First Internet Bancorp
Form 10-Q
May 03, 2017

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

FORM 10-Q

(Mark One)
þ QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the Quarterly Period ended March 31, 2017
OR
¨ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the Transition Period From ________ to ________.

Commission File Number 001-35750

First Internet Bancorp
(Exact Name of Registrant as Specified in Its Charter)

Indiana	20-3489991
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)
11201 USA Parkway Fishers, IN	46037
(Address of Principal Executive Offices)	(Zip Code)

(317) 532-7900
(Registrant’s Telephone Number, Including Area Code)

(Former Name, Former Address and Former Fiscal Year, if Changed Since Last Report)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes þ No ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or such shorter period that the registrant was required to submit and post such files). Yes þ No ¨

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company (as defined in Rule 12b-2 of the Exchange Act).

Large Accelerated Filer ¨	Accelerated Filer þ
Non-accelerated Filer ¨ (Do not check if a 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 pursuance to Section 13(a) of the Exchange Act. ¨

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

As of April 28, 2017, the registrant had 6,497,662 shares of common stock issued and outstanding.

Cautionary Note Regarding Forward-Looking Statements

This Quarterly Report on Form 10-Q contains “forward-looking statements” within the meaning of the federal securities laws. These statements are not historical facts, but rather statements based on the current expectations of First Internet Bancorp and its consolidated subsidiaries (“we,” “our,” “us” or the “Company”) regarding its business strategies, intended results and future performance. Forward-looking statements are generally preceded by terms such as “expects,” “believes,” “anticipates,” “intends,” “plan,” and similar expressions. Such statements are subject to certain risks and uncertainties including: general economic conditions, whether national or regional, and conditions in the lending markets in which we participate that may have an adverse effect on the demand for our loans and other products; our credit quality and related levels of nonperforming assets and loan losses, and the value and salability of the real estate that we own or that is the collateral for our loans; failures of or interruptions in the communication and information systems on which we rely to conduct our business that could reduce our revenues, increase our costs or lead to disruptions in our business; our plans to grow our commercial real estate and commercial and industrial loan portfolios which may carry greater risks of non-payment or other unfavorable consequences; our dependence on capital distributions from First Internet Bank of Indiana (the “Bank”); results of examinations of us by our regulators, including the possibility that our regulators may, among other things, require us to increase our allowance for loan losses or to write-down assets; changing bank regulatory conditions, policies or programs, whether arising as new legislation or regulatory initiatives, that could lead to restrictions on activities of banks generally, or the Bank in particular; more restrictive regulatory capital requirements; increased costs, including deposit insurance premiums; regulation or prohibition of certain income producing activities or changes in the secondary market for loans and other products; changes in market rates and prices that may adversely impact the value of securities, loans, deposits and other financial instruments and the interest rate sensitivity of our balance sheet; our liquidity requirements being adversely affected by changes in our assets and liabilities; the effect of legislative or regulatory developments, including changes in laws concerning taxes, banking, securities, insurance and other aspects of the financial services industry; competitive factors among financial services organizations, including product and pricing pressures and our ability to attract, develop and retain qualified banking professionals; the growth and profitability of noninterest or fee income being less than expected; the loss of any key members of senior management; the effect of changes in accounting policies and practices, as may be adopted by the Financial Accounting Standards Board (the “FASB”), the Securities and Exchange Commission (the “SEC”), the Public Company Accounting Oversight Board (the “PCAOB”) and other regulatory agencies; and the effect of fiscal and governmental policies of the United States federal government. Additional factors that may affect our results include those discussed in our most recent Annual Report on Form 10-K under the heading “Risk Factors” and in other reports filed with the SEC. We caution readers not to place undue reliance on any such forward-looking statements, which speak only as of the date made. The factors listed above could affect our financial performance and could cause our actual results for future periods to differ materially from any opinions or statements expressed with respect to future periods in any current statements.

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

PART I

ITEM 1. FINANCIAL STATEMENTS

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

	March 31, 2017 (Unaudited)	December 31, 2016
Assets		
Cash and due from banks	$4,137	$2,282
Interest-bearing deposits	48,961	37,170
Total cash and cash equivalents	53,098	39,452
Interest-bearing time deposits	250	250
Securities available-for-sale, at fair value (amortized cost of $483,370 and $471,070 in 2017 and 2016, respectively)	470,065	456,700
Securities held-to-maturity, at amortized cost (fair value of $18,804 and $16,197 in 2017 and 2016, respectively)	19,218	16,671
Loans held-for-sale (includes $8,692 and $27,101 at fair value in 2017 and 2016, respectively)	13,202	27,101
Loans	1,433,190	1,250,789
Allowance for loan losses	(11,894)	(10,981)
Net loans	1,421,296	1,239,808
Accrued interest receivable	6,868	6,708
Federal Home Loan Bank of Indianapolis stock	13,050	8,910
Cash surrender value of bank-owned life insurance	24,367	24,195
Premises and equipment, net	9,853	10,044
Goodwill	4,687	4,687
Other real estate owned	4,488	4,533
Accrued income and other assets	12,361	15,276
Total assets	$2,052,803	$1,854,335
Liabilities and Shareholders' Equity		
Liabilities		
Noninterest-bearing deposits	$34,427	$31,166
Interest-bearing deposits	1,522,692	1,431,701
Total deposits	1,557,119	1,462,867
Advances from Federal Home Loan Bank	289,985	189,981
Subordinated debt, net of unamortized discounts and debt issuance costs of $1,385 and $1,422 in 2017 and 2016, respectively	36,615	36,578
Accrued interest payable	148	112
Accrued expenses and other liabilities	11,445	10,855
Total liabilities	1,895,312	1,700,393
Commitments and Contingencies		
Shareholders' Equity		
Preferred stock, no par value; 4,913,779 shares authorized; issued and outstanding - none	—	—
Voting common stock, no par value; 45,000,000 shares authorized; 6,497,662 and 6,478,050 shares issued and outstanding in 2017 and 2016, respectively	119,627	119,506
	—	—

Nonvoting common stock, no par value; 86,221 shares authorized; issued and outstanding - none		
Retained earnings	46,139	43,704
Accumulated other comprehensive loss	(8,275)	(9,268)
Total shareholders' equity	157,491	153,942
Total liabilities and shareholders' equity	$2,052,803	$1,854,335

See Notes to Condensed Consolidated Financial Statements

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First Internet Bancorp
Condensed Consolidated Statements of Income – Unaudited
(Amounts in thousands except share and per share data)

	Three Months Ended March 31,	
	2017	2016
Interest Income		
Loans	$14,156	$11,189
Securities – taxable	2,367	1,169
Securities – non-taxable	697	165
Other earning assets	170	170
Total interest income	17,390	12,693
Interest Expense		
Deposits	4,699	2,888
Other borrowed funds	1,234	664
Total interest expense	5,933	3,552
Net Interest Income	11,457	9,141
Provision for Loan Losses	1,035	946
Net Interest Income After Provision for Loan Losses	10,422	8,195
Noninterest Income		
Service charges and fees	211	200
Mortgage banking activities	1,616	2,254
Loss on asset disposals	(2)	(16)
Other	306	102
Total noninterest income	2,131	2,540
Noninterest Expense		
Salaries and employee benefits	5,073	3,898
Marketing, advertising and promotion	518	464
Consulting and professional services	813	638
Data processing	237	274
Loan expenses	214	184
Premises and equipment	953	798
Deposit insurance premium	315	180
Other	575	569
Total noninterest expense	8,698	7,005
Income Before Income Taxes	3,855	3,730
Income Tax Provision	1,023	1,298
Net Income	$2,832	$2,432
Income Per Share of Common Stock		
Basic	$0.43	$0.54
Diluted	$0.43	$0.53
Weighted-Average Number of Common Shares Outstanding		
Basic	6,547,807	4,541,728
Diluted	6,602,200	4,575,555
Dividends Declared Per Share	$0.06	$0.06

See Notes to Condensed Consolidated Financial Statements

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

	Three Months Ended March 31,	
	2017	2016
Net income	$2,832	$2,432
Net unrealized holding gains on securities available-for-sale recorded within other comprehensive income before income tax	1,065	1,874
Income tax provision	72	667
Other comprehensive income	993	1,207
Comprehensive income	$3,825	$3,639

See Notes to Condensed Consolidated Financial Statements

First Internet Bancorp
Condensed Consolidated Statement of Shareholders' Equity - Unaudited
Three Months Ended March 31, 2017
(Amounts in thousands except per share data)

	Voting and Nonvoting Common Stock	Retained Earnings	Accumulated Other Comprehensive Loss	Total Shareholders' Equity
Balance, January 1, 2017	$ 119,506	$ 43,704	$ (9,268)	$ 153,942
Net income	—	2,832	—	2,832
Other comprehensive income	—	—	993	993
Dividends declared ($0.06 per share)	—	(397)	—	(397)
Recognition of the fair value of share-based compensation	285	—	—	285
Deferred stock rights and restricted stock units issued in lieu of cash dividends payable on outstanding deferred stock rights and restricted stock units	9	—	—	9
Common stock redeemed for the net settlement of share-based awards	(173)	—	—	(173)
Balance, March 31, 2017	$ 119,627	$ 46,139	$ (8,275)	$ 157,491

See Notes to Condensed Consolidated Financial Statements

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

	Three Months Ended March 31,	
	2017	2016
Operating Activities		
Net income	$2,832	$2,432
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	1,205	575
Increase in cash surrender value of bank-owned life insurance	(172)	(99)
Provision for loan losses	1,035	946
Share-based compensation expense	285	173
Loans originated for sale	(86,166)	(107,984)
Proceeds from sale of loans	102,275	116,965
Gain on loans sold	(1,837)	(1,600)
Increase in fair value of loans held-for-sale	(373)	(354)
Loss (gain) on derivatives	594	(300)
Net change in accrued income and other assets	2,294	(1,449)
Net change in accrued expenses and other liabilities	(1,740)	(1,319)
Net cash provided by operating activities	20,232	7,986
Investing Activities		
Net loan activity, excluding purchases	(173,702)	(78,894)
Proceeds from sale of other real estate owned	30	—
Maturities and calls of securities available-for-sale	20,565	6,088
Purchase of securities available-for-sale	(31,475)	(97,928)
Purchase of securities held-to-maturity	(2,550)	—
Purchase of Federal Home Loan Bank of Indianapolis stock	(4,140)	—
Purchase of premises and equipment	(184)	(268)
Loans purchased	(8,821)	(8,007)
Net cash used in investing activities	(200,277)	(179,009)
Financing Activities		
Net increase in deposits	94,252	287,124
Cash dividends paid	(388)	(267)
Proceeds from advances from Federal Home Loan Bank	192,000	40,000
Repayment of advances from Federal Home Loan Bank	(92,000)	(80,000)
Other, net	(173)	(42)
Net cash provided by financing activities	193,691	246,815
Net Increase in Cash and Cash Equivalents	13,646	75,792
Cash and Cash Equivalents, Beginning of Period	39,452	25,152
Cash and Cash Equivalents, End of Period	$53,098	$100,944
Supplemental Disclosures		
Cash paid during the period for interest	$5,897	$3,561
Cash paid during the period for taxes	—	1,521
Cash dividends declared, paid in subsequent period	390	269
Securities purchased during the period, settled in subsequent period	2,175	8,131

See Notes to Condensed Consolidated Financial Statements

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First Internet Bancorp
Notes to Condensed Consolidated Financial Statements – Unaudited
(Table amounts in thousands except share and per share data)

Note 1: Basis of Presentation

The accompanying unaudited condensed consolidated financial statements have been prepared in conformity with U.S. generally accepted accounting principles ("GAAP") for interim financial information and pursuant to the rules and regulations of the SEC. Accordingly, they do not include all of the information or footnotes necessary for a complete presentation of financial condition, results of operations, or cash flows in accordance with GAAP. In our opinion, all adjustments (consisting only of normal recurring adjustments) necessary for a fair presentation have been included. The results of operations for the three months ended March 31, 2017 are not necessarily indicative of the results expected for the year ending December 31, 2017 or any other period. The March 31, 2017 condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes included in the First Internet Bancorp Annual Report on Form 10-K for the year ended December 31, 2016.

The preparation of the condensed consolidated financial statements in conformity with GAAP requires management to make estimates, judgments, or assumptions that could have a material effect on the carrying value of certain assets and liabilities. These estimates, judgments, and assumptions affect the amounts reported in the condensed consolidated financial statements and the disclosures provided. The determination of the allowance for loan losses, valuations and impairments of investment securities, and the accounting for income tax expense are highly dependent upon management's estimates, judgments, and assumptions where changes in any of these could have a significant impact on the financial statements.

