

FARMERS & MERCHANTS BANCORP
Form 10-Q
November 08, 2013

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

FORM 10-Q

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

For the quarterly period ended September 30, 2013

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: 000-26099

FARMERS & MERCHANTS BANCORP
(Exact name of registrant as specified in its charter)

Delaware 94-3327828
(State or other jurisdiction of incorporation or organization) (I.R.S. Employer Identification No.)

111 W. Pine Street, Lodi, California 95240
(Address of principal Executive offices) (Zip Code)

Registrant's telephone number, including area code (209) 367-2300

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

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

Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See definition of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act (Check one):

Large accelerated filer Accelerated filer Non-accelerated filer Smaller Reporting Company
(Do not check if a smaller reporting company)

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

Number of shares of common stock of the registrant: Par value \$0.01, authorized 7,500,000 shares; issued and outstanding 777,882 as of October 31, 2013.

FARMERS & MERCHANTS BANCORP

FORM 10-Q

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31(a) Certification of the Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

31(b) Certification of the Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

32 Certifications of the Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

FARMERS & MERCHANTS BANCORP

Consolidated Balance Sheets

(in thousands)	Sept. 30, 2013 (Unaudited)	December 31, 2012	Sept. 30, 2012 (Unaudited)
Assets			
Cash and Cash Equivalents:			
Cash and Due From Banks	\$46,234	\$47,366	\$29,863
Interest Bearing Deposits with Banks	1,391	82,060	3,601
Total Cash and Cash Equivalents	47,625	129,426	33,464
Investment Securities:			
Available-for-Sale	421,765	417,991	463,177
Held-to-Maturity	70,961	68,392	68,960
Total Investment Securities	492,726	486,383	532,137
Loans & Leases			
Loans & Leases	1,297,811	1,246,902	1,210,027
Less: Allowance for Credit Losses	34,111	34,217	33,604
Loans & Leases, Net	1,263,700	1,212,685	1,176,423
Premises and Equipment, Net			
Premises and Equipment, Net	21,814	22,901	22,945
Bank Owned Life Insurance	51,652	50,253	48,799
Interest Receivable and Other Assets	87,259	73,038	70,633
Total Assets	\$ 1,964,776	\$ 1,974,686	\$ 1,884,401
Liabilities			
Deposits:			
Demand	\$435,778	\$462,251	\$369,635
Interest Bearing Transaction	257,650	259,141	238,223
Savings and Money Market	561,277	541,526	540,690
Time	439,081	459,108	482,957
Total Deposits	1,693,786	1,722,026	1,631,505
Federal Home Loan Bank Advances			
Federal Home Loan Bank Advances	5,900	-	482
Subordinated Debentures			
Subordinated Debentures	10,310	10,310	10,310
Interest Payable and Other Liabilities			
Interest Payable and Other Liabilities	43,739	37,317	35,773
Total Liabilities	1,753,735	1,769,653	1,678,070
Shareholders' Equity			
Preferred Stock: No Par Value. 1,000,000 Shares Authorized, None Issued or Outstanding			
Preferred Stock: No Par Value. 1,000,000 Shares Authorized, None Issued or Outstanding	-	-	-
Common Stock: Par Value \$0.01, 7,500,000 Shares Authorized, 777,882 Shares Issued and Outstanding at Sept. 30, 2013, December 31, 2012 and Sept. 30, 2012, respectively			
Common Stock: Par Value \$0.01, 7,500,000 Shares Authorized, 777,882 Shares Issued and Outstanding at Sept. 30, 2013, December 31, 2012 and Sept. 30, 2012, respectively	8	8	8

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Additional Paid-In Capital	75,014	75,014	75,014
Retained Earnings	136,357	123,012	122,170
Accumulated Other Comprehensive (Loss) Income, Net	(338)	6,999	9,139
Total Shareholders' Equity	211,041	205,033	206,331
Total Liabilities & Shareholders' Equity	\$ 1,964,776	\$ 1,974,686	\$ 1,884,401

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

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FARMERS & MERCHANTS BANCORP

Consolidated Statements of Income (Unaudited)

(in thousands except per share data)	Three Months		Nine Months	
	Ended September 30, 2013	2012	Ended September 30, 2013	2012
Interest Income				
Interest and Fees on Loans & Leases	\$16,679	\$16,505	\$48,030	\$49,283
Interest on Deposits with Banks	2	8	49	76
Interest on Investment Securities:				
Taxable	2,297	2,315	6,785	7,958
Exempt from Federal Tax	637	671	1,951	1,961
Total Interest Income	19,615	19,499	56,815	59,278
Interest Expense				
Deposits	632	935	1,943	2,967
Borrowed Funds	7	11	16	1,047
Subordinated Debentures	82	87	245	262
Total Interest Expense	721	1,033	2,204	4,276
Net Interest Income	18,894	18,466	54,611	55,002
Provision for Credit Losses	-	600	250	1,100
Net Interest Income After Provision for Credit Losses	18,894	17,866	54,361	53,902
Non-Interest Income				
Service Charges on Deposit Accounts	1,139	1,248	3,312	3,662
Net (Loss) Gain on Sale of Investment Securities	(1,137)	149	(248)	149
Increase in Cash Surrender Value of Life Insurance	473	500	1,399	1,412
Debit Card and ATM Fees	774	732	2,295	2,197
Net Gain on Deferred Compensation Investments	875	762	2,279	1,381
Other	1,324	662	2,872	1,986
Total Non-Interest Income	3,448	4,053	11,909	10,787
Non-Interest Expense				
Salaries and Employee Benefits	8,244	7,850	25,184	23,792
Net Gain on Deferred Compensation Investments	875	762	2,279	1,381
Occupancy	649	656	1,899	1,925
Equipment	705	686	2,078	2,282
Legal Fees	(69)	204	391	629
FDIC Insurance	246	243	732	728
Other	1,535	1,359	4,683	5,816
Total Non-Interest Expense	12,185	11,760	37,246	36,553
Income Before Income Taxes	10,157	10,159	29,024	28,136
Provision for Income Taxes	3,805	3,827	10,856	10,452
Net Income	\$6,352	\$6,332	\$18,168	\$17,684
Basic Earnings Per Common Share	\$8.17	\$8.13	\$23.36	\$22.70

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

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FARMERS & MERCHANTS BANCORP

Consolidated Statements of Comprehensive Income (Unaudited)

(in thousands)	Three Months Ended September 30,		Nine Months Ended September 30,	
	2013	2012	2013	2012
Net Income	\$6,352	\$6,332	\$18,168	\$17,684
Other Comprehensive Income (Loss)				
Increase (Decrease) in Net Unrealized Gains (Losses) on Available-for-Sale Securities	1,681	2,944	(12,907)	7,865
Reclassification Adjustment for Realized Losses (Gains) on Available-for-Sale Securities Included in Net Income	1,137	(149)	248	(149)
Deferred Tax (Expense) Benefit	(1,185)	(1,175)	5,322	(3,244)
Change in Net Unrealized Gains (Losses) on Available-for-Sale Securities, Net of Tax	1,633	1,620	(7,337)	4,472
Total Other Comprehensive Income (Loss)	1,633	1,620	(7,337)	4,472
Comprehensive Income	\$7,985	\$7,952	\$10,831	\$22,156

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

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FARMERS & MERCHANTS BANCORP

Consolidated Statements of Changes in Shareholders' Equity (Unaudited)

(in thousands except share data)

	Common Shares	Common Stock	Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss), Net	Total Shareholders' Equity
Balance, January 1, 2012	779,424	\$ 8	\$ 75,590	\$ 109,081	\$ 4,667	\$ 189,346
Net Income		-	-	17,684	-	17,684
Cash Dividends Declared on Common Stock (\$5.90 per share)		-	-	(4,595)	-	(4,595)
Repurchase of Stock	(1,542)	-	(576)	-	-	(576)
Change in Net Unrealized Gain on Securities Available for Sale, Net of Tax		-	-	-	4,472	4,472
Balance, September 30, 2012	777,882	\$ 8	\$ 75,014	\$ 122,170	\$ 9,139	\$ 206,331
Balance, January 1, 2013	777,882	\$ 8	\$ 75,014	\$ 123,012	\$ 6,999	\$ 205,033
Net Income		-	-	18,168	-	18,168
Cash Dividends Declared on Common Stock (\$6.20 per share)		-	-	(4,823)	-	(4,823)
Change in Net Unrealized Loss on Securities Available for Sale, Net of Tax		-	-	-	(7,337)	(7,337)
Balance, September 30, 2013	777,882	\$ 8	\$ 75,014	\$ 136,357	\$ (338)	\$ 211,041

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

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FARMERS & MERCHANTS BANCORP

Consolidated Statements of Cash Flows (Unaudited)

(in thousands)

Nine Months Ended
 Sept 30, 2013 Sept 30, 2012

Operating Activities:

