GUARANTY FEDERAL BANCSHARES INC
Form 10-Q
May 14, 2018

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM 10-Q

(Mark One) [X] **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended March 31, 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 0-23325

Guaranty Federal Bancshares, Inc.

(Exact name of registrant as specified in its charter)

Delaware	**43-1792717**
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification No.)
2144 E Republic Rd, Suite F200 **Springfield, Missouri**	**65804**
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code: (417) 520-4333

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 (§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 definitions of “large accelerated filer”, “accelerated filer”, “smaller reporting company” and “emerging growth company” in Rule 12b-2 of the Exchange Act. Large accelerated filer [ ] Accelerated filer [ ] Non-accelerated filer [ ] Smaller reporting company [X] Emerging growth company [ ]

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period of 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]

Indicate the number of shares outstanding of each of the issuer’s classes of common stock, as of the latest practicable date.

Class	Outstanding as of May 7, 2018
Common Stock, Par Value $0.10 per share	4,447,257 Shares

GUARANTY FEDERAL BANCSHARES, INC.

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PART I FINANCIAL INFORMATION

Item 1. Financial Statements

GUARANTY FEDERAL BANCSHARES, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
MARCH 31, 2018 (UNAUDITED) AND DECEMBER 31, 2017

	3/31/18	12/31/17
ASSETS		
Cash and due from banks	$3,871,850	$4,094,694
Interest-bearing deposits in other financial institutions	36,162,017	33,312,236
Cash and cash equivalents	40,033,867	37,406,930
Available-for-sale securities	81,943,424	81,478,673
Held-to-maturity securities	15,097	16,457
Stock in Federal Home Loan Bank, at cost	4,183,600	4,597,500
Mortgage loans held for sale	781,075	1,921,819
Loans receivable, net of allowance for loan losses of March 31, 2018 - $7,102,712 - December 31, 2017 - $7,107,418	637,957,786	629,605,009
Accrued interest receivable	2,525,967	2,449,847
Prepaid expenses and other assets	5,076,193	3,846,686
Foreclosed assets held for sale	350,001	282,785
Premises and equipment, net	11,948,116	10,607,094
Bank owned life insurance	19,852,638	19,740,623
Deferred and income taxes receivable	2,357,521	2,506,097
	$807,025,285	$794,459,520
LIABILITIES AND STOCKHOLDERS' EQUITY		
LIABILITIES		
Deposits	$632,998,549	$607,364,350
Federal Home Loan Bank advances	80,600,000	94,300,000
Subordinated debentures	15,465,000	15,465,000
Advances from borrowers for taxes and insurance	281,497	180,269
Accrued expenses and other liabilities	1,326,064	1,962,865
Accrued interest payable	519,635	295,543
	731,190,745	719,568,027
COMMITMENTS AND CONTINGENCIES	-	-
STOCKHOLDERS' EQUITY		
Capital Stock:		

Common stock, $0.10 par value; authorized 10,000,000 shares; issued March 31, 2018 and December 31, 2017 - 6,883,003 and 6,878,503 shares; respectively	688,300	687,850
Additional paid-in capital	50,844,042	50,856,069
Retained earnings, substantially restricted	61,502,282	60,679,308
Accumulated other comprehensive loss	(233,135)	(206,193)
	112,801,489	112,017,034
Treasury stock, at cost; March 31, 2018 and December 31, 2017 - 2,443,246 and 2,453,728 shares, respectively	(36,966,949)	(37,125,541)
	75,834,540	74,891,493
	$807,025,285	$794,459,520

See Notes to Condensed Consolidated Financial Statements

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GUARANTY FEDERAL BANCSHARES, INC.
CONDENSED CONSOLIDATED STATEMENTS OF INCOME
THREE MONTHS ENDED MARCH 31, 2018 AND 2017
(UNAUDITED)

	3/31/2018	3/31/2017
Interest Income		
Loans	$7,378,575	$6,246,510
Investment securities	449,369	475,469
Other	128,372	49,423
	7,956,316	6,771,402
Interest Expense		
Deposits	1,422,570	621,854
FHLB advances	333,527	399,927
Subordinated debentures	168,967	151,680
	1,925,064	1,173,461
Net Interest Income	6,031,252	5,597,941
Provision for Loan Losses	225,000	475,000
Net Interest Income After Provision for Loan Losses	5,806,252	5,122,941
Noninterest Income		
Service charges	317,166	267,106
Gain on sale of investment securities	3,183	-
Gain on sale of mortgage loans held for sale	379,557	408,614
Gain on sale of Small Business Administration loans	170,862	130,488
Net gain on foreclosed assets	44,331	38,073
Other income	403,940	385,084
	1,319,039	1,229,365
Noninterest Expense		
Salaries and employee benefits	3,173,424	2,857,771
Occupancy	770,407	486,229
FDIC deposit insurance premiums	78,298	53,112
Data processing	302,532	229,316
Advertising	131,250	131,250
Merger costs	228,000	-
Other expense	791,944	661,942

	5,475,855	4,419,620
Income Before Income Taxes	1,649,436	1,932,686
Provision for Income Taxes	293,691	503,445
Net Income Available to Common Shareholders	$1,355,745	$1,429,241
Basic Income Per Common Share	$0.31	$0.33
Diluted Income Per Common Share	$0.30	$0.32

See Notes to Condensed Consolidated Financial Statements

GUARANTY FEDERAL BANCSHARES, INC.
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
THREE MONTHS ENDED MARCH 31, 2018 AND 2017
(UNAUDITED)

	3/31/2018	3/31/2017
NET INCOME	$1,355,745	$1,429,241
OTHER ITEMS OF COMPREHENSIVE INCOME:		
Change in unrealized gain (loss) on investment securities available-for-sale, before income taxes	(1,298,792)	635,854
Change in unrealized gain on interest rate swaps, before income taxes	1,265,812	-
Less: Reclassification adjustment for realized gains on investment securities included in net income, before income taxes	(3,183)	-
Total other items of comprehensive income	(36,163)	635,854
Income tax expense (benefit) related to other items of comprehensive income	(9,221)	235,266
Other comprehensive income (loss)	(26,942)	400,588
TOTAL COMPREHENSIVE INCOME	$1,328,803	$1,829,829

See Notes to Condensed Consolidated Financial Statements

GUARANTY FEDERAL BANCSHARES, INC.
CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY
THREE MONTHS ENDED MARCH 31, 2018
(UNAUDITED)

