SOUTHERN FIRST BANCSHARES INC
Form 10-Q
August 04, 2015

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the Quarterly Period Ended June 30, 2015
OR
TRANSITION REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the Transition Period from to
Commission file number 000-27719

Southern First Bancshares, Inc.

(Exact name of registrant as specified in its charter)

South Carolina	**58-2459561**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
100 Verdae Boulevard, Suite 100	
Greenville, S.C.	**29606**
(Address of principal executive offices)	(Zip Code)

864-679-9000
(Registrant s telephone number, including area code)
Not Applicable
(Former name, former address, and former fiscal year, if changed since last report)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definitions of large accelerated filer, accelerated filer, and smaller reporting company in Rule 12b-2 of the Exchange Act.

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

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

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the latest practicable date: 6,236,144 shares of common stock, par value $0.01 per share, were issued and outstanding as of July 28, 2015.

SOUTHERN FIRST BANCSHARES, INC. AND SUBSIDIARY
June 30, 2015 Form 10-Q

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PART I. CONSOLIDATED FINANCIAL INFORMATION
Item 1. CONSOLIDATED FINANCIAL STATEMENTS

SOUTHERN FIRST BANCSHARES, INC. AND SUBSIDIARY
CONSOLIDATED BALANCE SHEETS

(dollars in thousands, except share data)	June 30, 2015 (Unaudited)	December 31, 2014 (Audited)
ASSETS		
Cash and cash equivalents:		
Cash and due from banks	$ 12,085	9,862
Interest-bearing deposits with banks	5,219	25,849
Federal funds sold	24,106	5,553
Total cash and cash equivalents	41,410	41,264
Investment securities:		
Investment securities available for sale	51,465	55,024
Other investments	5,532	6,522
Total investment securities	56,997	61,546
Loans held for sale	12,402	11,765
Loans	963,496	871,446
Less allowance for loan losses	(12,927)	(11,752)
Loans, net	950,569	859,694
Bank owned life insurance	22,382	22,050
Property and equipment, net	22,704	20,845
Deferred income taxes	5,929	5,509
Other assets	6,607	7,192
Total assets	$1,119,000	1,029,865
LIABILITIES		
Deposits	$ 894,524	788,907
Federal Home Loan Bank advances and other borrowings	115,200	135,200
Junior subordinated debentures	13,403	13,403
Other liabilities	8,206	9,363
Total liabilities	1,031,333	946,873
SHAREHOLDERS EQUITY		
Preferred stock, par value $.01 per share, 10,000,000 shares authorized, no shares issued and outstanding	-	-
Common stock, par value $.01 per share, 10,000,000 shares authorized, 6,236,144 and 6,219,002 shares issued and outstanding at June 30, 2015 and December 31, 2014, respectively	62	62
Nonvested restricted stock	(400)	(494)
Additional paid-in capital	69,192	68,785
Accumulated other comprehensive income (loss)	(112)	302
Retained earnings	18,925	14,337
Total shareholders equity	87,667	82,992
Total liabilities and shareholders equity	$1,119,000	1,029,865

See notes to consolidated financial statements that are an integral part of these consolidated statements.

SOUTHERN FIRST BANCSHARES, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF INCOME

(Unaudited)

(dollars in thousands, except share data)	For the three months ended June 30, 2015	For the three months ended June 30, 2014	For the six months ended June 30, 2015	For the six months ended June 30, 2014
Interest income				
Loans	$ 10,941	9,309	21,341	18,127
Investment securities	356	465	731	977
Federal funds sold	19	16	45	30
Total interest income	11,316	9,790	22,117	19,134
Interest expense				
Deposits	854	696	1,621	1,376
Borrowings	971	1,024	1,935	2,044
Total interest expense	1,825	1,720	3,556	3,420
Net interest income	9,491	8,070	18,561	15,714
Provision for loan losses	1,000	950	1,625	1,950
Net interest income after provision for loan losses	8,491	7,120	16,936	13,764
Noninterest income				
Loan and mortgage fee income	1,409	613	2,605	955
Service fees on deposit accounts	219	231	445	445
Income from bank owned life insurance	165	167	331	329
Gain on sale of investment securities	36	230	295	230
Other income	286	277	580	529
Total noninterest income	2,115	1,518	4,256	2,488
Noninterest expenses				
Compensation and benefits	4,106	3,514	8,382	6,925
Occupancy	842	730	1,579	1,457
Real estate owned expenses	93	12	855	25
Data processing and related costs	573	622	1,158	1,216
Insurance	213	203	415	395
Professional fees	233	294	466	517
Marketing	222	197	460	398
Other	364	743	791	1,152
Total noninterest expenses	6,646	6,315	14,106	12,085
Income before income tax expense	3,960	2,323	7,086	4,167
Income tax expense	1,400	757	2,498	1,351
Net income	2,560	1,566	4,588	2,816
Preferred stock dividend	-	253	-	445
Net income available to common shareholders	$ 2,560	1,313	4,588	2,371
Earnings per common share				
Basic	$ 0.41	0.28	0.74	0.51
Diluted	0.39	0.26	0.70	0.48
Weighted average common shares outstanding				
Basic	6,233,745	4,763,407	6,229,522	4,686,748
Diluted	6,533,658	5,036,553	6,524,317	4,957,000

See notes to consolidated financial statements that are an integral part of these consolidated statements.

SOUTHERN FIRST BANCSHARES, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(Unaudited)

(dollars in thousands)	For the three months ended June 30, 2015	For the three months ended June 30, 2014	For the six months ended June 30, 2015	For the six months ended June 30, 2014
Net income	$2,560	1,566	4,588	2,816
Other comprehensive income (loss):				
Unrealized gain (loss) on securities available for sale:				
Unrealized holding gain (loss) arising during the period, pretax	(689)	1,093	(332)	2,259
Tax (expense) benefit	234	(371)	113	(768)
Reclassification of realized gain	(36)	(230)	(295)	(230)
Tax expense	12	78	100	78
Other comprehensive income (loss)	(479)	570	(414)	1,339
Comprehensive income	$2,081	2,136	4,174	4,155

See notes to consolidated financial statements that are an integral part of these consolidated statements.

SOUTHERN FIRST BANCSHARES, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF SHAREHOLDERS EQUITY
FOR THE SIX MONTHS ENDED JUNE 30, 2015 AND 2014
(Unaudited)

	Common stock		**Preferred stock**		**Nonvested restricted**	**Additional paid-in**	**Accumulated other comprehensive income**	**Retained**	
(dollars in thousands, except share data)	**Shares**	**Amount**	**Shares**	**Amount**	**stock**	**capital**	**(loss)**	**earnings**	**Total**
December 31, 2013	**4,319,750**	**$ 43**	**15,299**	**$ 15,299**	**$ (636)**	**$ 43,585**	**$ (1,348)**	**$ 8,722**	**$ 65,665**
Net income	-	-	-	-	-	-	-	2,816	2,816
Preferred stock transactions:									
Redemption of preferred stock	-	-	(4,057)	(4,057)	-	-	-	-	(4,057)
Cash dividends on Series T preferred stock	-	-	-	-	-	-	-	(434)	(434)
Issuance of common stock	475,000	5	-	-	-	5,945	-	-	5,950
Proceeds from exercise of stock options	32,764	-	-	-	-	287	-	-	287
Issuance of restricted stock	2,000	-	-	-	(27)	27	-	-	-
Amortization of deferred compensation on restricted stock	-	-	-	-	98	-	-	-	98
Compensation expense related to stock options, net of tax	-	-	-	-	-	222	-	-	222
Other comprehensive income	-	-	-	-	-	-	1,339	-	1,339
June 30, 2014	**4,829,514**	**48**	**11,242**	**11,242**	**(565)**	**50,066**	**(9)**	**11,104**	**71,886**
December 31, 2014	**6,219,002**	**62**	**-**	**-**	**(494)**	**68,785**	**302**	**14,337**	**82,992**
Net income	-	-	-	-	-	-	-	4,588	4,588
Proceeds from exercise of stock options	17,142	-	-	-	-	117	-	-	117
Amortization of deferred compensation on restricted stock	-	-	-	-	94	-	-	-	94
Compensation expense related to stock options, net of tax	-	-	-	-	-	290	-	-	290
Other comprehensive loss	-	-	-	-	-	-	(414)	-	(414)
June 30, 2015	**6,236,144**	**$ 62**	**-**	**$ -**	**$ (400)**	**$ 69,192**	**$ (112)**	**$ 18,925**	**$ 87,667**

See notes to consolidated financial statements that are an integral part of these consolidated statements.