Net Income	\$ 18,168	\$ 17,684
Adjustments to Reconcile Net Income to Net Cash Provided by Operating Activities:		
Provision for Credit Losses	250	1,100
Depreciation and Amortization	1,152	1,293
Net Amortization of Investment Security Discounts & Premium	2,543	2,852
Net Loss (Gain) on Sale of Investment Securities	248	(149)
Net Gain on Sale of Property & Equipment	(705)	-
Net Change in Operating Assets & Liabilities:		
Net Increase in Interest Receivable and Other Assets	(10,253)	(1,418)
Net Increase in Interest Payable and Other Liabilities	6,422	2,472
Net Cash Provided by Operating Activities	17,825	23,834
Investing Activities:		
Purchase of Investment Securities Available-for-Sale	(221,100)	(122,966)
Proceeds from Sold, Matured, or Called Securities Available-for-Sale	195,339	144,383
Purchase of Investment Securities Held-to-Maturity	(355)	(10,569)
Proceeds from Matured or Called Securities Held-to-Maturity	4,278	4,675
Net Loans & Leases Paid, Originated or Acquired	(51,649)	(47,728)
Principal Collected on Loans & Leases Previously Charged Off	384	266
Additions to Premises and Equipment	(187)	(180)
Proceeds from Disposition of Property & Equipment	827	-
Net Cash Used by Investing Activities	(72,463)	(32,119)
Financing Activities:		
Net (Decrease) Increase in Deposits	(28,240)	5,308
Net Decrease in Securities Sold Under Agreement to Repurchase	-	(60,000)
Net Change in Other Borrowings	5,900	(48)
Common Stock Repurchases	-	(576)
Cash Dividends	(4,823)	(4,595)
Net Cash Used By Financing Activities	(27,163)	(59,911)
Decrease in Cash and Cash Equivalents	(81,801)	(68,196)
Cash and Cash Equivalents at Beginning of Period	129,426	101,660
Cash and Cash Equivalents at End of Period	\$ 47,625	\$ 33,464
Supplementary Data		
Loans Transferred to Foreclosed Assets (ORE)	\$ 3,458	\$ 58
Cash Payments Made for Income Taxes	\$ 13,886	\$ 11,568
Interest Paid	\$ 2,346	\$ 4,661

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

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FARMERS & MERCHANTS BANCORP

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

1. Significant Accounting Policies

Farmers & Merchants Bancorp (the “Company”) was organized March 10, 1999. Primary operations are related to traditional banking activities through its subsidiary Farmers & Merchants Bank of Central California (the “Bank”) which was established in 1916. The Bank’s wholly owned subsidiaries include Farmers & Merchants Investment Corporation and Farmers/Merchants Corp. Farmers & Merchants Investment Corporation has been dormant since 1991. Farmers/Merchants Corp. acts as trustee on deeds of trust originated by the Bank.

The Company’s other subsidiaries include F & M Bancorp, Inc. and FMCB Statutory Trust I. F & M Bancorp, Inc. was created in March 2002 to protect the name F & M Bank. During 2002 the Company completed a fictitious name filing in California to begin using the streamlined name “F & M Bank” as part of a larger effort to enhance the Company’s image and build brand name recognition. In December 2003, the Company formed a wholly owned subsidiary, FMCB Statutory Trust I. FMCB Statutory Trust I is a non-consolidated subsidiary per Generally Accepted Accounting Principles in the United States of America (“U.S. GAAP”) and was formed for the sole purpose of issuing Trust Preferred Securities.

The accounting and reporting policies of the Company conform to U.S. GAAP and prevailing practice within the banking industry. The following is a summary of the significant accounting and reporting policies used in preparing the consolidated financial statements.

Basis of Presentation

The accompanying consolidated financial statements and notes thereto have been prepared in accordance with accounting principles generally accepted in the United States of America for financial information.

These statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission (“SEC”) for interim reporting on Form 10-Q. Accordingly, certain disclosures normally presented in the notes to the annual consolidated financial statements prepared in accordance with U.S. GAAP have been omitted. The Company believes that the disclosures are adequate to make the information not misleading. These interim financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2012. The results of operations for the three-month and nine-month periods ended September 30, 2013 may not necessarily be indicative of future operating results.

The accompanying consolidated financial statements include the accounts of the Company and the Company’s wholly owned subsidiaries, F & M Bancorp, Inc. and the Bank, along with the Bank’s wholly owned subsidiaries, Farmers & Merchants Investment Corporation and Farmers/Merchants Corp. Significant inter-company transactions have been eliminated in consolidation.

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions. These estimates and assumptions affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates.

Certain amounts in the prior years' financial statements and related footnote disclosures have been reclassified to conform to the current-year presentation. These reclassifications had no effect on previously reported net income or total shareholders' equity. In the opinion of management, the accompanying consolidated financial statements reflect all adjustments (consisting only of normal recurring adjustments), which are necessary for a fair presentation of

financial results for the periods presented.

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Cash and Cash Equivalents

For purposes of the Consolidated Statements of Cash Flows, the Company has defined cash and cash equivalents as those amounts included in the balance sheet captions Cash and Due from Banks, Interest Bearing Deposits with Banks, Federal Funds Sold and Securities Purchased Under Agreements to Resell. Generally, these transactions are for one-day periods. For these instruments, the carrying amount is a reasonable estimate of fair value.

Investment Securities

Investment securities are classified at the time of purchase as held-to-maturity if it is management's intent and the Company has the ability to hold the securities until maturity. These securities are carried at cost, adjusted for amortization of premium and accretion of discount using a level yield of interest over the estimated remaining period until maturity. Losses, reflecting a decline in value judged by the Company to be other than temporary, are recognized in the period in which they occur.

Securities are classified as available-for-sale if it is management's intent, at the time of purchase, to hold the securities for an indefinite period of time and/or to use the securities as part of the Company's asset/liability management strategy. These securities are reported at fair value with aggregate unrealized gains or losses excluded from income and included as a separate component of shareholders' equity, net of related income taxes. Fair values are based on quoted market prices or broker/dealer price quotations on a specific identification basis. Gains or losses on the sale of these securities are computed using the specific identification method.

Trading securities, if any, are acquired for short-term appreciation and are recorded in a trading portfolio and are carried at fair value, with unrealized gains and losses recorded in non-interest income.

Management evaluates securities for other-than-temporary impairment ("OTTI") on at least a quarterly basis, and more frequently when economic or market conditions warrant such an evaluation. For securities in an unrealized loss position, management considers the extent and duration of the unrealized loss, and the financial condition and near-term prospects of the issuer. Management also assesses whether it intends to sell, or it is more likely than not that it will be required to sell, a security in an unrealized loss position before recovery of its amortized cost basis. If either of the criteria regarding intent or requirement to sell is met, the entire difference between amortized cost and fair value is recognized as impairment through earnings. For debt securities that do not meet the aforementioned criteria, the amount of impairment is split into two components as follows: (1) OTTI related to credit loss, which must be recognized in the income statement; and (2) OTTI related to other factors, which is recognized in other comprehensive income. The credit loss is defined as the difference between the present value of the cash flows expected to be collected and the amortized cost basis. For equity securities, the entire amount of impairment is recognized through earnings.

In order to determine OTTI for purchased beneficial interests that, on the purchase date, were not highly rated, the Company compares the present value of the remaining cash flows as estimated at the preceding evaluation date to the current expected remaining cash flows. OTTI is deemed to have occurred if there has been an adverse change in the remaining expected future cash flows.

Loans & Leases

Loans & leases are reported at the principal amount outstanding net of unearned discounts and deferred loan & lease fees and costs. Interest income on loans & leases is accrued daily on the outstanding balances using the simple interest method. Loan & lease origination fees are deferred and recognized over the contractual life of the loan or lease as an adjustment to the yield. Loans & leases are placed on non-accrual status when the collection of principal or interest is in doubt or when they become past due for 90 days or more unless they are both well-secured and in the process of collection. For this purpose a loan or lease is considered well-secured if it is collateralized by property having a net realizable value in excess of the amount of the loan or lease or is guaranteed by a financially capable party. When a loan or lease is placed on non-accrual status, the accrued and unpaid interest receivable is reversed and charged

against current income; thereafter, interest income is recognized only as it is collected in cash. Additionally, cash would be applied to principal if all principal was not expected to be collected. Loans & leases placed on non-accrual status are returned to accrual status when the loans or leases are paid current as to principal and interest and future payments are expected to be made in accordance with the contractual terms of the loan or lease.

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A loan or lease is considered impaired when, based on current information and events, it is probable that the Company will be unable to collect all amounts due, including principal and interest, according to the contractual terms of the original agreement. Impaired loans & leases are either: (1) non-accrual loans & leases; or (2) restructured loans & leases that are still accruing interest. Loans or leases determined to be impaired are individually evaluated for impairment. When a loan or lease is impaired, the Company measures impairment based on the present value of expected future cash flows discounted at the loan or lease's effective interest rate, except that as a practical expedient, it may measure impairment based on a loan or lease's observable market price, or the fair value of the collateral if the loan or lease is collateral dependent. A loan or lease is collateral dependent if the repayment of the loan or lease is expected to be provided solely by the underlying collateral.

A restructuring of a loan or lease constitutes a troubled debt restructuring (TDR) if the Company for economic or legal reasons related to the debtor's financial difficulties grants a concession to the debtor that it would not otherwise consider. Restructured loans & leases typically present an elevated level of credit risk as the borrowers are not able to perform according to the original contractual terms. Loans & leases that are reported as TDRs are considered impaired and measured for impairment as described above.