The condensed consolidated financial statements include the accounts of First Internet Bancorp (the "Company"), its wholly-owned subsidiary, First Internet Bank of Indiana (the "Bank"), and the Bank's two wholly-owned subsidiaries, First Internet Public Finance Corp. and JKH Realty Services, LLC. All significant intercompany accounts and transactions have been eliminated in consolidation.

The Company is subject to claims and lawsuits that arise primarily in the ordinary course of business. It is the opinion of management that the disposition or ultimate resolution of such claims and lawsuits will not have a material adverse effect on the consolidated financial position, results of operations, and cash flows of the Company.

Certain reclassifications have been made to the 2016 financial statements to conform to the presentation of the 2017 financial statements. These reclassifications had no effect on net income.

Note 2: Earnings Per Share

Earnings per share of common stock are based on the weighted-average number of basic shares and dilutive shares outstanding during the period.

The following is a reconciliation of the weighted-average common shares for the basic and diluted earnings per share computations for the three months ended March 31, 2017 and 2016.

	Three Months Ended March 31,	
	2017	2016
Basic earnings per share		
Net income	$2,832	$ 2,432
Weighted-average common shares	6,547,807	4,541,728
Basic earnings per common share	$0.43	$ 0.54
Diluted earnings per share		
Net income	$2,832	$ 2,432
Weighted-average common shares	6,547,807	4,541,728
Dilutive effect of warrants	17,940	11,293
Dilutive effect of equity compensation	36,453	22,534
Weighted-average common and incremental shares	6,602,200	4,575,555
Diluted earnings per common share	$0.43	$ 0.53
Number of warrants excluded from the calculation of diluted earnings per share as the exercise prices were greater than the average market price of the Company's common stock during the period	—	—

Note 3: Securities

The following tables summarize securities available-for-sale and securities held-to-maturity as of March 31, 2017 and December 31, 2016.

	March 31, 2017			
	Amortized	Gross Unrealized		Fair
	Cost	Gains	Losses	Value
Securities available-for-sale				
U.S. Government-sponsored agencies	$113,933	$168	$(814)	$113,287
Municipal securities	97,578	82	(5,232)	92,428
Mortgage-backed securities	235,879	39	(6,482)	229,436
Asset-backed securities	9,873	127	—	10,000
Corporate securities	23,107	—	(1,125)	21,982
Other securities	3,000	—	(68)	2,932
Total available-for-sale	$483,370	$416	$(13,721)	$470,065

	March 31, 2017			
	Amortized	Gross Unrealized		Fair
	Cost	Gains	Losses	Value
Securities held-to-maturity				
Municipal securities	$10,169	$—	$(466)	$9,703
Corporate securities	9,049	88	(36)	9,101
Total held-to-maturity	$19,218	$88	$(502)	$18,804

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	December 31, 2016			
	Amortized	Gross Unrealized		Fair
	Cost	Gains	Losses	Value
Securities available-for-sale				
U.S. Government-sponsored agencies	$92,599	$167	$(870)	$91,896
Municipal securities	97,647	85	(5,846)	91,886
Mortgage-backed securities	238,354	—	(6,713)	231,641
Asset-backed securities	19,470	65	(1)	19,534
Corporate securities	20,000	—	(1,189)	18,811
Other securities	3,000	—	(68)	2,932
Total available-for-sale	$471,070	$317	$(14,687)	$456,700

	December 31, 2016			
	Amortized	Gross Unrealized		Fair
	Cost	Gains	Losses	Value
Securities held-to-maturity				
Municipal securities	$10,171	$—	$(498)	$9,673
Corporate securities	6,500	24	—	6,524
Total held-to-maturity	$16,671	$24	$(498)	$16,197

The carrying value of securities at March 31, 2017 is shown below by their contractual maturity date. Actual maturities will differ because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Available-for-Sale	
	Amortized	Fair
	Cost	Value
One to five years	$966	$936
Five to ten years	38,782	38,038
After ten years	194,870	188,723
	234,618	227,697
Mortgage-backed securities	235,879	229,436
Asset-backed securities	9,873	10,000
Other securities	3,000	2,932
Total	$483,370	$470,065

	Held-to-Maturity	
	Amortized	Fair
	Cost	Value
Five to ten years	$12,448	$12,347
After ten years	6,770	6,457
Total	$19,218	$18,804

There were no sales of available-for-sale securities that resulted in gross gains or gross losses during the three months ended March 31, 2017 or 2016.

Certain investments in debt securities are reported in the condensed consolidated financial statements at an amount less than their historical cost. The total fair value of these investments at March 31, 2017 and December 31, 2016 was $427.0 million and $422.9 million, which was approximately 87% and 89%, respectively, of the Company's available-for-sale and held-to-maturity securities portfolios. These declines resulted primarily from fluctuations in market interest rates after purchase. Management believes the declines in fair value for these securities are temporary.

Should the impairment of any of these securities become other than temporary, the cost basis of the investment will be reduced with the resulting loss recognized in net income in the period the other-than-temporary impairment ("OTTI") is identified.

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

The unrealized losses on the Company's investments in securities issued by U.S. Government-sponsored agencies, municipal organizations and corporate entities were caused by interest rate changes. The contractual terms of those investments do not permit the issuer to settle the securities at a price less than the amortized cost bases of the investments. Because the Company does not intend to sell the investments and it is not likely that the Company will be required to sell the investments before recovery of their amortized cost bases, which may be maturity, the Company does not consider those investments to be other-than-temporarily impaired at March 31, 2017.

Mortgage-Backed Securities

The unrealized losses on the Company's investments in mortgage-backed securities were caused by interest rate changes. The Company expects to recover the amortized cost bases over the term of the securities. Because the Company does not intend to sell the investments and it is not likely that the Company will be required to sell the investments before recovery of their amortized cost bases, which may be maturity, the Company does not consider those investments to be other-than-temporarily impaired at March 31, 2017.

Other Securities

The unrealized losses on the Company's investments in other securities were caused by the investment in the Community Reinvestment Act Qualified Fund. Because the Company does not intend to sell the investment and it is not likely that the Company will be required to sell the investment before recovery of its amortized cost basis, the Company does not consider this investment to be other-than-temporarily impaired at March 31, 2017.

The following tables show the available-for-sale and held-to-maturity securities portfolios' gross unrealized losses and fair values, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position at March 31, 2017 and December 31, 2016.

	March 31, 2017					
	Less Than 12 Months		12 Months or Longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Securities available-for-sale						
U.S. Government-sponsored agencies	$83,928	$(786)	$201	$(28)	$84,129	$(814)
Municipal securities	86,004	(5,232)	—	—	86,004	(5,232)
Mortgage-backed securities	216,465	(6,395)	3,229	(87)	219,694	(6,482)
Corporate securities	3,088	(19)	18,894	(1,106)	21,982	(1,125)
Other securities	2,932	(68)	—	—	2,932	(68)
Total	$392,417	$(12,500)	$22,324	$(1,221)	$414,741	$(13,721)

	March 31, 2017					
	Less Than 12 Months		12 Months or Longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Securities held-to-maturity						

Municipal securities	$9,703	$(466)	$—	$—	$9,703	$(466)
Corporate securities	2,513	(36)	—	—	2,513	(36)
Total	$12,216	$(502)	$—	$—	$12,216	$(502)

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	December 31, 2016					
	Less Than 12 Months		12 Months or Longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Securities available-for-sale						
U.S. Government-sponsored agencies	$68,625	$(840)	$260	$(30)	$68,885	$(870)
Municipal securities	86,424	(5,846)	—	—	86,424	(5,846)
Mortgage-backed securities	231,641	(6,713)	—	—	231,641	(6,713)
Asset-backed securities	—	—	4,520	(1)	4,520	(1)
Corporate securities	—	—	18,811	(1,189)	18,811	(1,189)
Other securities	2,932	(68)	—	—	2,932	(68)
Total	$389,622	$(13,467)	$23,591	$(1,220)	$413,213	$(14,687)

	December 31, 2016					
	Less Than 12 Months		12 Months or Longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Securities held-to-maturity						
Municipal securities	$9,673	$(498)	$—	$—	$9,673	$(498)
Total	$9,673	$(498)	$—	$—	$9,673	$(498)

Note 4: Loans

Loans that management intends to hold until maturity are reported at their outstanding principal balance adjusted for unearned income, charge-offs, the allowance for loan losses, any unamortized deferred fees or costs on originated loans, and unamortized premiums or discounts on purchased loans.

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

Categories of loans include:

	March 31, 2017	December 31, 2016
Commercial loans		
Commercial and industrial	$97,487	$102,437
Owner-occupied commercial real estate	62,887	57,668
Investor commercial real estate	8,510	13,181
Construction	49,618	53,291
Single tenant lease financing	665,382	606,568
Public finance	77,995	—
Total commercial loans	961,879	833,145
Consumer loans		
Residential mortgage	246,014	205,554
Home equity	34,925	35,036
Other consumer	188,191	173,449
Total consumer loans	469,130	414,039
Total commercial and consumer loans	1,431,009	1,247,184

Deferred loan origination costs and premiums and discounts on purchased loans	2,181	3,605
Total loans	1,433,190	1,250,789
Allowance for loan losses	(11,894)	(10,981)
Net loans	$ 1,421,296	$ 1,239,808

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

Commercial and Industrial: Commercial and industrial loans' sources of repayment are primarily based on the identified cash flows of the borrower and secondarily on the underlying collateral provided by the borrower. The cash flows of borrowers, however, may not be as expected, and the collateral securing these loans may fluctuate in value. Loans are made for working capital, equipment purchases, or other purposes. Most commercial and industrial loans are secured by the assets being financed and may incorporate a personal guarantee.

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

Investor Commercial Real Estate: These loans are underwritten primarily based on the cash flow expected to be generated from the property and are secondarily supported by the value of the real estate. These loans typically incorporate a personal guarantee. This portfolio segment generally involves higher loan principal amounts, and the repayment of these loans is generally dependent on the successful operation of the property securing the loan or the business conducted on the property securing the loan. Investor commercial real estate loans may be more adversely affected by conditions in the real estate markets, changing industry dynamics, or the overall health of the general economy. The properties securing the Company's investor commercial real estate portfolio tend to be diverse in terms of property type and are typically located in the state of Indiana and markets adjacent to Indiana. Management monitors and evaluates commercial real estate loans based on property financial performance, collateral value, guarantor strength, and other risk grade criteria. As a general rule, the Company avoids financing special use projects or properties outside of its designated market areas unless other underwriting factors are present to mitigate these additional risks.

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

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

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

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

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

Other Consumer: These loans primarily consist of consumer loans and credit cards. Consumer loans may be secured by consumer assets such as horse trailers or recreational vehicles. Some consumer loans are unsecured, such as small installment loans, home improvement loans and certain lines of credit. Repayment of consumer loans is primarily dependent upon the personal income of the borrowers, which can be impacted by economic conditions in their market areas such as unemployment levels. Risk is mitigated by the fact that the loans are of smaller individual amounts and spread over a large number of borrowers in geographically diverse locations throughout the country.

Allowance for Loan Losses Methodology

Company policy is designed to maintain an adequate allowance for loan losses (“ALLL”). The portfolio is segmented by loan type, and the required ALLL for types of performing homogeneous loans which do not have a specific reserve is determined by applying a factor based on average historical losses, adjusted for current economic factors and portfolio trends. Management believes the historical loss experience methodology is appropriate in the current economic environment as it captures loss rates that are comparable to the current period being analyzed. Management adds qualitative factors for observable trends, changes in internal practices, changes in delinquencies and impairments, and external factors. Observable factors include changes in the composition and size of portfolios, as well as loan terms or concentration levels. The Company evaluates the impact of internal changes such as management and staff experience levels or modification to loan underwriting processes. Delinquency trends are scrutinized for both volume and severity of past due, nonaccrual, or classified loans as well as any changes in the value of underlying collateral. Finally, the Company considers the effect of other external factors such as national, regional, and local economic and business conditions, as well as competitive, legal, and regulatory requirements. Loans that are considered to be impaired are evaluated to determine the need for a specific allowance by applying at least one of three methodologies: present value of future cash flows; fair value of collateral less costs to sell; or the loan’s observable market price. All troubled debt restructurings (“TDR”) are considered impaired loans. Loans evaluated for impairment are removed from other pools to prevent double-counting. Accounting Standards Codification (“ASC”) Topic 310, Receivables, requires that impaired loans be measured based on the present value of expected future cash flows discounted at the loans’ effective interest rates or the fair value of the underlying collateral less costs to sell and allows existing methods for recognizing interest income.