SOUTHERN FIRST BANCSHARES, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

	For the six months ended June 30,	
(dollars in thousands)	**2015**	**2014**
Operating activities		
Net income	$ 4,588	2,816
Adjustments to reconcile net income to cash provided by operating activities:		
Provision for loan losses	1,625	1,950
Depreciation and other amortization	688	591
Accretion and amortization of securities discounts and premium, net	148	200
Gain on sale of investment securities available for sale	(295)	(230)
Gain on sale of real estate owned	(74)	-
Write-down of real estate owned	737	-
Compensation expense related to stock options and grants	384	320
Gain on sale of loans held for sale	(2,484)	(880)
Loans originated and held for sale	(106,754)	(37,555)
Proceeds from sale of loans held for sale	108,601	34,857
Increase in cash surrender value of bank owned life insurance	(332)	(329)
Increase in deferred tax asset	(207)	(856)
Decrease in other assets, net	165	90
Decrease in other liabilities	(1,157)	(13)
Net cash provided by operating activities	5,633	961
Investing activities		
Increase (decrease) in cash realized from:		
Origination of loans, net	(92,843)	(80,392)
Purchase of property and equipment	(2,547)	(1,456)
Purchase of investment securities:		
Available for sale	(9,352)	(2,073)
Other	(149)	-
Payments and maturity of investment securities:		
Available for sale	2,359	2,427
Other	1,140	157
Proceeds from sale of investment securities available for sale	10,071	10,427
Proceeds from sale of real estate owned	100	75
Net cash used for investing activities	(91,221)	(70,835)
Financing activities		
Increase (decrease) in cash realized from:		
Increase in deposits, net	105,617	67,050
Increase in other borrowings	-	3,000
Decrease in Federal Home Loan Bank advances and other borrowings	(20,000)	-
Cash dividend on preferred stock	-	(434)
Redemption of preferred stock	-	(4,057)
Issuance of common stock	-	5,950
Proceeds from the exercise of stock options and warrants	117	287
Net cash provided by financing activities	85,734	71,796
Net increase in cash and cash equivalents	146	1,922
Cash and cash equivalents at beginning of the period	41,264	39,203
Cash and cash equivalents at end of the period	$ 41,410	41,125
Supplemental information		
Cash paid for		
Interest	$ 3,634	3,320
Income taxes	2,705	2,207
Schedule of non-cash transactions		
Real estate acquired in settlement of loans	343	154
Unrealized gain (loss) on securities, net of income taxes	(219)	1,491

See notes to consolidated financial statements that are an integral part of these consolidated statements.

SOUTHERN FIRST BANCSHARES, INC. AND SUBSIDIARY
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 Nature of Business and Basis of Presentation

Business Activity
Southern First Bancshares, Inc. (the "Company") is a South Carolina corporation that owns all of the capital stock of Southern First Bank (the "Bank") and all of the stock of Greenville First Statutory Trust I and II (collectively, the "Trusts"). The Trusts are special purpose non-consolidated entities organized for the sole purpose of issuing trust preferred securities. The Bank's primary federal regulator is the Federal Deposit Insurance Corporation (the "FDIC"). The Bank is also regulated and examined by the South Carolina Board of Financial Institutions. The Bank is primarily engaged in the business of accepting demand deposits and savings deposits insured by the FDIC, and providing commercial, consumer and mortgage loans to the general public.

Basis of Presentation
The accompanying consolidated financial statements have been prepared in accordance with generally accepted accounting principles (GAAP) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all the information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the three and six month periods ended June 30, 2015 are not necessarily indicative of the results that may be expected for the year ending December 31, 2015. For further information, refer to the consolidated financial statements and footnotes thereto included in the Company s Annual Report on Form 10-K for the year ended December 31, 2014 as filed with the Securities and Exchange Commission on March 3, 2015. The consolidated financial statements include the accounts of the Company and the Bank. In accordance with Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 810, Consolidation, the financial statements related to the Trusts have not been consolidated.

Use of Estimates
The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the date of the consolidated financial statements and the reported amount of income and expenses during the reporting periods. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses, real estate acquired in the settlement of loans, fair value of financial instruments, evaluating other-than-temporary-impairment of investment securities and valuation of deferred tax assets.

Reclassifications
Certain amounts, previously reported, have been reclassified to state all periods on a comparable basis and had no effect on shareholders equity or net income.

Subsequent Events
Subsequent events are events or transactions that occur after the balance sheet date but before financial statements are issued. Recognized subsequent events are events or transactions that provide additional evidence about conditions that existed at the date of the balance sheet, including the estimates inherent in the process of preparing financial statements. Non-recognized subsequent events are events that provide evidence about conditions that did not exist at the date of the balance sheet but arose after that date. Management performed an evaluation to determine whether there have been any subsequent events since the balance sheet date and determined that no subsequent events occurred requiring accrual or disclosure.

NOTE 2 Preferred and Common Stock

On November 12, 2014, the Company issued 1,380,000 shares of its common stock in a public offering at $14.40 per share, including 180,000 shares which were sold to the underwriter pursuant to an option to purchase additional shares to cover any over-allotments. The net proceeds from the offering totaled approximately $18.4 million, after deducting the underwriting discount as well as estimated offering expenses.

Using proceeds from the public offering, on December 12, 2014, the Company completed the repurchase of the remaining 11,242 shares of Series T preferred stock outstanding at $1,000 par value from third party investors who purchased the shares in July 2012 through a Dutch auction conducted by the U.S. Treasury. As of December 31, 2014, the Company has no shares of preferred stock outstanding.

NOTE 3 Investment Securities

The amortized costs and fair value of investment securities are as follows:

					June 30, 2015
		Amortized	Gross Unrealized		Fair
(dollars in thousands)		Cost	Gains	Losses	Value
Available for sale					
US government agencies	$	9,133	18	307	8,844
SBA securities		5,072	-	169	4,903
State and political subdivisions		16,148	325	127	16,346
Mortgage-backed securities		21,281	250	159	21,372
Total investment securities available for sale	$	51,634	593	762	51,465

					December 31, 2014
		Amortized	Gross Unrealized		Fair
		Cost	Gains	Losses	Value
Available for sale					
US government agencies	$	8,763	9	215	8,557
SBA securities		5,336	-	182	5,154
State and political subdivisions		16,253	598	51	16,800
Mortgage-backed securities		24,214	341	42	24,513
Total investment securities available for sale	$	54,566	948	490	55,024

During the first quarter of 2015, the Company developed a need for additional liquidity as it experienced increased loan demand and, as a result, sold $5.8 million of its mortgage-backed securities and state and municipal obligations and recorded a net gain on sale of investment securities of $259,000. During the second quarter of 2015, we sold and subsequently reinvested $4.3 million of investment securities, recording a gain of $36,000 from the transaction.

Contractual maturities and yields on the Company s investment securities at June 30, 2015 and December 31, 2014 are shown in the following table. Expected maturities may differ from contractual maturities because issuers may have the right to call or prepay obligations with or without call or prepayment penalties.

									June 30, 2015
	Less than one year		One to five years		Five to ten years		Over ten years		Total
(dollars in thousands)	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield
Available for sale										
US government agencies	$ -	-	-	-	1,316	2.19%	7,528	2.42%	8,844	2.39%
SBA securities	-	-	-	-	-	-	4,903	1.88%	4,903	1.88%
State and political subdivisions	2,063	0.84%	-	-	7,529	3.07%	6,754	2.92%	16,346	2.72%
Mortgage-backed securities	-	-	-	-	1,155	1.77%	20,217	2.12%	21,372	2.10%
Total	$ 2,063	0.84%	-	-	10,000	2.79%	39,402	2.28%	51,465	2.32%

	Less than one year		One to five years		Five to ten years		Over ten years		December 31, 2014 Total	
	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield
Available for sale										
US government agencies	$ -	-	988	2.12%	-	-	7,569	2.43%	8,557	2.39%
SBA securities	-	-	-	-	-	-	5,154	1.88%	5,154	1.88%
State and political subdivisions	2,082	0.68%	399	3.14%	8,465	3.23%	5,854	3.00%	16,800	2.82%
Mortgage-backed securities	-	-	-	-	2,118	1.66%	22,395	2.62%	24,513	2.54%
Total	$ 2,082	0.68%	1,387	2.41%	10,583	2.91%	40,972	2.54%	55,024	2.54%

The tables below summarize gross unrealized losses on investment securities and the fair market value of the related securities at June 30, 2015 and December 31, 2014, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position.