Generally, the Company will not restructure loans or leases for customers unless: (i) the existing loan or lease is brought current as to principal and interest payments; and (ii) the restructured loan or lease can be underwritten to reasonable underwriting standards. If these standards are not met other actions will be pursued (e.g., foreclosure) to collect outstanding loan or lease amounts. After restructure a determination is made whether the loan or lease will be kept on accrual status based upon the underwriting and historical performance of the restructured credit.

Allowance for Credit Losses

The allowance for credit losses is an estimate of probable incurred credit losses inherent in the Company's loan & lease portfolio as of the balance-sheet date. The allowance is established through a provision for credit losses which is charged to expense. Additions to the allowance are expected to maintain the adequacy of the total allowance after credit losses and loan & lease growth. Credit exposures determined to be uncollectible are charged against the allowance. Cash received on previously charged off amounts is recorded as a recovery to the allowance. The overall allowance consists of two primary components, specific reserves related to impaired loans & leases and general reserves for inherent losses related to loans & leases that are not impaired.

The determination of the general reserve for loans & leases that are collectively evaluated for impairment is based on estimates made by management, to include, but not limited to, consideration of historical losses by portfolio segment, internal asset classifications, qualitative factors to include economic trends in the Company's service areas, industry experience and trends, geographic concentrations, estimated collateral values, the Company's underwriting policies, the character of the loan & lease portfolio, and probable losses inherent in the portfolio taken as a whole.

The Company maintains a separate allowance for each portfolio segment (loan & lease type). These portfolio segments include: (1) commercial real estate; (2) agricultural real estate; (3) real estate construction (including land and development loans); (4) residential 1st mortgages; (5) home equity lines and loans; (6) agricultural; (7) commercial; (8) consumer and other; and (9) leases. The allowance for credit losses attributable to each portfolio segment, which includes both individually evaluated impaired loans & leases and loans & leases that are collectively evaluated for impairment, is combined to determine the Company's overall allowance, which is included on the consolidated balance sheet.

The Company assigns a risk rating to all loans & leases and periodically performs detailed reviews of all such loans & leases over a certain threshold to identify credit risks and to assess the overall collectability of the portfolio. A credit grade is established at inception for smaller balance loans, such as consumer and residential real estate, and then updated only when the loan becomes contractually delinquent or when the borrower requests a modification. During these internal reviews, management monitors and analyzes the financial condition of borrowers and guarantors, trends

in the industries in which borrowers operate and the fair values of collateral securing these loans & leases. These credit quality indicators are used to assign a risk rating to each individual loan or lease. These risk ratings are also subject to examination by independent specialists engaged by the Company. The risk ratings can be grouped into five major categories, defined as follows:

Pass – A pass loan or lease is a strong credit with no existing or known potential weaknesses deserving of management's close attention.

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Special Mention – A special mention loan or lease has potential weaknesses that deserve management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan or lease or in the Company's credit position at some future date. Special Mention loans & leases are not adversely classified and do not expose the Company to sufficient risk to warrant adverse classification.

Substandard – A substandard loan or lease is not adequately protected by the current financial condition and paying capacity of the borrower or the value of the collateral pledged, if any. Loans or leases classified as substandard have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. Well defined weaknesses include a project's lack of marketability, inadequate cash flow or collateral support, failure to complete construction on time or the project's failure to fulfill economic expectations. They are characterized by the distinct possibility that the Company will sustain some loss if the deficiencies are not corrected.

Doubtful – Loans or leases classified doubtful have all the weaknesses inherent in those classified as substandard with the added characteristic that the weaknesses make collection or liquidation in full, based on currently known facts, conditions and values, highly questionable or improbable.

Loss – Loans or leases classified as loss are considered uncollectible. Once a loan or lease becomes delinquent and repayment becomes questionable, the Company will address collateral shortfalls with the borrower and attempt to obtain additional collateral. If this is not forthcoming and payment in full is unlikely, the Company will estimate its probable loss and immediately charge-off some or all of the balance.

The general reserve component of the allowance for credit losses also consists of reserve factors that are based on management's assessment of the following for each portfolio segment: (1) inherent credit risk; (2) historical losses; and (3) other qualitative factors. These reserve factors are inherently subjective and are driven by the repayment risk associated with each portfolio segment described below:

Real Estate Construction – Real Estate Construction loans, including land loans, generally possess a higher inherent risk of loss than other real estate portfolio segments. A major risk arises from the necessity to complete projects within specified cost and time lines. Trends in the construction industry significantly impact the credit quality of these loans, as demand drives construction activity. In addition, trends in real estate values significantly impact the credit quality of these loans, as property values determine the economic viability of construction projects.

Commercial Real Estate – Commercial real estate mortgage loans generally possess a higher inherent risk of loss than other real estate portfolio segments, except land and construction loans. Adverse economic developments or an overbuilt market impact commercial real estate projects and may result in troubled loans. Trends in vacancy rates of commercial properties impact the credit quality of these loans. High vacancy rates reduce operating revenues and the ability for properties to produce sufficient cash flow to service debt obligations.

Commercial – Commercial loans generally possess a lower inherent risk of loss than real estate portfolio segments because these loans are generally underwritten to existing cash flows of operating businesses. Debt coverage is provided by business cash flows and economic trends influenced by unemployment rates and other key economic indicators are closely correlated to the credit quality of these loans.

Agricultural Real Estate and Agricultural – Loans secured by crop production, livestock and related real estate are vulnerable to two risk factors that are largely outside the control of Company and borrowers: commodity prices and weather conditions.

Residential 1st Mortgages and Home Equity Lines and Loans – The degree of risk in residential real estate lending depends primarily on the loan amount in relation to collateral value, the interest rate and the borrower's ability to repay in an orderly fashion. These loans generally possess a lower inherent risk of loss than other real estate portfolio

segments, although this is not always true as evidenced by the weakness in residential real estate values over the past five years. Economic trends determined by unemployment rates and other key economic indicators are closely correlated to the credit quality of these loans. Weak economic trends indicate that the borrowers' capacity to repay their obligations may be deteriorating.

Consumer & Other – A consumer installment loan portfolio is usually comprised of a large number of small loans scheduled to be amortized over a specific period. Most installment loans are made for consumer purchases. Economic trends determined by unemployment rates and other key economic indicators are closely correlated to the credit quality of these loans. Weak economic trends indicate that the borrowers' capacity to repay their obligations may be deteriorating.

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Leases – Equipment leases subject the Company, as Lessor, to both the credit risk of the Lessee and the residual value risk of the equipment. Credit risks are underwritten using the same credit criteria the Company would make an equipment term loan under. Residual value risk is managed through the use of qualified, independent appraisers that establish the residual values the Company uses in structuring a lease.

At least quarterly, the Board of Directors reviews the adequacy of the allowance, including consideration of the relative risks in the portfolio, current economic conditions and other factors. If the Board of Directors and management determine that changes are warranted based on those reviews, the allowance is adjusted. In addition, the Company's and Bank's regulators, including the FRB, DFI and FDIC, as an integral part of their examination process, review the adequacy of the allowance. These regulatory agencies may require additions to the allowance based on their judgment about information available at the time of their examinations.

Allowance for Credit Losses on Off-Balance-Sheet Credit Exposures

The Company also maintains a separate allowance for off-balance-sheet commitments. Management estimates anticipated losses using historical data and utilization assumptions. The allowance for off-balance-sheet commitments is included in Interest Payable and Other Liabilities on the Company's Consolidated Balance Sheet.

Premises and Equipment

Premises, equipment, and leasehold improvements are stated at cost, less accumulated depreciation and amortization. Depreciation is computed principally by the straight line method over the estimated useful lives of the assets. Estimated useful lives of buildings range from 30 to 40 years, and for furniture and equipment from 3 to 7 years. Leasehold improvements are amortized over the lesser of the terms of the respective leases, or their useful lives, which are generally 5 to 10 years. Remodeling and capital improvements are capitalized while maintenance and repairs are charged directly to occupancy expense.

Other Real Estate

Other real estate, which is included in other assets, is expected to be sold and is comprised of properties acquired through foreclosure in satisfaction of indebtedness. Upon acquisition, these properties are recorded at fair value less estimated selling costs. Revised estimates to the fair value less cost to sell are reported as adjustments to the carrying amount of the asset, provided that such adjusted value is not in excess of the carrying amount at acquisition. Initial losses on properties acquired through full or partial satisfaction of debt are treated as credit losses and charged to the allowance for credit losses at the time of acquisition. Subsequent declines in value from the recorded amounts, routine holding costs, and gains or losses upon disposition, if any, are included in non-interest expense as incurred.

Income Taxes

The Company uses the liability method of accounting for income taxes. This method results in the recognition of deferred tax assets and liabilities that are reflected at currently enacted income tax rates applicable to the period in which the deferred tax assets or liabilities are expected to be realized or settled. As changes in tax laws or rates are enacted, deferred tax assets and liabilities are adjusted through the provision for income taxes. The deferred provision for income taxes is the result of the net change in the deferred tax asset and deferred tax liability balances during the year. This amount, combined with the current taxes payable or refundable, results in the income tax expense for the current year.

The Company follows the standards set forth in the "Income Taxes" topic of the FASB Accounting Standard Codification ("ASC"), which clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements. This standard prescribes a recognition threshold and measurement standard for the financial statement recognition and measurement of an income tax position taken or expected to be taken in a tax return. It also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition.