Provision for Loan Losses

A provision for estimated losses on loans is charged to income based upon management’s evaluation of the potential losses. Such an evaluation, which includes a review of all loans for which full repayment may not be reasonably assured, considers, among other matters, the estimated net realizable value of the underlying collateral, as applicable, economic conditions, loan loss experience, and other factors that are particularly susceptible to changes that could result in a material adjustment in the near term. While management attempts to use the best information available in making its evaluations, future allowance adjustments may be necessary if economic conditions change substantially from the assumptions used in making the evaluations.

Policy for Charging Off Loans

The Company’s policy is to charge off a loan at any point in time when it no longer can be considered a bankable asset, meaning collectible within the parameters of policy. A secured loan is generally charged down to the estimated fair value of the collateral, less costs to sell, no later than when it is 120 days past due as to principal or interest. An unsecured loan generally is charged off no later than when it is 180 days past due as to principal or interest. A home improvement loan generally is charged off no later than when it is 90 days past due as to principal or interest.

The following tables present changes in the balance of the ALLL during the three month periods ended March 31, 2017 and 2016.

	Three Months Ended March 31, 2017				
Allowance for loan losses:	Balance, Beginning of Period	Provision (Credit) Charged to Expense	Losses Charged Off	Recoveries	Balance, End of Period
Commercial and industrial	$1,352	$(73)	$—	$ 44	$1,323
Owner-occupied commercial real estate	582	53	—	—	635
Investor commercial real estate	168	(67)	—	—	101
Construction	544	(82)	—	—	462
Single tenant lease financing	6,248	605	—	—	6,853
Public finance	—	142	—	—	142
Residential mortgage	754	150	—	—	904
Home equity	102	(4)	—	3	101
Other consumer	1,231	311	(223)	54	1,373
Total	$10,981	$1,035	$(223)	$ 101	$11,894

	Three Months Ended March 31, 2016				
Allowance for loan losses:	Balance, Beginning of Period	Provision (Credit) Charged to Expense	Losses Charged Off	Recoveries	Balance, End of Period
Commercial and industrial	$1,367	$ 16	$—	$ —	$ 1,383
Owner-occupied commercial real estate	476	(1)	—	—	475
Investor commercial real estate	212	(15)	—	—	197
Construction	500	63	—	—	563
Single tenant lease financing	3,931	747	—	—	4,678
Residential mortgage	896	(50)	—	25	871
Home equity	125	(7)	—	2	120
Other consumer	844	193	(149)	45	933
Total	$8,351	$ 946	$(149)	$ 72	$ 9,220

The following tables present the recorded investment in loans based on portfolio segment and impairment method as of March 31, 2017, and December 31, 2016.

	Loans			Allowance for Loan Losses		
March 31, 2017	Ending Balance: Collectively Evaluated for Impairment	Ending Balance: Individually Evaluated for Impairment	Ending Balance	Ending Balance: Collectively Evaluated for Impairment	Ending Balance: Individually Evaluated for Impairment	Ending Balance
Commercial and industrial	$95,340	$ 2,147	$97,487	$1,278	$ 45	$1,323
Owner-occupied commercial real estate	62,887	—	62,887	635	—	635
Investor commercial real estate	8,510	—	8,510	101	—	101
Construction	49,618	—	49,618	462	—	462

Single tenant lease financing	665,382	—	665,382	6,853	—	6,853
Public finance	77,995	—	77,995	142	—	142
Residential mortgage	244,375	1,639	246,014	904	—	904
Home equity	34,925	—	34,925	101	—	101
Other consumer	188,071	120	188,191	1,373	—	1,373
Total	$1,427,103	$ 3,906	$1,431,009	$11,849	$ 45	$11,894

December 31, 2016	Loans Ending Balance: Collectively Evaluated for Impairment	Loans Ending Balance: Individually Evaluated for Impairment	Loans Ending Balance	Allowance for Loan Losses Ending Balance: Collectively Evaluated for Impairment	Allowance for Loan Losses Ending Balance: Individually Evaluated for Impairment	Allowance for Loan Losses Ending Balance
Commercial and industrial	$102,437	$ —	$102,437	$1,352	$ —	$1,352
Owner-occupied commercial real estate	57,668	—	57,668	582	—	582
Investor commercial real estate	13,181	—	13,181	168	—	168
Construction	53,291	—	53,291	544	—	544
Single tenant lease financing	606,568	—	606,568	6,248	—	6,248
Residential mortgage	203,842	1,712	205,554	754	—	754
Home equity	35,036	—	35,036	102	—	102
Other consumer	173,321	128	173,449	1,231	—	1,231
Total	$1,245,344	$ 1,840	$1,247,184	$10,981	$ —	$10,981

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

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

- "Special Mention" - Loans that possess some credit deficiency or potential weakness, which deserves close attention.

- "Substandard" - Loans that possess a defined weakness or weaknesses that jeopardize the liquidation of the debt. Loans characterized by the distinct possibility that the institution will sustain some loss if the deficiencies are not corrected. Loans that are inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any.

- "Doubtful" - Such loans have been placed on nonaccrual status and may be heavily dependent upon collateral possessing a value that is difficult to determine or based upon some near-term event that lacks clear certainty. These loans have all of the weaknesses of those classified as Substandard; however, based on existing conditions, these weaknesses make full collection of the principal balance highly improbable.

- "Loss" - Loans that are considered uncollectible and of such little value that continuing to carry them as assets is not warranted.

Nonaccrual Loans

Any loan which becomes 90 days delinquent or for which the full collection of principal and interest may be in doubt will be considered for nonaccrual status. At the time a loan is placed on nonaccrual status, all accrued but unpaid interest will be reversed from interest income. Placing the loan on nonaccrual status does not relieve the borrower of the obligation to repay interest. A loan placed on nonaccrual status may be restored to accrual status when all delinquent principal and interest has been brought current, and the Company expects full payment of the remaining contractual principal and interest.

The following tables present the credit risk profile of the Company's commercial and consumer loan portfolios based on rating category and payment activity as of March 31, 2017 and December 31, 2016.

	March 31, 2017			
	Pass	Special Mention	Substandard	Total
Commercial and industrial	$89,570	$ 5,321	$ 2,596	$97,487
Owner-occupied commercial real estate	62,238	639	10	62,887
Investor commercial real estate	8,510	—	—	8,510
Construction	49,618	—	—	49,618
Single tenant lease financing	664,036	1,346	—	665,382
Public finance	77,995	—	—	77,995
Total commercial loans	$951,967	$ 7,306	$ 2,606	$961,879

	March 31, 2017		
	Performing	Nonaccrual	Total
Residential mortgage	$244,805	$ 1,209	$246,014
Home equity	34,925	—	34,925
Other consumer	188,136	55	188,191
Total consumer loans	$467,866	$ 1,264	$469,130

	December 31, 2016			
	Pass	Special Mention	Substandard	Total
Commercial and industrial	$99,200	$ 2,746	$ 491	$102,437
Owner-occupied commercial real estate	57,657	—	11	57,668
Investor commercial real estate	13,181	—	—	13,181
Construction	53,291	—	—	53,291
Single tenant lease financing	605,190	1,378	—	606,568
Total commercial loans	$828,519	$ 4,124	$ 502	$833,145

	December 31, 2016		
	Performing	Nonaccrual	Total
Residential mortgage	$204,530	$ 1,024	$205,554
Home equity	35,036	—	35,036
Other consumer	173,390	59	173,449
Total consumer loans	$412,956	$ 1,083	$414,039

The following tables present the Company's loan portfolio delinquency analysis as of March 31, 2017 and December 31, 2016.

	March 31, 2017							
	30-59 Days Past Due	60-89 Days Past Due	90 Days or More Past Due	Total Past Due	Current	Total Commercial and Consumer Loans	Non-accrual Loans	Total Loans 90 Days or More Past Due and Accruing
Commercial and industrial	$134	$ 110	$ —	$ 244	$97,243	$97,487	$2,147	$ —
Owner-occupied commercial real estate	—	—	—	—	62,887	62,887	—	—
Investor commercial real estate	—	—	—	—	8,510	8,510	—	—
Construction	—	—	—	—	49,618	49,618	—	—
Single tenant lease financing	—	—	—	—	665,382	665,382	—	—
Public finance	—	—	—	—	77,995	77,995	—	—
Residential mortgage	—	—	1,177	1,177	244,837	246,014	1,209	—
Home equity	—	—	—	—	34,925	34,925	—	—
Other consumer	167	115	26	308	187,883	188,191	55	—
Total	$301	$ 225	$ 1,203	$ 1,729	$1,429,280	$1,431,009	$3,411	$ —

	December 31, 2016							
	30-59 Days Past Due	60-89 Days Past Due	90 Days or More Past Due	Total Past Due	Current	Total Commercial and Consumer Loans	Non-accrual Loans	Total Loans 90 Days or More Past Due and Accruing
Commercial and industrial	$27	$ —	$ —	$ 27	$102,410	$102,437	$—	$ —
Owner-occupied commercial real estate	—	—	—	—	57,668	57,668	—	—
Investor commercial real estate	—	—	—	—	13,181	13,181	—	—
Construction	—	—	—	—	53,291	53,291	—	—
Single tenant lease financing	—	—	—	—	606,568	606,568	—	—
Residential mortgage	—	347	991	1,338	204,216	205,554	1,024	—
Home equity	—	—	—	—	35,036	35,036	—	—
Other consumer	173	91	25	289	173,160	173,449	59	—
Total	$200	$ 438	$ 1,016	$ 1,654	$1,245,530	$1,247,184	$1,083	$ —

Impaired Loans

A loan is designated as impaired, in accordance with the impairment accounting guidance, when, based on current information or events, it is probable that the Company will be unable to collect all amounts due (principal and interest) according to the contractual terms of the loan agreement. Payments with delays generally not exceeding 90 days outstanding are not considered impaired. Certain nonaccrual and substantially all delinquent loans more than 90 days past due may be considered to be impaired. Generally, loans are placed on nonaccrual status at 90 days past due and accrued interest is reversed against earnings, unless the loan is well-secured and in the process of collection. The accrual of interest on impaired and nonaccrual loans is discontinued when, in management's opinion, the borrower may be unable to meet payments as they become due.

Impaired loans include nonperforming loans as well as loans modified in TDRs where concessions have been granted to borrowers experiencing financial difficulties. These concessions could include a reduction in the interest rate on the loan, payment extensions, forgiveness of principal, forbearance, or other actions intended to maximize collection.

ASC Topic 310, Receivables, requires that impaired loans be measured based on the present value of expected future cash flows discounted at the loans' effective interest rates or the fair value of the underlying collateral, less costs to sell, and allows existing methods for recognizing interest income.

The following table presents the Company's impaired loans as of March 31, 2017 and December 31, 2016.

	March 31, 2017			December 31, 2016		
	Recorded Balance	Unpaid Principal Balance	Specific Allowance	Recorded Balance	Unpaid Principal Balance	Specific Allowance
Loans without a specific valuation allowance						
Commercial and industrial	$2,037	$ 2,037	$ —	$—	$ —	$ —
Residential mortgage	1,639	1,751	—	1,712	1,824	—
Other consumer	120	159	—	128	184	—
Total	3,796	3,947	—	1,840	2,008	—
Loans with a specific valuation allowance						
Commercial and industrial	110	110	45	—	—	—
Total	110	110	45	—	—	—
Total impaired loans	$3,906	$ 4,057	$ 45	$1,840	$ 2,008	$ —

The table below presents average balances and interest income recognized for impaired loans during the three month periods ended March 31, 2017 and March 31, 2016.

	Three Months Ended March 31, 2017		Three Months Ended March 31, 2016	
	Average Balance	Interest Income	Average Balance	Interest Income
Loans without a specific valuation allowance				
Commercial and industrial	$ 535	$ —	$ —	$ —
Residential mortgage	1,692	—	1,068	3
Other consumer	140	—	155	2
Total	2,367	—	1,223	5
Loans with a specific valuation allowance				
Commercial and industrial	28	—	—	—
Total	28	—	—	—
Total impaired loans	$ 2,395	$ —	$ 1,223	$ 5

As of March 31, 2017 and December 31, 2016, the Company had $0.0 million and less than $0.1 million, respectively, in residential mortgage other real estate owned. There was $1.0 million at both March 31, 2017 and December 31, 2016, in the process of foreclosure.