	Less than 12 months			12 months or longer			June 30, 2015 Total		
(dollars in thousands)	#	Fair value	Unrealized losses	#	Fair value	Unrealized losses	#	Fair value	Unrealized losses
Available for sale									
US government agencies	3	$ 8,826	$ 307	-	$ -	$ -	3	$ 8,826	$ 307
SBA securities	-	-	-	2	4,903	169	2	4,903	169
State and political subdivisions	6	2,422	69	4	2,226	58	10	4,648	127
Mortgage-backed securities	8	11,592	159	-	-	-	8	11,592	159
Total	17	$22,840	$ 535	6	$ 7,129	$ 227	23	$29,969	$ 762

	Less than 12 months			12 months or longer			December 31, 2014 Total		
	#	Fair value	Unrealized losses	#	Fair value	Unrealized losses	#	Fair value	Unrealized losses
Available for sale									
US government agencies	-	$ -	$ -	2	$ 7,569	$ 215	2	$ 7,569	$ 215
SBA securities	-	-	-	2	5,154	182	2	5,154	182
State and political subdivisions	-	-	-	7	3,488	51	7	3,488	51
Mortgage-backed securities	3	4,407	11	2	4,756	31	5	9,163	42
Total	3	$ 4,407	$ 11	13	$20,967	$ 479	16	$25,374	$ 490

At June 30, 2015, the Company had 17 individual investments with a fair market value of $22.8 million that were in an unrealized loss position for less than 12 months and six individual investments with a fair market value of $7.1 million that were in an unrealized loss position for 12 months or longer. The unrealized losses were primarily attributable to changes in interest rates, rather than deterioration in credit quality. The individual securities are each investment grade securities. The Company considers the length of time and extent to which the fair value of available-for-sale debt securities have been less than cost to conclude that such securities are not other-than-temporarily impaired. We also consider other factors such as the financial condition of the issuer including credit ratings and specific events affecting the operations of the issuer, volatility of the security, underlying assets that collateralize the debt security, and other industry and macroeconomic conditions. As the Company has no intent to sell securities with unrealized losses and it is not more-likely-than-not that the Company will be required to sell these securities before recovery of amortized cost, we have concluded that these securities are not impaired on an other-than-temporary basis.

Other investments are comprised of the following and are recorded at cost which approximates fair value.

(dollars in thousands)	June 30, 2015	December 31, 2014
Federal Home Loan Bank stock	$ 5,005	6,020
Investment in Trust Preferred securities	403	403
Other investments	124	99
Total other investments	$ 5,532	6,522

The Company has evaluated the Federal Home Loan Bank (FHLB) stock for impairment and determined that the investment in the FHLB stock is not other than temporarily impaired as of June 30, 2015 and ultimate recoverability of the par value of this investment is probable. All of the FHLB stock is used to collateralize advances with the FHLB.

At June 30, 2015, $21.3 million of securities were pledged as collateral for repurchase agreements from brokers, and approximately $12.2 million of securities were pledged to secure client deposits. At December 31, 2014, $21.8 million of securities were pledged as collateral for repurchase agreements from brokers, and approximately $12.9 million of securities were pledged to secure client deposits.

NOTE 4 Loans and Allowance for Loan Losses

The following table summarizes the composition of our loan portfolio. Total gross loans are recorded net of deferred loan fees and costs, which totaled $1.9 million and $1.8 million as of June 30, 2015 and December 31, 2014, respectively.

	June 30, 2015		December 31, 2014	
(dollars in thousands)	Amount	% of Total	Amount	% of Total
Commercial				
Owner occupied RE	$232,997	24.2%	$191,061	21.9%
Non-owner occupied RE	207,623	21.6%	183,440	21.1%
Construction	33,570	3.5%	50,995	5.8%
Business	162,017	16.8%	149,986	17.2%
Total commercial loans	636,207	66.1%	575,482	66.0%
Consumer				
Real estate	166,404	17.3%	146,859	16.9%
Home equity	105,241	10.9%	95,629	11.0%
Construction	40,957	4.2%	39,226	4.5%
Other	14,687	1.5%	14,250	1.6%
Total consumer loans	327,289	33.9%	295,964	34.0%
Total gross loans, net of deferred fees	963,496	100.0%	871,446	100.0%
Less allowance for loan losses	(12,927)		(11,752)	
Total loans, net	$950,569		$859,694	

Maturities and Sensitivity of Loans to Changes in Interest Rates

The information in the following tables summarizes the loan maturity distribution by type and related interest rate characteristics based on the contractual maturities of individual loans, including loans which may be subject to renewal at their contractual maturity. Renewal of such loans is subject to review and credit approval, as well as modification of terms upon maturity. Actual repayments of loans may differ from the maturities reflected below, because borrowers have the right to prepay obligations with or without prepayment penalties.

(dollars in thousands)	One year or less	After one but within five years	After five years	June 30, 2015 Total
Commercial				
Owner occupied RE	$ 22,954	125,545	84,498	232,997
Non-owner occupied RE	38,321	132,549	36,753	207,623
Construction	13,429	15,467	4,674	33,570
Business	72,776	76,802	12,439	162,017
Total commercial loans	147,480	350,363	138,364	636,207
Consumer				
Real estate	25,794	42,669	97,941	166,404
Home equity	6,151	31,292	67,798	105,241
Construction	17,578	2,623	20,756	40,957
Other	7,409	5,787	1,491	14,687
Total consumer loans	56,932	82,371	187,986	327,289
Total gross loans, net of deferred fees	$ 204,412	432,734	326,350	963,496
Loans maturing after one year with:				
Fixed interest rates				$ 560,046
Floating interest rates				199,038

	One year or less	After one but within five years	After five years	December 31, 2014 Total
Commercial				
Owner occupied RE	$ 20,737	98,110	72,214	191,061
Non-owner occupied RE	46,718	104,402	32,320	183,440
Construction	11,923	25,145	13,927	50,995
Business	75,718	65,899	8,369	149,986
Total commercial loans	155,096	293,556	126,830	575,482
Consumer				
Real estate	21,571	41,549	83,739	146,859
Home equity	5,645	28,394	61,590	95,629
Construction	13,531	2,073	23,622	39,226
Other	7,278	5,637	1,335	14,250
Total consumer	48,025	77,653	170,286	295,964
Total gross loan, net of deferred fees	$ 203,121	371,209	297,116	871,446
Loans maturing after one year with :				
Fixed interest rates				494,058
Floating interest rates				174,267

Portfolio Segment Methodology

Commercial

Commercial loans are assessed for estimated losses by grading each loan using various risk factors identified through periodic reviews. We apply historic grade-specific loss factors to each loan class. In the development of our statistically derived loan grade loss factors, we observe historical losses over 12 quarters for each loan grade. These loss estimates are adjusted as appropriate based on additional analysis of external loss data or other risks identified from current economic conditions and credit quality trends. The allowance also includes an amount for the estimated impairment on nonaccrual commercial loans and commercial loans modified in a troubled debt restructuring (TDR), whether on accrual or nonaccrual status.

Consumer
For consumer loans, we determine the allowance on a collective basis utilizing historical losses over 12 quarters to represent our best estimate of inherent loss. We pool loans, generally by loan class with similar risk characteristics. The allowance also includes an amount for the estimated impairment on nonaccrual consumer loans and consumer loans modified in a TDR, whether on accrual or nonaccrual status.

Credit Quality Indicators

Commercial
We manage a consistent process for assessing commercial loan credit quality by monitoring our loan grading trends and past due statistics. All loans are subject to individual risk assessment. Our risk categories include Pass, Special Mention, Substandard, and Doubtful, each of which is defined by banking regulatory agencies. Delinquency statistics are also an important indicator of credit quality in the establishment of our allowance for credit losses.

We categorize our loans into risk categories based on relevant information about the ability of the borrower to service their debt such as current financial information, historical payment experience, credit documentation, public information, and current economic trends, among other factors. A description of the general characteristics of the risk grades is as follows:

Pass These loans range from minimal credit risk to average however still acceptable credit risk.

Special mention A special mention loan has potential weaknesses that deserve management s close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan or the institution s credit position at some future date.

Substandard A substandard loan is inadequately protected by the current sound worth and paying capacity of the obligor or of the collateral pledged, if any. Loans so classified must have a well-defined weakness, or weaknesses, that may jeopardize the liquidation of the debt. A substandard loan is characterized by the distinct possibility that the Bank will sustain some loss if the deficiencies are not corrected.

Doubtful A doubtful loan has all of the weaknesses inherent in one classified as substandard with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of the currently existing facts, conditions and values, highly questionable and improbable.

The tables below provide a breakdown of outstanding commercial loans by risk category.

					June 30, 2015
(dollars in thousands)	Owner occupied RE	Non-owner occupied RE	Construction	Business	Total
Pass	$227,441	197,847	31,639	152,923	609,850
Special mention	3,774	3,326	-	4,935	12,035
Substandard	1,782	6,450	1,931	4,159	14,322
Doubtful	-	-	-	-	-
	$232,997	207,623	33,570	162,017	636,207

					December 31, 2014
	Owner occupied RE	Non-owner occupied RE	Construction	Business	Total
Pass	$184,158	173,711	48,140	140,432	546,441
Special mention	5,035	3,376	129	4,715	13,255
Substandard	1,868	6,353	2,726	4,839	15,786
Doubtful	-	-	-	-	-
	$191,061	183,440	50,995	149,986	575,482

The following tables provide past due information for outstanding commercial loans and include loans on nonaccrual status as well as accruing TDRs.

