FIRST MERCHANTS CORP
Form 10-Q
August 09, 2018

FORM 10-Q
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

[x] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE

SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended June 30, 2018
OR
[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE

SECURITIES EXCHANGE ACT OF 1934

For the Transition Period from _______ to _______

Commission File Number 0-17071

FIRST MERCHANTS CORPORATION
(Exact name of registrant as specified in its charter)

Indiana	35-1544218
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
200 East Jackson Street, Muncie, IN	47305-2814
(Address of principal executive offices)	(Zip code)

(Registrant’s telephone number, including area code): (765) 747-1500

Not Applicable
(Former name, former address and former fiscal year,
if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15 (d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes [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 (Section 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).
Yes [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 [X]	Accelerated filer [ ]	Non-accelerated filer [ ] (Do not check if smaller reporting company)
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]

As of July 31, 2018, there were 49,560,536 outstanding common shares of the registrant.

1

Table of Contents
TABLE OF CONTENTS

FIRST MERCHANTS CORPORATION

Table of Contents
GLOSSARY OF DEFINED TERMS

FIRST MERCHANTS CORPORATION

Arlington Bank	The Arlington Bank, which was acquired by the Corporation on May 19, 2017.
ASC	Accounting Standards Codification
Bank	First Merchants Bank, a wholly-owned subsidiary of the Corporation
CET1	Common Equity Tier 1
CMT	Constant Maturity Treasury
Corporation	First Merchants Corporation
ESPP	Employee Stock Purchase Plan
FDIC	Federal Deposit Insurance Corporation
FHLB	Federal Home Loan Bank
FTE	Fully taxable equivalent
GAAP	Generally Accepted Accounting Principles
IAB	Independent Alliance Banks, Inc., which was acquired by the Corporation on July 14, 2017.
OREO	Other real estate owned
RSA	Restricted Stock Awards
TEFRA	Tax Equity and Fiscal Responsibility Act. The TEFRA disallowance reduces the amount of interest expense an entity may deduct for the purpose of carrying tax-free investment securities.

Table of Contents

PART I. FINANCIAL INFORMATION

ITEM 1. CONSOLIDATED CONDENSED FINANCIAL STATEMENTS

(table dollar amounts in thousands, except share data)

CONSOLIDATED CONDENSED BALANCE SHEETS

	June 30, 2018 (Unaudited)	December 31, 2017
ASSETS		
Cash and cash equivalents	$133,893	$154,905
Interest-bearing time deposits	36,599	35,027
Investment securities available for sale	1,096,837	999,947
Investment securities held to maturity (fair value of $519,643 and $568,208)	522,846	560,655
Loans held for sale	2,046	7,216
Loans, net of allowance for loan losses of $77,543 and $75,032	7,003,516	6,676,167
Premises and equipment	94,397	95,852
Federal Home Loan Bank stock	24,588	23,825
Interest receivable	38,530	37,130
Goodwill	445,355	445,355
Other intangibles	27,704	31,148
Cash surrender value of life insurance	222,905	223,557
Other real estate owned	9,071	10,373
Tax asset, deferred and receivable	24,619	23,983
Other assets	51,809	42,338
TOTAL ASSETS	$9,734,715	$9,367,478
LIABILITIES		
Deposits:		
Noninterest-bearing	$1,571,194	$1,761,553
Interest-bearing	5,932,621	5,410,977
Total Deposits	7,503,815	7,172,530
Borrowings:		
Federal funds purchased	109,000	144,038
Securities sold under repurchase agreements	122,513	136,623
Federal Home Loan Bank advances	469,261	414,377
Subordinated debentures and term loans	138,352	139,349
Total Borrowings	839,126	834,387
Interest payable	4,807	4,390
Other liabilities	46,639	52,708
Total Liabilities	8,394,387	8,064,015
COMMITMENTS AND CONTINGENT LIABILITIES		
STOCKHOLDERS' EQUITY		
Cumulative Preferred Stock, $1,000 par value, $1,000 liquidation value:		
Authorized - 600 shares		
Issued and outstanding - 125 shares	125	125
Common Stock, $.125 stated value:		
Authorized - 100,000,000 shares		
Issued and outstanding - 49,280,188 and 49,158,238 shares	6,160	6,145
Additional paid-in capital	836,549	834,870

Retained earnings	522,362	465,231
Accumulated other comprehensive loss	(24,868)	(2,908)
Total Stockholders' Equity	1,340,328	1,303,463
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$9,734,715	$9,367,478

See NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS.

Table of Contents
PART I. FINANCIAL INFORMATION
ITEM 1. CONSOLIDATED CONDENSED FINANCIAL STATEMENTS
(table dollar amounts in thousands, except share data)

CONSOLIDATED CONDENSED STATEMENTS OF INCOME
(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2018	2017	2018	2017
INTEREST INCOME				
Loans receivable:				
Taxable	$84,663	$59,386	$162,930	$115,743
Tax exempt	3,632	2,492	7,228	4,825
Investment securities:				
Taxable	5,434	4,180	10,530	8,488
Tax exempt	6,246	5,091	12,372	10,094
Deposits with financial institutions	633	114	764	158
Federal Home Loan Bank stock	263	204	667	393
Total Interest Income	100,871	71,467	194,491	139,701
INTEREST EXPENSE				
Deposits	12,165	5,137	21,167	9,261
Federal funds purchased	61	103	441	331
Securities sold under repurchase agreements	172	110	345	198
Federal Home Loan Bank advances	1,845	1,177	4,004	2,155
Subordinated debentures and term loans	2,057	1,840	4,047	3,657
Total Interest Expense	16,300	8,367	30,004	15,602
NET INTEREST INCOME	84,571	63,100	164,487	124,099
Provision for loan losses	1,663	2,875	4,163	5,260
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	82,908	60,225	160,324	118,839
OTHER INCOME				
Service charges on deposit accounts	5,038	4,438	9,815	8,612
Fiduciary and wealth management fees	3,150	2,609	6,566	5,249
Other customer fees	5,362	5,406	10,778	10,269
Increase in cash surrender value of life insurance	907	817	1,985	1,715
Gains on life insurance benefits	100	2,154	198	2,154
Net gains and fees on sales of loans	1,600	1,617	3,421	2,892
Net realized gains on sales of available for sale securities	1,122	567	2,731	1,165
Other income	912	826	2,258	1,224
Total Other Income	18,191	18,434	37,752	33,280
OTHER EXPENSES				
Salaries and employee benefits	32,192	27,076	64,418	52,808
Net occupancy	4,348	3,965	9,018	8,181
Equipment	3,556	2,907	7,224	5,714
Marketing	1,474	792	2,358	1,357
Outside data processing fees	3,462	3,086	6,426	5,702
Printing and office supplies	324	275	658	539