	Common Stock	Additional Paid-In Capital	Treasury Stock	Retained Earnings	Accumulated Other Comprehensive Loss	Total
Balance, January 1, 2018	$687,850	$50,856,069	$(37,125,541)	$60,679,308	$ (206,193)	$74,891,493
Net income	-	-	-	1,355,745	-	1,355,745
Other comprehensive income (loss)	-	-	-	-	(26,942)	(26,942)
Dividends on common stock ($0.12 per share)	-	-	-	(532,771)	-	(532,771)
Stock award plans	-	(35,357)	158,592	-	-	123,235
Stock options exercised	450	23,330	-	-	-	23,780
Balance, March 31, 2018	$688,300	$50,844,042	$(36,966,949)	$61,502,282	$ (233,135)	$75,834,540

See Notes to Condensed Consolidated Financial Statements

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GUARANTY FEDERAL BANCSHARES, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
THREE MONTHS ENDED MARCH 31, 2018 AND 2017
(UNAUDITED)

	3/31/2018	**3/31/2017**
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	$1,355,745	$1,429,241
Items not requiring (providing) cash:		
Deferred income taxes	(26,484)	(375,774)
Depreciation	331,330	230,186
Provision for loan losses	225,000	475,000
Gain on sale of Small Business Administration loans	(170,862)	(130,488)
Gain on sale of mortgage loans held for sale and investment securities	(382,740)	(408,614)
Gain on sale of foreclosed assets	(54,910)	(76,462)
Amortization of deferred income, premiums and discounts	113,284	183,994
Stock award plan expense	123,235	136,782
Origination of loans held for sale	(13,144,364)	(14,032,641)
Proceeds from sale of loans held for sale	14,664,665	14,384,621
Increase in cash surrender value of bank owned life insurance	(112,015)	(116,092)
Changes in:		
Accrued interest receivable	(76,120)	15,706
Prepaid expenses and other assets	36,306	(250,972)
Accounts payable and accrued expenses	(414,507)	(132,064)
Income taxes receivable/payable	141,574	609,055
Net cash provided by operating activities	2,609,137	1,941,478
CASH FLOWS FROM INVESTING ACTIVITIES		
Net change in loans	(8,457,089)	(46,986,724)
Principal payments on available-for-sale securities	1,360,549	1,756,038
Principal payments on held-to-maturity securities	1,360	3,335
Purchase of premises and equipment	(1,672,352)	(401,640)
Purchase of available-for-sale securities	(3,777,647)	-
Proceeds from sale of available-for-sale securities	565,935	-
Redemption of FHLB stock	413,900	101,500
Purchase of tax credit investments	-	(48,955)
Proceeds (payments) from sale of foreclosed assets held for sale	54,910	960,388
Net cash used in investing activities	(11,510,434)	(44,616,058)
CASH FLOWS FROM FINANCING ACTIVITIES		

Cash dividends paid	(530,973)	(441,003)
Net increase in demand deposits, NOW accounts and savings accounts	19,272,583	49,337,734
Net increase (decrease) in certificates of deposit	6,361,616	(3,293,022)
Proceeds from FHLB advances	166,250,000	67,300,000
Repayments of FHLB advances	(179,950,000)	(70,900,000)
Advances from borrowers for taxes and insurance	101,228	84,661
Stock options exercised	23,780	-
Net cash provided by financing activities	11,528,234	42,088,370
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	2,626,937	(586,210)
CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD	37,406,930	9,088,441
CASH AND CASH EQUIVALENTS, END OF PERIOD	$40,033,867	$8,502,231

See Notes to Condensed Consolidated Financial Statements

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Note 1: Basis of Presentation

The accompanying unaudited interim condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles (GAAP) for interim financial information and with the instructions to Form 10-Q and Rule 8-03 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting only of normal recurring accruals) considered necessary for a fair presentation have been included.

These condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in Guaranty Federal Bancshares, Inc.'s (the "Company") Annual Report on Form 10-K for the year ended December 31, 2017 ("2017 Annual Report") filed with the Securities and Exchange Commission (the "SEC"). The results of operations for the periods are not necessarily indicative of the results to be expected for the full year. The condensed consolidated balance sheet of the Company as of December 31, 2017, has been derived from the audited consolidated balance sheet of the Company as of that date. Certain information and note disclosures normally included in the Company's annual financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted.

Note 2: Principles of Consolidation

The accompanying condensed consolidated financial statements include the accounts of the Company and its wholly owned subsidiary, Guaranty Bank (the "Bank"). All significant intercompany transactions and balances have been eliminated in consolidation.

Note 3: Securities

The amortized cost and approximate fair values of securities classified as available-for-sale were as follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized (Losses)	Approximate Fair Value
As of March 31, 2018				
Debt Securities:				
Municipals	$33,772,192	$52,108	$(858,930)	$32,965,370
Corporates	3,000,000	60,791	-	3,060,791
Government sponsored mortgage-backed securities and SBA loan pools	47,274,879	12,439	(1,370,055)	45,917,263
	$84,047,071	$125,338	$(2,228,985)	$81,943,424

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	Amortized Cost	Gross Unrealized Gains	Gross Unrealized (Losses)	Approximate Fair Value
As of December 31, 2017				
Debt Securities:				
Municipals	$33,908,207	$253,872	$(263,621)	$33,898,458
Corporates	3,000,000	65,000	-	3,065,000
Government sponsored mortgage-backed securities and SBA loan pools	45,414,845	9,283	(908,913)	44,515,215
	$82,323,052	$328,155	$(1,172,534)	$81,478,673

Maturities of available-for-sale debt securities as of March 31, 2018:

	Amortized Cost	Approximate Fair Value
1-5 years	$434,711	$434,909
6-10 years	10,751,633	10,600,771
After 10 years	25,585,848	24,990,481
Government sponsored mortgage-backed securities and SBA loan pools not due on a single maturity date	47,274,879	45,917,263
	$84,047,071	$81,943,424

The amortized cost and approximate fair values of securities classified as held to maturity are as follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized (Losses)	Approximate Fair Value
As of March 31, 2018				
Debt Securities:				
Government sponsored mortgage-backed securities	$ 15,097	$ 253	$ (82)	$ 15,268

	Amortized Cost	Gross Unrealized	Gross Unrealized	Approximate Fair Value

		Gains	(Losses)	
As of December 31, 2017				
Debt Securities:				
Government sponsored mortgage-backed securities	$ 16,457	$ 327	$ (55)	$ 16,729

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Maturities of held-to-maturity securities as of March 31, 2018:

	Amortized Cost	Approximate Fair Value
Government sponsored mortgage-backed securities not due on a single maturity date	$ 15,097	$ 15,268

The book value of securities pledged as collateral, to secure public deposits and for other purposes, amounted to $45,622,168 and $35,774,863 as of March 31, 2018 and December 31, 2017, respectively. The approximate fair value of pledged securities amounted to $44,265,603 and $35,355,969 as of March 31, 2018 and December 31, 2017, respectively.