Note 5: Premises and Equipment

The following table summarizes premises and equipment at March 31, 2017 and December 31, 2016.

	March 31, 2017	December 31, 2016
Land	$ 2,500	$ 2,500
Building and improvements	5,626	5,441
Furniture and equipment	7,077	7,079
Less: accumulated depreciation	(5,350)	(4,976)
Total	$ 9,853	$ 10,044

Note 6: Goodwill

As of March 31, 2017 and December 31, 2016, the carrying amount of goodwill was $4.7 million. There have been no changes in the carrying amount of goodwill for the periods ended March 31, 2017 and December 31, 2016. Goodwill is tested for impairment on an annual basis as of August 31, or whenever events or changes in circumstances indicate the carrying amount of goodwill exceeds its implied fair value. No events or changes in circumstances have occurred since the August 31, 2016 annual impairment test that would suggest it was more likely than not goodwill impairment existed.

Note 7: Subordinated Debt

In June 2013, the Company issued a subordinated debenture (the “2021 Debenture”) in the principal amount of $3.0 million. The 2021 Debenture bears a fixed interest rate of 8.00% per year, payable quarterly, and is scheduled to mature on June 28, 2021. The 2021 Debenture may be repaid, without penalty, at any time after June 28, 2016. The 2021 Debenture is intended to qualify as Tier 2 capital under regulatory guidelines.

In connection with the 2021 Debenture, the Company also issued a warrant to purchase up to 48,750 shares of common stock at an initial per share exercise price equal to $19.33. The warrant became exercisable on June 28, 2014 and, unless previously exercised, will expire on June 28, 2021. The Company has the right to force an exercise of the warrant after the 2021 Debenture has been repaid in full if the volume-weighted average price of a share of its common stock exceeds $30.00 for any 20-day period since the issuance date of the 2021 Debenture.

The Company used the Black-Scholes option pricing model to assign a fair value of $0.3 million to the warrant as of June 28, 2013. The following assumptions were used to value the warrant: a risk-free interest rate of 0.66% per the U.S. Treasury yield curve in effect at the date of issuance, an expected dividend yield of 1.19% calculated using the dividend rate and stock price at the date of the issuance, and an expected volatility of 34% based on the estimated volatility of the Company’s stock over the expected term of the warrant, which was estimated to be three years.

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

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

The following table presents the principal balance and unamortized discount and debt issuance costs for the 2021 Debenture, the 2025 Note and the 2026 Notes as of March 31, 2017 and December 31, 2016.

	March 31, 2017		December 31, 2016	
	Principal	Unamortized Discount and Debt Issuance Costs	Principal	Unamortized Discount and Debt Issuance Costs
2021 Debenture	$3,000	$ —	$3,000	$ —
2025 Note	10,000	(205)	10,000	(210)
2026 Notes	25,000	(1,180)	25,000	(1,212)
Total	$38,000	$ (1,385)	$38,000	$ (1,422)

Note 8: Benefit Plans

Employment Agreement

The Company has entered into an employment agreement with its Chief Executive Officer that provides for the continuation of salary and certain benefits for a specified period of time under certain conditions. Under the terms of the agreement, these payments could occur in the event of a change in control of the Company, as defined in the agreement, along with other specific conditions.

2013 Equity Incentive Plan

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

The Company recorded $0.3 million and $0.2 million of share-based compensation expense for the three month periods ended March 31, 2017 and 2016, respectively, related to awards made under the 2013 Plan.

The following table summarizes the status of the 2013 Plan awards as of March 31, 2017, and activity for the three months ended March 31, 2017.

	Restricted Stock Units	Weighted-Average Grant Date Fair Value Per Share	Restricted Stock Awards	Weighted-Average Grant Date Fair Value Per Share	Deferred Stock Units	Weighted-Average Grant Date Fair Value Per Share
Nonvested at December 31, 2016	49,781	$ 23.07	16,330	$ 19.06	—	$ —
Granted	42,392	31.00	5,628	31.00	2	30.05
Vested	(19,835)	22.43	(14,413)	18.99	(2)	30.05
Nonvested at March 31, 2017	72,338	$ 27.89	7,545	$ 28.10	—	$ —

At March 31, 2017, the total unrecognized compensation cost related to nonvested awards was $2.0 million with a weighted-average expense recognition period of 2.4 years.

Directors Deferred Stock Plan

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

The following table summarizes the status of deferred stock rights related to the Directors Deferred Stock Plan for the three months ended March 31, 2017.

	Deferred Stock Rights
Outstanding, beginning of period	82,377
Granted	156
Exercised	—
Outstanding, end of period	82,533

All deferred stock rights granted during the 2017 period were additional rights issued in lieu of cash dividends payable on outstanding deferred stock rights.

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Note 9: Fair Value of Financial Instruments

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

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

Level 2	Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities
Level 3	Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities

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

Available-for-Sale Securities

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

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

In certain cases where Level 1 or Level 2 inputs are not available, securities are classified within Level 3 of the hierarchy. Fair values are calculated using discounted cash flows. Discounted cash flows are calculated based off of the anticipated future cash flows updated to incorporate loss severities. Rating agency and industry research reports as well as default and deferral activity are reviewed and incorporated into the calculation. The Company did not own any securities classified within Level 3 of the hierarchy as of March 31, 2017 or December 31, 2016.

Loans Held-for-Sale (mandatory pricing agreements)

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

Forward Contracts

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

Interest Rate Lock Commitments

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

The following tables present the fair value measurements of assets and liabilities recognized in the accompanying condensed consolidated balance sheets measured at fair value on a recurring basis and the level within the fair value hierarchy in which the fair value measurements fall at March 31, 2017 and December 31, 2016.

		March 31, 2017		
		Fair Value Measurements Using		
	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
U.S. Government-sponsored agencies	$113,287	$ —	$ 113,287	$ —
Municipal securities	92,428	—	92,428	—
Mortgage-backed securities	229,436	—	229,436	—
Asset-backed securities	10,000	—	10,000	—
Corporate securities	21,982	—	21,982	—
Other securities	2,932	2,932	—	—
Total available-for-sale securities	470,065	2,932	467,133	—
Loans held-for-sale (mandatory pricing agreements)	8,692	—	8,692	—
Forward contracts	(191)	(191)	—	—
IRLCs	645	—	—	645

		December 31, 2016		
		Fair Value Measurements Using		
	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
U.S. Government-sponsored agencies	$91,896	$ —	$ 91,896	$ —
Municipal securities	91,886	—	91,886	—
Mortgage-backed securities	231,641	—	231,641	—
Asset-backed securities	19,534	—	19,534	—
Corporate securities	18,811	—	18,811	—
Other securities	2,932	2,932	—	—
Total available-for-sale securities	456,700	2,932	453,768	—
Loans held-for-sale (mandatory pricing agreements)	27,101	—	27,101	—
Forward contracts	438	438	—	—
IRLCs	610	—	—	610

The following tables reconcile the beginning and ending balances of recurring fair value measurements recognized in the accompanying condensed consolidated balance sheets using significant unobservable (Level 3) inputs for the three month periods ended March 31, 2017 and March 31, 2016.

	Three Months Ended Interest Rate Lock Commitments
Balance, January 1, 2017	$ 610
Total realized gains	
Included in net income	35
Balance, March 31, 2017	$ 645
Balance, January 1, 2016	$ 582
Total realized gains	
Included in net income	701
Balance, March 31, 2016	$ 1,283

The following describes valuation methodologies and inputs used for assets measured at fair value on a nonrecurring basis as well as the general classification of such assets pursuant to the valuation hierarchy.

Impaired Loans

Loans for which it is probable that the Company will not collect all principal and interest due according to contractual terms are measured for impairment. The amount of the impairment may be determined based on the fair value of the underlying collateral, less costs to sell, the estimated present value of future cash flows or the loan's observable market price.

If the impaired loan is identified as collateral dependent, the fair value of the underlying collateral, less costs to sell, is used to measure impairment. This method requires obtaining a current independent appraisal of the collateral and applying a discount factor to the value. If the impaired loan is not collateral dependent, the Company utilizes a discounted cash flow analysis to measure impairment.

Impaired loans with a specific valuation allowance based on the value of the underlying collateral or a discounted cash flow analysis are classified as Level 3 assets.

There were no impaired loans that were measured at fair value on a nonrecurring basis at March 31, 2017 or December 31, 2016.

Significant Unobservable (Level 3) Inputs

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

	Fair Value at March	Valuation Technique	Significant Unobservable Inputs	Range

	31, 2017			
IRLCs	645	Discounted cash flow	Loan closing rates	43% - 99%

	Fair Value at December 31, 2016	Valuation Technique	Significant Unobservable Inputs	Range
IRLCs	$ 610	Discounted cash flow	Loan closing rates	43% - 99%

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

Cash and Cash Equivalents

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

Interest-Bearing Time Deposits

The fair value of these financial instruments approximates carrying value.

Securities Held-to-Maturity

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

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

The fair value of these loans approximates carrying value.

Loans

The fair value of loans is estimated by discounting future cash flows using current rates at which similar loans would be made to borrowers with similar credit ratings and remaining maturities.

Accrued Interest Receivable

The fair value of these financial instruments approximates carrying value.

Federal Home Loan Bank of Indianapolis Stock

The fair value approximates carrying value.

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

Advances from Federal Home Loan Bank

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

Subordinated Debt

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

Accrued Interest Payable

The fair value of these financial instruments approximates carrying value.

Commitments

The fair value of commitments to extend credit are based on fees currently charged to enter into similar agreements with similar maturities and interest rates. The Company determined that the fair value of commitments was zero based on the contractual value of outstanding commitments at each of March 31, 2017 and December 31, 2016.

The following tables present the carrying value and estimated fair value of all financial assets and liabilities at March 31, 2017 and December 31, 2016.

	March 31, 2017 Fair Value Measurements Using				
	Carrying Amount	Fair Value	Quoted Prices In Active Market for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Cash and cash equivalents	$53,098	$53,098	$53,098	$ —	$ —
Interest-bearing time deposits	250	250	250	—	—
Securities held-to-maturity	19,218	18,804	—	18,804	—
Loans held-for-sale (best efforts pricing agreements)	4,510	4,510	—	4,510	
Loans	1,433,190	1,429,980	—	—	1,429,980
Accrued interest receivable	6,868	6,868	6,868	—	—
Federal Home Loan Bank of Indianapolis stock	13,050	13,050	—	13,050	—
Deposits	1,557,119	1,534,456	531,294	—	1,003,162
Advances from Federal Home Loan Bank	289,985	277,435	—	277,435	—
Subordinated debt	36,615	39,027	25,520	13,507	—
Accrued interest payable	148	148	148	—	—

	December 31, 2016 Fair Value Measurements Using				
	Carrying Amount	Fair Value	Quoted Prices In Active Market for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Cash and cash equivalents	$39,452	$39,452	$39,452	$ —	$ —
Interest-bearing time deposits	250	250	250	—	—
Securities held-to-maturity	16,671	16,197	—	16,197	—
Loans	1,250,789	1,244,918	—	—	1,244,918
Accrued interest receivable	6,708	6,708	6,708	—	—
Federal Home Loan Bank of Indianapolis stock	8,910	8,910	—	8,910	—
Deposits	1,462,867	1,441,794	492,435	—	949,359
Advances from Federal Home Loan Bank	189,981	186,258	—	186,258	—
Subordinated debt	36,578	38,425	24,900	13,525	—
Accrued interest payable	112	112	112	—	—

Note 10: Mortgage Banking Activities

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

During the three months ended March 31, 2017 and 2016, the Company originated mortgage loans held-for-sale of $86.2 million and $108.0 million, respectively, and sold $102.3 million and $117.0 million of mortgage loans, respectively, into the secondary market.

The following table presents the components of income from mortgage banking activities for the three months ended March 31, 2017 and 2016.

	Three Months Ended March 31,	
	2017	2016
Gain on loans sold	$1,837	$1,600
Gain resulting from the change in fair value of loans held-for-sale	373	354
Gain (loss) resulting from the change in fair value of derivatives	(594)	300
Net revenue from mortgage banking activities	$1,616	$2,254

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

Note 11: Derivative Financial Instruments

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

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

The following table presents the notional amount and fair value of IRLCs and forward contracts utilized by the Company at March 31, 2017 and December 31, 2016.