Intangible asset amortization	1,718	991	3,444	1,894
FDIC assessments	711	579	1,430	1,149
Other real estate owned and foreclosure expenses	362	731	764	1,262
Professional and other outside services	1,789	3,266	3,330	5,000
Other expenses	3,568	3,648	8,121	6,809
Total Other Expenses	53,504	47,316	107,191	90,415
INCOME BEFORE INCOME TAX	47,595	31,343	90,885	61,704
Income tax expense	7,961	7,207	14,572	14,375
NET INCOME AVAILABLE TO COMMON STOCKHOLDERS	$39,634	$24,136	$76,313	$47,329
Per Share Data:				
Basic Net Income Available to Common Stockholders	$0.80	$0.57	$1.55	$1.14
Diluted Net Income Available to Common Stockholders	$0.80	$0.57	$1.54	$1.13
Cash Dividends Paid	$0.22	$0.18	$0.40	$0.33
Average Diluted Shares Outstanding (in thousands)	49,451	42,244	49,440	41,735

See NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS.

Table of Contents
PART I. FINANCIAL INFORMATION
ITEM 1. CONSOLIDATED CONDENSED FINANCIAL STATEMENTS
(table dollar amounts in thousands, except share data)

CONSOLIDATED CONDENSED STATEMENTS OF COMPREHENSIVE INCOME
(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2018	2017	2018	2017
Net income	$39,634	$24,136	$76,313	$47,329
Other comprehensive income (loss), net of tax:				
Unrealized holding gain (loss) on securities available for sale arising during the period, net of tax of $683, $3,033, $4,874 and $8,476	(2,570)	5,632	(20,268)	15,741
Unrealized gain on cash flow hedges arising during the period, net of tax of $61, $142, $167 and $131	230	(262)	874	(239)
Reclassification adjustment for net gains included in net income, net of tax of $214, $110, $516 and $226	(803)	(206)	(1,940)	(420)
Defined benefit pension plan amortization of prior service cost, net of tax of $31 and $63	—	(58)	—	(117)
Total other comprehensive income (loss), net of tax	(3,143)	5,106	(21,334)	14,965
Comprehensive income	$36,491	$29,242	$54,979	$62,294

See NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS.

6

Table of Contents
PART I. FINANCIAL INFORMATION
ITEM 1. CONSOLIDATED CONDENSED FINANCIAL STATEMENTS
(table dollar amounts in thousands, except share data)

CONSOLIDATED CONDENSED STATEMENT OF STOCKHOLDERS' EQUITY
(Unaudited)

	Preferred		Common Stock		Additional		Accumulated Other	
	Shares	Amount	Shares	Amount	Paid in Capital	Retained Earnings	Comprehensive Income (Loss)	Total
Balances, December 31, 2017	125	$ 125	49,158,238	$6,145	$834,870	$465,231	$ (2,908)	$1,303,463
Comprehensive income:								
Net income						76,313		76,313
Other comprehensive income (loss), net of tax							(21,334)	(21,334)
Cash dividends on common stock ($.40 per share)						(19,808)		(19,808)
Reclassification adjustment under ASU 2018-02						626	(626)	—
Share-based compensation			98,021	12	1,641			1,653
Stock issued under employee benefit plans			9,205	1	343			344
Stock issued under dividend reinvestment and stock purchase plan			12,111	2	553			555
Stock options exercised			44,932	6	947			953
Stock redeemed			(42,319)	(6)	(1,805)			(1,811)
Balances, June 30, 2018	125	$ 125	49,280,188	$6,160	$836,549	$522,362	$ (24,868)	$1,340,328

See NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS.

Table of Contents
PART I. FINANCIAL INFORMATION
ITEM 1. CONSOLIDATED CONDENSED FINANCIAL STATEMENTS
(table dollar amounts in thousands, except share data)

CONSOLIDATED CONDENSED STATEMENTS OF CASH FLOWS
(Unaudited)

	Six Months ended	
	June 30, 2018	June 30, 2017
Cash Flow From Operating Activities:		
Net income	$76,313	$47,329
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	4,163	5,260
Depreciation and amortization	4,409	3,669
Change in deferred taxes	3,043	3,697
Share-based compensation	1,653	1,061
Loans originated for sale	(178,913)	(127,275)
Proceeds from sales of loans held for sale	186,556	136,014
Gains on sales of loans held for sale	(2,473)	(2,220)
Gains on sales of securities available for sale	(2,731)	(1,165)
Increase in cash surrender of life insurance	(1,985)	(1,715)
Gains on life insurance benefits	(198)	(2,154)
Change in interest receivable	(1,400)	(750)
Change in interest payable	417	123
Other adjustments	(7,132)	(4,379)
Net cash provided by operating activities	81,722	57,495
Cash Flows from Investing Activities:		
Net change in interest-bearing deposits	(1,572)	(23,554)
Purchases of:		
Securities available for sale	(260,786)	(104,956)
Securities held to maturity		(30,220)
Proceeds from sales of securities available for sale	100,293	41,180
Proceeds from maturities of:		
Securities available for sale	36,124	32,838
Securities held to maturity	36,750	36,150
Change in Federal Home Loan Bank stock	(763)	40
Net change in loans	(337,800)	(257,201)
Net cash and cash equivalents received in acquisition		48,528
Proceeds from the sale of other real estate owned	1,746	4,703
Proceeds from life insurance benefits	2,835	5,415
Other adjustments	3,082	(608)
Net cash used in investing activities	(420,091)	(247,685)
Cash Flows from Financing Activities:		
Net change in :		
Demand and savings deposits	291,984	127,901
Certificates of deposit and other time deposits	39,301	79,922
Borrowings	901,407	697,727
Repayment of borrowings	(895,568)	(688,153)

Cash dividends on common stock	(19,808)	(14,001)
Stock issued under employee benefit plans	344	246
Stock issued under dividend reinvestment and stock purchase plans	555	446
Stock options exercised	953	2,082
Stock redeemed	(1,811)	(1,257)
Net cash provided by financing activities	317,357	204,913
Net Change in Cash and Cash Equivalents	(21,012)	14,723
Cash and Cash Equivalents, January 1	154,905	127,927
Cash and Cash Equivalents, June 30	$133,893	$142,650
Additional cash flow information:		
Interest paid	$29,587	$15,235
Income tax paid (refunded)	8,019	10,000
Loans transferred to other real estate owned	252	7,556
Non-cash investing activities using trade date accounting	210	7,759
In conjunction with the acquisitions, liabilities were assumed as follows:		
Fair value of assets acquired		$338,725
Cash paid in acquisition		(4)
Less: Common stock issued		82,588
Liabilities assumed	$—	$256,133

See NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS.

