addition, federal and state regulatory agencies, as an integral part of their examination process, and independent consultants engaged by the Bank, periodically review the loan portfolio and the allowance. Such reviews may result in adjustments to the allowance based upon their analysis of the information available at the time of each examination.

The Company makes provisions for loan losses in amounts necessary to maintain the allowance at an appropriate level, as established by use of the allowance methodology previously discussed. The provision for loan losses was $1.5 million in the first six months of 2017 compared to $4.2 million in the first six months of 2016. The decrease in the provision in the first six months of 2017 reflects continued improved loan portfolio credit quality, that offset the effects of loan growth on the provision over the past year.

The Company typically sells a substantial portion of its fixed-rate residential mortgage originations in the secondary mortgage market. Concurrent with such sales, the Company is required to make customary representations and warranties to the purchasers about the mortgage loans and the manner in which they were originated. The related sale agreements grant the purchasers recourse back to the Company, which could require the Company to repurchase loans or to share in any losses incurred by the purchasers. This recourse exposure typically extends for a period of nine to eighteen months after the sale of the loan although the time frame for repurchase requests can extend for an indefinite period. Such transactions could be due to a number of causes including borrower fraud or early payment default. The Company has seen a very limited number of repurchase and indemnity demands from purchasers for such events and routinely monitors its exposure in this regard. The Company maintains a liability of $0.5 million for probable losses due to repurchases.

The Company periodically engages in whole loan sale transactions of its residential mortgage loans as a part its interest rate risk management strategy. The Company sold $18.1 million of loans on a servicing-retained basis during the three and six months ended June 30, 2017, and realized a total gain on sale of $219 thousand. Servicing asset associated with these sales during the six months ended June 30, 2017, was $138 thousand. Income earned by the Company on its loan servicing rights is derived primarily from contractually specified servicing fees and other ancillary fees. Such income earned for the three and six months ended June 30, 2017, was not significant.

Mortgage loan servicing rights are accounted for at amortized cost and are monitored for impairment on an ongoing basis. At June 30, 2017, and December 31, 2016, the amortized cost of the Company's mortgage loan servicing rights was $562 thousand and $418 thousand, respectively. The Company did not incur any impairment losses during the six months ended June 30, 2017.

Allowance for Loan Losses

During the second quarter of 2017, there were no changes in the Company’s methodology for assessing the appropriateness of the allowance for loan losses from the prior year. Variations can occur over time in the estimation of the allowance as a result of the credit performance of borrowers.

At June 30, 2017, total non-performing loans were $32.2 million, or 0.78% of total loans, compared to $31.9 million, or 0.81% of total loans, at December 31, 2016. The allowance represented 140% of non-performing loans at June 30, 2017 as compared to 138% at December 31, 2016. The allowance for loan losses as a percent of total loans was 1.09% at June 30, 2017 as compared to 1.12% at December 31, 2016.

Continued analysis of the actual loss history on the problem credits in 2016 and 2017 provided an indication that the coverage of the inherent losses on the problem credits was adequate. The Company continues to monitor the impact of the economic conditions on our commercial customers together with the reduced inflow of non-accruals and criticized loans. The improvement in these credit metrics supports management’s outlook for continued improved credit quality performance.

The balance of impaired loans was $24.6 million, with specific allowances of $5.8 million against those loans at June 30, 2017, as compared to $24.1 million with allowances of $4.8 million, at December 31, 2016.

The Company's borrowers are concentrated in nine counties in Maryland, three counties in Virginia and in Washington D.C. Commercial and residential mortgages, including home equity loans and lines, represented 77% of total loans at both June 30, 2017 and December 31, 2016. Certain loan terms may create concentrations of credit risk and increase the Company’s exposure to loss. These include terms that permit the deferral of principal payments or payments that are smaller than normal interest accruals (negative amortization); loans with high loan-to-value ratios; loans, such as option adjustable-rate mortgages, that may expose the borrower to future increases in repayments that are in excess of increases that would result solely from increases in market interest rates; and interest-only loans. The Company does not make loans that provide for negative amortization or option adjustable-rate mortgages.