	March 31, 2017		December 31, 2016	
	Notional Amount	Fair Value	Notional Amount	Fair Value
Asset Derivatives				
Derivatives not designated as hedging instruments				
IRLCs	$26,980	$645	$36,311	$610
Forward contracts	—	—	61,000	438
Liability Derivatives				
Derivatives not designated as hedging instruments				
Forward contracts	37,500	(191)	—	—

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Fair values of derivative financial instruments were estimated using changes in mortgage interest rates from the date the Company entered into the IRLC and the balance sheet date. The following table summarizes the periodic changes in the fair value of the derivative financial instruments on the condensed consolidated statements of income for the three month periods ended March 31, 2017 and 2016.

	Amount of gain / (loss) recognized in the three months ended	
	March 31, 2017	March 31, 2016
Asset Derivatives		
Derivatives not designated as hedging instruments		
IRLCs	$ 35	$ 701
Liability Derivatives		
Derivatives not designated as hedging instruments		
Forward contracts	(629)	(401)

Note 12: Recent Accounting Pronouncements

Accounting Standards Update ("Update") 2014-09, Revenue from Contracts with Customers (Topic 606) (May 2014)

The amendments in this Update clarify the principals for recognizing revenue and develop a common revenue standard among industries. The core principle of the guidance 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. The guidance provides steps to follow to achieve the core principle. An entity should disclose sufficient information to enable users of financial statements to understand the nature, amount, timing and uncertainty of revenue and cash flows arising from contracts with customers.

The entity should apply the amendments using one of two retrospective methods described in the amendment. Accounting Standard Update 2015-14, Revenue from Contracts with Customers (Topic 606) delayed the effective date for public entities to annual reporting periods beginning after December 15, 2017, including interim reporting periods within that reporting period. Several subsequent amendments have been issued that provide clarifying guidance and are effective with the adoption of the original Update. Early adoption is permitted only as of annual reporting periods beginning after December 15, 2016, including interim reporting periods within that reporting period. The Company is in its preliminary stages of evaluating the impact of these amendments and currently cannot reasonably quantify the impact of the adoption of the amendments as a result of the complexity and extensive changes from the amendments. The Company expects to begin developing processes and procedures during 2017 to ensure it is fully compliant with the amendments at adoption date.

Accounting Standards Update 2016-02, Leases (Topic 842) (February 2016)

In February 2016, the Financial Accounting Standards Board amended its standards with respect to the accounting for leases. The amended standard serves to replace all current GAAP guidance on this topic and requires that an operating lease be recognized by the lessee on the balance sheet as a "right-of-use" asset along with a corresponding liability representing the rent obligation. Key aspects of current lessor accounting remain unchanged from existing guidance. This standard is expected to result in an increase to assets and liabilities recognized and, therefore, increase risk-weighted assets for regulatory capital purposes. The amended standard requires the use of the modified retrospective transition approach for existing leases that have not expired before the date of initial application and will become effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018. Earlier application of the amended standard is permitted. The Company does not expect to early adopt and is currently in the process of fully evaluating the amendments on the consolidated financial statements and will subsequently implement updated processes and accounting policies as deemed necessary. The overall impact of the new standard on financial condition, results of operations and regulatory capital cannot yet be determined.

Accounting Standards Update 2016-09, Compensation - Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting (March 2016)

This Update is part of an initiative to reduce complexity in accounting standards (the "Simplification Initiative") implemented by the Financial Accounting Standards Board. The objective of the Simplification Initiative is to identify, evaluate, and improve areas of GAAP for which cost and complexity can be reduced while maintaining or improving the usefulness of the information provided to users of financial statements. The areas for simplification in this Update involve several aspects of the accounting for share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. Below is a summary of simplifications for the current GAAP areas contained in this Update.

•Accounting for Income Taxes: All excess tax benefits and tax deficiencies (including tax benefits of dividends on share-based payment awards) should be recognized as income tax expense or benefit in the income statement. The tax effects of exercised or vested awards should be treated as discrete items in the reporting period in which they occur. An entity also should recognize excess tax benefits regardless of whether the benefit reduces taxes payable in the current period.

•Classification of Excess Tax Benefits on the Statement of Cash Flows: Excess tax benefits should be classified along with other income tax cash flows as an operating activity.

•Forfeitures: An entity can make an entity-wide accounting policy election to either estimate the number of awards that are expected to vest (current GAAP) or account for forfeitures when they occur.

•Minimum Statutory Tax Withholding Requirements: The threshold to qualify for equity classification permits withholding up to the maximum statutory tax rates in the applicable jurisdictions.

•Classification of Employee Taxes Paid on the Statement of Cash Flows When an Employer Withholds Shares for Tax-Withholding Purposes: Cash paid by an employer when directly withholding shares for tax-withholding purposes should be classified as a financing activity.

For public business entities, the amendments in this Update were effective for fiscal years beginning after December 15, 2016, including interim periods within those fiscal years. Amendments related to the timing of when excess tax benefits are recognized, minimum statutory withholding requirements and forfeitures should be applied using a modified retrospective transition method by means of a cumulative-effect adjustment to equity as of the beginning of the period in which the guidance is adopted. Amendments related to the presentation of employee taxes paid on the statement of cash flows when an employer withholds shares to meet the minimum statutory withholding requirement should be applied retrospectively. Amendments requiring recognition of excess tax benefits and tax deficiencies in the income statement should be applied prospectively. An entity may elect to apply the amendments related to the presentation of excess tax benefits on the statement of cash flows using either a prospective transition method or a retrospective transition method. Adoption of this Update had a $0.1 million reduction to the Company's income tax provision in the first quarter 2017.

Accounting Standards Update 2016-13, Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments (June 2016)

The main objective of this Update is to provide financial statement users with more decision-useful information about the expected credit losses on financial instruments and other commitments to extend credit held by a reporting entity at each reporting date. To achieve this objective, the amendments in this Update replace the incurred loss impairment methodology in current GAAP with a methodology that reflects expected credit losses and requires consideration of a broader range of reasonable and supportable information to inform credit loss estimates.

The amendments affect entities holding financial assets that are not accounted for at fair value through net income. The amendments affect loans, debt securities, off-balance-sheet credit exposures, and any other financial assets not excluded from the scope that have the contractual right to receive cash. The amendments in this Update affect an entity to varying degrees depending on the credit quality of the assets held by the entity, their duration, and how the entity applies current GAAP. There is diversity in practice in applying the incurred loss methodology, which means that before transition some entities may be more aligned, under current GAAP, than others to the new measure of expected credit losses. The following describes the main provisions of this Update.

•Assets Measured at Amortized Cost: The amendments in this Update require a financial asset (or a group of financial assets) measured at amortized cost basis to be presented at the net amount expected to be collected. The allowance for credit losses is a valuation account that is deducted from the amortized cost basis of the financial asset(s) to present the net carrying value at the amount expected to be collected on the financial asset. The income statement reflects the measurement of credit losses for newly recognized financial assets, as well as the expected increases or decreases of expected credit losses that have taken place during the period. The measurement of expected credit losses is based on relevant information about past events, including historical experience, current conditions, and reasonable and supportable forecasts that affect the collectability of the reported amount. An entity must use judgment in determining the relevant information and estimation methods that are appropriate in its circumstances.

•Available-for-Sale Debt Securities: Credit losses relating to available-for-sale debt securities should be recorded through an allowance for credit losses. Available-for-sale accounting recognizes that value may be realized either through collection of contractual cash flows or through sale of the security. Therefore, the amendments limit the amount of the allowance for credit losses to the amount by which fair value is below amortized cost because the classification as available-for-sale is premised on an investment strategy that recognizes that the investment could be sold at fair value, if cash collection would result in the realization of an amount less than fair value.

For public business entities that are U.S. Securities and Exchange Commission filers, the amendments in this Update are effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. All entities may adopt the amendments in this Update earlier as of the fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. An entity will apply the amendments in this Update through a cumulative-effect adjustment to retained earnings as of the beginning of the first reporting period in which the guidance is effective (that is, a modified-retrospective approach). A prospective transition approach is required for debt securities for which an other-than-temporary impairment had been recognized before the effective date. The effect of a prospective transition approach is to maintain the same amortized cost basis before and after the effective date of this Update.

The Company does not expect to early adopt and is currently evaluating the impact of the amendments on the Company’s consolidated financial statements and cannot determine or reasonably quantify the impact of the adoption of the amendments due to the complexity and extensive changes. The Company intends to develop processes and procedures during the next two years to ensure it is fully compliant with the amendments at adoption date. The Company has formed an implementation committee and has begun evaluating the data needed for implementation.

Accounting Standards Update 2017-08, Receivables - Nonrefundable Fees and Other Costs (SubTopic 310-20): Premium Amortization on Purchased Callable Debt Securities (March 2017)

The amendments in this Update shorten the amortization period for certain callable debt securities held at a premium. Specifically, the amendments require the premium to be amortized to the earliest call date. Under current GAAP, entities generally amortize the premium as an adjustment of yield over the contractual life of the instrument. The amendments do not require an accounting change for securities held at a discount; the discount continues to be amortized to maturity.

The amendments in this Update affect all entities that hold investments in callable debt securities that have an amortized cost basis in excess of the amount that is repayable by the issuer at the earliest call date (that is, at a premium). For public business entities, the amendments in this Update are effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018. Early adoption is permitted, including adoption in an interim period. If an entity early adopts the amendments in an interim period, any adjustments should be reflected as of the beginning of the fiscal year that includes that interim period. An entity should apply the amendments in this Update on a modified retrospective basis through a cumulative-effect adjustment directly to retained earnings as of the beginning of the period of adoption. Additionally, in the period of adoption, an entity should provide disclosures about a change in accounting principle. The Company does not expect to early adopt and is currently evaluating the impact of the amendments on the Company's consolidated financial statements.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our condensed consolidated financial statements and related notes appearing elsewhere in this report. This discussion and analysis includes certain forward-looking statements that involve risks, uncertainties, and assumptions. You should review the "Risk Factors" section of our Annual Report on Form 10-K for the year ended December 31, 2016 for a discussion of important factors that could cause actual results to differ materially from the results described in or implied by such forward-looking statements. See also "Cautionary Note Regarding Forward-Looking Statements" at the beginning of this report.

Overview

First Internet Bancorp ("we," "our," "us," or the "Company") is a bank holding company that conducts its business activities through its wholly-owned subsidiary, First Internet Bank of Indiana, an Indiana chartered bank (the "Bank"). The Bank was the first state-chartered, Federal Deposit Insurance Corporation ("FDIC") insured Internet bank and commenced banking operations in 1999. The Company was incorporated under the laws of the State of Indiana on September 15, 2005. On March 21, 2006, we consummated a plan of exchange by which we acquired all of the outstanding shares of the Bank.

We offer a wide range of commercial, small business, consumer and municipal banking products and services. We conduct our consumer and small business deposit operations primarily through online channels on a nationwide basis and have no traditional branch offices. Our residential mortgage products are offered nationwide primarily through an online direct-to-consumer platform and are supplemented with Central Indiana-based mortgage and construction lending. Our consumer lending products are primarily originated on a nationwide basis over the Internet as well as through relationships with dealerships and financing partners.

Our commercial banking products and services are delivered through a relationship banking model and include commercial real estate ("CRE") banking, commercial and industrial ("C&I") banking and public finance. Through our CRE team, we offer single tenant lease financing on a nationwide basis in addition to traditional investor commercial real estate and construction loans primarily within Central Indiana and adjacent markets. To meet the needs of commercial borrowers and depositors located primarily in Central Indiana, Phoenix, Arizona and adjacent markets, our C&I banking team provides credit solutions such as lines of credit, term loans, owner-occupied commercial real estate loans and corporate credit cards as well as treasury management services. Our public finance team, established in early 2017, provides a range of public and municipal lending and leasing products to government entities on a nationwide basis.

Results of Operations

The following table presents a summary of the Company's financial performance for the five most recent quarters.