Realized gains and losses are recorded as net securities gains. Gains on sales of securities are determined on the specific identification method. Gross gains of $3,183 and $0 as of March 31, 2018 and March 31, 2017, respectively, were realized from the sale of available-for-sale securities. The tax effect of these net gains was $700 and $0 as of March 31, 2018 and March 31, 2017, respectively.

The Company evaluates all securities quarterly to determine if any unrealized losses are deemed to be other than temporary. Certain investment securities are valued at less than their historical cost. These declines are primarily the result of the rate for these investments yielding less than current market rates, or declines in stock prices of equity securities. Based on evaluation of available evidence, management believes the declines in fair value for these securities are temporary. It is management's intent to hold the debt securities to maturity or until recovery of the unrealized loss. Should the impairment of any of these debt securities become other than temporary, the cost basis of the investment will be reduced and the resulting loss recognized in net income in the period the other-than-temporary impairment is identified, to the extent the loss is related to credit issues, and to other comprehensive income to the extent the decline on debt securities is related to other factors and the Company does not intend to sell the security prior to recovery of the unrealized loss.

Certain other investments in debt and equity securities are reported in the financial statements at an amount less than their historical cost. Total fair value of these investments at March 31, 2018 and December 31, 2017, was $68,482,288 and $62,107,660, respectively, which is approximately 84% and 76% of the Company's investment portfolio.

The following table shows gross unrealized losses and fair value, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position at March 31, 2018 and December 31, 2017.

	March 31, 2018					
	Less than 12 Months		12 Months or More		Total	
Description of Securities	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Municipals	$19,061,837	$(483,654)	$8,559,989	$(375,277)	$27,621,826	$(858,931)
Government sponsored mortgage-backed securities and SBA loan pools	19,768,125	(497,936)	21,092,337	(872,118)	40,860,462	(1,370,054)
	$38,829,962	$(981,590)	$29,652,326	$(1,247,395)	$68,482,288	$(2,228,985)

	December 31, 2017					
	Less than 12 Months		12 Months or More		Total	
Description of Securities	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Municipals	$11,024,593	$(103,747)	$8,802,796	$(159,874)	$19,827,389	$(263,621)
Government sponsored mortgage-backed securities and SBA loan pools	20,088,694	(253,907)	22,191,577	(655,006)	42,280,271	(908,913)
	$31,113,287	$(357,654)	$30,994,373	$(814,880)	$62,107,660	$(1,172,534)

Note 4: Loans and Allowance for Loan Losses

Categories of loans at March 31, 2018 and December 31, 2017 include:

	March 31, 2018	December 31, 2017
Real estate - residential mortgage:		
One to four family units	$105,840,035	$106,300,790
Multi-family	81,982,799	85,225,074
Real estate - construction	81,228,819	64,743,582
Real estate - commercial	254,715,822	261,866,285
Commercial loans	97,830,737	94,522,840
Consumer and other loans	24,107,835	24,716,447
Total loans	645,706,047	637,375,018
Less:		
Allowance for loan losses	(7,102,712)	(7,107,418)
Deferred loan fees/costs, net	(645,549)	(662,591)
Net loans	$637,957,786	$629,605,009

Classes of loans by aging at March 31, 2018 and December 31, 2017 were as follows:

As of March 31, 2018

	30-59 Days Past Due	60-89 Days Past Due	90 Days and more Past Due	Total Past Due	Current	Total Loans Receivable	Total Loans > 90 Days and Accruing
	(In Thousands)						
Real estate - residential mortgage:							
One to four family units	$374	$ 63	$2,090	$2,527	$103,313	$ 105,840	$ -
Multi-family	-	-	-	-	81,983	81,983	-
Real estate - construction	-	-	-	-	81,229	81,229	-
Real estate - commercial	90	-	-	90	254,626	254,716	-
Commercial loans	306	-	75	381	97,449	97,830	-
Consumer and other loans	102	-	-	102	24,006	24,108	-
Total	$872	$ 63	$2,165	$3,100	$642,606	$ 645,706	$ -

As of December 31, 2017

	30-59 Days Past Due	60-89 Days Past Due	90 Days and more Past Due	Total Past Due	Current	Total Loans Receivable	Total Loans > 90 Days and Accruing
	(In Thousands)						
Real estate - residential mortgage:							
One to four family units	$510	$731	$2,495	$3,736	$102,565	$ 106,301	$ -
Multi-family	775	-	-	775	84,450	85,225	-
Real estate - construction	-	-	-	-	64,744	64,744	-
Real estate - commercial	243	135	-	378	261,488	261,866	-
Commercial loans	276	-	588	864	93,659	94,523	-
Consumer and other loans	8	8	-	16	24,700	24,716	-
Total	$1,812	$874	$3,083	$5,769	$631,606	$ 637,375	$ -

Nonaccruing loans are summarized as follows:

	March 31, 2018	December 31, 2017
Real estate - residential mortgage:		
One to four family units	$4,258,645	$4,423,074
Multi-family	-	-
Real estate - construction	4,354,409	4,452,409
Real estate - commercial	161,491	161,491
Commercial loans	655,581	802,628
Consumer and other loans	-	121,915
Total	$9,430,126	$9,961,517

The following tables present the activity in the allowance for loan losses based on portfolio segment for the three months ended March 31, 2018 and 2017:

March 31, 2018	Construction	Commercial Real Estate	One to four family	Multi-family	Commercial	Consumer and Other	Unallocated	Total
	(In Thousands)							
Allowance for loan losses:								
Balance, beginning of period	$2,244	$ 1,789	$946	$ 464	$ 1,031	$ 454	$ 179	$7,107
Provision charged to expense	(40)	87	167	23	20	(8)	(24)	$225
Losses charged off	-	-	-	-	(96)	(168)	-	$(264)
Recoveries	19	-	-	-	3	13	-	$35
Balance, end of period	$2,223	$ 1,876	$1,113	$ 487	$ 958	$ 291	$ 155	$7,103