8

PART I. FINANCIAL INFORMATION
ITEM 1. NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS
(table dollar amounts in thousands, except share data)
(Unaudited)

NOTE 1

GENERAL

Financial Statement Preparation

The significant accounting policies followed by the Corporation and its wholly owned subsidiaries for interim financial reporting are consistent with the accounting policies followed for annual financial reporting. All adjustments, which are of a normal recurring nature and are in the opinion of management necessary for a fair statement of the results for the periods reported, have been included in the accompanying Consolidated Condensed Financial Statements.

The Consolidated Condensed Balance Sheet of the Corporation as of December 31, 2017, has been derived from the audited consolidated balance sheet of the Corporation as of that date. Certain information and note disclosures normally included in the Corporation’s annual financial statements, prepared in accordance with accounting principles generally accepted in the United States of America, have been condensed or omitted. These consolidated condensed financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Corporation’s Annual Report on Form 10-K for the year ended December 31, 2017 filed with the Securities and Exchange Commission. The results of operations for the three and six months ended June 30, 2018, are not necessarily indicative of the results to be expected for the year. Reclassifications have been made to prior financial statements to conform to the current financial statement presentation. These reclassifications had no effect on net income.

Recent Accounting Changes

ASU 2018-02 "Income Statement - Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income" ("ASU 2018-02") allows a reclassification from accumulated other comprehensive income (loss) to retained earnings for the stranded tax effects caused by the revaluation of deferred taxes resulting from the newly enacted corporate tax rate in the Tax Cuts and Jobs Act. The ASU is effective in years beginning after December 15, 2018, but permits early adoption in a period for which financial statements have not yet been issued. The Corporation elected to early adopt the ASU as of January 1, 2018. The adoption of the guidance resulted in an insignificant cumulative-effect adjustment that decreased accumulated other comprehensive income (loss) and increased retained earnings in the first quarter of 2018.

ASU 2017-07 "Compensation - Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost" ("ASU 2017-07") applies to all employers, including not-for-profit entities, that offer to their employees defined benefit pension plans, other postretirement benefit plans, or other types of benefits accounted for under Topic 715, Compensation - Retirement Benefits. The amendments require that an employer report the service cost component in the same line item or items as other compensation costs arising from services rendered by the pertinent employees during the period. The other components of net benefit cost are required to be presented in the income statement separately from the service cost component and outside a subtotal of income from operations, if one is presented. If a separate line item or items are used to present the other components of net benefit cost, that line item or items must be appropriately described. If a separate line item or items are not used, the line item or items used in the income statement to present the other components of net benefit cost must be disclosed. The amendments also allow only the service cost component to be eligible for capitalization when applicable (e.g., as a cost of internally manufactured inventory or a self-constructed asset). The amendments are effective for public business entities for annual periods beginning after December 15, 2017, including interim periods within those annual periods. For other entities, the amendments are effective for annual periods beginning after December 15, 2018, and interim periods within annual periods beginning after December 15, 2019. Early adoption is permitted as of the beginning of an annual period for which financial statements (interim or annual) have not been issued or made available for issuance. The Corporation adopted this ASU in the first quarter of 2018. It did not have a significant impact on the Corporation’s consolidated financial statements.

ASU 2016-15 "Statement of Cash Flows (Topic 230)" ("ASU 2016-15") is intended to reduce the diversity in practice around how certain transactions are classified within the statement of cash flows. ASU 2016-15 became effective for the Corporation on January 1, 2018 and did not have a significant impact on the Corporation's financial statements.

ASU 2016-01 "Financial Instruments - Overall (Subtopic 825-10): Recognition of Financial Assets and Financial Liabilities" ("ASU 2016-01") makes targeted amendments to the guidance for recognition, measurement, presentation and disclosure of financial instruments. ASU 2016-01 requires equity investments, other than equity method investments, to be measured at fair value with changes in fair value recognized in net income. The ASU requires a cumulative-effect adjustment to retained earnings as of the beginning of the reporting period of adoption to reclassify the cumulative change in fair value of equity securities previously recognized in accumulated other comprehensive income (loss). ASU 2016-01 became effective for the Corporation on January 1, 2018. The adoption of the guidance did not result in any cumulative effect adjustment in the first quarter of 2018. ASU 2016-01 also emphasizes the existing requirement to use exit prices to measure fair value for disclosure purposes and clarifies that entities should not make use of a practicability exception in determining the fair value of loans. Accordingly, the Corporation refined the calculation used to determine the disclosed fair value of loans held for investment as part of adopting this standard. The refined calculation did not have a significant impact on the fair value disclosures included in NOTE 9. DISCLOSURES ABOUT FAIR VALUE OF ASSETS AND LIABILITIES of these Notes to Consolidated Condensed Financial Statements.

ASU 2014-09 "Revenue from Contracts with Customers (Topic 606)" ("ASU 2014-09") implements a common revenue standard that clarifies the principles for recognizing revenue. The core principle of ASU 2014-09 is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. ASU 2014-09 establishes a five-step model which entities must follow to recognize revenue and removes inconsistencies and weaknesses in existing guidance. The guidance does not apply to revenue associated with financial instruments, including loans and investment securities that are accounted for under other GAAP, which comprises a significant portion of our revenue stream. ASU 2014-09 became effective for the Corporation on January 1, 2018. The adoption of ASU 2014-09 did not result in a change to the accounting for any of the in-scope revenue streams; as such, no cumulative effect adjustment was recorded. Additional information related to revenue generated from contracts with customers is detailed below.

Revenue Recognition

ASU 2014-09 establishes principles for reporting information about the nature, amount, timing and uncertainty of revenue and cash flows arising from the entity's contracts to provide goods or services to customers. The core principle requires an entity to recognize revenue to depict the transfer of goods or services to customers in an amount that reflects the consideration that it expects to be entitled to receive in exchange for those goods or services recognized as performance obligations are satisfied.