(dollars in thousands except for share and per share data)	Three Months Ended March 31, 2017	December 31, 2016	September 30, 2016	June 30, 2016	March 31, 2016
Income Statement Summary:					
Net interest income	$11,457	$ 10,904	$ 10,338	$9,306	$9,141
Provision for loan losses	1,035	256	2,204	924	946
Noninterest income	2,131	2,891	4,898	3,748	2,540
Noninterest expense	8,698	8,158	8,413	7,875	7,005
Income tax provision	1,023	1,671	1,521	1,421	1,298
Net income	$2,832	$ 3,710	$ 3,098	$2,834	$2,432
Per Share Data:					
Earnings per share - basic	$0.43	$ 0.65	$ 0.55	$0.57	$0.54
Earnings per share - diluted	$0.43	$ 0.64	$ 0.55	$0.57	$0.53
Dividends declared per share	$0.06	$ 0.06	$ 0.06	$0.06	$0.06
Book value per common share	$24.24	$ 23.76	$ 24.79	$24.52	$23.98
Tangible book value per common share [1]	$23.52	$ 23.04	$ 23.94	$23.67	$22.93
Common shares outstanding	6,497,662	6,478,050	5,533,050	5,533,050	4,497,284
Average common shares outstanding:					
Basic	6,547,807	5,722,615	5,597,867	4,972,759	4,541,728
Diluted	6,602,200	5,761,931	5,622,181	4,992,025	4,575,555
Performance Ratios:					
Return on average assets	0.60 %	0.81 %	0.71 %	0.71 %	0.72 %
Return on average shareholders' equity	7.42 %	10.85 %	9.08 %	9.67 %	9.20 %
Return on average tangible common equity [1]	7.65 %	11.24 %	9.41 %	10.07 %	9.63 %
Net interest margin	2.50 %	2.42 %	2.42 %	2.39 %	2.78 %
Net interest margin - FTE [1,2]	2.57 %	2.48 %	2.47 %	2.43 %	2.80 %
Capital Ratios:					
Total shareholders' equity to assets	7.67 %	8.30 %	7.52 %	7.97 %	7.06 %
Tangible common equity to tangible assets ratio [1]	7.46 %	8.07 %	7.28 %	7.72 %	6.77 %
Tier 1 leverage ratio	8.41 %	8.65 %	7.62 %	8.08 %	7.65 %
Common equity tier 1 capital ratio	10.88 %	11.54 %	10.07 %	10.66 %	9.38 %
Tier 1 capital ratio	10.88 %	11.54 %	10.07 %	10.66 %	9.38 %
Total risk-based capital ratio	14.16 %	15.01 %	13.67 %	12.54 %	11.38 %

[1] This information represents a non-GAAP financial measure. See the "Reconciliation of Non-GAAP Financial Measures" for a reconciliation of these measures to their most directly comparable GAAP measures.
[2] On a fully-taxable equivalent ("FTE") basis assuming a 35% tax rate. Net interest income is adjusted to reflect income from assets such as municipal loans and securities that are exempt from Federal income taxes. This is to recognize the income tax savings that facilitates a comparison between taxable and tax-exempt assets. The Company believes that it is a standard practice in the banking industry to present net interest margin and net interest income on a fully-taxable equivalent basis as these measures provide useful information to make peer comparisons.

During the first quarter 2017, net income was $2.8 million, or $0.43 per diluted share, compared to first quarter 2016 net income of $2.4 million, or $0.53 per diluted share, representing an increase in net income of $0.4 million, or 16.4%. The comparability of diluted earnings per share between the first quarter 2017 and first quarter 2016 is impacted by the effect on average diluted shares outstanding resulting from the Company's issuance of an aggregate of

1,980,766 shares of common stock through equity offerings completed during May and December 2016.

The increase in net income in the first quarter 2017 compared to the first quarter 2016 was primarily due to a $2.3 million, or 25.3%, increase in net interest income and a $0.3 million, or 21.2%, decrease in income tax expense, partially offset by a $1.7 million, or 24.2%, increase in noninterest expense, a $0.4 million, or 16.1%, decrease in noninterest income and a $0.1 million, or 9.4%, increase in provision for loan losses.

During the first quarter 2017, return on average assets (“ROAA”) and return on average shareholders’ equity (“ROAE”) were 0.60% and 7.42%, respectively, compared to 0.72% and 9.20%, respectively, for the first quarter 2016. The decline in ROAA was a result of the Company’s growth in quarterly average assets of $552.9 million, or 40.9%, outpacing the quarterly net income growth of 16.4%. The decline in ROAE was a result of the Company’s growth in quarterly average shareholders’ equity of $48.5 million, or 45.7%, which also outpaced quarterly net income growth. The increase in average shareholders’ equity was impacted by the equity offerings completed in May and December 2016 which resulted in net proceeds of $46.2 million of common equity. While most significant components driving the results of operations were directionally consistent with average asset growth and average shareholders’ equity growth, net income growth was impacted by the decrease in noninterest income driven by lower revenue from mortgage banking activities (see Noninterest Income for further discussion of mortgage banking activities).

Consolidated Average Balance Sheets and Net Interest Income Analyses

For the periods presented, the following tables provide the average balances of interest-earning assets and interest-bearing liabilities and the related yields and cost of funds. The tables do not reflect any effect of income taxes. Balances are based on the average of daily balances. Nonaccrual loans are included in average loan balances.

(dollars in thousands)	Three Months Ended								
	March 31, 2017			December 31, 2016			March 31, 2016		
	Average Balance	Interest/Dividends	Yield/Cost	Average Balance	Interest/Dividends	Yield/Cost	Average Balance	Interest/Dividends	Yield/Cost
Assets									
Interest-earning assets									
Loans, including loans held-for-sale	$1,338,694	$14,156	4.29 %	$1,253,756	$13,660	4.33 %	$1,020,168	$11,189	4.41 %
Securities - taxable	381,522	2,367	2.52 %	384,286	2,262	2.34 %	202,898	1,169	2.32 %
Securities - non-taxable	93,323	697	3.03 %	95,044	686	2.87 %	22,179	165	2.99 %
Other earning assets	45,392	170	1.52 %	57,081	156	1.09 %	78,291	170	0.87 %
Total interest-earning assets	1,858,931	17,390	3.79 %	1,790,167	16,764	3.73 %	1,323,536	12,693	3.86 %
Allowance for loan losses	(11,299)			(10,711)			(8,655)		
Noninterest-earning assets	58,104			52,093			37,951		
Total assets	$1,905,736			$1,831,549			$1,352,832		
Liabilities									
Interest-bearing liabilities									
Interest-bearing demand deposits	$88,295	$119	0.55 %	$83,930	$116	0.55 %	$81,338	$111	0.55 %
Regular savings accounts	28,333	47	0.67 %	28,157	41	0.58 %	25,021	36	0.58 %
Money market accounts	347,696	696	0.81 %	360,166	648	0.72 %	350,809	616	0.71 %
Certificates and brokered deposits	986,353	3,837	1.58 %	973,484	3,862	1.58 %	575,976	2,125	1.48 %
Total interest-bearing deposits	1,450,677	4,699	1.31 %	1,445,737	4,667	1.28 %	1,033,144	2,888	1.12 %
Other borrowed funds	262,573	1,234	1.91 %	213,109	1,193	2.23 %	185,618	664	1.44 %
Total interest-bearing liabilities	1,713,250	5,933	1.40 %	1,658,846	5,860	1.41 %	1,218,762	3,552	1.17 %
	31,463			30,336			22,899		

Noninterest-bearing deposits									
Other noninterest-bearing liabilities	6,225			6,393			4,893		
Total liabilities	1,750,938			1,695,575			1,246,554		
Shareholders' equity	154,798			135,974			106,278		
Total liabilities and shareholders' equity	$1,905,736			$1,831,549			$1,352,832		
Net interest income		$ 11,457			$ 10,904			$ 9,141	
Interest rate spread [1]			2.39 %			2.32 %			2.69 %
Net interest margin [2]			2.50 %			2.42 %			2.78 %
Net interest margin - FTE [3]			2.57 %			2.48 %			2.80 %

[1] Yield on total interest-earning assets minus cost of total interest-bearing liabilities

[2] Net interest income divided by total average interest-earning assets (annualized)

[3] On a FTE basis assuming a 35% tax rate. Net interest income is adjusted to reflect income from assets such as municipal loans and securities that are exempt from Federal income taxes. This is to recognize the income tax savings that facilitates a comparison between taxable and tax-exempt assets. The Company believes that it is a standard practice in the banking industry to present net interest margin and net interest income on a fully-taxable equivalent basis as these measures provide useful information to make peer comparisons.

Rate/Volume Analysis

The following table illustrates the impact of changes in the volume of interest-earning assets and interest-bearing liabilities and interest rates on net interest income for the periods indicated. The change in interest not due solely to volume or rate has been allocated in proportion to the absolute dollar amounts of the change in each.

	Rate/Volume Analysis of Net Interest Income					
(dollars in thousands)	Three Months Ended March 31, 2017 vs. December 31, 2016			Three Months Ended March 31, 2017 vs. March 31, 2016		
	Due to Changes in			Due to Changes in		
	Volume	Rate	Net	Volume	Rate	Net
Interest income						
Loans, including loans held-for-sale	$1,320	$(824)	$496	$4,981	$(2,014)	$2,967
Securities – taxable	(110)	215	105	1,091	107	1,198
Securities – non-taxable	(71)	82	11	530	2	532
Other earning assets	(163)	177	14	(366)	366	—
Total	976	(350)	626	6,236	(1,539)	4,697
Interest expense						
Interest-bearing deposits	4	28	32	1,276	535	1,811
Other borrowed funds	868	(827)	41	319	251	570
Total	872	(799)	73	1,595	786	2,381
Increase (decrease) in net interest income	$104	$449	$553	$4,641	$(2,325)	$2,316

Net interest income for the first quarter 2017 was $11.5 million, an increase of $2.3 million, or 25.3%, compared to $9.1 million for the first quarter 2016. The increase in net interest income was the result of a $4.7 million, or 37.0%, increase in total interest income to $17.4 million for the first quarter 2017 from $12.7 million for the first quarter 2016. The increase in total interest income was partially offset by a $2.4 million, or 67.0%, increase in total interest expense to $5.9 million for the first quarter 2017 from $3.6 million for the first quarter 2016.

The increase in total interest income was due primarily to an increase in interest earned on loans resulting from an increase of $318.5 million, or 31.2%, in the average balance of loans, including loans held-for-sale, partially offset by a decline of 12 basis points ("bps") in the yield on loans, including loans held-for-sale. In addition, the average balance of securities increased $249.8 million, or 111.0%, and the yield earned on the securities portfolio increased 24 bps for the first quarter 2017 compared to the first quarter 2016.

The increase in total interest expense was driven primarily by an increase of $417.5 million, or 40.4%, in the average balance of interest-bearing deposits for the first quarter 2017 compared to the first quarter 2016, as well as a 19 bp increase in the cost of funds related to interest-bearing deposits. The increase in the cost of interest-bearing deposits was primarily due to a $419.9 million, or 74.6%, increase in average certificates of deposits balances and a 14 bp increase in the related cost of those deposits. Interest expense related to other borrowed funds also contributed to the increase in total interest expense due to a $77.0 million, or 41.5%, increase in the average balance of other borrowed funds for the first quarter 2017 compared to the first quarter 2016 as well as an increase of 47 bps in the cost of other borrowed funds. Included in the increase in the average balance of other borrowed funds was the Company's issuance of $25.0 million of subordinated notes during September 2016 with a current fixed interest rate of 6.00%. Additionally, the average balance of the Federal Home Loan Bank advances increased $53.1 million, or 30.7%, and the related cost of funds increased 12 bps compared to first quarter 2016.

Net interest margin (“NIM”) was 2.50% for the first quarter 2017 compared to 2.78% for the first quarter 2016. The decline in NIM for the first quarter 2017 compared to the first quarter 2016 was driven primarily by an increase of 23 bps in the cost of interest-bearing liabilities as well as the decline of 7 bps in the yield earned on interest-earning assets. On a fully-taxable equivalent basis, NIM was 2.57% for the first quarter 2017 compared to 2.80% for the first quarter 2016.

Noninterest Income

The following table presents noninterest income for the five most recent quarters.