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When tax returns are filed, it is highly certain that some positions taken would be sustained upon examination by the taxing authorities, while others are subject to uncertainty about the merits of the position taken or the amount of the position that would be ultimately sustained. The benefit of a tax position is recognized in the financial statements in the period during which, based on all available evidence, management believes it is more likely than not that the position will be sustained upon examination, including the resolution of appeals or litigation processes, if any. Tax positions taken are not offset or aggregated with other positions. Tax positions that meet the more-likely-than-not recognition threshold are measured as the largest amount of tax benefit that is more than 50 percent likely of being realized upon settlement with the applicable taxing authority. The portion of the benefits associated with tax positions taken that exceeds the amount measured as described above is reflected as a liability for unrecognized tax benefits in the accompanying consolidated balance sheet along with any associated interest and penalties that would be payable to the taxing authorities upon examination.

Interest expense and penalties associated with unrecognized tax benefits, if any, are included in the provision for income taxes in the Consolidated Statements of Income.

Dividends and Basic Earnings Per Common Share

The Company's common stock is not traded on any exchange. The shares are primarily held by local residents and are not actively traded. Basic earnings per common share amounts are computed by dividing net income by the weighted average number of common shares outstanding for the period. There are no common stock equivalent shares. Therefore, there is no presentation of diluted basic earnings per common share. See Note 6.

Segment Reporting

The "Segment Reporting" topic of the FASB ASC requires that public companies report certain information about operating segments. It also requires that public companies report certain information about their products and services, the geographic areas in which they operate, and their major customers. The Company is a holding company for a community bank, which offers a wide array of products and services to its customers. Pursuant to its banking strategy, emphasis is placed on building relationships with its customers, as opposed to building specific lines of business. As a result, the Company is not organized around discernible lines of business and prefers to work as an integrated unit to customize solutions for its customers, with business line emphasis and product offerings changing over time as needs and demands change. Therefore, the Company only reports one segment.

Derivative Instruments and Hedging Activities

The "Derivatives and Hedging" topic of the FASB ASC establishes accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts, and for hedging activities. All derivatives, whether designated in hedging relationships or not, are required to be recorded on the balance sheet at fair value. Changes in the fair value of those derivatives are accounted for depending on the intended use of the derivative and the resulting designation under specified criteria. If the derivative is designated as a fair value hedge, the changes in the fair value of the derivative and of the hedged item attributable to the hedged risk are recognized in earnings. If the derivative is designated as a cash flow hedge, designed to minimize interest rate risk, the effective portions of the change in the fair value of the derivative are recorded in other comprehensive income (loss), net of related income taxes. Ineffective portions of changes in the fair value of cash flow hedges are recognized in earnings.

From time to time, the Company utilizes derivative financial instruments such as interest rate caps, floors, swaps, and collars. These instruments are purchased and/or sold to reduce the Company's exposure to changing interest rates. The Company marks to market the value of its derivative financial instruments and reflects gain or loss in earnings in the period of change or in other comprehensive income (loss). The Company was not utilizing any derivative instruments as of or for the period ended September 30, 2013, December 31, 2012 or September 30, 2012.

Comprehensive Income

The “Comprehensive Income” topic of the FASB ASC establishes standards for the reporting and display of comprehensive income and its components in the financial statements. Other comprehensive income (loss) refers to revenues, expenses, gains, and losses that generally accepted accounting principles recognize as changes in value to an enterprise but are excluded from net income. For the Company, comprehensive income includes net income and changes in fair value of its available-for-sale investment securities.

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Loss Contingencies

Loss contingencies, including claims and legal actions arising in the ordinary course of business, are recorded as liabilities when the likelihood of loss is probable and an amount or range of loss can be reasonably estimated. Management does not believe there now are such matters that will have a material effect on the financial statements.

2. Investment Securities

The amortized cost, fair values, and unrealized gains and losses of the securities available-for-sale are as follows (in thousands):

	Amortized Cost	Gross Unrealized Gains	Losses	Fair/Book Value
September 30, 2013				
Government Agency & Government-Sponsored Entities	\$ 28,404	\$239	\$-	\$ 28,643
Mortgage Backed Securities ⁽¹⁾	342,963	4,928	5,814	342,077
Corporate Securities	49,696	250	185	49,761
Other	1,284	-	-	1,284
Total	\$ 422,347	\$ 5,417	\$ 5,999	\$ 421,765

	Amortized Cost	Gross Unrealized Gains	Losses	Fair/Book Value
December 31, 2012				
Government Agency & Government-Sponsored Entities	\$ 26,546	\$277	\$-	\$ 26,823
Obligations of States and Political Subdivisions	5,665	-	-	5,665
Mortgage Backed Securities ⁽¹⁾	341,212	11,570	10	352,772
Corporate Securities	22,318	252	12	22,558
Other	10,173	-	-	10,173
Total	\$ 405,914	\$ 12,099	\$ 22	\$ 417,991

	Amortized Cost	Gross Unrealized Gains	Losses	Fair/Book Value
September 30, 2012				
Government Agency & Government-Sponsored Entities	\$ 46,655	\$316	\$-	\$ 46,971
Obligations of States and Political Subdivisions	5,704	-	-	5,704
Mortgage Backed Securities ⁽¹⁾	374,582	15,230	-	389,812
Corporate Securities	14,641	223	-	14,864
Other	5,826	-	-	5,826
Total	\$ 447,408	\$ 15,769	\$-	\$ 463,177

⁽¹⁾ All Mortgage Backed Securities consist of securities collateralized by residential real estate and were issued by an agency or government sponsored entity of the U.S. government.

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The book values, estimated fair values and unrealized gains and losses of investments classified as held-to-maturity are as follows (in thousands):

	Book	Gross		Fair
	Value	Unrealized	Losses	Value
September 30, 2013		Gains		
Obligations of States and Political Subdivisions	\$67,717	\$965	\$ 741	\$67,941
Mortgage Backed Securities ⁽¹⁾	121	1	-	122
Other	3,123	-	-	3,123
Total	\$70,961	\$966	\$ 741	\$71,186

	Book	Gross		Fair
	Value	Unrealized	Losses	Value
December 31, 2012		Gains		
Obligations of States and Political Subdivisions	\$65,694	\$2,296	\$ 3	\$67,987
Mortgage Backed Securities ⁽¹⁾	484	12	-	496
Other	2,214	-	-	2,214
Total	\$68,392	\$2,308	\$ 3	\$70,697

	Book	Gross		Fair
	Value	Unrealized	Losses	Value
September 30, 2012		Gains		
Obligations of States and Political Subdivisions	\$66,098	\$2,623	\$ -	\$68,721
Mortgage Backed Securities ⁽¹⁾	640	20	-	660
Other	2,222	-	-	2,222
Total	\$68,960	\$2,643	\$ -	\$71,603

⁽¹⁾ All Mortgage Backed Securities consist of securities collateralized by residential real estate and were issued by an agency or government sponsored entity of the U.S. government.

Fair values are based on quoted market prices or dealer quotes. If a quoted market price or dealer quote is not available, fair value is estimated using quoted market prices for similar securities.

The amortized cost and estimated fair values of investment securities at September 30, 2013 by contractual maturity are shown in the following tables (in thousands):

	Available-for-Sale		Held-to-Maturity	
	Amortized	Fair/Book	Book	Fair
September 30, 2013	Cost	Value	Value	Value
Within One Year	\$19,689	\$19,756	\$1,625	\$1,630
After One Year Through Five Years	56,416	56,526	18,543	18,876
After Five Years Through Ten Years	3,279	3,406	31,911	32,538
After Ten Years	-	-	18,761	18,020
	79,384	79,688	70,840	71,064

Investment Securities Not Due at a Single Maturity Date:

Mortgage Backed Securities	342,963	342,077	121	122
Total	\$422,347	\$421,765	\$70,961	\$71,186

Expected maturities of mortgage backed securities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

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The following tables show those investments with gross unrealized losses and their market value aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position at the dates indicated (in thousands):

	Less Than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
September 30, 2013						
<u>Securities Available-for-Sale</u>						
Mortgage Backed Securities	\$ 129,198	\$ 5,814	\$ -	\$ -	\$ 129,198	\$ 5,814
Corporate Securities	19,881	185	-	-	19,881	185
Total	\$ 149,079	\$ 5,999	\$ -	\$ -	\$ 149,079	\$ 5,999

Securities Held-to-Maturity

Obligations of States and Political Subdivisions	\$ 9,411	\$ 741	\$ -	\$ -	\$ 9,411	\$ 741
Total	\$ 9,411	\$ 741	\$ -	\$ -	\$ 9,411	\$ 741

	Less Than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
December 31, 2012						

Securities Available-for-Sale

Mortgage Backed Securities	\$ 4,542	\$ 10	\$ -	\$ -	\$ 4,542	\$ 10
Corporate Securities	3,442	12	-	-	3,442	12
Total	\$ 7,984	\$ 22	\$ -	\$ -	\$ 7,984	\$ 22

Securities Held-to-Maturity

Obligations of States and Political Subdivisions	\$ 528	\$ 3	\$ -	\$ -	\$ 528	\$ 3
Total	\$ 528	\$ 3	\$ -	\$ -	\$ 528	\$ 3

No securities were in a continuous unrealized loss position at September 30, 2012.