					June 30, 2015
(dollars in thousands)	Owner occupied RE	Non-owner occupied RE	Construction	Business	Total
Current	$ 232,277	202,967	33,038	160,363	628,645
30-59 days past due	-	1,452	-	252	1,704
60-89 days past due	-	-	-	14	14
Greater than 90 Days	720	3,204	532	1,388	5,844
	$ 232,997	207,623	33,570	162,017	636,207

					December 31, 2014
	Owner occupied RE	Non-owner occupied RE	Construction	Business	Total
Current	$ 190,801	180,577	50,212	148,317	569,907
30-59 days past due	-	49	-	35	84
60-89 days past due	-	246	-	155	401
Greater than 90 Days	260	2,568	783	1,479	5,090
	$ 191,061	183,440	50,995	149,986	575,482

As of June 30, 2015 and December 31, 2014, loans 30 days or more past due represented 0.97% and 0.73% of our total loan portfolio, respectively. Commercial loans 30 days or more past due were 0.78% and 0.64% of our total loan portfolio as of June 30, 2015 and December 31, 2014, respectively.

Consumer

We manage a consistent process for assessing consumer loan credit quality by monitoring our loan grading trends and past due statistics. All loans are subject to individual risk assessment. Our categories include Pass, Special Mention, Substandard, and Doubtful, which are defined above. Delinquency statistics are also an important indicator of credit quality in the establishment of our allowance for loan losses.

The tables below provide a breakdown of outstanding consumer loans by risk category.

					June 30, 2015
(dollars in thousands)	Real estate	Home equity	Construction	Other	Total
Pass	$163,612	101,210	40,957	14,523	320,302
Special mention	790	2,976	-	135	3,901
Substandard	2,002	1,055	-	29	3,086
Doubtful	-	-	-	-	-
	$166,404	105,241	40,957	14,687	327,289

					December 31, 2014
	Real estate	**Home equity**	**Construction**	**Other**	**Total**
Pass	$144,070	91,084	39,226	14,013	288,393
Special mention	953	3,268	-	139	4,360
Substandard	1,836	1,277	-	98	3,211
Doubtful	-	-	-	-	-
	$146,859	95,629	39,226	14,250	295,964

The following tables provide past due information for outstanding consumer loans and include loans on nonaccrual status as well as accruing TDRs.

					June 30, 2015
(dollars in thousands)	**Real estate**	**Home equity**	**Construction**	**Other**	**Total**
Current	$ 165,065	104,846	40,957	14,632	325,500
30-59 days past due	455	145	-	51	651
60-89 days past due	465	130	-	4	599
Greater than 90 Days	419	120	-	-	539
	$ 166,404	105,241	40,957	14,687	327,289

					December 31, 2014
	Real estate	**Home equity**	**Construction**	**Other**	**Total**
Current	$ 146,362	95,311	39,226	14,247	294,146
30-59 days past due	40	-	-	-	40
60-89 days past due	-	130	-	3	133
Greater than 90 Days	457	188	-	-	645
	$ 146,859	95,629	39,226	14,250	295,964

As of June 30, 2015 and December 31, 2014, consumer loans 30 days or more past due were 0.19% and 0.09%, respectively, of total loans.

Nonperforming assets

The following table shows the nonperforming assets and the related percentage of nonperforming assets to total assets and gross loans. Generally, a loan is placed on nonaccrual status when it becomes 90 days past due as to principal or interest, or when we believe, after considering economic and business conditions and collection efforts, that the borrower s financial condition is such that collection of the contractual principal or interest on the loan is doubtful. A payment of interest on a loan that is classified as nonaccrual is recognized as a reduction in principal when received.

Following is a summary of our nonperforming assets, including nonaccruing TDRs.

(dollars in thousands)	June 30, 2015	December 31, 2014
Commercial		
Owner occupied RE	$ 720	322
Non-owner occupied RE	3,018	2,344
Construction	-	783
Business	1,178	1,408
Consumer		
Real estate	419	457
Home equity	250	188
Construction	-	-
Other	1	1
Nonaccruing troubled debt restructurings	1,087	1,147
Total nonaccrual loans, including nonaccruing TDRs	6,673	6,650
Other real estate owned	2,887	3,307
Total nonperforming assets	$ 9,560	9,957
Nonperforming assets as a percentage of:		
Total assets	0.85%	0.97%
Gross loans	0.99%	1.14%
Total loans over 90 days past due	6,383	5,735
Loans over 90 days past due and still accruing	-	-
Accruing troubled debt restructurings	$ 8,173	8,562

Impaired Loans

The table below summarizes key information for impaired loans. Our impaired loans include loans on nonaccrual status and loans modified in a TDR, whether on accrual or nonaccrual status. These impaired loans may have estimated impairment which is included in the allowance for loan losses. Our commercial and consumer impaired loans are evaluated individually to determine the related allowance for loan losses.

				June 30, 2015
		Recorded investment		
(dollars in thousands)	Unpaid Principal Balance	Impaired loans	Impaired loans with related allowance for loan losses	Related allowance for loan losses
Commercial				
Owner occupied RE	$ 1,531	1,506	1,506	490
Non-owner occupied RE	8,342	4,997	3,091	778
Construction	1,931	1,931	532	166
Business	4,591	4,126	2,946	2,266
Total commercial	16,395	12,560	8,075	3,700
Consumer				
Real estate	1,702	1,664	1,346	631
Home equity	406	406	157	157
Construction	-	-	-	-
Other	216	216	216	216
Total consumer	2,324	2,286	1,719	1,004
Total	$18,719	14,846	9,794	4,704

			December 31, 2014	
	Unpaid Principal Balance	Impaired loans	Recorded investment Impaired loans with related allowance for loan losses	Related allowance for loan losses
Commercial				
Owner occupied RE	$ 1,122	1,122	1,060	371
Non-owner occupied RE	5,813	4,522	2,777	801
Construction	5,268	2,726	1,315	324
Business	5,385	4,565	3,528	2,464
Total commercial	17,588	12,935	8,680	3,960
Consumer				
Real estate	1,620	1,620	1,299	585
Home equity	347	347	347	191
Construction	-	-	-	-
Other	310	310	310	310
Total consumer	2,277	2,277	1,956	1,086
Total	$19,865	15,212	10,636	5,046

The following table provides the average recorded investment in impaired loans and the amount of interest income recognized on impaired loans after impairment by portfolio segment and class.

	Three months ended June 30, 2015		Three months ended June 30, 2014	
(dollars in thousands)	Average recorded investment	Recognized interest ncome	Average recorded investment	Average recorded investment
Commercial				
Owner occupied RE	$ 1,292	10	1,662	2
Non-owner occupied RE	5,153	24	6,646	22
Construction	1,935	23	1,768	-
Business	4,194	33	4,713	42
Total commercial	12,574	90	14,789	66
Consumer				
Real estate	1,685	12	2,355	12
Home equity	376	8	161	2
Construction	-	-	-	-
Other	219	2	277	3
Total consumer	2,280	22	2,793	17
Total	$ 14,854	112	17,582	83

	Six months ended June 30, 2015		Six months ended June 30, 2014		Year ended December 31, 2014	
(dollars in thousands)	Average recorded investment	Recognized interest income	Average recorded investment	Recognized interest income	Average recorded investment	Recognized interest income
Commercial						
Owner occupied RE	$ 1,236	31	1,753	3	1,568	47
Non-owner occupied RE	4,942	47	6,305	53	5,693	104
Construction	2,198	41	1,802	14	1,977	75
Business	4,318	70	4,703	83	4,522	154
Total commercial	12,694	189	14,563	153	13,760	380
Consumer						
Real estate	1,664	24	2,172	25	2,094	53
Home equity	366	9	187	4	251	10
Construction	-	-	-	-	-	-
Other	249	4	260	5	282	13
Total consumer	2,279	37	2,619	34	2,627	76
Total	$14,973	226	17,182	187	16,387	456

Allowance for Loan Losses

The allowance for loan loss is management s estimate of credit losses inherent in the loan portfolio. The allowance for loan losses is established as losses are estimated to have occurred through a provision for loan losses charged to earnings. Loan losses are charged against the allowance when management believes the uncollectibility of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance. The allowance for loan losses is evaluated on a regular basis by management and is based upon management s periodic review of the collectability of the loans in light of historical experience, the nature and volume of the loan portfolio, adverse situations that may affect the borrower s ability to repay, estimated value of any underlying collateral and prevailing economic conditions. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available.

We have an established process to determine the adequacy of the allowance for loan losses that assesses the losses inherent in our portfolio. While we attribute portions of the allowance to specific portfolio segments, the entire allowance is available to absorb credit losses inherent in the total loan portfolio. Our process involves procedures to appropriately consider the unique risk characteristics of our commercial and consumer loan portfolio segments. For each portfolio segment, impairment is measured individually for each impaired loan. Our allowance levels are influenced by loan volume, loan grade or delinquency status, historic loss experience and other economic conditions.