(dollars in thousands)	Three Months Ended				
	March 31, 2017	December 31, 2016	September 30, 2016	June 30, 2016	March 31, 2016
Service charges and fees	$211	$ 196	$ 207	$215	$ 200
Mortgage banking activities	1,616	2,407	4,442	3,295	2,254
Gain on sale of securities	—	—	—	177	—
Gain (loss) on asset disposals	(2)	(4)	5	(48)	(16)
Other	306	292	244	109	102
Total noninterest income	$2,131	$ 2,891	$ 4,898	$3,748	$ 2,540

During the first quarter 2017, noninterest income was $2.1 million, representing a decrease of $0.4 million, or 16.1%, compared to $2.5 million for the first quarter 2016. The decrease in noninterest income was primarily driven by a decrease of $0.6 million, or 28.3%, in revenue from mortgage banking activities. In the first quarter 2017 as compared to first quarter 2016, there was a decline in mortgages held-for-sale (“HFS”) commitment/lock and sale activity, a decline in gain on sale margins, and an increased percentage of mortgages HFS being sold through best efforts as opposed to mandatory commitments, which resulted in a timing difference related to revenue recognition. Historically, a large percentage of the mortgages originated by the Company had been conventional 15- and 30-year fixed rate mortgages, which are sold in the secondary market. With the increase in conventional mortgage interest rates since fourth quarter 2016, the Company has seen a shift in consumer behavior with a preference for adjustable rate mortgages, which are typically held for investment on the balance sheet. Accordingly, portfolio mortgage originations increased during the first quarter 2017 compared to first quarter 2016 while mortgages HFS volume declined, contributing to the decline in revenue from mortgage banking activities.

Noninterest Expense

The following table presents noninterest expense for the five most recent quarters.

(dollars in thousands)	Three Months Ended				
	March 31, 2017	December 31, 2016	September 30, 2016	June 30, 2016	March 31, 2016
Salaries and employee benefits	$5,073	$ 4,610	$ 4,550	$4,329	$ 3,898
Marketing, advertising and promotion	518	471	454	434	464
Consulting and professional services	813	709	901	895	638
Data processing	237	292	286	275	274
Loan expenses	214	267	240	200	184
Premises and equipment	953	955	983	963	798
Deposit insurance premium	315	344	420	215	180
Other	575	510	579	564	569
Total noninterest expense	$8,698	$ 8,158	$ 8,413	$7,875	$ 7,005

Noninterest expense for the first quarter 2017 was $8.7 million, compared to $7.0 million for the first quarter 2016. The increase of $1.7 million, or 24.2%, compared to the first quarter 2016 was primarily due to an increase of $1.2 million in salaries and employee benefits, an increase of $0.2 million in consulting and professional services, an increase of $0.2 million in premises and equipment and an increase of $0.1 million in deposit insurance premium. The increase in salaries and employee benefits resulted from personnel growth and higher claims experience related to medical, prescription drug and dental insurance. The increase in consulting and professional fees were due to expenses incurred in the normal course of business commensurate with the Company’s growth. The increase in premises and equipment was due to the Company's build out of its corporate headquarters facility and further investments in technology. The increase in deposit insurance premium was due to the new methodology implemented by the FDIC as of July 1, 2016, which places a heavier weighting on year-over-year asset growth used to determine the cost of FDIC deposit insurance.

Income tax provision was $1.0 million for the first quarter 2017, resulting in an effective tax rate of 26.5%, compared to $1.3 million and an effective tax rate of 34.8% for the first quarter 2016. The decrease in the effective tax rate was due primarily to an increase in tax-exempt earning assets resulting from growth in the municipal bond portfolio and public finance loan portfolio as well as a $0.1 million income tax benefit associated with equity compensation vesting events that occurred during the first quarter 2017.

Financial Condition

The following table presents summary balance sheet data for the last five quarters.
(dollars in thousands)

Balance Sheet Data:	March 31, 2017	December 31, 2016	September 30, 2016	June 30, 2016	March 31, 2016
Total assets	$2,052,803	$ 1,854,335	$ 1,824,196	$1,702,468	$1,527,719
Loans	1,433,190	1,250,789	1,198,932	1,111,622	1,040,683
Securities available-for-sale	470,065	456,700	470,978	433,806	315,311
Securities held-to-maturity	19,218	16,671	5,500	—	—
Loans held-for-sale	13,202	27,101	32,471	44,503	29,491
Noninterest-bearing deposits	34,427	31,166	32,938	28,066	28,945
Interest-bearing deposits	1,522,692	1,431,701	1,460,663	1,360,867	1,214,233
Total deposits	1,557,119	1,462,867	1,493,601	1,388,933	1,243,178
Total shareholders' equity	157,491	153,942	137,154	135,679	107,830

Total assets increased $198.5 million, or 10.7%, to $2.1 billion at March 31, 2017 compared to $1.9 billion at December 31, 2016. Balance sheet expansion during the first quarter 2017 was primarily driven by strong loan growth as loan balances increased $182.4 million, or 14.6%, compared to December 31, 2016.

Loan Portfolio Analysis

The following table presents a detailed listing of the Company's loan portfolio for the last five quarters.

(dollars in thousands)	March 31, 2017		December 31, 2016		September 30, 2016		June 30, 2016		March 31, 2016	
Commercial loans										
Commercial and industrial	$97,487	6.8 %	$102,437	8.2 %	$107,250	8.9 %	$111,130	10.0 %	$106,431	10.2 %
Owner-occupied commercial real estate	62,887	4.4 %	57,668	4.6 %	45,540	3.8 %	46,543	4.2 %	47,010	4.5 %
Investor commercial real estate	8,510	0.6 %	13,181	1.1 %	12,752	1.1 %	12,976	1.2 %	14,756	1.4 %
Construction	49,618	3.5 %	53,291	4.3 %	56,391	4.7 %	53,368	4.8 %	52,591	5.1 %
Single tenant lease financing	665,382	46.4 %	606,568	48.5 %	571,972	47.6 %	500,937	45.1 %	445,534	42.8 %
Public finance	77,995	5.4 %	—	0.0 %	—	0.0 %	—	0.0 %	—	0.0 %
Total commercial loans	961,879	67.1 %	833,145	66.7 %	793,905	66.1 %	724,954	65.3 %	666,322	64.0 %
Consumer loans										

Residential mortgage	246,014	17.2 %	205,554	16.4 %	200,889	16.8 %	202,107	18.2 %	208,636	20.1 %
Home equity	34,925	2.4 %	35,036	2.8 %	37,849	3.2 %	38,981	3.5 %	40,000	3.8 %
Other consumer	188,191	13.1 %	173,449	13.8 %	163,158	13.6 %	141,756	12.7 %	121,323	11.7 %
Total consumer loans	469,130	32.7 %	414,039	33.0 %	401,896	33.6 %	382,844	34.4 %	369,959	35.6 %
Deferred loan origination costs and premiums and discounts on purchased loans	2,181	0.2 %	3,605	0.3 %	3,131	0.3 %	3,824	0.3 %	4,402	0.4 %
Total loans	1,433,190	100.0%	1,250,789	100.0%	1,198,932	100.0%	1,111,622	100.0%	1,040,683	100.0%
Allowance for loan losses	(11,894)		(10,981)		(10,561)		(10,016)		(9,220)	
Net loans	$1,421,296		$1,239,808		$1,188,371		$1,101,606		$1,031,463	

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Total loans rose to $1.4 billion as of March 31, 2017, an increase of $182.4 million, or 14.6%, compared to December 31, 2016. The growth in commercial loan balances was impacted by production in the Company's new public finance lending area with balances totaling $78.0 million at quarter end. Furthermore, production in single tenant lease financing remained strong as balances increased $58.8 million, or 9.7%, compared to December 31, 2016. The growth in consumer loans was driven by the recent rise in conventional mortgage interest rates, leading to a shift in consumer behavior with a preference for adjustable rate mortgages ("ARMs") since late 2016. The Company's residential mortgage portfolio, which includes ARMs, increased $40.5 million, or 19.7%, compared to December 31, 2016. Furthermore, other consumer loan balances increased $14.7 million, or 8.5%, compared to December 31, 2016, driven primarily by increased production in trailer, recreational vehicle and home improvement loans.

Asset Quality

Nonperforming loans are comprised of nonaccrual loans and loans 90 days past due and accruing. Nonperforming assets include nonperforming loans, other real estate owned and other nonperforming assets, which consist of repossessed assets. The following table provides a detailed listing of the Company's nonperforming assets for the last five quarters.

(dollars in thousands)	March 31, 2017	December 31, 2016	September 30, 2016	June 30, 2016	March 31, 2016
Nonaccrual loans					
Commercial loans:					
Commercial and industrial	$2,147	$ —	$ —	$4,716	$—
Total commercial loans	2,147	—	—	4,716	—
Consumer loans:					
Residential mortgage	1,209	1,024	1,025	844	103
Other consumer	55	59	108	74	69
Total consumer loans	1,264	1,083	1,133	918	172
Total nonaccrual loans	3,411	1,083	1,133	5,634	172
Past Due 90 days and accruing loans					
Consumer loans:					
Residential mortgage	—	—	—	—	195
Other consumer	—	—	—	5	—
Total consumer loans	—	—	—	5	195
Total past due 90 days and accruing loans	—	—	—	5	195
Total nonperforming loans	3,411	1,083	1,133	5,639	367
Other real estate owned					
Investor commercial real estate	4,488	4,488	4,488	4,488	4,488
Residential mortgage	—	45	45	—	—
Total other real estate owned	4,488	4,533	4,533	4,488	4,488
Other nonperforming assets	93	85	69	46	75
Total nonperforming assets	$7,992	$ 5,701	$ 5,735	$10,173	$4,930
Total nonperforming loans to total loans	0.24 %	0.09 %	0.09 %	0.51 %	0.04 %
Total nonperforming assets to total assets	0.39 %	0.31 %	0.31 %	0.60 %	0.32 %
Allowance for loan losses to total loans	0.83 %	0.88 %	0.88 %	0.90 %	0.89 %

Allowance for loan losses to nonperforming loans	348.7 %	1,013.9 %	932.1 %	177.6 %	2,512.3 %

Troubled Debt Restructurings

The following table provides a summary of troubled debt restructurings for the last five quarters.

(dollars in thousands)	March 31, 2017	December 31, 2016	September 30, 2016	June 30, 2016	March 31, 2016
Troubled debt restructurings – nonaccrual	$ —	$ —	$ 1	$ —	$ —
Troubled debt restructurings – performing	$ 496	$ 757	$ 1,067	$ 1,082	$ 1,100
Total troubled debt restructurings	$ 496	$ 757	$ 1,068	$ 1,082	$ 1,100

The increase of $2.3 million, or 40.2%, in total nonperforming assets as of March 31, 2017 compared to December 31, 2016 was due primarily to an increase in nonaccrual loans. Total nonperforming loans increased $2.3 million, or 215.0%, to $3.4 million as of March 31, 2017 compared to $1.1 million as of December 31, 2016. This increase was primarily driven by a $1.9 million commercial and industrial credit that was placed on nonaccrual status during the quarter. As a result, the ratio of nonperforming loans to total loans increased to 0.24% as of March 31, 2017 compared to 0.09% as of December 31, 2016. The ratio of nonperforming assets to total assets also increased to 0.39% as of March 31, 2017 compared to 0.31% as of December 31, 2016 due primarily to the increase in nonaccrual loans.

As of March 31, 2017 and December 31, 2016, the Company had one commercial property in other real estate owned with a carrying value of $4.5 million. This property consists of two buildings which are residential units adjacent to a university campus. Improvements to the property have been made in collaboration with the university and the property continues to be occupied. As of December 31, 2016, the Company also had residential mortgage other real estate owned of less than $0.1 million.

Allowance for Loan Losses

The following table provides a rollforward of the allowance for loan losses for the last five quarters.

(dollars in thousands)	Three Months Ended				
	March 31, 2017	December 31, 2016	September 30, 2016	June 30, 2016	March 31, 2016
Balance, beginning of period	$ 10,981	$ 10,561	$ 10,016	$ 9,220	$ 8,351
Provision charged to expense	1,035	256	2,204	924	946
Losses charged off	(223)	(71)	(1,737)	(232)	(149)
Recoveries	101	235	78	104	72
Balance, end of period	$ 11,894	$ 10,981	$ 10,561	$ 10,016	$ 9,220
Net charge-offs (recoveries) to average loans	0.04 %	(0.05)%	0.57 %	0.05 %	0.03 %

The allowance for loan losses was $11.9 million as of March 31, 2017, compared to $11.0 million as of December 31, 2016. The increase of $0.9 million, or 8.3%, was due primarily to the growth in single tenant lease financing, public finance and residential mortgage loan balances. During the first quarter 2017, the Company recorded net charge-offs of $0.1 million, compared to net charge-offs of $0.1 million during the first quarter 2016. The net charge-offs for both the first quarter 2017 and 2016 were primarily driven by charge-offs in other consumer loans.