As of September 30, 2013, the Company held 352 investment securities of which 60 were in a loss position for less than twelve months. No securities were in a loss position for twelve months or more. Management periodically evaluates each investment security for other-than-temporary impairment relying primarily on industry analyst reports and observations of market conditions and interest rate fluctuations. Management believes it will be able to collect all amounts due according to the contractual terms of the underlying investment securities.

Securities of Government Agency and Government Sponsored Entities – There were no unrealized losses on the Company's investments in securities of government agency and government sponsored entities at September 30, 2013, December 31, 2012 and September 30, 2012.

Mortgage Backed Securities - The unrealized losses on the Company's investment in mortgage backed securities were \$5.8 million, \$10,000, and \$0 at September 30, 2013, December 31, 2012, and September 30, 2012, respectively. The unrealized losses on the Company's investment in mortgage backed securities were caused by interest rate fluctuations. The contractual cash flows of these investments are guaranteed by an agency or government sponsored entity of the U.S. government. Accordingly, it is expected that the securities would not be settled at a price less than the amortized cost of the Company's investment. Because the decline in market value is attributable to changes in interest rates and

not credit quality, and because the Company does not intend to sell the securities and it is more likely than not that the Company will not have to sell the securities before recovery of their cost basis, the Company does not consider these investments to be other-than-temporarily impaired at September 30, 2013 and December 31, 2012, respectively.

Obligations of States and Political Subdivisions - The financial problems experienced by certain municipalities over the past five years, along with the financial stresses exhibited by some of the large monoline bond insurers have increased the overall risk associated with bank-qualified municipal bonds. As of September 30, 2013, over ninety-four percent of the Company's bank-qualified municipal bond portfolio is rated at either the issue or issuer level, and all of these ratings are "investment grade." The Company monitors the status of the six percent of the portfolio that is not rated and at the current time does not believe any of them to be exhibiting financial problems that could result in a loss in any individual security.

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The unrealized losses on the Company's investment in obligation of states and political subdivision were \$741,000, \$3,000, and \$0 at September 30, 2013, December 31, 2012 and September 30, 2012, respectively. Management believes that any unrealized losses on the Company's investments in obligations of states and political subdivisions were primarily caused by interest rate fluctuations. The contractual terms of these investments do not permit the issuer to settle the securities at a price less than the amortized cost of the investment. Because the Company does not intend to sell the securities and it is more likely than not that the Company will not have to sell the securities before recovery of their cost basis, the Company does not consider these investments to be other-than-temporarily impaired at September 30, 2013 and December 31, 2012.

Corporate Securities - The unrealized losses on the Company's investment in corporate securities were \$185,000, \$12,000, and \$0 at September 30, 2013, December 31, 2012, and September 30, 2012, respectively. Changes in the prices of corporate securities are primarily influenced by: (1) changes in market interest rates; (2) changes in perceived credit risk in the general economy or in particular industries; (3) changes in the perceived credit risk of a particular company; and (4) day to day trading supply, demand and liquidity. Because the Company does not intend to sell the securities and it is more likely than not that the Company will not have to sell the securities before recovery of their cost basis, the Company does not consider these investments to be other-than-temporarily impaired at September 30, 2013 and December 31, 2012.

Proceeds from sales and calls of securities available-for-sale were as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(in thousands)	2013	2012	2013	2012
Proceeds	\$28,297	\$17,766	\$77,912	\$44,296
Gains	\$285	149	1,189	149
Losses	\$1,422	-	1,437	-

Pledged Securities

As of September 30, 2013, securities carried at \$310.5 million were pledged to secure public deposits, FHLB borrowings, and other government agency deposits as required by law. This amount was \$296.9 million at December 31, 2012, and \$307.2 million at September 30, 2012.

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3. Allowance for Credit Losses

The following tables show the allocation of the allowance for credit losses by portfolio segment and by impairment methodology at the dates indicated (in thousands):

	Commercial Real Estate	Agricultural Real Estate	Real Estate Construction	Residential 1st Mortgages	Home Equity Lines & Loans	Agricultural	Commercial	Consumer & Other	Leases	Unallocated	Total
September 30, 2013											
Year-To-Date Allowance for Credit Losses:											
Beginning Balance- January 1, 2013											
	\$6,464	\$2,877	\$986	\$1,219	\$3,235	\$10,437	\$7,963	\$182	\$-	\$854	\$34,217
Charge-Offs	(6)	(575)	-	(16)	(23)	(23)	(4)	(93)	-	-	(740)
Recoveries	-	-	-	-	30	36	281	37	-	-	384
Provision	(382)	911	(48)	(130)	(492)	(1,190)	1,551	42	-	(12)	250
Ending Balance- September 30, 2013	\$6,076	\$3,213	\$938	\$1,073	\$2,750	\$9,260	\$9,791	\$168	\$-	\$842	\$34,111
Third Quarter Allowance for Credit Losses:											
Beginning Balance- July 1, 2013											
	\$5,732	\$3,481	\$977	\$1,037	\$2,984	\$10,557	\$9,075	\$168	\$-	\$224	\$34,235
Charge-Offs	(6)	(175)	-	-	(1)	-	-	(29)	-	-	(211)
Recoveries	-	-	-	-	10	16	45	16	-	-	87
Provision	350	(93)	(39)	36	(243)	(1,313)	671	13	-	618	-
Ending Balance- September 30, 2013	\$6,076	\$3,213	\$938	\$1,073	\$2,750	\$9,260	\$9,791	\$168	\$-	\$842	\$34,111
Ending Balance Individually Evaluated for Impairment											
	-	-	-	50	132	122	1,856	53	-	-	2,213
Ending Balance Collectively Evaluated for Impairment	6,076	3,213	938	1,023	2,618	9,138	7,935	115	-	842	31,898
Loans:											
Ending Balance	\$401,626	\$311,401	\$27,099	\$143,577	\$37,160	\$221,569	\$145,793	\$5,063	\$4,523	\$-	\$1,297,000

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Ending Balance Individually Evaluated for Impairment	278	849	-	781	529	586	2,169	53	-	-	5,245
Ending Balance Collectively Evaluated for Impairment	401,348	310,552	27,099	142,796	36,631	220,983	143,624	5,010	4,523	-	1,292,

	Commercial Real Estate	Agricultural Real Estate	Real Estate Construction	Residential 1st Mortgages	Home Equity Lines & Loans	Agricultural	Commercial	Consumer & Other	Leases	Unallocated	Total
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Year-To-Date Allowance for Credit Losses:

Beginning Balance- January 1, 2012	\$5,823	\$2,583	\$1,933	\$1,251	\$3,746	\$8,127	\$8,733	\$207	\$-	\$614	\$33,017
Charge-Offs	-	-	-	(152)	(259)	(294)	(198)	(145)	-	-	(1,048)
Recoveries	-	90	-	53	14	61	117	63	-	-	398
Provision	641	204	(947)	67	(266)	2,543	(689)	57	-	240	1,850
Ending Balance- December 31, 2012	\$6,464	\$2,877	\$986	\$1,219	\$3,235	\$10,437	\$7,963	\$182	\$-	\$854	\$34,217
Ending Balance Individually Evaluated for Impairment	-	-	-	-	173	996	144	61	-	-	1,374
Ending Balance Collectively Evaluated for Impairment	6,464	2,877	986	1,219	3,062	9,441	7,819	121	-	854	32,843
Loans: Ending Balance	\$350,548	\$311,992	\$32,680	\$140,257	\$42,042	\$221,032	\$143,293	\$5,058	\$-	\$-	\$1,246,
Ending Balance Individually Evaluated	289	5,423	-	657	980	3,937	250	61	-	-	11,597

for
Impairment
Ending
Balance
Collectively
Evaluated
for
Impairment

350,259	306,569	32,680	139,600	41,062	217,095	143,043	4,997	-	-	1,235,
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	Commercial Real Estate	Agricultural Real Estate	Real Estate Construction	Residential 1st Mortgages	Home Equity Lines & Loans	Agricultural	Commercial	Consumer & Other	Leases	Unallocated	Total
September 30, 2012											
Year-To-Date Allowance for Loan Losses:											
Beginning Balance- January 1, 2012	\$5,823	\$2,583	\$1,933	\$1,251	\$3,746	\$8,127	\$8,733	\$207	\$-	\$614	\$33,017
Charge-Offs	-	-	-	(81)	(138)	(240)	(198)	(122)	-	-	(779)
Recoveries	-	89	-	16	12	61	41	47	-	-	266
Provision	(1,490)	990	(72)	356	(105)	311	1,084	12	-	14	1,100
Ending Balance- September 30, 2012	\$4,333	\$3,662	\$1,861	\$1,542	\$3,515	\$8,259	\$9,660	\$144		\$628	\$33,604
Third Quarter Allowance for Loan Losses:											
Beginning Balance- July 1, 2012	\$4,377	\$2,633	\$1,900	\$1,451	\$3,514	\$7,834	\$9,538	\$140	\$-	\$1,711	\$33,098
Charge-Offs	-	-	-	(80)	(22)	-	-	(34)	-	-	(136)
Recoveries	-	-	-	16	2	-	9	15	-	-	42
Provision	(44)	1,029	(39)	155	21	425	113	23	-	(1,083)	600
Ending Balance- September 30, 2012	\$4,333	\$3,662	\$1,861	\$1,542	\$3,515	\$8,259	\$9,660	\$144	\$-	\$628	\$33,604
Ending Balance Individually Evaluated for Impairment	-	-	-	-	248	548	146	20	-	-	962
Ending Balance Collectively Evaluated for Impairment	4,333	3,662	1,861	1,542	3,267	7,711	9,514	124	-	628	32,642
Loans: Ending Balance	\$335,664	\$293,864	\$32,701	\$137,464	\$43,990	\$193,053	\$167,777	\$5,514	\$-	\$-	\$1,210,029
Ending Balance Individually Evaluated	295	2,551	-	493	1,048	2,652	257	20	-	-	7,316

for
Impairment
Ending
Balance
Collectively
Evaluated
for
Impairment

335,369	291,313	32,701	136,971	42,942	190,401	167,520	5,494	-	-	1,202,71
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The following tables show the loan & lease portfolio allocated by management's internal risk ratings at the dates indicated (in thousands):