The following table summarizes the activity related to our allowance for loan losses by commercial and consumer portfolio segments:

	Six months ended June 30, 2015								
	Commercial				Consumer				
(dollars in thousands)	Owner occupied RE	Non-owner occupied RE	Construction	Business	Real Estate	Home equity	Construction	Other	Total
Balance, beginning of period	$1,645	2,332	614	3,625	1,714	1,162	236	424	11,752
Provision for loan losses	643	574	(216)	272	263	131	36	(78)	1,625
Loan charge-offs	(24)	(204)	-	(218)	(39)	(13)	-	(1)	(499)
Loan recoveries	-	6	-	42	-	1	-	-	49
Net loan charge-offs	(24)	(198)	-	(176)	(39)	(12)	-	(1)	(450)
Balance, end of period	$2,264	2,708	398	3,721	1,938	1,281	272	345	12,927
Net charge-offs to average loans (annualized)									0.10%
Allowance for loan losses to gross loans									1.34%
Allowance for loan losses to nonperforming loans									193.73%

	Six months ended June 30, 2014								
	Commercial					Consumer			
(dollars in thousands)	Owner occupied RE	Non-owner occupied RE	Construction	Business	Real Estate	Home equity	Construction	Other	Total
Balance, beginning of period	$ 1,880	2,633	397	3,329	1,091	644	99	140	10,213
Provision for loan losses	(299)	1,661	29	207	178	100	36	38	1,950
Loan charge-offs	-	(1,084)	-	-	-	(76)	-	(4)	(1,164)
Loan recoveries	-	-	-	103	-	1	-	-	104
Net loan charge-offs	-	(1,084)	-	103	-	(75)	-	(4)	(1,060)
Balance, end of period	$ 1,581	3,210	426	3,639	1,269	669	135	174	11,103
Net charge-offs to average loans (annualized)									0.28%
Allowance for loan losses to gross loans									1.37%
Allowance for loan losses to nonperforming loans									90.30%

The following table disaggregates our allowance for loan losses and recorded investment in loans by impairment methodology.

	June 30, 2015					
	Allowance for loan losses			Recorded investment in loans		
(dollars in thousands)	Commercial	Consumer	Total	Commercial	Consumer	Total
Individually evaluated	$ 3,700	1,004	4,704	12,560	2,286	14,846
Collectively evaluated	5,391	2,832	8,223	623,647	325,003	948,650
Total	$ 9,091	3,836	12,927	636,207	327,289	963,496

	December 31, 2014					
	Allowance for loan losses			Recorded investment in loans		
	Commercial	Consumer	Total	Commercial	Consumer	Total
Individually evaluated	$ 3,960	1,086	5,046	12,935	2,277	15,212
Collectively evaluated	4,256	2,450	6,706	562,547	293,687	856,234
Total	$ 8,216	3,536	11,752	575,482	295,964	871,446

NOTE 5 Troubled Debt Restructurings

At June 30, 2015, we had 37 loans totaling $9.3 million and at December 31, 2014 we had 37 loans totaling $9.7 million, which we considered as TDRs. The Company considers a loan to be a TDR when the debtor experiences financial difficulties and the Company grants a concession to the debtor that it would not normally consider. Concessions can relate to the contractual interest rate, maturity date, or payment structure of the note. As part of our workout plan for individual loan relationships, we may restructure loan terms to assist borrowers facing financial challenges in the current economic environment. To date, we have restored three commercial loans previously classified as TDRs to accrual status.

The following table summarizes the concession at the time of modification and the recorded investment in our TDRs before and after their modification during the six months ended June 30, 2015 and 2014, respectively.

(dollars in thousands)	Renewals deemed a concession	Reduced or deferred payments	Converted to interest only	Maturity date extensions	Total Number of loans	Pre-modification outstanding recorded investment	Post-modification outstanding recorded investment
	For the six months ended June 30, 2015						
Commercial							
Owner occupied RE	-	-	-	-	-	$ -	$ -
Non-owner occupied RE	1	-	-	1	2	112	112
Construction	-	-	-	-	-	-	-
Business	-	-	-	1	1	21	21
Consumer							
Real estate	-	-	-	-	-	-	-
Home equity	-	-	-	-	-	-	-
Construction	-	-	-	-	-	-	-
Other	-	-	-	-	-	-	-
Total loans	1	-	-	2	3	$ 133	$ 133

(dollars in thousands)	Renewals deemed a concession	Reduced or deferred payments	Converted to interest only	Maturity date extensions	Total Number of loans	Pre-modification outstanding recorded investment	Post-modification outstanding recorded investment
	For the six months ended June 30, 2014						
Commercial							
Owner occupied RE	-	-	-	-	-	$ -	$ -
Non-owner occupied RE	-	-	-	1	1	49	49
Construction	-	-	-	-	-	-	-
Business	1	-	-	2	3	371	372
Consumer							
Real estate	-	-	1	-	1	116	116
Home equity	-	-	-	-	-	-	-
Construction	-	-	-	-	-	-	-
Other	2	-	-	-	2	126	126
Total loans	3	-	1	3	7	$ 662	$ 663

The following table summarizes loans modified as TDRs at June 30, 2015 and 2014 for which there was a payment default (60 days past due) within 12 months of the restructuring date.

	For the six months ended June 30,			
	2015		2014	
(dollars in thousands)	Number of Loans	Recorded Investment	Number of Loans	Recorded Investment
Commercial				
Owner occupied RE	-	$ -	-	$ -
Non-owner occupied RE	-	-	2	3,357
Construction	-	-	-	-
Business	-	-	1	98
Consumer				
Real estate	-	-	-	-
Home equity	-	-	-	-
Construction	-	-	-	-
Other	-	-	-	-
Total loans	-	$ -	3	$ 3,455

NOTE 6 Fair Value Accounting

FASB ASC 820, Fair Value Measurement and Disclosures, defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. FASB ASC 820 also establishes 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 market price in active markets
Quoted prices in active markets for identical assets or liabilities. Level 1 assets and liabilities include certain debt and equity securities that are traded in an active exchange market.

Level 2 Significant other observable inputs
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 2 assets and liabilities include fixed income securities and mortgage-backed securities that are held in the Company s available-for-sale portfolio and valued by a third-party pricing service, as well as certain impaired loans.

Level 3 Significant unobservable inputs
Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. Level 3 assets and liabilities include financial instruments whose value is determined using pricing models, discounted cash flow methodologies, or similar techniques, as well as instruments for which the determination of fair value requires significant management judgment or estimation. These methodologies may result in a significant portion of the fair value being derived from unobservable data.

Following is a description of valuation methodologies used for assets recorded at fair value.

Investment Securities
Securities available for sale are valued on a recurring basis at quoted market prices where available. If quoted market prices are not available, fair values are based on quoted market prices of comparable securities. Level 1 securities include those traded on an active exchange, such as the New York Stock Exchange or U.S. Treasury securities that are traded by dealers or brokers in active over-the-counter markets and money market funds. Level 2 securities include mortgage-backed securities and debentures issued by government sponsored entities, municipal bonds and corporate debt securities. In certain cases where there is limited activity or less transparency around inputs to valuations, securities are classified as Level 3 within the valuation hierarchy. Securities held to maturity are valued at quoted market prices or dealer quotes similar to securities available for sale. The carrying value of Other Investments, such as Federal Reserve Bank and FHLB stock, approximates fair value based on their redemption provisions.

Loans Held for Sale
Loans held for sale include mortgage loans and are carried at the lower of cost or market value. The fair values of mortgage loans held for sale are based on current market rates from investors within the secondary market for loans with similar characteristics. Carrying value approximates fair value.

Loans
The Company does not record loans at fair value on a recurring basis. However, from time to time, a loan may be considered impaired and an allowance for loan losses may be established. Loans for which it is probable that payment of interest and principal will not be made in accordance with the contractual terms of the loan agreement are considered impaired. Once a loan is identified as individually impaired, management measures the impairment in accordance with FASB ASC 310, Receivables. The fair value of impaired loans is estimated using one of several methods, including collateral value, market value of similar debt, enterprise value, liquidation value, and discounted cash flows. Those impaired loans not requiring an allowance represent loans for which the fair value of the expected repayments or collateral exceed the recorded investments in such loans. At June 30, 2015, a significant portion of the impaired loans were evaluated based on the fair value of the collateral. In accordance with FASB ASC 820, Fair Value Measurement and Disclosures, impaired loans where an allowance is established based on the fair value of collateral require classification in the fair value hierarchy. When the fair value of the collateral is based on an observable market price or a current appraised value, the Company considers the impaired loan as nonrecurring Level 2. The Company s current loan and appraisal policies require the Bank to obtain updated appraisals on an as is basis at renewal, or in the case of an impaired loan, on an annual basis, either through a new external appraisal or an appraisal evaluation. When an appraised value is not available or management determines the fair value of the collateral is further impaired below the appraised value and there is no observable market price, the Company considers the impaired loan as nonrecurring Level 3. The fair value of impaired loans may also be estimated using the

present value of expected future cash flows to be realized on the loan, which is also considered a Level 3 valuation. These fair value estimates are subject to fluctuations in assumptions about the amount and timing of expected cash flows as well as the choice of discount rate used in the present value calculation.

Other Real Estate Owned (OREO)

OREO, consisting of properties obtained through foreclosure or in satisfaction of loans, is reported at the lower of cost or fair value, determined on the basis of current appraisals, comparable sales, and other estimates of value obtained principally from independent sources, adjusted for estimated selling costs (Level 2). At the time of foreclosure, any excess of the loan balance over the fair value of the real estate held as collateral is treated as a charge against the allowance for loan losses. Gains or losses on sale and generally any subsequent adjustments to the value are recorded as a component of real estate owned activity. When an appraised value is not available or management determines the fair value of the collateral is further impaired below the appraised value and there is no observable market price, the Company considers the OREO as nonrecurring Level 3.