Summary of Loan Loss Experience

The following table presents the activity in the allowance for loan losses for the periods indicated:

(Dollars in thousands)	**Six Months Ended June 30, 2017**	Year Ended December 31, 2016
Balance, January 1	**$ 44,067**	$ 40,895
Provision for loan losses	**1,516**	5,546
Loan charge-offs:		
Residential real estate:		
Residential mortgage	**(9)**	(1,404)
Residential construction	**-**	-
Commercial real estate:		
Commercial investor	**-**	(197)
Commercial owner occupied	**-**	-
Commercial AD&C	**-**	(48)
Commercial business	**(411)**	(597)
Consumer	**(404)**	(888)
Total charge-offs	**(824)**	(3,134)
Loan recoveries:		
Residential real estate:		
Residential mortgage	**28**	358
Residential construction	**14**	32
Commercial real estate:		
Commercial investor	**83**	133
Commercial owner occupied	**-**	5
Commercial AD&C	**103**	40
Commercial business	**44**	44
Consumer	**48**	148
Total recoveries	**320**	760
Net charge-offs	**(504)**	(2,374)
Balance, period end	**$ 45,079**	$ 44,067
Net charge-offs to average loans	**0.03%**	0.06%
Allowance for loan losses to loans	**1.09%**	1.12%

Analysis of Credit Risk

The following table presents information with respect to non-performing assets and 90-day delinquencies for the periods indicated:

(Dollars in thousands)	**June 30, 2017**	December 31, 2016
Non-accrual loans:		
Residential real estate:		
Residential mortgage	**$ 7,101**	$ 7,257
Residential construction	**187**	195
Commercial real estate:		
Commercial investor	**6,934**	8,107
Commercial owner occupied	**4,926**	4,823
Commercial AD&C	**137**	137
Commercial business	**6,807**	5,833
Consumer	**3,111**	2,859
Total non-accrual loans	**29,203**	29,211
Loans 90 days past due		
Residential real estate:		
Residential mortgage	**-**	232
Residential construction	**-**	-
Commercial real estate:		
Commercial investor	**-**	-
Commercial owner occupied	**424**	-
Commercial AD&C	**-**	-
Commercial business	**-**	-
Consumer	**4**	-
Total 90 days past due loans	**428**	232
Restructured loans (accruing)	**2,569**	2,489
Total non-performing loans	**32,200**	31,932
Other real estate owned, net	**1,460**	1,911
Total non-performing assets	**$ 33,660**	$ 33,843
Non-performing loans to total loans	**0.78%**	0.81%
Non-performing assets to total assets	**0.64%**	0.66%
Allowance for loan to non-performing loans	**140.00%**	138.00%

Market Risk Management

The Company's net income is largely dependent on its net interest income. Net interest income is susceptible to interest rate risk to the extent that interest-bearing liabilities mature or re-price on a different basis than interest-earning assets. When interest-bearing liabilities mature or re-price more quickly than interest-earning assets in a given period, a significant increase in market rates of interest could adversely affect net interest income. Similarly, when interest-earning assets mature or re-price more quickly than interest-bearing liabilities, falling interest rates could result in a decrease in net interest income. Net interest income is also affected by changes in the portion of interest-earning assets that are funded by interest-bearing liabilities rather than by other sources of funds, such as noninterest-bearing deposits and stockholders' equity.

The Company's interest rate risk management goals are (1) to increase net interest income at a growth rate consistent with the growth rate of total assets, and (2) to minimize fluctuations in net interest margin as a percentage of interest-earning assets. Management attempts to achieve these goals by balancing, within policy limits, the volume of floating-rate liabilities with a similar volume of floating-rate assets; by keeping the average maturity of fixed-rate asset and liability contracts reasonably matched; by maintaining a pool of administered core deposits; and by adjusting pricing rates to market conditions on a continuing basis.