The majority of the Corporation's revenue-generating transactions are not subject to ASU 2014-09, including revenue generated from financial instruments, such as loans, letters of credit, derivatives and investment securities, as well as revenue related to mortgage servicing activities, as these activities are subject to other GAAP discussed elsewhere within the disclosures. The Corporation has evaluated the nature of its contracts with customers and determined that further disaggregation of revenue from contracts with customers into more granular categories beyond what is presented in the Consolidated Condensed Statements of Income was not necessary. Descriptions of revenue-generating activities that are within the scope of ASU 2014-09, which are presented in our income statements are as follows:

Service charges on deposit accounts: The Corporation earns fees from its deposit customers for transaction-based, account maintenance and overdraft services. Transaction-based fees, which include services such as ATM use fees, stop payment charges, statement rendering and ACH fees, are recognized at the time the transaction is executed, which is the point in time the Corporation fulfills the customer's request. Account maintenance fees, which relate primarily to monthly maintenance, are earned monthly, representing the period which the Corporation satisfies the performance obligation. Overdraft fees are recognized at the point in time that the overdraft occurs. Service charges on deposits are withdrawn from the customer's account balance.

Fiduciary activities: This represents monthly fees due from wealth management customers as consideration for managing the customers' assets. Wealth management and trust services include custody of assets, investment management, fees for trust services and similar fiduciary activities. These fees are primarily earned over time as the Corporation provides the contracted monthly or quarterly services and are generally assessed based on the market value of assets under management at month-end. Fees that are transaction-based are recognized at the point in time that the transaction is executed.

Investment Brokerage Fees: The Corporation earns fees from investment brokerage services provided to its customers by a third-party service provider. The Corporation receives commissions from the third-party provider on a monthly basis based upon customer activity for the month. The fees are paid to us by the third party on a monthly basis and are recognized when received.

Interchange income: The Corporation earns interchange fees from debit and credit cardholder transactions conducted through the Visa and MasterCard payment networks. Interchange fees from cardholder transactions represent a percentage of the underlying transaction value and are recognized concurrent with the transaction processing services provided to the cardholder.

Gains (Losses) on Sales of OREO: The Corporation records a gain or loss from the sale of OREO when control of the property transfers to the buyer, which generally occurs at the time of an executed deed. When the Corporation finances the sale of OREO to the buyer, the Corporation assesses whether the buyer is committed to perform their obligations under the contract and whether collectability of the transaction price is probable. Once these criteria are met, the OREO asset is derecognized and the gain or loss on sale is recorded upon the transfer of control of the property to the buyer. In determining the gain or loss on the sale, the Corporation adjusts the transaction price and related gain (loss) on sale if a significant financing component is present.

NOTE 2

ACQUISITIONS

Independent Alliance Banks, Inc.

On November 21, 2016, the Corporation purchased 495,112 shares, or 12.1 percent, of IAB's outstanding common stock from an IAB shareholder for $19.8 million, or $40.00 per share. On July 14, 2017, the Corporation acquired the remaining shares of IAB common stock. IAB, an Indiana Corporation, merged with and into the Corporation, whereupon the separate corporate existence of IAB ceased and the Corporation survived. Immediately following the merger, IAB's wholly-owned subsidiary, iAB Financial Bank, merged with and into the Bank, with the Bank continuing as the surviving bank.

(table dollar amounts in thousands, except share data)

IAB was headquartered in Fort Wayne, Indiana and had 16 banking centers serving the Fort Wayne market. Pursuant to the merger agreement, each IAB shareholder received 1.653 shares of the Corporation's common stock for each outstanding share of IAB common stock held. The Corporation issued approximately 6.0 million shares of common stock. The transaction value for the remaining shares of common stock, not owned by the Corporation, was approximately $238.8 million, resulting in a total purchase price of $258.6 million. The Corporation engaged in this transaction with the expectation that it would be accretive to income and add a new market area with a demographic profile consistent with many of the current Indiana markets served by the Bank. Goodwill resulted from this transaction due to the expected synergies and economies of scale.

In the third quarter of 2017, ASC 805-10 - Business Combinations, required the Corporation to remeasure the 12.1 percent equity interest in IAB's common stock and recognize the resulting gain or loss, if any, in earnings. The remeasurement was based upon the closing price of IAB's common stock immediately prior to the acquisition announcement, and prior to the Corporation obtaining control of IAB. The trading price of IAB's common stock subsequent to the acquisition announcement included a control or acquisition premium and was not indicative of the fair value of the Corporation's pre-existing equity interest immediately prior to the acquisition announcement. The fair value of the equity interest in IAB's common stock after the remeasurement was $19.8 million. The Corporation recorded a $50,000 loss in the third quarter of 2017 as a result of the remeasurement.

Under the acquisition method of accounting, the total purchase price is allocated to net tangible and intangible assets based on their current estimated fair values on the date of the acquisition. Based on valuations of the fair value of tangible and intangible assets acquired and liabilities assumed, which are based on assumptions that are subject to change, the purchase price for the IAB acquisition is detailed in the following table.

	Fair Value
Cash and cash equivalents	$6,016
Interest-bearing time deposits	248,212
Investment securities	4,078
Loans held for sale	594
Loans	725,382
Premises and equipment	10,107
Federal Home Loan Bank stock	4,810
Interest receivable	3,445
Cash surrender value of life insurance	26,964
Other assets	11,780
Deposits	(862,271)
Securities sold under repurchase agreements	(17,915)
Federal Home Loan Bank Advances	(47,575)
Subordinated debentures	(10,583)
Interest payable	(1,005)
Other liabilities	(14,472)
Net tangible assets acquired	87,567
Other Intangible assets	17,403
Goodwill	153,636

Purchase price	$258,606

Of the total purchase price, $17,403,000 has been allocated to other intangible assets. Approximately $13.6 million was allocated to a core deposit intangible, which will be amortized over its estimated life of 10 years. Approximately $3.8 million was allocated to a non-compete intangible, which will be amortized over its estimated life of 2 years. The remaining purchase price has been allocated to goodwill, which is not deductible for tax purposes.

Acquired loan data for IAB can be found in the table below:

	Fair Value of Acquired Loans at Acquisition Date	Gross Contractual Amounts Receivable at Acquisition Date	Best Estimate at Acquisition Date of Contractual Cash Flows Not Expected to be Collected
Acquired receivables subject to ASC 310-30	$ 4,838	$ 14,131	$ 8,352
Acquired receivables not subject to ASC 310-30	$ 720,544	$ 864,613	$ 9,786

Purchased loans with evidence of credit deterioration since origination and for which it is probable at the date of acquisition that the acquirer will not collect all contractually required principal and interest payments are accounted for under ASC 310-30, Loans Acquired with Deteriorated Credit Quality. The difference between contractually required payments and the cash flows expected to be collected at acquisition is referred to as the nonaccretable difference. The accretable portion of the fair value discount or premium is the difference between the expected cash flows and the net present value of expected cash flows, with such difference accreted into earnings over the term of the loans.