March 31, 2017	Construction	Commercial Real Estate	One to four family	Multi-family	Commercial	Consumer and Other	Unallocated	Total
	(In Thousands)							
Allowance for loan losses:								
Balance, beginning of period	$1,377	$ 1,687	$ 856	$ 206	$ 1,168	$ 337	$ 111	$5,742
	(96)	55	(33)	67	(287)	5	764	$475

Provision charged to expense								
Losses charged off	-	-	(11)	-	-	(70)	-	$(81)
Recoveries	18	-	6	-	2	10	-	$36
Balance, end of period	$1,299	$ 1,742	$ 818	$ 273	$ 883	$ 282	$ 875	$6,172

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

March 31, 2018	Construction	Commercial Real Estate	One to four family	Multi-family	Commercial	Consumer and Other	Unallocated	Total
	(In Thousands)							
Allowance for loan losses:								
Ending balance: individually evaluated for impairment	$741	$ -	$302	$ -	$ 219	$ 10	$ -	$1,272
Ending balance: collectively evaluated for impairment	$1,482	$ 1,876	$811	$ 487	$ 739	$ 281	$ 155	$5,831
Loans:								
Ending balance: individually evaluated for impairment	$4,354	$ 161	$4,259	$ 762	$ 656	$ 81	$ -	$10,273
Ending balance: collectively evaluated for impairment	$76,875	$ 254,555	$101,581	$ 81,221	$ 97,174	$ 24,027	$ -	$635,433

December 31, 2017	Construction	Commercial Real Estate	One to four family	Multi-family	Commercial	Consumer and Other	Unallocated	Total
	(In Thousands)							
Allowance for loan losses:								
Ending balance: individually evaluated for impairment	$738	$ -	$127	$ -	$ 246	$ 138	$ -	$1,249
Ending balance: collectively evaluated for impairment	$1,506	$ 1,789	$819	$ 464	$ 785	$ 316	$ 179	$5,858
Loans:								
Ending balance: individually evaluated for impairment	$4,452	$ 161	$4,424	$ 775	$ 739	$ 276	$ -	$10,827
Ending balance: collectively evaluated for impairment	$60,292	$ 261,705	$101,877	$ 84,450	$ 93,784	$ 24,440	$ -	$626,548

The allowance for loan losses is established as losses are estimated to have occurred through a provision for loan losses charged to income. Loan losses are charged against the allowance when management believes the uncollectability of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance.

The allowance for loan losses is evaluated on a regular basis by management and is based upon management's periodic review of the collectability of the loans in light of historical experience, the nature and volume of the loan portfolio, adverse situations that may affect the borrower's ability to repay, estimated value of any underlying collateral and prevailing economic conditions. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available.

The allowance consists of allocated and general components. The allocated component relates to loans that are classified as impaired. For those loans that are classified as impaired, an allowance is established when the discounted cash flows or collateral value of the impaired loan is lower than the carrying value of that loan. The general component covers nonclassified loans and is based on historical charge-off experience and expected loss given default derived from the Bank's internal risk rating process. Other adjustments may be made to the allowance for pools of loans after an assessment of internal or external influences on credit quality that are not fully reflected in the historical loss or risk rating data.

A loan is considered impaired when, based on current information and events, it is probable that the Bank will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record and the amount of the shortfall in relation to the principal and interest owed. Impairment is measured on a loan-by-loan basis by either the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's obtainable market price or the fair value of the collateral if the loan is collateral dependent.

Groups of loans with similar risk characteristics are collectively evaluated for impairment based on the group's historical loss experience adjusted for changes in trends, conditions and other relevant factors that affect repayment of the loans.

The following table summarizes the recorded investment in impaired loans at March 31, 2018 and December 31, 2017:

	March 31, 2018			December 31, 2017		
	Recorded Balance	Unpaid Principal Balance	Specific Allowance	Recorded Balance	Unpaid Principal Balance	Specific Allowance
	(In Thousands)					
Loans without a specific valuation allowance						
Real estate - residential mortgage:						
One to four family units	$1,778	$1,778	$ -	$3,180	$3,180	$ -
Multi-family	762	762	-	775	775	-
Real estate - construction	2,742	2,742	-	2,840	2,840	-
Real estate - commercial	161	161	-	161	161	-
Commercial loans	170	170	-	465	465	-
Consumer and other loans	-	-	-	3	3	-
Loans with a specific valuation allowance						
Real estate - residential mortgage:						
One to four family units	$2,481	$2,481	$ 302	$1,244	$1,244	$ 127
Multi-family	-	-	-	-	-	-
Real estate - construction	1,612	2,845	741	1,612	2,845	738
Real estate - commercial	-	-	-	-	-	-
Commercial loans	486	486	219	274	274	246
Consumer and other loans	81	81	10	273	273	138
Total						
Real estate - residential mortgage:						
One to four family units	$4,259	$4,259	$ 302	$4,424	$4,424	$ 127
Multi-family	762	762	-	775	775	-
Real estate - construction	4,354	5,587	741	4,452	5,685	738
Real estate - commercial	161	161	-	161	161	-
Commercial loans	656	656	219	739	739	246
Consumer and other loans	81	81	10	276	276	138
Total	$10,273	$11,506	$ 1,272	$10,827	$12,060	$ 1,249

The following table summarizes average impaired loans and related interest recognized on impaired loans for the three months ended March 31, 2018 and 2017:

	For the Three Months Ended March 31, 2018			For the Three Months Ended March 31, 2017		
	Average Investment in Impaired Loans	Interest Income Recognized		Average Investment in Impaired Loans	Interest Income Recognized	
	(In Thousands)					
Loans without a specific valuation allowance						
Real estate - residential mortgage:						
One to four family units	$2,688	$	-	$1,888	$	-
Multi-family	765		5	-		-
Real estate - construction	2,775		-	2,990		-
Real estate - commercial	161		-	521		-
Commercial loans	349		-	601		-
Consumer and other loans	2		-	10		-
Loans with a specific valuation allowance						
Real estate - residential mortgage:						
One to four family units	$1,607	$	-	$41	$	-
Multi-family	-		-	-		-
Real estate - construction	1,612		-	2,415		-
Real estate - commercial	-		-	-		-
Commercial loans	323		-	550		-
Consumer and other loans	181		-	87		-
Total						
Real estate - residential mortgage:						
One to four family units	$4,295	$	-	$1,929	$	-
Multi-family	765		5	-		-
Real estate - construction	4,387		-	5,405		-
Real estate - commercial	161		-	521		-
Commercial loans	672		-	1,151		-
Consumer and other loans	183		-	97		-
Total	$10,463	$	5	$9,103	$	-

At March 31, 2018, the Bank's impaired loans shown in the table above included loans that were classified as troubled debt restructurings ("TDR"). The restructuring of a loan is considered a TDR if both (i) the borrower is experiencing financial difficulties and (ii) the creditor has granted a concession.