Assets and Liabilities Recorded at Fair Value on a Recurring Basis

The tables below present the recorded amount of assets and liabilities measured at fair value on a recurring basis as of June 30, 2015 and December 31, 2014.

				June 30, 2015
(dollars in thousands)	**Level 1**	**Level 2**	**Level 3**	**Total**
Assets				
Securities available for sale				
US government agencies	$ -	8,844	-	8,844
SBA securities	-	4,903	-	4,903
State and political subdivisions	-	16,346	-	16,346
Mortgage-backed securities	-	21,372	-	21,372
Total assets measured at fair value on a recurring basis	$ -	51,465	-	51,465

				December 31, 2014
	Level 1	**Level 2**	**Level 3**	**Total**
Assets				
Securities available for sale				
US government agencies	$ -	8,557	-	8,557
SBA securities	-	5,154	-	5,154
State and political subdivisions	-	16,800	-	16,800
Mortgage-backed securities	-	24,513	-	24,513
Total assets measured at fair value on a recurring basis	$ -	55,024	-	55,024

The Company has no liabilities carried at fair value or measured at fair value on a recurring basis as of June 30, 2015 and December 31, 2014.

Assets and Liabilities Recorded at Fair Value on a Nonrecurring Basis

The Company is predominantly an asset based lender with real estate serving as collateral on more than 80% of loans as of June 30, 2015. Loans which are deemed to be impaired are valued net of the allowance for loan losses, and other real estate owned is valued at the lower of cost or net realizable value of the underlying real estate collateral. Such market values are generally obtained using independent appraisals, which the Company considers to be level 2 inputs. The tables below present the recorded amount of assets and liabilities measured at fair value on a nonrecurring basis as of June 30, 2015 and December 31, 2014.

				As of June 30, 2015
(dollars in thousands)	Level 1	Level 2	Level 3	Total
Assets				
Impaired loans	$ -	9,678	464	10,142
Other real estate owned	-	2,458	429	2,887
Total assets measured at fair value on a nonrecurring basis	$ -	12,136	893	13,029

				As of December 31, 2014
	Level 1	Level 2	Level 3	Total
Assets				
Impaired loans	$ -	9,461	705	10,166
Other real estate owned	-	3,040	267	3,307
Total assets measured at fair value on a nonrecurring basis	$ -	12,501	972	13,473

The Company has no liabilities carried at fair value or measured at fair value on a nonrecurring basis as of June 30, 2015 and December 31, 2014.

For Level 3 assets and liabilities measured at fair value on a recurring or nonrecurring basis as of June 30, 2015, the significant unobservable inputs used in the fair value measurements were as follows:

	Valuation Technique	Significant Unobservable Inputs	Range of Inputs
Impaired loans	Appraised Value/ Discounted Cash Flows	Discounts to appraisals or cash flows for estimated holding and/or selling costs or age of appraisal	0-25%
Other real estate owned	Appraised Value/ Comparable Sales	Discounts to appraisals for estimated holding or selling costs	0-25%

Fair Value of Financial Instruments

Financial instruments require disclosure of fair value information, whether or not recognized in the consolidated balance sheets, when it is practical to estimate the fair value. A financial instrument is defined as cash, evidence of an ownership interest in an entity or a contractual obligation which requires the exchange of cash. Certain items are specifically excluded from the disclosure requirements, including the Company s common stock, premises and equipment and other assets and liabilities.

The following is a description of valuation methodologies used to estimate fair value for certain other financial instruments.

Fair value approximates carrying value for the following financial instruments due to the short-term nature of the instrument: cash and due from banks, federal funds sold, federal funds purchased, and securities sold under agreement to repurchase.

Deposits Fair value for demand deposit accounts and interest-bearing accounts with no fixed maturity date is equal to the carrying value. The fair value of certificate of deposit accounts are estimated by discounting cash flows from expected maturities using current interest rates on similar instruments.

FHLB Advances and Other Borrowings Fair value for FHLB advances and other borrowings are estimated by discounting cash flows from expected maturities using current interest rates on similar instruments.

Junior subordinated debentures Fair value for junior subordinated debentures are estimated by discounting cash flows from expected maturities using current interest rates on similar instruments.

The Company has used management s best estimate of fair value based on the above assumptions. Thus, the fair values presented may not be the amounts that could be realized in an immediate sale or settlement of the instrument. In addition, any income taxes or other expenses, which would be incurred in an actual sale or settlement, are not taken into consideration in the fair value presented.

The estimated fair values of the Company s financial instruments at June 30, 2015 and December 31, 2014 are as follows:

					June 30, 2015
(dollars in thousands)	Carrying Amount	Fair Value	Level 1	Level 2	Level 3
Financial Assets:					
Cash and cash equivalents	$ 41,410	41,410	41,410	-	-
Other investments, at cost	5,532	5,532	-	-	5,532
Loans held for sale	12,402	12,402	-	12,402	-
Loans, net	950,569	952,186	-	9,678	942,508
Financial Liabilities:					
Deposits	894,524	846,216	-	846,216	-
FHLB and other borrowings	115,200	122,866	-	122,866	-
Junior subordinated debentures	13,403	12,251	-	12,251	-

					December 31, 2014
	Carrying Amount	Fair Value	Level 1	Level 2	Level 3
Financial Assets:					
Cash and cash equivalents	$ 41,264	41,264	41,264	-	-
Other investments, at cost	6,522	6,522	-	-	6,522
Loans held for sale	11,765	11,765	-	11,765	-
Loans, net	859,694	860,215	-	9,461	850,754
Financial Liabilities:					
Deposits	788,907	748,497	-	748,497	-
FHLB and other borrowings	135,200	144,156	-	144,156	-
Junior subordinated debentures	13,403	6,823	-	6,823	-

NOTE 7 Earnings Per Common Share

The following schedule reconciles the numerators and denominators of the basic and diluted earnings per share computations for the three and six month periods ended June 30, 2015 and 2014. Dilutive common shares arise from the potentially dilutive effect of the Company s stock options that were outstanding at June 30, 2015. The assumed conversion of stock options can create a difference between basic and dilutive net income per common share. At June 30, 2015 and 2014, there were 170,875 and 114,124 options, respectively, that were not considered in computing diluted earnings per common share because they were anti-dilutive.

(dollars in thousands, except share data)		Three months ended June 30, 2015	Three months ended June 30, 2014	Six months ended June 30, 2015	Six months ended June 30, 2014
Numerator:					
Net income	$	2,560	1,566	4,588	2,816
Less: Preferred stock dividend		-	253	-	445
Net income available to common shareholders	$	2,560	1,313	4,588	2,371
Denominator:					
Weighted-average common shares outstanding basic		6,233,745	4,763,407	6,229,522	4,686,748
Common stock equivalents		299,913	273,146	294,795	270,252
Weighted-average common shares outstanding diluted		6,533,658	5,036,553	6,524,317	4,957,000
Earnings per common share:					
Basic	$	0.41	0.28	0.74	0.51
Diluted	$	0.39	0.26	0.70	0.48

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

The following discussion reviews our results of operations for the three and six month periods ended June 30, 2015 as compared to the three and six month periods ended June 30, 2014 and assesses our financial condition as of June 30, 2015 as compared to December 31, 2014. You should read the following discussion and analysis in conjunction with the accompanying consolidated financial statements and the related notes and the consolidated financial statements and the related notes for the year ended December 31, 2014 included in our Annual Report on Form 10-K for that period. Results for the three and six month periods ended June 30, 2015 are not necessarily indicative of the results for the year ending December 31, 2015 or any future period.

Cautionary Warning Regarding forward-looking statements

This report, including information included or incorporated by reference in this report, contains statements which constitute forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. Forward-looking statements may relate to our financial condition, results of operations, plans, objectives, or future performance. These statements are based on many assumptions and estimates and are not guarantees of future performance. Our actual results may differ materially from those anticipated in any forward-looking statements, as they will depend on many factors about which we are unsure, including many factors which are beyond our control. The words may, would, could, should, will, expect, anticipate, predict, project, potential, believe, continue, assume, intend, plan, and es expressions, are meant to identify such forward-looking statements. Potential risks and uncertainties that could cause our actual results to differ from those anticipated in any forward-looking statements include, but are not limited to, those described under Item 1A- Risk Factors of our Annual Report on Form 10-K for the year ended December 31, 2014, as well as the following:

Restrictions or conditions imposed by our regulators on our operations;

Increases in competitive pressure in the banking and financial services industries;

Changes in access to funding or increased regulatory requirements with regard to funding;

Changes in deposit flows;

Credit losses as a result of declining real estate values, increasing interest rates, increasing unemployment, changes in payment behavior or other factors;

Credit losses due to loan concentration;

Changes in the amount of our loan portfolio collateralized by real estate and weaknesses in the real estate market;

Our ability to attract and retain key personnel;

Changes in the interest rate environment which could reduce anticipated or actual margins;

Changes in political conditions or the legislative or regulatory environment, including governmental initiatives affecting the financial services industry;

Changes in economic conditions resulting in, among other things, a deterioration in credit quality;

Changes occurring in business conditions and inflation;

Cybersecurity breaches, including potential business disruptions or financial losses;

Changes in technology;

The adequacy of the level of our allowance for loan losses and the amount of loan loss provisions required in future periods;

Examinations by our regulatory authorities, including the possibility that the regulatory authorities may, among other things, require us to increase our allowance for loan losses or write-down assets;

Changes in monetary and tax policies;

The rate of delinquencies and amounts of loans charged-off;

The rate of loan growth in recent years and the lack of seasoning of a portion of our loan portfolio;

Our ability to maintain appropriate levels of capital and to comply with our capital ratio requirements;

Adverse changes in asset quality and resulting credit risk-related losses and expenses;

Changes in accounting policies and practices; and

Other risks and uncertainties detailed in this Quarterly Report on Form 10-Q and, from time to time, in our other filings with the Securities and Exchange Commission (the SEC).