PART I. FINANCIAL INFORMATION
ITEM 1. NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS
(table dollar amounts in thousands, except share data)
(Unaudited)

The Arlington Bank

On May 19, 2017, the Corporation acquired 100 percent of Arlington Bank. Arlington Bank, an Ohio savings bank, merged with and into the Bank, with the Bank continuing as the surviving bank. Arlington Bank was headquartered in Columbus, Ohio and had 3 banking centers serving the Columbus, Ohio market. Pursuant to the merger agreement, each Arlington Bank shareholder received 2.7245 shares of the Corporation's common stock for each outstanding share of Arlington Bank common stock held. The Corporation issued approximately 2.1 million shares of common stock, which was valued at approximately $82.6 million. The Corporation engaged in this transaction with the expectation that it would be accretive to income and expand the existing footprint in Columbus, Ohio. Goodwill resulted from this transaction due to the expected synergies and economies of scale.

Under the acquisition method of accounting, the total purchase price is allocated to net tangible and intangible assets based on their current estimated fair values on the date of the acquisition. Based on valuations of the fair value of tangible and intangible assets acquired and liabilities assumed, which are based on assumptions that are subject to change, the purchase price for the Arlington Bank acquisition is detailed in the following table.

	Fair Value
Cash and cash equivalents	$48,532
Interest-bearing time deposits	292
Loans held for sale	7,626
Loans	224,680
Premises and equipment	1,986
Federal Home Loan Bank stock	1,091
Interest receivable	653
Other assets	1,620
Deposits	(252,783)
Interest payable	(244)
Other liabilities	(3,106)
Net tangible assets acquired	30,347
Core deposit intangible	4,526
Goodwill	47,719
Purchase price	$82,592

Of the total purchase price, $4,526,000 has been allocated to a core deposit intangible that will be amortized over its estimated life of 10 years. The remaining purchase price has been allocated to goodwill, which is not deductible for tax purposes.

Acquired loan data for Arlington Bank can be found in the table below:

	Fair Value of Acquired Loans at	Gross Contractual Amounts	Best Estimate at Acquisition

	Acquisition Date	Receivable at Acquisition Date	Date of Contractual Cash Flows Not Expected to be Collected
Acquired receivables subject to ASC 310-30	$ 2,625	$ 6,183	$ 2,891
Acquired receivables not subject to ASC 310-30	$ 222,055	$ 308,857	$ 2,741

Pro Forma Financial Information

The results of operations of Arlington Bank and IAB have been included in the Corporation's consolidated financial statements since the acquisition dates. The following schedule includes pro forma results for the year ended December 31, 2017, as if the Arlington Bank and IAB acquisitions occurred as of the beginning of the period presented.

	2017
Total revenue (net interest income plus other income)	$380,324
Net income	$95,009
Net income available to common shareholders	
Earnings per share:	
Basic	$1.94
Diluted	$1.93

(table dollar amounts in thousands, except share data)

The pro forma information includes adjustments for interest income on loans, interest expense on deposits and borrowings, premises expense for banking centers acquired and amortization of intangibles arising from the transaction and the related income tax effects. The pro forma information for the year ended December 31, 2017 includes operating revenue of $9.0 million and $21.4 million from the Arlington Bank and IAB acquisitions since the date of acquisition, respectively. Additionally, $15.4 million, net of tax, of expenses directly attributable to the Arlington Bank and IAB acquisitions were included in the year ended December 31, 2017 pro forma information. The pro forma information is presented for information purposes only and is not indicative of the results of operations that actually would have been achieved had the acquisitions been consummated as of that time, nor is it intended to be a projection of future results.

NOTE 3

INVESTMENT SECURITIES

The amortized cost, gross unrealized gains, gross unrealized losses and approximate market value of the Corporation's investment securities at the dates indicated were:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available for sale at June 30, 2018				
U.S. Government-sponsored agency securities	$11,491	$ 4	$ 23	$11,472
State and municipal	546,737	5,555	7,419	544,873
U.S. Government-sponsored mortgage-backed securities	553,187	258	12,984	540,461
Corporate obligations	31			31
Total available for sale	1,111,446	5,817	20,426	1,096,837
Held to maturity at June 30, 2018				
U.S. Government-sponsored agency securities	22,618		755	21,863
State and municipal	225,084	2,626	955	226,755
U.S. Government-sponsored mortgage-backed securities	274,144	586	4,699	270,031
Foreign Investments	1,000		6	994
Total held to maturity	522,846	3,212	6,415	519,643
Total Investment Securities	$1,634,292	$ 9,029	$ 26,841	$1,616,480

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available for sale at December 31, 2017				
State and municipal	$510,852	$ 16,932	$ 1,091	$526,693
U.S. Government-sponsored mortgage-backed securities	473,325	964	3,423	470,866
Corporate obligations	31			31
Equity securities	2,357			2,357

Total available for sale	986,565	17,896	4,514	999,947
Held to maturity at December 31, 2017				
U.S. Government-sponsored agency securities	22,618		435	22,183
State and municipal	235,594	6,295	244	241,645
U.S. Government-sponsored mortgage-backed securities	301,443	3,341	1,404	303,380
Foreign Investment	1,000			1,000
Total held to maturity	560,655	9,636	2,083	568,208
Total Investment Securities	$1,547,220	$ 27,532	$ 6,597	$1,568,155

The amortized cost and fair value of available for sale and held to maturity securities at June 30, 2018 and December 31, 2017, by contractual maturity, are shown below. Expected maturities will differ from contractual maturities because issuers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Available for Sale		Held to Maturity	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Maturity Distribution at June 30, 2018:				
Due in one year or less	$545	$548	$24,829	$25,203
Due after one through five years	9,984	10,051	59,713	59,075
Due after five through ten years	79,118	80,457	53,004	53,453
Due after ten years	468,612	465,320	111,156	111,881
	558,259	556,376	248,702	249,612
U.S. Government-sponsored mortgage-backed securities	553,187	540,461	274,144	270,031
Total Investment Securities	$1,111,446	$1,096,837	$522,846	$519,643

PART I. FINANCIAL INFORMATION
ITEM 1. NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS
(table dollar amounts in thousands, except share data)
(Unaudited)

	Available for Sale		Held to Maturity	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Maturity Distribution at December 31, 2017				
Due in one year or less	$425	$425	$12,015	$12,158
Due after one through five years	5,040	5,204	76,146	76,334
Due after five through ten years	74,921	78,806	54,441	55,679
Due after ten years	430,497	442,289	116,610	120,657
	510,883	526,724	259,212	264,828
U.S. Government-sponsored mortgage-backed securities	473,325	470,866	301,443	303,380
Equity securities	2,357	2,357		
Total Investment Securities	$986,565	$999,947	$560,655	$568,208

The carrying value of securities pledged as collateral, to secure borrowings and for other purposes, was $484,218,000 at June 30, 2018, and $475,999,000 at December 31, 2017 .