In assessing whether or not a borrower is experiencing financial difficulties, the Bank considers information currently available regarding the financial condition of the borrower. This information includes, but is not limited to, whether (i) the debtor is currently in payment default on any of its debt; (ii) a payment default is probable in the foreseeable future without the modification; (iii) the debtor has declared or is in the process of declaring bankruptcy and (iv) the debtor's projected cash flow is sufficient to satisfy the contractual payments due under the original terms of the loan without a modification.

The Bank considers all aspects of the modification to loan terms to determine whether or not a concession has been granted to the borrower. Key factors considered by the Bank include the debtor's ability to access funds at a market rate for debt with similar risk characteristics, the significance of the modification relative to unpaid principal balance or collateral value of the debt, and the significance of a delay in the timing of payments relative to the original contractual terms of the loan. The most common concessions granted by the Bank generally include one or more modifications to the terms of the debt, such as (i) a reduction in the interest rate for the remaining life of the debt, (ii) an extension of the maturity date at an interest rate lower than the current market rate for new debt with similar risk, (iii) a reduction on the face amount or maturity amount of the debt as stated in the original loan, (iv) a temporary period of interest-only payments, (v) a reduction in accrued interest, and (vi) an extension of amortization.

The following table summarizes, by class, loans that were newly classified as TDRs for the three months ended March 31, 2018:

	Number of Loans	Pre-Modification Outstanding Recorded Balance	Post-Modification Outstanding Recorded Balance
Real estate - residential mortgage:			
One to four family units	-	$ -	$ -
Multi-family	-	-	-
Real estate - construction	-	-	-
Real estate - commercial	-	-	-
Commercial loans	2	510,420	414,515
Consumer and other loans	-	-	-
Total	2	$ 510,420	$ 414,515

The following table summarizes, by type of concession, loans that were newly classified as TDRs for the three months ended March 31, 2018:

	Interest Rate	Term	Combination	Total Modification
Real estate - residential mortgage:				
One to four family units	$ -	$ -	$ -	$ -
Multi-family	-	-	-	-
Real estate - construction	-	-	-	-
Real estate - commercial	-	-	-	-
Commercial loans	-	-	414,515	414,515
Consumer and other loans	-	-	-	-
Total	$ -	$ -	$ 414,515	$ 414,515

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The following table presents the carrying balance of TDRs as of March 31, 2018 and December 31, 2017:

	March 31, 2018	December 31, 2017
Real estate - residential mortgage:		
One to four family units	$1,248,510	$1,290,462
Multi-family	-	-
Real estate - construction	4,354,410	4,452,409
Real estate - commercial	5,653,777	5,666,096
Commercial loans	580,301	214,529
Consumer and other loans	-	118,855
Total	$11,836,998	$11,742,351

The Bank has allocated $976,551 and $372,321 of specific reserves to customers whose loan terms have been modified in TDR as of March 31, 2018 and December 31, 2017, respectively.

There were no TDRs for which there was a payment default within twelve months following the modification during the three months ending March 31, 2018 and 2017. A loan is considered to be in payment default once it is 90 days contractually past due under the modified terms.

As part of the on-going monitoring of the credit quality of the Bank’s loan portfolio, management tracks loans by an internal rating system. All loans are assigned an internal credit quality rating based on an analysis of the borrower’s financial condition. The criteria used to assign quality ratings to extensions of credit that exhibit potential problems or well-defined weaknesses are primarily based upon the degree of risk and the likelihood of orderly repayment, and their effect on the Bank’s safety and soundness. The following are the internally assigned ratings:

Pass: This rating represents loans that have strong asset quality and liquidity along with a multi-year track record of profitability.

Special mention: This rating represents loans that are currently protected but are potentially weak. The credit risk may be relatively minor, yet constitute an increased risk in light of the circumstances surrounding a specific loan.

Substandard: This rating represents loans that show signs of continuing negative financial trends and unprofitability and therefore, is inadequately protected by the current sound worth and paying capacity of the obligor or of the collateral pledged, if any.

Doubtful: This rating represents loans that have all the weaknesses of substandard classified loans with the additional characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions and values, highly questionable and improbable.

Risk characteristics applicable to each segment of the loan portfolio are described as follows.

Real estate-Residential 1-4 family: The residential 1-4 family real estate loans are generally secured by owner-occupied 1-4 family residences. Repayment of these loans is primarily dependent on the personal income and credit rating of the borrowers. Credit risk in these loans can be impacted by economic conditions within the Bank’s market areas that might impact either property values or a borrower’s personal income. Risk is mitigated by the fact that the loans are of smaller individual amounts and spread over a large number of borrowers.

Real estate-Construction: Construction and land development real estate loans are usually based upon estimates of costs and estimated value of the completed project and include independent appraisal reviews and a financial analysis of the developers and property owners. Sources of repayment of these loans may include permanent loans, sales of developed property or an interim loan commitment from the Bank until permanent financing is obtained. These loans are considered to be higher risk than other real estate loans due to their ultimate repayment being sensitive to interest rate changes, general economic conditions and the availability of long-term financing. Credit risk in these loans may be impacted by the creditworthiness of a borrower, property values and the local economies in the Bank’s market areas.

Real estate-Commercial: Commercial real estate loans typically involve larger principal amounts, and repayment of these loans is generally dependent on the successful operations of the property securing the loan or the business conducted on the property securing the loan. These loans are viewed primarily as cash flow loans and secondarily as loans secured by real estate. Credit risk in these loans may be impacted by the creditworthiness of a borrower, property values and the local economies in the Bank's market areas.

Commercial: The commercial portfolio includes loans to commercial customers for use in financing working capital needs, equipment purchases and expansions. The loans in this category are repaid primarily from the cash flow of a borrower's principal business operation. Credit risk in these loans is driven by creditworthiness of a borrower and the economic conditions that impact the cash flow stability from business operations.