September 30, 2013	Pass	Special Mention	Substandard	Total Loans
Loans:				
Commercial Real Estate	\$389,137	\$7,765	\$ 4,724	\$401,626
Agricultural Real Estate	307,736	2,497	1,168	311,401
Real Estate Construction	25,467	1,632	-	27,099
Residential 1st Mortgages	142,036	780	761	143,577
Home Equity Lines & Loans	36,090	-	1,070	37,160
Agricultural	220,504	464	601	221,569
Commercial	135,303	8,958	1,532	145,793
Consumer & Other	4,761	-	302	5,063
Leases	4,523	-	-	4,523
Total	\$1,265,557	\$22,096	\$ 10,158	\$1,297,811

December 31, 2012	Pass	Special Mention	Substandard	Total Loans
Loans:				
Commercial Real Estate	\$326,037	\$15,528	\$ 8,983	\$350,548
Agricultural Real Estate	299,642	6,605	5,745	311,992
Real Estate Construction	26,445	6,235	-	32,680
Residential 1st Mortgages	137,998	1,192	1,067	140,257
Home Equity Lines & Loans	40,866	-	1,176	42,042
Agricultural	216,164	1,168	3,700	221,032
Commercial	137,217	5,586	490	143,293
Consumer & Other	4,737	-	321	5,058
Total	\$1,189,106	\$36,314	\$ 21,482	\$1,246,902

September 30, 2012	Pass	Special Mention	Substandard	Total Loans
Loans:				
Commercial Real Estate	\$313,441	\$15,910	\$ 6,313	\$335,664
Agricultural Real Estate	273,823	9,887	10,154	293,864
Real Estate Construction	24,856	3,217	4,628	32,701
Residential 1st Mortgages	135,473	1,211	780	137,464
Home Equity Lines & Loans	41,975	-	2,015	43,990
Agricultural	186,398	2,300	4,355	193,053
Commercial	161,685	5,634	458	167,777
Consumer & Other	5,195	-	319	5,514
Total	\$1,142,846	\$38,159	\$ 29,022	\$1,210,027

See "Note 1. Significant Accounting Policies - Allowance for Credit Losses" for a description of the internal risk ratings used by the Company. There were no loans or leases outstanding at September 30, 2013, December 31, 2012, and September 30, 2012 rated doubtful or loss.

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The following tables show an aging analysis of the loan & lease portfolio by the time past due at the dates indicated (in thousands):

	90 Days			Total Past Due	Current	Total Loans
	30-89 Days Past Due	or More and Still Accruing	Nonaccrual			
September 30, 2013						
Loans:						
Commercial Real Estate	\$ 592	\$ -	\$ 176	\$ 768	\$ 400,858	\$ 401,626
Agricultural Real Estate	-	-	849	849	310,552	311,401
Real Estate Construction	-	-	-	-	27,099	27,099
Residential 1st Mortgages	-	-	455	455	143,122	143,577
Home Equity Lines & Loans	121	-	243	364	36,796	37,160
Agricultural	-	-	99	99	221,470	221,569
Commercial	-	-	1,944	1,944	143,849	145,793
Consumer & Other	108	-	17	125	4,938	5,063
Leases	-	-	-	-	4,523	4,523
Total	\$ 821	\$ -	\$ 3,783	\$ 4,604	\$ 1,293,207	\$ 1,297,811

	90 Days			Total Past Due	Current	Total Loans
	30-89 Days Past Due	or More and Still Accruing	Nonaccrual			
December 31, 2012						
Loans:						
Commercial Real Estate	\$ 150	\$ -	\$ -	\$ 150	\$ 350,398	\$ 350,548
Agricultural Real Estate	-	-	5,423	5,423	306,569	311,992
Real Estate Construction	-	-	-	-	32,680	32,680
Residential 1st Mortgages	23	-	445	468	139,789	140,257
Home Equity Lines & Loans	70	-	213	283	41,759	42,042
Agricultural	-	-	3,198	3,198	217,834	221,032
Commercial	293	-	-	293	143,000	143,293
Consumer & Other	11	-	19	30	5,028	5,058
Total	\$ 547	\$ -	\$ 9,298	\$ 9,845	\$ 1,237,057	\$ 1,246,902

	90 Days			Total Past Due	Current	Total Loans
	30-89 Days Past Due	or More and Still Accruing	Nonaccrual			
September 30, 2012						
Loans:						
Commercial Real Estate	\$-	\$ -	\$ -	\$-	\$ 335,664	\$ 335,664
Agricultural Real Estate	-	-	2,551	2,551	291,313	293,864
Real Estate Construction	-	-	-	-	32,701	32,701
Residential 1st Mortgages	-	-	279	279	137,185	137,464
Home Equity Lines & Loans	101	-	528	629	43,361	43,990
Agricultural	-	-	2,374	2,374	190,679	193,053
Commercial	-	-	-	-	167,777	167,777
Consumer & Other	56	-	20	76	5,438	5,514

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Total	\$ 157	\$ -	\$ 5,752	\$ 5,909	\$ 1,204,118	\$ 1,210,027
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The following tables show information related to impaired loans & leases for the periods indicated (in thousands):

September 30, 2013	Recorded Investment	Unpaid Principal Balance	Related Allowance	Three Months Ended Sept. 30, 2013		Nine Months Ended Sept. 30, 2013	
				Average Recorded Investment	Average Interest Recognized	Average Recorded Investment	Average Interest Recognized
With no related allowance recorded:							
Commercial Real Estate	\$ 279	\$ 299	\$ -	\$1,626	\$ 2	\$953	\$ 6
Agricultural Real Estate	850	1,173	-	2,616	-	3,777	-
Residential 1st Mortgages	535	588	-	533	4	643	11
Home Equity Lines & Loans	287	306	-	331	3	379	5
Agricultural	99	121	-	278	-	1,239	-
Commercial	85	85	-	89	2	99	6
	\$ 2,135	\$ 2,572	\$ -	\$5,473	\$ 11	\$7,090	\$ 28
With an allowance recorded:							
Commercial Real Estate	\$ -	\$ -	\$ -	\$4	\$ -	\$2	\$ -
Agricultural Real Estate	-	-	-	725	-	1,221	-
Residential 1st Mortgages	246	246	50	123	-	27	-
Home Equity Lines & Loans	243	290	132	243	-	195	-
Agricultural	488	488	122	766	8	1,562	24
Commercial	2,084	2,095	1,856	1,251	2	436	6
Consumer & Other	53	56	53	55	1	185	3
	\$ 3,114	\$ 3,175	\$ 2,213	\$3,167	\$ 11	\$3,628	\$ 33
Total	\$ 5,249	\$ 5,747	\$ 2,213	\$8,640	\$ 22	\$10,718	\$ 61

December 31, 2012	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Interest	
				Recorded Investment	Income Recognized
With no related allowance recorded:					
Commercial Real Estate	\$ 289	\$289	\$ -	\$ 506	\$ 20
Agricultural Real Estate	5,437	5,454	-	2,611	-
Residential 1st Mortgages	658	761	-	458	3
Home Equity Lines & Loans	792	871	-	775	23
Agricultural	1,932	1,954	-	1,159	19
Commercial	106	106	-	144	6
	\$ 9,214	\$9,435	\$ -	\$ 5,653	\$ 71
With an allowance recorded:					
Residential 1st Mortgages	\$ -	\$-	\$ -	\$ 54	\$ -
Home Equity Lines & Loans	194	237	173	182	4
Agricultural	2,006	2,019	996	997	1
Commercial	144	144	144	159	4
Consumer & Other	61	63	61	31	-
	\$ 2,405	\$2,463	\$ 1,374	\$ 1,423	\$ 9
Total	\$ 11,619	\$ 11,898	\$ 1,374	\$ 7,076	\$ 80

Three Months Ended Sept. 30, 2012
 Nine Months Ended Sept. 30, 2012

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September 30, 2012	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Interest Recorded Investment	Average Interest Income Recognized	Average Interest Recorded Investment	Average Interest Income Recognized
With no related allowance recorded:							
Commercial Real Estate	\$ 295	\$ 295	\$ -	\$297	\$ 6	\$789	\$ 15
Agricultural Real Estate	2,558	2,551	-	2,036	-	1,402	-
Residential 1st Mortgages	494	521	-	438	-	512	-
Home Equity Lines & Loans	785	862	-	743	6	717	17
Agricultural	2,106	2,111	-	1,197	5	594	15
Commercial	111	111	-	115	2	169	4
	\$ 6,349	\$ 6,451	\$ -	\$4,826	\$ 19	\$4,183	\$ 51
With an allowance recorded:							
Commercial Real Estate	\$ -	\$ -	\$ -	\$-	\$ -	\$503	\$ -
Residential 1st Mortgages	-	-	-	54	-	72	-
Home Equity Lines & Loans	269	314	248	174	1	152	3
Agricultural	547	1,551	548	567	-	749	-
Commercial	146	146	146	196	2	157	2
Consumer & Other	20	22	20	21	-	22	-
	\$ 982	\$ 2,033	\$ 962	\$1,012	\$ 3	\$1,655	\$ 5
Total	\$ 7,331	\$ 8,484	\$ 962	\$5,838	\$ 22	\$5,838	\$ 56

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Total recorded investment shown in the prior table will not equal the total ending balance of loans & leases individually evaluated for impairment on the allocation of allowance table. This is because the calculation of recorded investment for purposes of this table takes into account charge-offs, net deferred loan & lease fees & costs, unamortized premium or discount, and accrued interest.