The book value of securities sold under agreements to repurchase amounted to $125,412,000 at June 30, 2018, and $136,639,000 at December 31, 2017.

Gross gains on the sales and redemptions of available for sale securities for the three and six months ended June 30, 2018 and 2017 are shown below.

	Three Months Ended June 30,		Six Months Ended June 30,	
	2018	2017	2018	2017
Sales and Redemptions of Available for Sale Securities:				
Gross gains	$1,122	$567	$2,731	$1,165
Gross losses				

The following tables show the Corporation's gross unrealized losses and fair value, aggregated by investment category and length of time the individual securities have been in a continuous unrealized loss position at June 30, 2018, and December 31, 2017:

	Less than 12 Months		12 Months or Longer		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
Temporarily Impaired Available for Sale Securities at June 30, 2018						

U.S. Government-sponsored agency securities	$6,468	$ 23			$6,468	$ 23
State and municipal	252,460	5,573	$28,187	$ 1,846	280,647	7,419
U.S. Government-sponsored mortgage-backed securities	410,442	9,466	62,943	3,518	473,385	12,984
Total Temporarily Impaired Available for Sale Securities	669,370	15,062	91,130	5,364	760,500	20,426
Temporarily Impaired Held to Maturity Securities at June 30, 2018						
U.S. Government-sponsored agency securities	9,834	285	12,029	470	21,863	755
State and municipal	23,507	339	15,021	616	38,528	955
U.S. Government-sponsored mortgage-backed securities	171,516	2,878	38,947	1,821	210,463	4,699
Corporate Obligations	994	6			994	6
Total Temporarily Impaired Held to Maturity Securities	205,851	3,508	65,997	2,907	271,848	6,415
Total Temporarily Impaired Investment Securities	$875,221	$ 18,570	$157,127	$ 8,271	$1,032,348	$ 26,841

	Less than 12 Months		12 Months or Longer		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
Temporarily Impaired Available for Sale Securities at December 31, 2017						
State and municipal	$13,296	$ 198	$35,324	$ 893	$48,620	$ 1,091
U.S. Government-sponsored mortgage-backed securities	182,755	1,520	68,667	1,903	251,422	3,423
Total Temporarily Impaired Available for Sale Securities	196,051	1,718	103,991	2,796	300,042	4,514
Temporarily Impaired Held to Maturity Securities at December 31, 2017						
U.S. Government-sponsored agency securities	9,988	131	12,196	304	22,184	435
State and municipal	2,430	36	15,805	208	18,235	244
U.S. Government-sponsored mortgage-backed securities	62,508	485	43,078	919	105,586	1,404
Total Temporarily Impaired Held to Maturity Securities	74,926	652	71,079	1,431	146,005	2,083
Total Temporarily Impaired Investment Securities	$270,977	$ 2,370	$175,070	$ 4,227	$446,047	$ 6,597

(table dollar amounts in thousands, except share data)

Certain investments in debt and equity securities are reported in the financial statements at an amount less than their historical cost as indicated in the table below.

	June 30, 2018	December 31, 2017
Investments reported at less than historical cost:		
Historical cost	$ 1,059,191	$ 452,644
Fair value	$ 1,032,348	$ 446,047
Percent of the Corporation's investment portfolio	63.7 %	28.6 %

Except as discussed below, management believes the decline in fair value for these securities was temporary. Should the impairment of any of these securities become other-than-temporary, the cost basis of the investment will be reduced and the resulting loss recognized in net income during the period the OTTI is identified.

The Corporation’s management has evaluated all securities with unrealized losses for OTTI as of June 30, 2018. The evaluations are based on the nature of the securities, the extent and duration of the loss and the intent and ability of the Corporation to hold these securities either to maturity or through the expected recovery period.

In determining the fair value of the investment securities portfolio, the Corporation utilizes a third party for portfolio accounting services, including market value input, for those securities classified as Level 1 and Level 2 in the fair value hierarchy. The Corporation has obtained an understanding of what inputs are being used by the vendor in pricing the portfolio and how the vendor classified these securities based upon these inputs. From these discussions, the Corporation’s management is comfortable that the classifications are proper. The Corporation has gained trust in the data for two reasons: (a) independent spot testing of the data is conducted by the Corporation through obtaining market quotes from various brokers on a periodic basis; and (b) actual gains or loss resulting from the sale of certain securities has proven the data to be accurate over time. Fair value of securities classified as Level 3 in the valuation hierarchy was determined using a discounted cash flow model that incorporated market estimates of interest rates and volatility in markets that have not been active.

State and Municipal and U.S. Government-Sponsored Agency Securities

The unrealized losses on the Corporation's investments in securities of state and political subdivisions and U.S. Government-Sponsored Agency securities were caused by interest rate increases. The contractual terms of those investments do not permit the issuer to settle the securities at a price less than the amortized cost basis of the investments. Because the Corporation does not intend to sell the investments and it is not more likely than not that the Corporation will be required to sell the investments before recovery of their amortized cost basis, which may be maturity, the Corporation does not consider those investments to be other-than-temporarily impaired at June 30, 2018. The state and municipal securities portfolio contains unrealized losses of $7,419,000 on two hundred twenty-three securities and $955,000 on forty-eight securities in the available for sale and held to maturity portfolios, respectively. The U.S. Government-Sponsored Agency securities portfolio contains unrealized losses of $23,000 on five securities and $755,000 on five securities in the available for sale and held to maturity portfolios, respectively.

U.S. Government-Sponsored Mortgage-Backed Securities

The unrealized losses on the Corporation's investment in mortgage-backed securities were a result of interest rate changes. The Corporation expects to recover the amortized cost basis over the term of the securities. Because the decline in market value is attributable to changes in interest rates and not credit quality, and because the Corporation does not intend to sell the investments and it is not more likely than not that the Corporation will be required to sell the investments before recovery of their amortized cost basis, which may be maturity, the Corporation does not consider those investments to be other-than-temporarily impaired at June 30, 2018. The mortgage-backed securities portfolio contains unrealized losses of $12,984,000 on one hundred fourteen securities and $4,699,000 on eighty securities in the available for sale and held to maturity portfolios, respectively. All these securities are issued by a U.S. government-sponsored entity.

NOTE 4

LOANS AND ALLOWANCE

The Corporation’s primary lending focus is small business and middle market commercial, commercial real estate and residential real estate, which results in portfolio diversification. The following tables show the composition of the loan portfolio, the allowance for loan losses and credit quality characteristics by collateral classification, excluding loans held for sale. Loans held for sale as of June 30, 2018, and December 31, 2017, were $2,046,000 and $7,216,000, respectively.