Consumer: The consumer loan portfolio consists of various term and line of credit loans such as automobile loans and loans for other personal purposes. Repayment for these types of loans will come from a borrower's income sources that are typically independent of the loan purpose. Credit risk is driven by consumer economic factors (such as unemployment and general economic conditions in the Bank's market area) and the creditworthiness of a borrower.

The following tables provide information about the credit quality of the loan portfolio using the Bank's internal rating system as of March 31, 2018 and December 31, 2017:

March 31, 2018	Construction	Commercial Real Estate	One to four family	Multi-family	Commercial	Consumer and Other	Total
	(In Thousands)						
Rating:							
Pass	$76,778	$ 244,309	$97,103	$ 81,220	$ 96,355	$ 24,027	$619,792
Special Mention	-	6,573	3,133	-	296	-	10,002
Substandard	4,451	3,834	5,604	763	1,179	81	15,912
Doubtful	-	-	-	-	-	-	-
Total	$81,229	$ 254,716	$105,840	$ 81,983	$ 97,830	$ 24,108	$645,706

December 31, 2017	Construction	Commercial Real Estate	One to four family	Multi-family	Commercial	Consumer and Other	Total
	(In Thousands)						
Rating:							
Pass	$60,291	$ 254,658	$96,723	$ 84,450	$ 93,102	$ 24,440	$613,664
Special Mention	-	5,578	3,799	-	200	-	9,577

Substandard	4,453	1,630	5,779	775	708	276	13,621
Doubtful	-	-	-	-	513	-	513
Total	$64,744	$ 261,866	$106,301	$ 85,225	$ 94,523	$ 24,716	$637,375

For loans amortized at cost, interest income is accrued based on the unpaid principal balance. Loan origination fees net of certain direct origination costs, are deferred and amortized as a level yield adjustment over the respective term of the loan.

The accrual of interest on loans is discontinued at the time the loan is 90 days past due unless the loan is well-secured and in process of collection. Past due status is based on contractual terms of the loan. In all cases, loans are placed on nonaccrual or charged off at an earlier date if collection of principal or interest is considered doubtful.

All interest accrued but not collected for loans that are placed on nonaccrual or charged off is reversed against interest income. The interest on these loans is accounted for on the cash-basis or cost-recovery method, until qualifying for return to accrual. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

Note 5: Benefit Plans

The Company has stock-based employee compensation plans, which are described in the Company's 2017 Annual Report.

The following tables below summarize transactions under the Company's equity plans for the three months ended March 31, 2018:

Stock Options

	Number of shares		
	Incentive Stock Option	Non-Incentive Stock Option	Weighted Average Exercise Price
Balance outstanding as of January 1, 2018	46,000	25,000	$ 15.74
Granted	-	-	-
Exercised	(4,500)	-	5.28
Forfeited	(20,000)	(10,000)	28.71
Balance outstanding as of March 31, 2018	21,500	15,000	$ 6.37
Options exercisable as of March 31, 2018	21,500	15,000	$ 6.37

The total intrinsic value of stock options exercised for the three months ended March 31, 2018 and 2017 was $79,130 and $0, respectively. The total intrinsic value of outstanding stock options (including exercisable) was $625,260 and

$566,840 at March 31, 2018 and 2017, respectively.

Restricted Stock

	Number of Shares	Weighted Average Grant-Date Fair Value
Balance of shares non-vested as of January 1, 2018	45,550	$ 16.44
Granted	12,838	22.41
Vested	(22,597)	16.49
Forfeited	-	-
Balance of shares non-vested as of March 31, 2018	35,791	$ 18.54

In February 2018, the Company granted 5,852 shares of restricted stock to directors pursuant to the 2015 Equity Plan that have a cliff vesting at the end of one year and thus, expensed over that same period. These shares had a grant date market price of $22.41 per share. The total amount of expense for restricted stock grants to directors (including all previous years grants) during the three months ended March 31, 2018 and 2017 was $34,649 and $33,120, respectively.

For the three months ended March 31, 2018 and 2017, the Company granted 6,986 and 5,926 shares, respectively, of restricted stock to officers that have a cliff vesting at the end of three years. The expense is being recognized over the applicable vesting period. The total amount of expense for restricted stock grants to officers (including all previous years grants) during the three months ended March 31, 2018 and 2017 was $53,748 and $57,687, respectively.

Performance Stock Units

	Performance Stock Units	Weighted Average Grant-Date Fair Value
Balance of shares non-vested as of January 1, 2018	55,823	$ 20.48
Granted	-	-
Vested	-	-
Forfeited	-	-
Balance of shares non-vested as of March 31, 2018	55,823	$ 20.48

On March 29, 2017, the Company granted restricted stock units representing 55,823 hypothetical shares of common stock to officers. There are three possible levels of incentive awards: threshold (25%); target (50%); and maximum (100%). The restricted stock units vest based on two financial performance factors over the period from March 29, 2017 to December 31, 2019 (the “Performance Period”). The two performance measurements of the Company (and the weight given to each measurement) applicable to each award level are as follows: (i) Total Assets (50%) and (ii) Return on Average Assets (50%). In determining compensation expense, the fair value of the restricted stock unit awards was determined based on the closing price of the Company’s common stock on the date of grant, which was $20.48 per share. The expense is being recognized over the applicable vesting period. Due to the fact that the measurements cannot be determined at the time of the grant, the Company currently estimates that the most likely outcome is the achievement between the target and maximum levels. If during the Performance Period, additional information becomes available to lead the Company to believe a different level will be achieved for the Performance Period, the Company will reassess the number of units that will vest for the grant and adjust its compensation expense accordingly on a prospective basis. The total amount of expense for restricted stock units during the three months ended March 31, 2018 and 2017 was $84,504 and $1,654, respectively.

Total stock-based compensation expense recognized for the three months ended March 31, 2018 and 2017 was $172,901 and $92,461, respectively. As of March 31, 2018, there was $1,033,295 of unrecognized compensation expense related to nonvested restricted stock awards, which will be recognized over the remaining vesting period.