The Company's board of directors has established a comprehensive interest rate risk management policy, which is administered by management's Asset Liability Management Committee ("ALCO"). The policy establishes limits on risk, which are quantitative measures of the percentage change in net interest income (a measure of net interest income at risk) and the fair value of equity capital (a measure of economic value of equity or "EVE" at risk) resulting from a hypothetical change in U.S. Treasury interest rates for maturities from one day to thirty years. The Company measures the potential adverse impacts that changing interest rates may have on its short-term earnings, long-term value, and liquidity by employing simulation analysis through the use of computer modeling. The simulation model captures optionality factors such as call features and interest rate caps and floors embedded in investment and loan portfolio contracts. As with any method of gauging interest rate risk, there are certain shortcomings inherent in the interest rate modeling methodology used by the Company. When interest rates change, actual movements in different categories of interest-earning assets and interest-bearing liabilities, loan prepayments, and withdrawals of time and other deposits, may deviate significantly from assumptions used in the model. As an example, certain money market deposit accounts are assumed to reprice at 100% of the interest rate change in each of the up rate shock scenarios even though this is not a contractual requirement. As a practical matter, management would likely lag the impact of any upward movement in market rates on these accounts as a mechanism to manage the bank's net interest margin. Finally, the methodology does not measure or reflect the impact that higher rates may have on adjustable-rate loan customers' ability to service their debts, or the impact of rate changes on demand for loan, lease, and deposit products.

The Company prepares a current base case and eight alternative simulations at least once a quarter and reports the analysis to the board of directors. In addition, more frequent forecasts are produced when interest rates are particularly uncertain or when other business conditions so dictate.

The statement of condition is subject to quarterly testing for eight alternative interest rate shock possibilities to indicate the inherent interest rate risk. Average interest rates are shocked by +/- 100, 200, 300, and 400 basis points ("bp"), although the Company may elect not to use particular scenarios that it determines are impractical in a current rate environment. It is management's goal to structure the balance sheet so that net interest earnings at risk over a twelve-month period and the economic value of equity at risk do not exceed policy guidelines at the various interest rate shock levels.

The Company augments its quarterly interest rate shock analysis with alternative external interest rate scenarios on a monthly basis. These alternative interest rate scenarios may include non-parallel rate ramps and non-parallel yield curve twists. If a measure of risk produced by the alternative simulations of the entire balance sheet violates policy guidelines, ALCO is required to develop a plan to restore the measure of risk to a level that complies with policy limits within two quarters.

Measures of net interest income at risk produced by simulation analysis are indicators of an institution's short-term performance in alternative rate environments. These measures are typically based upon a relatively brief period, usually one year. They do not necessarily indicate the long-term prospects or economic value of the institution.

Estimated Changes in Net Interest Income

Change in Interest Rates:	+ 400 bp	+ 300 bp	+ 200 bp	+ 100 bp	- 100 bp	- 200 bp	-300 bp	400 bp
Policy Limit	23.50%	17.50%	15.00%	10.00%	10.00%	15.00%	17.50%	23.50%
June 30, 2017	**(4.71%)**	**(3.12%)**	**(1.54%)**	**(0.49%)**	**(2.78%)**	**N/A**	**N/A**	**N/A**
December 31, 2016	(8.55%)	(5.76%)	(2.84%)	(1.20%)	N/A	N/A	N/A	N/A

As shown above, measures of net interest income at risk improved from December 31, 2016 at all shock levels. All measures remained well within prescribed policy limits.

The decrease in the risk position with respect to net interest income from December 31, 2016 to June 30, 2017 at all shock levels was the result of further restructuring of FHLB advances in 2017 and the elimination of subordinated debt in January. The elimination of the optionality associated with the related interest rates will reduce the Company's exposure to potential future increases in interest rates.

The measures of equity value at risk indicate the ongoing economic value of the Company by considering the effects of changes in interest rates on all of the Company's cash flows, and by discounting the cash flows to estimate the present value of assets and liabilities. The difference between these discounted values of the assets and liabilities is the economic value of equity, which, in theory, approximates the fair value of the Company's net assets.

Estimated Changes in Economic Value of Equity (EVE)

Change in Interest Rates:	+ 400 bp	+ 300 bp	+ 200 bp	+ 100 bp	- 100 bp	- 200 bp	-300 bp	-400 bp
Policy Limit	35.00%	25.00%	20.00%	10.00%	10.00%	20.00%	25.00%	35.00%
June 30, 2017	**(15.26%)**	**(10.61%)**	**(6.06%)**	**(2.73%)**	**(2.94%)**	**N/A**	**N/A**	**N/A**
December 31, 2016	(14.83%)	(10.72%)	(6.42%)	(2.86%)	N/A	N/A	N/A	N/A

Measures of the economic value of equity ("EVE") at risk decreased from December 31, 2016 to June 30, 2017 in most shock scenarios. EVE's exposure position is the result of increases in zero cost funding levels and the reduced exposure of the Company's borrowing to rising rate scenarios.