At September 30, 2013, the Company allocated \$364,000 of specific reserves to \$2.0 million of troubled debt restructured loans, of which \$1.5 million were performing. The Company had no commitments at September 30, 2013 to lend additional amounts to customers with outstanding loans that are classified as troubled debt restructurings.

During the three and nine month periods ending September 30, 2013, the terms of certain loans were modified as troubled debt restructurings. The modification of the terms of such loans included one or a combination of the following: a reduction of the stated interest rate of the loan; an extension of the maturity date at a stated rate of interest lower than the current market rate for new debt with similar risk; or a permanent reduction of the recorded investment in the loan.

Modifications involving a reduction of the stated interest rate of the loan were for periods of 5 years. Modifications involving an extension of the maturity date were for periods ranging from 6 months to 10 years.

The following table presents loans by class, modified as troubled debt restructured loans & leases for the three and nine-month periods ended September 30, 2013 (in thousands):

	Three Months Ended September 30, 2013		Nine Months Ended September 30, 2013	
	Pre-Modification Number of Loans Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment	Pre-Modification Number of Loans Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
Troubled Debt Restructurings				
Residential 1st Mortgages	- \$ -	\$ -	4 \$ 306	\$ 290
Home Equity Lines & Loans	- -	- -	2 195	184
Commercial	- -	- -	2 292	292
Total	- \$ -	\$ -	8 \$ 793	\$ 766

The TDRs described above increased the allowance for credit losses by \$0 and \$4,000 and resulted in charge-offs of \$0 and \$27,000 for the three and nine-month period ending September 30, 2013.

As of September 30, 2013, there was one commercial loan with an outstanding balance of \$277,000 that was previously modified as a troubled debt restructuring within the previous 12 months that subsequently defaulted during the nine months ended September 30, 2013. This defaulted loan did not increase the allowance for credit loss and did not result in any charge offs during the twelve-month period ending September 30, 2013.

At December 31, 2012, the Company allocated \$401,000 of specific reserves to \$2.6 million of troubled debt restructured loans, of which \$2.3 million were performing. The Company had no commitments at December 31, 2012, to lend additional amounts to customers with outstanding loans that are classified as troubled debt restructurings.

During the twelve-month period ending December 31, 2012, the terms of certain loans were modified as troubled debt restructurings. The modification of the terms of such loans included one or a combination of the following: a reduction of the stated interest rate of the loan; an extension of the maturity date at a stated rate of interest lower than the current market rate for new debt with similar risk; or a permanent reduction of the recorded investment in the loan.

Modifications involving a reduction of the stated interest rate of the loan were for periods ranging from 2 years to 5 years. Modifications involving an extension of the maturity date were for periods ranging from 6 months to 10 years.

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The following table presents loans by class modified as troubled debt restructured loans during the twelve-month period ended December 31, 2012 (in thousands):

	December 31, 2012	
	Pre-Modification Number of Outstanding Loans Recorded	Post-Modification Outstanding Investment
Troubled Debt Restructurings		
Commercial Real Estate	1 \$ 116	\$ 116
Residential 1st Mortgages	2 216	201
Home Equity Lines & Loans	7 529	480
Agricultural	4 858	858
Commercial	3 273	273
Consumer & Other	1 41	41
Total	18 \$ 2,033	\$ 1,969

The TDRs described above increased the allowance for credit losses by \$53,000 and resulted in charge-offs of \$64,000 during the year ended December 31, 2012.

During the twelve-month period ended December 31, 2012, there were no payment defaults on loans modified as troubled debt restructurings within twelve months following the modification.

At September 30, 2012, the Company allocated \$187,000 of specific reserves to \$2.1 million of troubled debt restructured loans, of which \$1.6 million were performing. The Company had no commitments at September 30, 2012 to lend additional amounts to customers with outstanding loans that are classified as troubled debt restructurings.

During the three and nine month periods ending September 30, 2012, the terms of certain loans were modified as troubled debt restructurings. The modification of the terms of such loans included one or a combination of the following: a reduction of the stated interest rate of the loan; an extension of the maturity date at a stated rate of interest lower than the current market rate for new debt with similar risk; or a permanent reduction of the recorded investment in the loan.

Modifications involving a reduction of the stated interest rate of the loan were for periods of 5 years. Modifications involving an extension of the maturity date were for periods ranging from 6 months to 15 years.

The following table presents loans by class modified as troubled debt restructured loans for the three and nine-month periods ended September 30, 2012 (in thousands):

	Three Months Ended September 30, 2012		Nine Months Ended September 30, 2012	
	Pre-Modification Number of Outstanding Loans Recorded	Post-Modification Outstanding Investment	Pre-Modification Number of Outstanding Loans Recorded	Post-Modification Outstanding Investment
Troubled Debt Restructurings				
Commercial Real Estate	- \$ -	\$ -	1 \$ 116	\$ 116
Residential 1st Mortgages	1 185	173	5 331	312
Home Equity Lines & Loans	1 46	43	4 414	369
Agricultural	2 175	175	3 355	355
Commercial	- -	-	3 273	273
Total	4 \$ 406	\$ 391	16 \$ 1,489	\$ 1,425

The TDR's described above increased the allowance for credit losses by \$0 and \$19,000 and resulted in charge-offs of \$15,000 and \$64,000 for the three and nine months ended September 30, 2012.

During the three and nine-months ended September 30, 2012, there were no payment defaults on loans modified as troubled debt restructurings within twelve months following the modification.

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4. Fair Value Measurements

The Company follows the “Fair Value Measurement and Disclosures” topic, which establishes a framework for measuring fair value in U.S. GAAP and expands disclosures about fair value measurements. This standard applies whenever other standards require, or permit, assets or liabilities to be measured at fair value but does not expand the use of fair value in any new circumstances. In this standard, the FASB clarifies the principle that fair value should be based on the assumptions market participants would use when pricing the asset or liability. In support of this principle, this standard establishes a fair value hierarchy that prioritizes the information used to develop those assumptions. The fair value hierarchy is as follows:

Level 1 inputs – Unadjusted quoted prices in active markets for identical assets or liabilities that the entity has the ability to access at the measurement date.

Level 2 inputs - Inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. These might include quoted prices for similar assets and liabilities in active markets, and inputs other than quoted prices that are observable for the asset or liability, such as interest rates and yield curves that are observable at commonly quoted intervals.

Level 3 inputs - Unobservable inputs for determining the fair values of assets or liabilities that reflect an entity’s own assumptions about the assumptions that market participants would use in pricing the assets or liabilities.

Management monitors the availability of observable market data to assess the appropriate classification of financial instruments within the fair value hierarchy. Changes in economic conditions or model-based valuation techniques may require the transfer of financial instruments from one fair value level to another. In such instances, the transfer is reported at the beginning of the reporting period.

Management evaluates the significance of transfers between levels based upon the nature of the financial instrument and size of the transfer relative to total assets, total liabilities or total earnings.

Securities classified as available-for-sale are reported at fair value on a recurring basis utilizing Level 1, 2 and 3 inputs. For these securities, the Company obtains fair value measurements from an independent pricing service. The fair value measurements consider observable data that may include dealer quotes, market spreads, cash flows, the U.S. Treasury yield curve, live trading levels, trade execution data, market consensus prepayment speeds, credit information and the bond’s terms and conditions, among other things.

The Company does not record all loans & leases at fair value on a recurring basis. However, from time to time, a loan or lease is considered impaired and an allowance for credit losses is established. Once a loan or lease is identified as individually impaired, management measures impairment in accordance with the “Receivables” topic. The fair value of impaired loans & leases is estimated using one of several methods, including collateral value when the loan & lease is collateral dependent, market value of similar debt, enterprise value, and discounted cash flows. Those impaired loans & leases not requiring an allowance represent loans & leases for which the fair value of the expected repayments or collateral exceed the recorded investments in such loans & leases. Impaired loans & leases where an allowance is established based on the fair value of collateral require classification in the fair value hierarchy. When the fair value of the collateral is based on an observable market price or a current appraised value which uses observable data, the Company records the impaired loan or lease as nonrecurring Level 2. When an appraised value is not available or management determines the fair value of the collateral is further impaired below the appraised value or the appraised value contains a significant unobservable assumption, and there is no observable market price, the Company records the impaired loan or lease as nonrecurring Level 3.