Table of Contents
PART I. FINANCIAL INFORMATION
ITEM 1. NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS
(table dollar amounts in thousands, except share data)
(Unaudited)

The following table illustrates the composition of the Corporation's loan portfolio by loan class for the periods indicated:

	June 30, 2018	December 31, 2017
Commercial and industrial loans	$1,657,591	$1,493,493
Agricultural production financing and other loans to farmers	89,093	121,757
Real estate loans:		
Construction	714,866	612,219
Commercial and farmland	2,652,782	2,562,691
Residential	965,720	962,765
Home equity	518,699	514,021
Individuals' loans for household and other personal expenditures	92,809	86,935
Lease financing receivables, net of unearned income	1,945	2,527
Other commercial loans	387,554	394,791
Loans	$7,081,059	$6,751,199
Allowance for loan losses	(77,543)	(75,032)
Net Loans	$7,003,516	$6,676,167

Allowance, Credit Quality and Loan Portfolio

The Corporation maintains an allowance for loan losses to cover probable credit losses identified during its loan review process. Management believes the allowance for loan losses is adequate to cover probable losses inherent in the loan portfolio at June 30, 2018. The process for determining the adequacy of the allowance for loan losses is critical to the Corporation's financial results. It requires management to make difficult, subjective and complex judgments to estimate the effect of uncertain matters. The allowance for loan losses considers current factors, including economic conditions and ongoing internal and external examinations, and will increase or decrease as deemed necessary to ensure it remains adequate. In addition, the allowance as a percentage of charge-offs and nonperforming loans will change at different points in time based on credit performance, portfolio mix and collateral values.

The allowance for loan losses is maintained through the provision for loan losses, which is a charge against earnings. The allowance is increased by provision expense and decreased by charge-offs less recoveries. All charge-offs are approved by the Bank's senior credit officers and in accordance with established policies. The Bank charges off a loan when a determination is made that all or a portion of the loan is uncollectable. The amount provided for loan losses in a given period may be greater than or less than net loan losses experienced during the period, and is based on management's judgment as to the appropriate level of the allowance for loan losses. The determination of the provision amount is based on management's ongoing review and evaluation of the loan portfolio, including an internally administered loan "watch" list and independent loan reviews. The evaluation takes into consideration identified credit problems, the possibility of losses inherent in the loan portfolio that are not specifically identified and management's judgment as to the impact of the current environment and economic conditions on the portfolio.

The allowance consists of specific impairment reserves as required by ASC 310-10-35, a component for historical losses in accordance with ASC 450 and the consideration of current environmental factors in accordance with ASC 450. A loan is deemed impaired when, based on current information or events, it is probable that all amounts due of principal and interest according to the contractual terms of the loan agreement will not be collected.

The historical loss allocation for loans not deemed impaired according to ASC 450 is the product of the volume of loans within the non-impaired criticized and non-criticized risk grade classifications, each segmented by call code, and the historical loss factor for each respective classification and call code segment. The historical loss factors are based upon actual loss experience within each risk and call code classification. The historical look back period for non-criticized loans looks to the most recent rolling-four-quarter average and aligns with the look back period for non-impaired criticized loans. Each of the rolling four quarter periods used to obtain the average, include all charge-offs for the previous twelve-month period, therefore the historical look back period includes seven quarters. The resulting allocation is reflective of current conditions. Criticized loans are grouped based on the risk grade assigned to the loan. Loans with a special mention grade are assigned a loss factor, and loans with a classified grade but not impaired are assigned a separate loss factor. The loss factor computation for this allocation includes a segmented historical loss migration analysis of risk grades to charge-off.

In addition to the specific reserves and historical loss components of the allowance, consideration is given to various environmental factors to ensure that losses inherent in the portfolio are reflected in the allowance for loan losses. The environmental component adjusts the historical loss allocations for non-impaired loans to reflect relevant current conditions that, in management's opinion, have an impact on loss recognition. Environmental factors that management reviews in the analysis include: national and local economic trends and conditions; trends in growth in the loan portfolio and growth in higher risk areas; levels of, and trends in, delinquencies and non-accruals; experience and depth of lending management and staff; adequacy of, and adherence to, lending policies and procedures including those for underwriting; industry concentrations of credit; and adequacy of risk identification systems and controls through the internal loan review and internal audit processes.

PART I. FINANCIAL INFORMATION
ITEM 1. NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS
(table dollar amounts in thousands, except share data)
(Unaudited)

In conformance with ASC 805 and ASC 820, purchased loans are recorded at the acquisition date fair value. Such loans are included in the allowance to the extent a specific impairment is identified that exceeds the fair value adjustment on an impaired loan or the historical loss and environmental factor analysis indicates losses inherent in a purchased portfolio exceeds the fair value adjustment on the portion of the purchased portfolio not deemed impaired.

The following tables summarize changes in the allowance for loan losses by loan segment for the three and six months ended June 30, 2018 and June 30, 2017:

	Three Months Ended June 30, 2018					
	Commercial	Commercial Real Estate	Consumer	Residential	Finance Leases	Total
Allowance for loan losses:						
Balances, March 31, 2018	$30,768	$ 27,705	$ 3,896	$ 14,049	$ 2	$76,420
Provision for losses	471	954	60	178		1,663
Recoveries on loans	1,283	1,213	98	596		3,190
Loans charged off	(1,057)	(2,141)	(133)	(399)		(3,730)
Balances, June 30, 2018	$31,465	$ 27,731	$ 3,921	$ 14,424	$ 2	$77,543

	Six Months Ended June 30, 2018					
	Commercial	Commercial Real Estate	Consumer	Residential	Finance Leases	Total
Allowance for loan losses:						
Balances, December 31, 2017	$30,418	$ 27,343	$ 3,732	$ 13,537	$ 2	$75,032
Provision for losses	1,311	1,038	334	1,480		4,163
Recoveries on loans	1,402	1,552	187	750		3,891
Loans charged off	(1,666)	(2,202)	(332)	(1,343)		(5,543)
Balances, June 30, 2018	$31,465	$ 27,731	$ 3,921	$ 14,424	$ 2	$77,543

	Three Months Ended June 30, 2017					
	Commercial	Commercial Real Estate	Consumer	Residential	Finance Leases	Total
Allowance for loan losses:						
Balances, March 31, 2017	$28,524	$ 24,320	$ 3,120	$ 12,259	$ 2	$68,225
Provision for losses	161	1,402	286	1,026		2,875
Recoveries on loans	297	175	101	153		726
Loans charged off	(76)	(661)	(135)	(483)		(1,355)
Balances, June 30, 2017	$28,906	$ 25,236	$ 3,372	$ 12,955	$ 2	$70,471