Note 6: Income Per Common Share

	For three months ended March 31, 2018		
	Income Available to Common Stockholders	Weighted Average Common Shares Outstanding	Per Common Share
Basic Income per Common Share	$1,355,745	4,391,717	$ 0.31
Effect of Dilutive Securities		75,069	
Diluted Income per Common Share	$1,355,745	4,466,786	$ 0.30

	For three months ended March 31, 2017		
	Income Available to Common Stockholders	Weighted Average Common Shares Outstanding	Per Common Share
Basic Income per Common Share	$1,429,241	4,363,071	$ 0.33
Effect of Dilutive Securities		56,952	
Diluted Income per Common Share	$1,429,241	4,420,023	$ 0.32

Stock options to purchase 58,500 shares of common stock were outstanding during the three months ended March 31, 2017 but were not included in the computation of diluted income per common share because their exercise price was greater than the average market price of the common shares.

Note 7: New Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2014-09, (Topic 606): *Revenue from Contracts with Customers* ("ASU 2014-09"). The scope of the guidance applies to revenue arising from contracts with customers, except for the following: lease contracts, insurance contracts, contractual rights and obligations within the scope of other guidance and nonmonetary exchanges between entities in the same line of business to facilitate sales to customers. The core principle of the new guidance was that an entity should recognize revenue to reflect the transfer of goods and services to customers in an amount equal to the consideration that the entity receives or expects to receive. ASU 2014-09 did not significantly impact the timing or approach to revenue recognition for financial institutions. Initially, the amendments were effective for public entities for annual reporting periods beginning after December 15, 2016, however, the FASB issued ASU 2015-14 *Revenue from Contracts with Customers (Topic 606) – Deferral of the Effective Date*" which deferred the effective date of ASU 2014-09 by one year to annual and interim periods beginning after December 15, 2017. The guidance does not apply to revenue associated with financial instruments, including loans and securities that are accounted for under GAAP, which comprises a significant portion of our revenue stream. The Company adopted ASU 2014-09 during the first quarter of 2018 and completed an evaluation of the impact of the revenue streams which are included in the scope of these updates, such as deposit fees and revenue from the sale of other real estate owned. The Company analyzed each revenue stream under Topic 606 and determined that there were no material changes to existing recognition practices. The Company concluded that the adoption of this update did not change significantly from our current practice of recognizing the in-scope non-interest income. In addition, we did not retroactively revise prior period amount or record a cumulative adjustment to retained earnings upon adoption.

Descriptions of our significant revenue-generating transactions that are within the scope of the new revenue recognition standards, which are presented in the consolidated statements of comprehensive income as components of non-interest income, are as follows:

Service Charges on Deposit Accounts – Services charges on deposit accounts include general service fees for monthly account maintenance, account analysis fees, non-sufficient funds fees, wire transfer fees and other deposit account related fees. Revenue is recognized when the performance obligation is completed which is generally monthly for account maintenance services or when a transaction has been completed (such as a wire transfer). Payment for service charges on deposit accounts is received immediately or in the following month through a direct charge to customers' accounts.

Gains/Losses on Sales of OREO – Gains/Losses on sales of OREO are recorded from the sale when control of the property transfers to the buyer, which generally occurs at the time of an executed deed.

In January 2016, the FASB issued ASU 2016-01, Financial Instruments- Overall (Subtopic 825-10): *Recognition and Measurement of Financial Assets and Financial Liabilities* ("ASU 2016-01"). ASU 2016-01 simplifies the impairment assessment of equity investments, clarifies reporting disclosure requirements for financial instruments measured at amortized cost, and requires the exit price notion be disclosed when measuring fair value of financial instruments. ASU 2016-01 details the required separate presentation in other comprehensive income for the change in fair value of a liability related to change in instrument specific credit risk and details the required separate presentation of financial assets and liabilities by measurement category and clarifies the guidance for a valuation allowance on deferred tax assets related to available-for-sale securities. ASU 2016-01 was effective for annual and interim reporting periods beginning after December 15, 2017. ASU 2016-01 was effective for the Company on January 1, 2018 and did not have a material impact on our consolidated financial statements. See Note 9- Disclosures about Fair Value of Assets and Liabilities for further information regarding the valuation method for loans.

In February 2016, the FASB issued ASU 2016-02, *Leases* ("ASU 2016-02"). ASU 2016-02 establishes a right-of-use (ROU) model that requires a lessee to record a ROU asset and a lease liability on the balance sheet for all leases with terms longer than 12 months. Leases will be classified as either finance or operating, with classification affecting the pattern of expense recognition in the income statement. ASU 2016-02 is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. A modified retrospective transition approach is required for lessees for capital and operating leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements, with certain practical expedients available. The Company is currently evaluating the impact and have determined that the provisions of ASU 2016-02 will result in an increase in assets to recognize the present value of the lease obligations with a corresponding increase in liabilities; however, we do not expect this to have a material impact to the Company's results of operations or cash flows.

In June 2016, the FASB issued ASU 2016-13, Financial Instruments-Credit Losses (Topic 326): *Measurement of Credit Losses on Financial Instruments*. Among other things, the amendments in this ASU require the measurement of all expected credit losses for financial assets held at the reporting date based on historical experience, current conditions, and reasonable and supportable forecasts. Financial institutions and other organizations will now use forward-looking information to better inform their credit loss estimates. Many of the loss estimation techniques applied today will still be permitted, although the inputs to those techniques will change to reflect the full amount of expected credit losses. In addition, the ASU amends the accounting for credit losses on available-for-sale debt securities and purchased financial assets with credit deterioration. For SEC filers, the amendments in this ASU are effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2019, with later effective dates for non-SEC registrant public companies and other organizations. Early adoption will be permitted for all organizations for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018. The Company has formed a committee that is assessing our data and evaluating the impact of adopting ASU 2016-13. The Company has also selected a third party vendor to assist in generating loan level cash flows and disclosures.

In August 2016, the FASB issued ASU 2016-15, Statement of Cash Flows (Topic 230): *Classification of Certain Cash Receipts and Cash Payments.* The update was intended to reduce the diversity in practice around how certain transactions are classified within the statement of cash flows with respect to eight types of cash flows. This new accounting guidance was effective for interim and annual reporting periods beginning after December 15, 2017. Adoption of ASU 2016-15 did not significantly impact the Company's consolidated financial statements.