Other Real Estate (“ORE”) is reported at fair value on a non-recurring basis. When the fair value of the ORE is based on an observable market price or a current appraised value which uses observable data, the Company records the ORE as nonrecurring Level 2. When an appraised value is not available or management determines the fair value of the collateral is further impaired below the appraised value or the appraised value contains a significant unobservable assumption, and there is no observable market price, the Company records the ORE as nonrecurring Level 3. Other real estate is reported in Interest Receivable and Other Assets on the Company’s Consolidated Balance Sheets.

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The following tables present information about the Company's assets and liabilities measured at fair value on a recurring basis and indicate the fair value hierarchy of the valuation techniques utilized by the Company to determine such fair value for the periods indicated.

		Fair Value Measurements At September 30, 2013, Using Quoted Prices in Active Markets for Other Significant Identical Observable Unobservable Assets Inputs Inputs (Level (Level 2) (Level 3)			
(in thousands)	Fair Value	Total	1)	(Level 2)	(Level 3)
Available-for-Sale Securities:					
Government Agency & Government-Sponsored Entities	\$28,643	\$23,587	\$ 5,056	\$ -	
Mortgage Backed Securities	342,077	-	342,077	-	
Corporate Securities	49,761	8,171	41,590	-	
Other	1,284	974	310	-	
Total Assets Measured at Fair Value On a Recurring Basis	\$421,765	\$32,732	\$ 389,033	\$ -	

		Fair Value Measurements At December 31, 2012, Using Quoted Prices in Active Markets for Other Significant Identical Observable Unobservable Assets Inputs Inputs (Level (Level 2) (Level 3)			
(in thousands)	Fair Value	Total	1)	(Level 2)	(Level 3)
Available-for-Sale Securities:					
Government Agency & Government-Sponsored Entities	\$26,823	\$21,731	\$ 5,092	\$ -	
Obligations of States and Political Subdivisions	5,665	-	-	5,665	
Mortgage Backed Securities	352,772	-	352,772	-	
Corporate Securities	22,558	4,020	18,538	-	
Other	10,173	9,863	310	-	
Total Assets Measured at Fair Value On a Recurring Basis	\$417,991	\$35,614	\$ 376,712	\$ 5,665	

		Fair Value Measurements At September 30, 2012, Using Quoted Prices in Active Markets for Other Significant Identical Observable Unobservable Assets Inputs Inputs		
Fair Value	Total	1)	(Level 2)	(Level 3)

(in thousands)	Total	for Identical Assets (Level 1)	(Level 2)	(Level 3)
Available-for-Sale Securities:				
Government Agency & Government-Sponsored Entities	\$46,971	\$10,627	\$ 36,344	\$ -
Obligations of States and Political Subdivisions	5,704	-	-	5,704
Mortgage Backed Securities	389,812	-	389,812	-
Corporate Securities	14,864	-	14,864	-
Other	5,826	5,516	310	-
Total Assets Measured at Fair Value On a Recurring Basis	\$463,177	\$16,143	\$ 441,330	\$ 5,704

Fair values for Level 2 available-for-sale investment securities are based on quoted market prices for similar securities. During the three and nine-months ended September 30, 2013, \$5.6 million were transferred out of level 3 available-for-sale investment securities into held-to-maturity investment securities. During the three and nine-months ended September 30, 2012, there were no transfers in or out of level 1, 2, or 3. The following table presents changes in level 3 assets measured at fair value on a recurring basis.

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(in thousands)	Three Months		Nine Months	
	Ended		Ended	
	September 30,		September 30,	
	2013	2012	2013	2012
Balance at Beginning of Period	\$5,612	\$5,724	\$5,665	\$5,782
Total Realized and Unrealized Gains/(Losses) Included in Income	-	-	-	-
Total Unrealized Gains/(Losses) Included in Other Comprehensive Income	-	-	-	-
Purchase of Securities	-	-	-	-
Sales, Maturities, and Calls of Securities	(31)	(20)	(84)	(78)
Net Transfers out of Available for Sale Securities	(5,581)	-	(5,581)	-
Balance at End of Period	\$-	\$5,704	\$-	\$5,704

Available-for-sale investments securities categorized as Level 3 assets primarily consist of obligations of states and political subdivisions. These bonds were issued by local housing authorities and have no active market. These bonds are carried at historical cost, which approximates fair value, unless economic conditions for the municipality changes to a degree requiring a valuation adjustment. Due to the difficulty in valuing the senior housing authority bonds and the fact that the Company owns 100% of these bonds that were issued by a relationship banking customer, we transferred these bonds out of the available-for-sale category and into the held-to-maturity category as the Company intends to hold these bonds until maturity.

The following tables present information about the Company's impaired loans & leases and other real estate, classes of assets or liabilities that the Company carries at fair value on a non-recurring basis, and indicates the fair value hierarchy of the valuation techniques utilized by the Company to determine such fair value for the periods indicated. Not all impaired loans & leases are carried at fair value. Impaired loans & leases are only included in the following tables when their fair value is based upon an appraisal of the collateral, and if that appraisal results in a partial charge-off or the establishment of a specific reserve.

(in thousands)	Fair Value	Fair Value Measurements At September 30, 2013, Using		
		Quoted Prices in Active Markets for Other Identifiable Assets (Level 1)	Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Impaired Loans				
Residential 1st Mortgage	\$477	\$-	\$-	\$ 477
Home Equity Lines and Loans	293	-	-	293
Agricultural	366	-	-	366
Commercial	228	-	-	228
Total Impaired Loans	1,364	-	-	1,364
Other Real Estate				
Real Estate Construction	2,398	-	-	2,398
Agricultural Real Estate	1,268	-	-	1,268
Total Other Real Estate	3,666	-	-	3,666

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Total Assets Measured at Fair Value On a Non-Recurring Basis \$5,030 \$- \$ - \$ 5,030

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	Fair Value Measurements At December 31, 2012, Using Quoted Prices in Active Markets for Other Observable Inputs (Level 1) (Level 2) (Level 3)			
	Fair Value Total	Identifiable Assets (Level 1)	Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
(in thousands)				
Impaired Loans				
Residential 1st Mortgage	\$235	\$-	\$ -	\$ 235
Home Equity Lines and Loans	462	-	-	462
Agricultural	1,010	-	-	1,010
Total Impaired Loans	1,707	-	-	1,707
Other Real Estate				
Real Estate Construction	2,553	-	-	2,553
Total Other Real Estate	2,553	-	-	2,553
Total Assets Measured at Fair Value On a Non-Recurring Basis	\$4,260	\$-	\$ -	\$ 4,260

	Fair Value Measurements At September 30, 2012, Using Quoted Prices in Active Markets for Other Observable Inputs (Level 1) (Level 2) (Level 3)			
	Fair Value Total	Identifiable Assets (Level 1)	Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
(in thousands)				
Impaired Loans				
Residential 1st Mortgage	\$200	\$-	\$ -	\$ 200
Home Equity Lines and Loans	466	-	-	466
Total Impaired Loans	666	-	-	666
Other Real Estate				
Real Estate Construction	2,553	-	-	2,553
Total Other Real Estate	2,553	-	-	2,553
Total Assets Measured at Fair Value On a Non-Recurring Basis	\$3,219	\$-	\$ -	\$ 3,219

5. Fair Value of Financial Instruments

U.S. GAAP requires disclosure of fair value information about financial instruments, whether or not recognized on the balance sheet, for which it is practical to estimate that value. The estimated fair value amounts have been determined by the Company using available market information and appropriate valuation methodologies. The use of assumptions and various valuation techniques, as well as the absence of secondary markets for certain financial instruments, will likely reduce the comparability of fair value disclosures between financial institutions. In some cases, book value is a

reasonable estimate of fair value due to the relatively short period of time between origination of the instrument and its expected realization.

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The following tables summarize the book value and estimated fair value of financial instruments for the periods indicated:

September 30, 2013 (in thousands)	Carrying Amount	Fair Value of Financial Instruments Using Quoted Prices in Active Markets for							
		Identical Assets (Level 1)	Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total Estimated Fair Value				
Assets:									
Cash and Cash Equivalents	\$47,625	\$47,625	\$ -	\$ -					\$47,625
Investment Securities Available-for-Sale:									
Government Agency & Government-Sponsored Entities	28,643	23,587	5,056	-					28,643
Mortgage Backed Securities	342,077	-	342,077	-					342,077
Corporate Securities	49,761	8,171	41,590	-					49,761
Other	1,284	974	310	-					1,284
Total Investment Securities Available-for-Sale	421,765	32,732	389,033	-					421,765
Investment Securities Held-to-Maturity:									
Obligations of States and Political Subdivisions	67,717	-	55,188	12,753					67,941
Mortgage Backed Securities	121	-	122	-					122
Other	3,123	-	3,123	-					3,123
Total Investment Securities Held-to-Maturity	70,961	-	58,433	12,753					71,186
FHLB Stock	7,187	N/	A	N/	A	N/	A	N/	A
Loans & Leases, Net of Deferred Fees & Allowance:									
Commercial Real Estate	395,550	-	-			399,792			399,792
Agricultural Real Estate	308,188	-	-			313,920			313,920
Real Estate Construction	26,161	-	-			26,437			26,437
Residential 1st Mortgages	142,504	-	-			145,778			145,778
Home Equity Lines and Loans									