	Six Months Ended June 30, 2017					
	Commercial	Commercial Real Estate	Consumer	Residential	Finance Leases	Total
Allowance for loan losses:						
Balances, December 31, 2016	$27,696	$ 23,661	$ 2,923	$ 11,755	$ 2	$66,037
Provision for losses	1,358	1,649	535	1,718		5,260
Recoveries on loans	663	739	202	390		1,994
Loans charged off	(811)	(813)	(288)	(908)		(2,820)

Balances, June 30, 2017	$28,906	$ 25,236	$ 3,372	$ 12,955	$ 2	$70,471

Table of Contents
PART I. FINANCIAL INFORMATION
ITEM 1. NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS
(table dollar amounts in thousands, except share data)
(Unaudited)

The tables below show the Corporation’s allowance for loan losses and loan portfolio by loan segment as of the periods indicated. There was no related allowance for loan losses for loans acquired with deteriorated credit quality at June 30, 2018 or December 31, 2017.

	June 30, 2018					
	Commercial	Commercial Real Estate	Consumer	Residential	Finance Leases	Total
Allowance Balances:						
Individually evaluated for impairment	$76			$421		$497
Collectively evaluated for impairment	31,389	27,731	$ 3,921	14,003	$ 2	77,046
Total Allowance for Loan Losses	$31,465	$27,731	$ 3,921	$14,424	$ 2	$77,543
Loan Balances:						
Individually evaluated for impairment	$1,746	$10,251	$ 10	$2,069		$14,076
Collectively evaluated for impairment	2,129,626	3,338,815	92,799	1,480,769	$ 1,945	7,043,954
Loans acquired with deteriorated credit quality	2,866	18,582		1,581		23,029
Loans	$2,134,238	$3,367,648	$ 92,809	$1,484,419	$ 1,945	$7,081,059

	December 31, 2017					
	Commercial	Commercial Real Estate	Consumer	Residential	Finance Leases	Total
Allowance Balances:						
Individually evaluated for impairment	$666	$567		$404		$1,637
Collectively evaluated for impairment	29,752	26,776	$ 3,732	13,133	$ 2	73,395
Total Allowance for Loan Losses	$30,418	$27,343	$ 3,732	$13,537	$ 2	$75,032
Loan Balances:						
Individually evaluated for impairment	$3,345	$17,432	$ 5	$2,429		$23,211
Collectively evaluated for impairment	2,005,275	3,135,481	86,930	1,472,821	$ 2,527	6,703,034
Loans acquired with deteriorated credit quality	1,421	21,997		1,536		24,954
Loans	$2,010,041	$3,174,910	$ 86,935	$1,476,786	$ 2,527	$6,751,199

Loans individually evaluated for impairment are comprised of commercial and consumer loans deemed impaired in accordance with ASC 310-10 and include loans acquired with deteriorated credit quality totaling $268,000 and $315,000 at June 30, 2018 and December 31, 2017, respectively.

The risk characteristics of the Corporation’s material portfolio segments are as follows:

Commercial

Commercial lending is primarily based on the identified cash flows of the borrower and secondarily on the underlying collateral provided by the borrower. The cash flows of borrowers, however, may not be as expected and the collateral securing these loans may fluctuate in value. Most commercial loans are secured by the tangible assets being financed such as equipment or real estate or other business assets such as accounts receivable or inventory and may incorporate a personal guarantee. Other loans may be unsecured, secured but under-collateralized or otherwise made on the basis of the enterprise value of an organization. In the case of loans secured by accounts receivable, the availability of funds for the repayment of these loans may be substantially dependent on the ability of the borrower to collect amounts due from its customers.

Commercial real estate

These loans are viewed primarily as cash flow loans and secondarily as loans secured by real estate. Commercial real estate lending typically involves higher loan principal amounts and the repayment of these loans is generally dependent on the successful operation of the property securing the loan or the business conducted on the property securing the loan. Commercial real estate loans may be more adversely affected by conditions in the real estate markets or in the general economy. Management monitors and evaluates commercial real estate loans based on collateral and risk grade criteria. In addition, management tracks the level of owner-occupied commercial real estate loans versus non-owner occupied loans.

(table dollar amounts in thousands, except share data)

Consumer and Residential

With respect to residential loans that are secured by 1-4 family residences and are typically owner occupied, the Corporation generally establishes a maximum loan-to-value ratio and requires private mortgage insurance if that ratio is exceeded. Home equity loans are secured by a subordinate interest in 1-4 family residences, and consumer loans are secured by consumer assets such as automobiles or recreational vehicles. Some consumer loans are unsecured such as small installment loans and certain lines of credit. Repayment of these loans is primarily dependent on the personal income and credit rating of the borrowers, which can be impacted by economic conditions in their market areas such as unemployment levels. Repayment on loans secured by 1-4 family residences can be impacted by changes in property values. Risk is mitigated by the fact that the loans are of smaller individual amounts and spread over a large number of borrowers.

Loans are reclassified to a non-accruing status when, in management's judgment, the collateral value and financial condition of the borrower do not justify accruing interest. When the interest accrual is discontinued, all unpaid accrued interest is reversed against earnings when considered uncollectable. Payments subsequently received on non-accrual loans are applied to principal. A loan is returned to accrual status when principal and interest are no longer past due and collectability is probable, typically after a minimum of six consecutive months of performance. Payments received on impaired accruing or delinquent loans are applied to interest income as accrued.

The following table summarizes the Corporation's non-accrual loans by loan class as of the periods indicated:

	June 30, 2018	December 31, 2017
Commercial and industrial loans	$2,736	$ 3,275
Agriculture production financing and other loans to farmers	640	1,027
Real estate loans:		
Construction	695	65
Commercial and farmland	9,431	12,951
Residential	5,522	9,444
Home equity	1,082	1,928
Individuals' loans for household and other personal expenditures	37	34
Total	$20,143	$ 28,724

Impaired loans include loans deemed impaired according to the guidance set forth in ASC 310-10. Commercial loans under $500,000 and consumer loans, with the exception of troubled debt restructures, are not individually evaluated for impairment.

Allowable methods for determining the amount of impairment include estimating fair value using the fair value of the collateral for collateral dependent loans. If the impaired loan is identified as collateral dependent, then the fair value method for measuring the amount of impairment is utilized. This method requires obtaining a current independent appraisal of the collateral and applying a discount factor, which includes selling costs if applicable,