In May 2017, the FASB issued ASU 2017-09, Compensation-Stock Compensation (Subtopic 718): *Scope of Modification Accounting.* ASU 2017-09 clarifies when changes to terms or conditions of a share-based payment award must be accounted for as a modification. Under the new guidance, an entity does not apply modification accounting to a share-based payment award if all of the following are the same immediately before and after the change: (i) the fair value of the award, (ii) the vesting conditions of the award, and (iii) the classification of the award as either an equity or liability instrument. ASU 2017-09 was effective for the fiscal years, and interim periods within those fiscal years, beginning after December 15, 2017. The guidance requires companies to apply the requirements prospectively to awards modified on or after the adoption date. ASU 2017-09 was effective for the Company on January 1, 2018 and did not have a material impact on our consolidated financial statements.

In July 2017, the FASB issued ASU 2017-11, Earnings Per Share (Topic 260); Distinguishing Liabilities from Equity (Topic 480); Derivatives and Hedging (Topic 815): *(Part 1) Accounting for certain financial instruments with down round features and (Part II), Replacement of the indefinite deferral for mandatory redeemable financial instruments of certain nonpublic entities and certain mandatory redeemable non-controlling interests with a scope exception*. Part I of the update addresses the complexity of accounting for certain financial instruments with down round features such as warrants or convertible instruments and will be effective for interim and annual reporting periods beginning after December 15, 2019. The Company is currently evaluating the impact of our pending adoption of the new standard on our consolidated financial statements, but at this time do not believe the standard will have a significant impact on the financial statements.

In August 2017, the FASB issued ASU 2017-12, Derivatives and Hedging (Topic 815): *Targeted improvements to accounting for hedging activities.* The purpose of this updated guidance is to better align financial reporting for hedging activities with the economic objectives of those activities. The amendments in this update are effective for fiscal years beginning after December 15, 2018, with early adoption, including adoption in an interim period, permitted. The standard requires the modified retrospective transition approach as of the date of adoption. The Company is currently evaluating the impact that this standard will have on its Consolidated Financial Statements.

In February 2018, the FASB issued ASU 2018-02, Income Statement-Reporting Comprehensive Income (Topic 220): *Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income*. This ASU provides financial statement preparers with an option to reclassify stranded tax effects within accumulated other comprehensive income to retained earnings in each period in which the effect of the change in the U.S. federal corporate income tax rate in the Tax Cuts and Jobs Act (or portion thereof) are recorded. This standard is effective for all organizations for fiscal years beginning after December 15, 2018, and interim periods within those fiscal years. Early adoption is permitted. Organizations should apply the proposed amendments either in the period of adoption or retrospectively to each period (or periods) in which the effect of the change in the U.S. federal corporate income tax rate in the Tax Cuts and Jobs Act is recognized. The Company elected to early adopt ASU 2018-02 and, as a result, reclassified $31,818 from accumulated other comprehensive income to retained earnings as of December 31, 2017. The reclassification impacted the Consolidated Balance Sheet and the Consolidated Statement of Stockholder’s Equity as of and for the year ended December 31, 2017.

Note 8: Derivative Financial Instruments

The Company records all derivative financial instruments at fair value in the financial statements. Derivatives are used as a risk management tool to hedge the exposure to changes in interest rates or other identified market risks.

When a derivative is intended to be a qualifying hedged instrument, the Company prepares written hedge documentation that designates the derivative as 1) a hedge of fair value of a recognized asset or liability (fair value hedge) or 2) a hedge of a forecasted transaction, such as, the variability of cash flows to be received or paid related to a recognized asset or liability (cash flow hedge). The written documentation includes identification of, among other items, the risk management objective, hedging instrument, hedged item, and methodologies for assessing and measuring hedge effectiveness and ineffectiveness, along with support for management’s assertion that the hedge will be highly effective.

In June 2017, the Company entered into a forward start interest rate swap agreement totaling $50 million notional amount to hedge against interest rate risk on FHLB advances. As a cash flow hedge, the portion of the change in the fair value of the derivative that has been deemed highly effective is recognized in other comprehensive income until the related cash flows from the hedged item are recognized in earnings. At March 31, 2018, the Company reported a $1,431,255 unrealized gain, net of a $402,260 tax effect, in other comprehensive income related to this cash flow hedge. The Company documents, both at inception and periodically over the life of the hedge, its analysis of actual and expected hedge effectiveness. To the extent that the hedge of future cash flows is deemed ineffective, changes in the fair value of the derivative are recognized in earnings as a component of other noninterest expense. For the quarter ended March 31, 2018, there was no ineffectiveness attributable to the cash flow hedge.

A summary of the Company’s derivative financial instruments at March 31, 2018 is shown in the following table:

Forward Start Inception Date	Termination Date	Derivative Type	Notional Amount	Rate Paid	Rate Hedged	Estimated Fair Value at March 31, 2018
2/28/2018	2/28/2025	Interest rate swap	$ 50,000,000	2.12 %	3 month LIBOR Floating	$ 1,833,515

Note 9: Disclosures about Fair Value of Assets and Liabilities

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

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

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

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

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

Available-for-sale securities: Where quoted market prices are available in an active market, securities are classified within Level 1 of the valuation hierarchy. Level 1 securities include equity securities. If quoted market prices are not available, then fair values are estimated by using pricing models, quoted prices of securities with similar characteristics or discounted cash flows. For these investments, the inputs used by the pricing service to determine fair value may include one or a combination of observable inputs such as benchmark yields, reported trades, broker/dealer quotes, issuer spreads, two-sided markets, benchmark securities, bid offers and reference data market research publications and are classified within Level 2 of the valuation hierarchy. Level 2 securities include U.S. government agencies, municipal securities and government sponsored mortgage-backed securities. The Company has no Level 3 securities.

Derivative financial instruments (Cash flow hedge): The Company's open derivative positions are interest rate swap agreements. Those classified as Level 2 open derivative positions are valued using externally developed pricing models based on observable market inputs provided by a third party and validated by management. The Company has considered counterparty credit risk in the valuation of its interest rate swap assets.

The following table presents the fair value measurements of assets recognized in the accompanying condensed consolidated balance sheets measured at fair value on a recurring basis and the level within the fair value hierarchy in which the fair value measurements fall at March 31, 2018 and December 31, 2017 (dollar amounts in thousands):

3/31/2018

Financial assets:

	Level 1 inputs	Level 2 inputs	Level 3 inputs	Total fair value
Debt securities:				
Municipals	$ -	$32,965	$ -	$32,965
Corporates	-	3,061	-	3,061
Government sponsored mortgage-backed securities and SBA loan pools	-	45,917	-	45,917
Available-for-sale securities	$ -	$81,943	$ -	$81,943