Liquidity Management

Liquidity is measured by a financial institution's ability to raise funds through loan and lease repayments, maturing investments, deposit growth, borrowed funds, capital and the sale of highly marketable assets such as investment securities and residential mortgage loans. The Company's liquidity position, considering both internal and external sources available, exceeded anticipated short-term and long-term needs at June 30, 2017. Management considers core deposits, defined to include all deposits other than time deposits of $100 thousand or more, to be a relatively stable funding source. Core deposits equaled 70% of total interest-earning assets at June 30, 2017. In addition, loan and lease payments, maturities, calls and pay downs of securities, deposit growth and earnings contribute a flow of funds available to meet liquidity requirements. In assessing liquidity, management considers operating requirements, the seasonality of deposit flows, investment, loan and deposit maturities and calls, expected funding of loans and deposit withdrawals, and the market values of available-for-sale investments, so that sufficient funds are available on short notice to meet obligations as they arise and to ensure that the Company is able to pursue new business opportunities.

Liquidity is measured using an approach designed to take into account, in addition to factors already discussed above, the Company's growth and mortgage banking activities. Also considered are changes in the liquidity of the investment portfolio due to fluctuations in interest rates. Under this approach, implemented by the Funds Management Subcommittee of ALCO under formal policy guidelines, the Company's liquidity position is measured weekly, looking forward at thirty day intervals from thirty (30) to three hundred sixty (360) days. The measurement is based upon the projection of funds sold or purchased position, along with ratios and trends developed to measure dependence on purchased funds and core growth. Resulting projections as of June 30, 2017, show short-term investments exceeding short-term borrowings by $21 million over the subsequent 360 days. This projected excess of liquidity versus requirements provides the Company with flexibility in how it funds loans and other earning assets.

The Company also has external sources of funds, which can be drawn upon when required. The main sources of external liquidity are available lines of credit with the Federal Home Loan Bank of Atlanta and the Federal Reserve. The line of credit with the Federal Home Loan Bank of Atlanta totaled $1.6 billion, of which $1.5 billion was available for borrowing based on pledged collateral, with $670 million borrowed against it as of June 30, 2017. The line of credit at the Federal Reserve totaled $343 million, all of which was available for borrowing based on pledged collateral, with no borrowings against it as of June 30, 2017. Other external sources of liquidity available to the Company in the form of unsecured lines of credit granted by correspondent banks totaled $70 million at June 30, 2017, against which there were no outstanding borrowings. In addition, the Company had a secured line of credit with a correspondent bank of $20 million as of June 30, 2017. Based upon its liquidity analysis, including external sources of liquidity available, management believes the liquidity position was appropriate at June 30, 2017.

The parent company ("Bancorp") is a separate legal entity from the Bank and must provide for its own liquidity. In addition to its operating expenses, Bancorp is responsible for paying any dividends declared to its common shareholders and interest and principal on outstanding debt. Bancorp's primary source of income is dividends received from the Bank. The amount of dividends that the Bank may declare and pay to Bancorp in any calendar year, without the receipt of prior approval from the Federal Reserve, cannot exceed net income for that year to date plus retained net income (as defined) for the preceding two calendar years. Based on this requirement, as of June 30, 2017, the Bank could have declared a dividend of $24 million to Bancorp. At June 30, 2017, Bancorp had liquid assets of $13 million.

Arrangements to fund credit products or guarantee financing take the form of loan commitments (including lines of credit on revolving credit structures) and letters of credit. Approvals for these arrangements are obtained in the same manner as loans. Generally, cash flows, collateral value and risk assessment are considered when determining the amount and structure of credit arrangements.