If any of these risks or uncertainties materialize, or if any of the assumptions underlying such forward-looking statements proves to be incorrect, our results could differ materially from those expressed in, implied or projected by, such forward-looking statements. For information with respect to factors that could cause actual results to differ from the expectations stated in the forward-looking statements, see Risk Factors under Part I, Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2014. We urge investors to consider all of these factors carefully in evaluating the forward-looking statements contained in this Quarterly Report on Form 10-Q. We make these forward-looking statements as of the date of this document and we do not intend, and assume no obligation, to update the forward-looking statements or to update the reasons why actual results could differ from those expressed in, or implied or projected by, the forward-looking statements.

OVERVIEW

Our business model continues to be client-focused, utilizing relationship teams to provide our clients with a specific banker contact and support team responsible for all of their banking needs. The purpose of this structure is to provide a consistent and superior level of professional service, and we believe it provides us with a distinct competitive advantage. We consider exceptional client service to be a critical part of our culture, which we refer to as "ClientFIRST."

At June 30, 2015, we had total assets of $1.1 billion, an 8.7% increase from total assets of $1.0 billion at December 31, 2014. The largest components of our total assets are net loans and securities which were $950.6 million and $57.0 million, respectively, at June 30, 2015. Comparatively, our net loans and securities totaled $859.7 million and $61.5 million, respectively, at December 31, 2014. Our liabilities and shareholders equity at June 30, 2015 totaled $1.0 billion and $87.7 million, respectively, compared to liabilities of $946.9 million and shareholders equity of $83.0 million at December 31, 2014. The principal component of our liabilities is deposits which were $894.5 million and $788.9 million at June 30, 2015 and December 31, 2014, respectively.

Like most community banks, we derive the majority of our income from interest received on our loans and investments. Our primary source of funds for making these loans and investments is our deposits, on which we pay interest. Consequently, one of the key measures of our success is our amount of net interest income, or the difference between the income on our interest-earning assets, such as loans and investments, and the expense on our interest-bearing liabilities, such as deposits and borrowings. Another key measure is the spread between the yield we earn on these interest-earning assets and the rate we pay on our interest-bearing liabilities, which is called our net interest spread. In addition to earning interest on our loans and investments, we earn income through fees and other charges to our clients.

Our net income to common shareholders was $2.6 million and $1.3 million for the three months ended June 30, 2015 and 2014, respectively, an increase of $1.2 million, or 95.0%. Diluted earnings per share (EPS) was $0.39, for the second quarter of 2015 as compared to $0.26 for the same period in 2014. The increase in net income resulted primarily from increases in net interest income and noninterest income, partially offset by an increase in noninterest expense.

Our net income to common shareholders was $4.6 million and $2.4 million for the six months ended June 30, 2015 and 2014, respectively, an increase of $2.2 million, or 93.5%. Diluted EPS was $0.70 for the six months ended June 30, 2015 as compared to $0.48 for the same period in 2014. The increase in net income resulted primarily from increases in net interest income and noninterest income, partially offset by an increase in noninterest expense.

Economic conditions, competition, and the monetary and fiscal policies of the Federal government significantly affect most financial institutions, including the Bank. Lending and deposit activities and fee income generation are influenced by levels of business spending and investment, consumer income, consumer spending and savings, capital market activities, and competition among financial institutions, as well as customer preferences, interest rate conditions and prevailing market rates on competing products in our market areas.

Effect of Economic Trends

Markets in the United States and elsewhere have experienced extreme volatility and disruption since the latter half of 2007. While the economy as a whole has steadily improved since 2009, the weaker economic conditions are expected to continue through 2015. Financial institutions recently experienced credit losses above historical levels and elevated levels of non-performing assets, charge-offs and foreclosures. In light of these conditions, financial institutions continue to face heightened levels of scrutiny from federal and state regulators. These factors negatively influenced, and likely will continue to negatively influence, earning asset yields at a time when the market for deposits is intensely competitive. As a result, financial institutions experienced, and may continue to experience, pressure on loan yields, deposit and other borrowing costs, liquidity, and capital.

RESULTS OF OPERATIONS

Net Interest Income and Margin

Our level of net interest income is determined by the level of earning assets and the management of our net interest margin. Our net interest income was $9.5 million for the three month period ended June 30, 2015, a 17.6% increase over net interest income of $8.1 million for the same period in 2014. In comparison, our average earning assets increased 15.0%, or $134.2 million, during the second quarter of 2015 compared to the second quarter of 2014, while our interest bearing liabilities increased by $89.1 million during the same period. The increase in average earning assets is primarily related to an increase in average loans, while the increase in average interest-bearing liabilities is primarily a result of an increase in interest bearing deposits.

We have included a number of tables to assist in our description of various measures of our financial performance. For example, the Average Balances, Income and Expenses, Yields and Rates table reflects the average balance of each category of our assets and liabilities as well as the yield we earned or the rate we paid with respect to each category during the three and six month periods ended June 30, 2015 and 2014. A review of this table shows that our loans typically provide higher interest yields than do other types of interest-earning assets, which is why we direct a substantial percentage of our earning assets into our loan portfolio. Similarly, the Rate/Volume Analysis table demonstrates the effect of changing interest rates and changing volume of assets and liabilities on our financial condition during the periods shown. We also track the sensitivity of our various categories of assets and liabilities to changes in interest rates, and we have included tables to illustrate our interest rate sensitivity with respect to interest-earning accounts and interest-bearing accounts.

The following tables set forth information related to our average balance sheets, average yields on assets, and average costs of liabilities. We derived these yields by dividing income or expense by the average balance of the corresponding assets or liabilities. We derived average balances from the daily balances throughout the periods indicated. During the same periods, we had no securities purchased with agreements to resell. All investments owned have an original maturity of over one year. Nonaccrual loans are included in the following tables. Loan yields have been reduced to reflect the negative impact on our earnings of loans on nonaccrual status. The net of capitalized loan costs and fees are amortized into interest income on loans.

Average Balances, Income and Expenses, Yields and Rates

	For the Three Months Ended June 30,					
			2015			2014
(dollars in thousands)	Average Balance	Income/ Expense	Yield/ Rate(1)	Average Balance	Income/ Expense	Yield/ Rate(1)
Interest-earning assets						
Federal funds sold	$ 24,461	$ 19	0.31%	$ 23,367	$ 16	0.27%
Investment securities, taxable	41,719	254	2.44%	49,519	324	2.62%
Investment securities, nontaxable (2)	14,679	165	4.50%	22,019	227	4.14%
Loans (3)	946,670	10,941	4.64%	798,410	9,309	4.68%
Total interest-earning assets	1,027,529	11,379	4.44%	893,315	9,876	4.43%
Noninterest-earning assets	53,282			49,062		
Total assets	$ 1,080,811			$ 942,377		
Interest-bearing liabilities						
NOW accounts	$ 175,304	77	0.18%	$ 143,972	52	0.14%
Savings & money market	243,326	245	0.40%	186,409	146	0.31%
Time deposits	283,259	532	0.75%	272,178	498	0.73%
Total interest-bearing deposits	701,889	854	0.49%	602,559	696	0.46%
FHLB advances and other borrowings	115,248	890	3.10%	125,434	944	3.02%
Junior subordinated debentures	13,403	81	2.42%	13,403	80	2.39%
Total interest-bearing liabilities	830,540	1,825	0.88%	741,396	1,720	0.93%
Noninterest-bearing liabilities	162,888			129,572		
Shareholders equity	87,383			71,409		
Total liabilities and shareholders equity	$ 1,080,811			$ 942,377		
Net interest spread			3.56%			3.50%
Net interest income (tax equivalent) / margin		$ 9,554	3.73%		$ 8,156	3.66%
Less: tax-equivalent adjustment (2)		63			86	
Net interest income		$ 9,491			$ 8,070	

(1) Annualized for the three month period.
(2) The tax-equivalent adjustment to net interest income adjusts the yield for assets earning tax-exempt income to a comparable yield on a taxable basis.
(3) Includes loans held for sale.