The allowance for loan losses as a percentage of total loans decreased to 0.83% as of March 31, 2017, compared to 0.88% as of December 31, 2016. The decline in the allowance as a percentage of total loans was due primarily to the growth in the public finance and residential mortgage portfolios as these loan categories have lower loss reserve factors than other commercial and consumer loan types, except for home equity loans. Due to the increase in nonaccrual loans, the allowance for loan losses as a percentage of nonperforming loans decreased to 348.7% as of

March 31, 2017, compared to 1,013.9% as of December 31, 2016.

Investment Securities

The following tables present the amortized cost and approximate fair value of our investment portfolio by security type for the last five quarters.

(dollars in thousands)

Amortized Cost	March 31, 2017	December 31, 2016	September 30, 2016	June 30, 2016	March 31, 2016
Securities available-for-sale					
U.S. Government-sponsored agencies	$113,933	$ 92,599	$ 85,630	$75,133	$60,511
Municipal securities	97,578	97,647	96,665	78,594	35,016
Mortgage-backed securities	235,879	238,354	244,780	233,886	177,337
Asset-backed securities	9,873	19,470	19,464	19,457	19,451
Corporate securities	23,107	20,000	20,000	20,000	20,000
Other securities	3,000	3,000	3,000	3,000	3,000
Total available-for-sale	483,370	471,070	469,539	430,070	315,315
Securities held-to-maturity					
Municipal securities	10,169	10,171	—	—	—
Corporate securities	9,049	6,500	5,500	—	—
Total held-to-maturity	19,218	16,671	5,500	—	—
Total securities	$502,588	$ 487,741	$ 475,039	$430,070	$315,315

(dollars in thousands)

Approximate Fair Value	March 31, 2017	December 31, 2016	September 30, 2016	June 30, 2016	March 31, 2016
Securities available-for-sale					
U.S. Government-sponsored agencies	$113,287	$ 91,896	$ 85,990	$75,678	$60,792
Municipal securities	92,428	91,886	97,501	80,798	35,639
Mortgage-backed securities	229,436	231,641	246,085	235,911	177,989
Asset-backed securities	10,000	19,534	19,496	19,332	18,892
Corporate securities	21,982	18,811	18,880	19,074	18,978
Other securities	2,932	2,932	3,026	3,013	3,021
Total available-for-sale	470,065	456,700	470,978	433,806	315,311
Securities held-to-maturity					
Municipal securities	9,703	9,673	—	—	—
Corporate securities	9,101	6,524	5,578	—	—
Total held-to-maturity	18,804	16,197	5,578	—	—
Total securities	$488,869	$ 472,897	$ 476,556	$433,806	$315,311

The approximate fair value of investment securities available-for-sale increased $13.4 million, or 2.9%, to $470.1 million as of March 31, 2017 compared to $456.7 million as of December 31, 2016. The increase was due primarily to increases of $21.4 million in U.S. Government-sponsored agencies and $3.2 million in corporate securities, offset by a decline of $9.5 million in asset-backed securities. The increases in U.S. Government-sponsored agencies and corporate securities were due primarily to purchases of floating rate instruments during the quarter. The decline in asset-backed securities were due to certain securities that were called by the issuer during the quarter. As of March 31, 2017, the Company had securities with an amortized cost basis of $19.2 million designated as held-to-maturity compared to $16.7 million as of December 31, 2016.

Deposits

The following table presents the composition of the Company's deposit base for the last five quarters.

(dollars in thousands)	March 31, 2017			December 31, 2016			September 30, 2016			June 30, 2016			March 31, 2016		
Noninterest-bearing deposits	$34,427	2.2	%	$31,166	2.1	%	$32,938	2.2	%	$28,066	2.0	%	$28,945	2.3	%
Interest-bearing demand deposits	94,461	6.1	%	93,074	6.4	%	84,939	5.7	%	83,031	6.0	%	89,180	7.2	%
Regular savings accounts	31,291	2.0	%	27,955	1.9	%	27,661	1.8	%	28,900	2.1	%	27,279	2.2	%
Money market accounts	371,115	23.8	%	340,240	23.3	%	364,517	24.4	%	373,932	26.9	%	366,195	29.5	%
Certificates of deposits	1,023,294	65.7	%	964,819	65.9	%	970,684	65.0	%	862,150	62.1	%	718,733	57.8	%
Brokered deposits	2,531	0.2	%	5,613	0.4	%	12,862	0.9	%	12,854	0.9	%	12,846	1.0	%
Total deposits	$1,557,119	100.0	%	$1,462,867	100.0	%	$1,493,601	100.0	%	$1,388,933	100.0	%	$1,243,178	100.0	%

Total deposits increased $94.3 million, or 6.4%, to $1.6 billion as of March 31, 2017 compared to $1.5 billion as of December 31, 2016. This increase was due primarily to increases of $58.5 million, or 6.1%, in certificates of deposits, $30.9 million, or 9.1%, in money market accounts, $3.3 million, or 11.9%, in regular savings accounts, $3.3 million, or 10.5%, in noninterest-bearing deposits and $1.4 million, or 1.5%, in interest-bearing demand deposits.

Recent Common Stock Offerings

In May 2016, the Company and the Bank entered into a Sales Agency Agreement with Sandler O'Neill & Partners, L.P. ("Sandler") to sell shares (the "ATM Shares") of the Company's common stock having an aggregate gross sales price of up to $25.0 million, from time to time, through an "at-the-market" equity offering program (the "ATM Program"). The sales, if any, of the ATM Shares, may be made in sales deemed to be "at-the-market offerings" as defined in Rule 415 under the Securities Act of 1933, as amended, including sales made directly on or through The NASDAQ Stock Market, or another market for the Company's common stock, sales made to or through a market maker other than on an exchange or otherwise, in negotiated transactions at market prices prevailing at the time of sale or at negotiated prices, or as otherwise agreed with Sandler. Subject to the terms and conditions of the Sales Agency Agreement, upon its acceptance of written instructions from the Company, Sandler will use its commercially reasonable efforts to sell on the Company's behalf all of the designated ATM Shares. The Sales Agency Agreement provides for the Company to pay Sandler a commission of up to 3.0% of the gross sales price per share sold through it as sales agent under the Sales Agency Agreement. The Company may also sell ATM Shares under the Sales Agency Agreement to Sandler, as principal for its own account, at a price per share agreed upon at the time of sale. Actual sales will depend on a variety of factors to be determined by the Company from time to time. The Company has no obligation to sell any of the ATM Shares under the Sales Agency Agreement, and may at any time suspend solicitation and offers under the Sales Agency Agreement. In addition, the Company has agreed to indemnify Sandler against certain liabilities on customary terms. The Company has sold a total of 139,811 ATM Shares through the ATM Program for gross proceeds of approximately $3.4 million.

As of March 31, 2017, approximately $21.6 million remained available for sale under the ATM Program.

In May 2016, the Company and the Bank separately entered into an Underwriting Agreement with Sandler, pursuant to which the Company sold an additional 895,955 shares of common stock at $24.00 per share, resulting in gross proceeds to the Company of $21.5 million.

In December 2016, the Company and the Bank also entered into an Underwriting Agreement with Keefe, Bruyette & Woods, a Stifel Company, pursuant to which the Company sold 945,000 shares of common stock at $26.50 per share, resulting in gross proceeds to the Company of $25.0 million.

The net proceeds to the Company from the above offerings after deducting underwriting discounts and commissions and offering expenses was $46.2 million.

Recent Debt Offerings

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

Capital

The Company and the Bank are subject to various regulatory capital requirements administered by state and federal banking agencies. Capital adequacy guidelines and, additionally for banks, prompt corrective action regulations, involve quantitative measures of assets, liabilities, and certain off-balance-sheet items calculated under regulatory accounting practices. Capital amounts and classifications are also subject to qualitative judgments by regulators about components, risk weighting and other factors.

The Basel III Capital Rules became effective for the Company and the Bank on January 1, 2015, subject to a phase-in period for certain provisions. Quantitative measures established by the Basel III Capital Rules to ensure capital adequacy require the maintenance of minimum amounts and ratios of Common Equity Tier 1 capital, Tier 1 capital and Total capital, as defined in the regulations, to risk-weighted assets, and of Tier 1 capital to adjusted quarterly average assets (“Leverage Ratio”).

When fully phased in on January 1, 2019, the Basel III Capital Rules will require the Company and the Bank to maintain: 1) a minimum ratio of Common Equity Tier 1 capital to risk-weighted assets of 4.5%, plus a 2.5% “capital conservation buffer” (resulting in a minimum ratio of Common Equity Tier 1 capital to risk-weighted assets of 7.0% upon full implementation); 2) a minimum ratio of Tier 1 capital to risk-weighted assets of 6.0%, plus the capital conservation buffer (resulting in a minimum Tier 1 capital ratio of 8.5% upon full implementation); 3) a minimum ratio of Total capital to risk-weighted assets of 8.0%, plus the capital conservation buffer (resulting in a minimum Total capital ratio of 10.5% upon full implementation); and 4) a minimum Leverage Ratio of 4.0%.

The implementation of the capital conservation buffer began on January 1, 2016 at the 0.625% level and will be phased in over a four-year period increasing by increments of that amount on each subsequent January 1 until it reaches 2.5% on January 1, 2019. The capital conservation buffer is designed to absorb losses during periods of economic stress. Failure to maintain the minimum Common Equity Tier 1 capital ratio plus the capital conservation buffer will result in potential restrictions on a banking institution’s ability to pay dividends, repurchase stock and/or pay discretionary compensation to its employees.

The following tables present actual and required capital ratios as of March 31, 2017 and December 31, 2016 for the Company and the Bank under the Basel III Capital Rules. The minimum required capital amounts presented include the minimum required capital levels as of March 31, 2017 and December 31, 2016 based on the phase-in provisions of the Basel III Capital Rules and the minimum required capital levels as of January 1, 2019 when the Basel III Capital Rules have been fully phased-in. Capital levels required to be considered well capitalized are based upon prompt corrective action regulations, as amended to reflect the changes under the Basel III Capital Rules.

	Actual		Minimum Capital Required - Basel III Phase-In Schedule		Minimum Capital Required - Basel III Fully Phased-In		Minimum Required to be Considered Well Capitalized	
(dollars in thousands)	Capital Amount	Ratio	Capital Amount	Ratio	Capital Amount	Ratio	Capital Amount	Ratio
As of March 31, 2017:								
Common equity tier 1 capital to risk-weighted assets								
Consolidated	$161,037	10.88%	$85,090	5.75%	$103,588	7.00 %	N/A	N/A
Bank	166,200	11.27%	84,797	5.75%	103,231	7.00 %	$95,857	6.50 %
Tier 1 capital to risk-weighted assets								
Consolidated	161,037	10.88%	107,288	7.25%	125,786	8.50 %	N/A	N/A
Bank	166,200	11.27%	106,917	7.25%	125,352	8.50 %	117,978	8.00 %
Total capital to risk-weighted assets								
Consolidated	209,546	14.16%	136,885	9.25%	155,382	10.50%	N/A	N/A
Bank	178,094	12.08%	136,412	9.25%	154,846	10.50%	147,472	10.00%
Leverage ratio								
Consolidated	161,037	8.41 %	76,631	4.00%	76,631	4.00 %	N/A	N/A
Bank	166,200	8.69 %	76,498	4.00%	76,498	4.00 %	95,622	5.00 %

	Actual		Minimum Capital Required - Basel III Phase-In Schedule		Minimum Capital Required - Basel III Fully Phased-In		Minimum Required to be Considered Well Capitalized	
(dollars in thousands)	Capital Amount	Ratio	Capital Amount	Ratio	Capital Amount	Ratio	Capital Amount	Ratio
As of December 31, 2016:								
Common equity tier 1 capital to risk-weighted assets								
Consolidated	$158,479	11.54%	$70,366	5.13%	$96,110	7.00 %	N/A	N/A
Bank	162,617	11.88%	70,145	5.13%	95,807	7.00 %	$88,964	6.50 %
Tier 1 capital to risk-weighted assets								
Consolidated	158,479	11.54%	90,961	6.63%	116,705	8.50 %	N/A	N/A
Bank	162,617	11.88%	90,675	6.63%	116,337	8.50 %	109,494	8.00 %
Total capital to risk-weighted assets								
Consolidated	206,038	15.01%	118,421	8.63%	144,165	10.50%	N/A	N/A
Bank	173,598	12.68%	118,048	8.63%	143,711	10.50%	136,868	10.00%
Leverage ratio								
Consolidated	158,479	8.65 %	73,311	4.00%	73,311	4.00 %	N/A	N/A

Bank	162,617