Commitments to extend credit in the form of consumer, commercial real estate and business at the dates indicated were as follows:

(In thousands)	**June 30, 2017**	December 31, 2016
Commercial	**$ 396,241**	$ 334,552
Real estate-development and construction	**118,625**	97,524
Real estate-residential mortgage	**20,126**	22,970
Lines of credit, principally home equity and business lines	**1,007,806**	949,939
Standby letters of credit	**71,195**	68,748
Total commitments to extend credit and available credit lines	**$ 1,613,993**	$ 1,473,733

Commitments to extend credit are agreements to provide financing to a customer with the provision that there are no violations of any condition established in the agreement. Commitments generally have interest rates determined by current market rates, expirations dates or other termination clauses and may require payment of a fee. Lines of credit typically represent unused portions of lines of credit that were provided and remain available as long as there is no violation of any contractual condition. Commitments to extend credit are evaluated on a case by case basis periodically. Many of the commitments are expected to expire without being drawn upon. It would be highly unlikely that all customers would draw on their lines of credit in full at any time and, therefore, the total commitment amount or line of credit amounts do not necessarily represent future cash requirements.

Item 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

See "Financial Condition - Market Risk and Interest Rate Sensitivity" in Management's Discussion and Analysis of Financial Condition and Results of Operations, above, which is incorporated herein by reference.

Item 4. CONTROLS AND PROCEDURES

The Company's management, under the supervision and with the participation of the Company's Chief Executive Officer and Chief Financial Officer, evaluated as of the last day of the period covered by this report, the effectiveness of the design and operation of the Company's disclosure controls and procedures, as defined in Rule 13a-15 under the Securities Exchange Act of 1934. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures were effective. There were no changes in the Company's internal controls over financial reporting (as defined in Rule 13a-15 under the Securities Act of 1934) during the three months ended June 30, 2017 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II - OTHER INFORMATION

Item 1. Legal Proceedings

In the normal course of business, the Company becomes involved in litigation arising from the banking, financial and other activities it conducts. Management, after consultation with legal counsel, does not anticipate that the ultimate liability, if any, arising from these matters will have a material effect on the Company's financial condition, operating results or liquidity.

Item 1A. Risk Factors

There have been no material changes in the risk factors as discussed in the 2016 Annual Report on Form 10-K.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

The Company re-approved a stock repurchase program in August 2015 that permits the repurchase of up to 5% of the Company's outstanding shares of common stock or approximately 1,200,000 shares. Repurchases which will be conducted through open market purchases or privately negotiated transactions, will be made depending on market conditions and other factors. The following table provides information regarding repurchase transactions executed during the quarter ended June 30, 2017.

Period	Total number of shares purchased	Average price paid per share	Total number of shares purchased as part of publicly announced plans or programs	Maximum number that may yet be purchased under the plans or programs
April 1, 2017 through April 30, 2017	-	N/A	-	463,861
May 1, 2017 through May 31, 2017	-	N/A	-	463,861
June 1, 2017 through June 30, 2017	-	N/A	-	463,861

Item 3. Defaults Upon Senior Securities – None

Item 4. Mine Safety Disclosures – Not applicable

Item 5. Other Information - None

Item 6. Exhibits

Exhibit 31(a) Certification of Chief Executive Officer

Exhibit 31(b) Certification of Chief Financial Officer

Exhibit 32(a) Certification of Chief Executive Officer pursuant to 18 U.S. Section 1350

Exhibit 32(b) Certification of Chief Financial Officer pursuant to 18 U.S. Section 1350

Exhibit 101 The following materials from the Sandy Spring Bancorp, Inc. Quarterly Report on Form 10-Q for the quarter end June 30, 2017 formatted in Extensible Business Reporting Language (XBRL): (i) the Condensed Consolidated Statements of Condition; (ii) The Condensed Consolidated Statements of Income; (iii) The Condensed Consolidated Statements of Comprehensive Income; (iv) The Condensed Consolidated Statements of Cash Flows; (v) The Condensed Consolidated Statements of Changes in Stockholders' Equity; (vi) related notes.

Signatures

Pursuant to the requirements of Section 13 of the Securities Exchange Act of 1934, the Registrant has duly caused this quarterly report to be signed on its behalf by the undersigned, thereunto duly authorized.

SANDY SPRING BANCORP, INC.

(Registrant)

By: /s/ Daniel J. Schrider________

Daniel J. Schrider

President and Chief Executive Officer

Date: August 4, 2017

By: /s/ Philip J. Mantua_________

Philip J. Mantua

Executive Vice President and Chief Financial Officer

Date: August 4, 2017