Our net interest margin, on a tax-equivalent basis, was 3.73% for the three months ended June 30, 2015 compared to 3.66% for the second quarter of 2014. The increase in net interest margin as compared to the same period in 2014, was driven primarily by a five basis point reduction in the cost of our interest-bearing liabilities, assisted by a one basis point increase in the yield on our interest-earning assets.

Our average interest-earning assets increased by $134.2 million as compared to the same quarter in 2014, while the yield on these assets increased by one basis point. The increase in average interest-earning assets was driven by a $148.3 million increase in our average loan balances for the second quarter of 2015, compared to the same period in 2014; however, our loan yield decreased by four basis points during the same period. The decline in yield on our loan portfolio was driven primarily by loans being originated or renewed at market rates which are lower than those in the past.

In addition, our average interest-bearing liabilities increased by $89.1 million during the second quarter of 2015 as compared to the first quarter of 2014, while the cost of our interest-bearing liabilities declined by five basis points during the same period. The reduction in cost during the 2015 period resulted primarily from a $99.3 million increase in our interest-bearing deposits which have a lower cost than our other interest-bearing liabilities. We do not anticipate further significant reductions in the rates on our interest-bearing deposits or FHLB advances and other borrowings in the future as these rates are currently at historically low rates.

Our net interest spread was 3.56% for the three months ended June 30, 2015 compared to 3.50% for the same period in 2014. The net interest spread is the difference between the yield we earn on our interest-earning assets and the rate we pay on our interest-bearing liabilities. The five basis point reduction in rate on our interest-bearing liabilities, assisted by the one basis point increase in yield on our interest-earning assets, resulted in a six basis point increase in our net interest spread for the 2015 period.

	For the Six Months Ended June 30,					
			2015			2014
	Average	Income/	Yield/	Average	Income/	Yield/
(dollars in thousands)	Balance	Expense	Rate(1)	Balance	Expense	Rate(1)
Interest-earning assets						
Federal funds sold	$ 29,392	$ 45	0.31%	$ 24,184	$ 30	0.25%
Investment securities, taxable	42,097	526	2.52%	50,001	682	2.75%
Investment securities, nontaxable (2)	15,042	331	4.43%	22,928	477	4.20%
Loans	924,869	21,341	4.65%	776,144	18,126	4.71%
Total interest-earning assets	1,011,400	22,243	4.43%	873,257	19,315	4.46%
Noninterest-earning assets	53,618			48,865		
Total assets	$ 1,065,018			$ 922,122		
Interest-bearing liabilities						
NOW accounts	$ 169,102	150	0.18%	$ 147,435	111	0.15%
Savings & money market	240,222	447	0.38%	174,694	266	0.31%
Time deposits	280,091	1,024	0.74%	272,710	999	0.74%
Total interest-bearing deposits	689,415	1,621	0.47%	594,839	1,376	0.47%
Note payable and other borrowings	119,987	1,774	2.98%	124,784	1,884	3.04%
Junior subordinated debentures	13,403	161	2.42%	13,403	160	2.41%
Total interest-bearing liabilities	822,805	3,556	0.87%	733,026	3,420	0.94%
Noninterest-bearing liabilities	155,971			118,883		
Shareholders equity	86,242			70,213		
Total liabilities and shareholders equity	$ 1,065,018			$ 922,122		
Net interest spread			3.56%			3.52%
Net interest income (tax equivalent) / margin		$ 18,687	3.73%		$ 15,895	3.67%
Less: tax-equivalent adjustment (2)		126			181	
Net interest income		$ 18,561			$ 15,714	

(1) Annualized for the six month period.
(2) The tax-equivalent adjustment to net interest income adjusts the yield for assets earning tax-exempt income to a comparable yield on a taxable basis.
(3) Includes loans held for sale.

Our net interest margin, on a tax-equivalent basis, was 3.73% for the six months ended June 30, 2015 compared to 3.67% for the six months ended June 30, 2014. The six basis point increase in net interest margin during the six months ended June 30, 2015 was driven primarily by a seven basis point reduction in the cost of our interest bearing liabilities, partially offset by a three basis point reduction in the yield on our interest-earning assets compared to the same period in 2014.

During the first six months of 2015, our average interest-earning assets increased by $138.1 million as compared to the same period in 2014; however, the yield on our interest-earning assets declined by three basis points during 2015. The increase in interest-earning assets was driven by a $148.7 million increase in average loans, partially offset by a $15.8 million decrease in average investment securities, while the decline in yield on interest earning assets was driven primarily by a six basis point reduction in yield on our loan portfolio.

In addition, our average interest-bearing liabilities increased by $89.8 million during the six month period ended June 30, 2015 as compared to the same period in 2014, while the cost of our interest-bearing liabilities declined by seven basis points. The reduction in cost of our interest-bearing liabilities is a result of the $94.6 million increase in interest-bearing deposits which are at lower rates than our other interest-bearing liabilities.

Our net interest spread was 3.56% for the six months ended June 30, 2015 compared to 3.52% for the same period in 2014. The seven basis point reduction in cost on our interest-bearing liabilities, partially offset by a three basis point decline in yield on our earning assets, resulted in the four basis point increase in our net interest spread for the 2015 period.

Rate/Volume Analysis

Net interest income can be analyzed in terms of the impact of changing interest rates and changing volume. The following table sets forth the effect which the varying levels of interest-earning assets and interest-bearing liabilities and the applicable rates have had on changes in net interest income for the periods presented.

								Three Months Ended
	June 30, 2015 vs. 2014 Increase (Decrease) Due to				June 30, 2014 vs. 2013 Increase (Decrease) Due to			
(dollars in thousands)	Volume	Rate	Rate/ Volume	Total	Volume	Rate	Rate/ Volume	Total
Interest income								
Loans	$1,729	(82)	(15)	1,632	1,553	(601)	(111)	841
Investment securities	(99)	(13)	3	(109)	(45)	94	(10)	39
Federal funds sold	1	2	-	3	(3)	1	-	(2)
Total interest income	1,631	(93)	(12)	1,526	1,505	(506)	(121)	878
Interest expense								
Deposits	126	27	5	158	243	(230)	(41)	(28)
FHLB advances and other borrowings	(77)	25	(2)	(54)	(38)	11	-	(27)
Junior subordinated debt	-	1	-	1	-	(7)	-	(7)
Total interest expense	49	53	3	105	205	(226)	(41)	(62)
Net interest income	$1,582	(146)	(15)	1,421	1,300	(280)	(80)	940

Net interest income, the largest component of our income, was $9.5 million for the three month period ended June 30, 2015 and $8.1 million for the three months ended June 30, 2014, a $1.4 million, or 17.6% increase during the second quarter of 2015. The increase in net interest income is due to a $1.5 million increase in interest income, partially offset by a $105,000 increase in interest expense. During the second quarter of 2015, the primary driver of the increase in net interest income was the $134.2 million increase in our average interest-earning assets as compared to the second quarter of 2014.

								Six Months Ended
	June 30, 2015 vs. 2014 Increase (Decrease) Due to				June 30, 2014 vs. 2013 Increase (Decrease) Due to			
(dollars in thousands)	Volume	Rate	Rate/ Volume	Total	Volume	Rate	Rate/ Volume	Total
Interest income								
Loans	$ 3,473	(217)	(42)	3,214	2,773	(1,182)	(197)	1,394
Investment securities	(211)	(45)	10	(246)	(112)	226	(27)	87
Federal funds sold	6	7	2	15	(2)	-	-	(2)
Total interest income	3,268	(255)	(30)	2,983	2,659	(956)	(224)	1,479
Interest expense								
Deposits	254	(8)	(1)	245	274	(364)	(64)	(154)
Note payable and other	(72)	(39)	1	(110)	(128)	74	(6)	(60)
Junior subordinated debt	-	1	-	1	-	(13)	-	(13)
Total interest expense	182	(46)	-	136	146	(303)	(70)	(227)
Net interest income	$ 3,086	(209)	(30)	2,847	2,513	(653)	(154)	1,706

Net interest income for the six months ended June 30, 2015 was $18.6 million compared to $15.7 million for the first six months ended June 30, 2014, a $2.8 million, or 18.1% increase during the first six months of 2015 compared to the same period in 2014. The increase in net interest income is due to a $3.0 million increase in interest income, offset in part by a $136,000 increase in interest expense. The $138.1 million increase in average earning assets during the six months ended June 30, 2015 as compared to six months ended June 30, 2014 was the primary driver of the increase in net interest income during the 2015 period.

Provision for Loan Losses

We have established an allowance for loan losses through a provision for loan losses charged as an expense on our consolidated statements of income. We review our loan portfolio periodically to evaluate our outstanding loans and to measure both the performance of the portfolio and the adequacy of the allowance for loan losses. Please see the discussion below under Balance Sheet Review Allowance for Loan Losses for a description of the factors we consider in determining the amount of the provision we expense each period to maintain this allowance.

For the three months ended June 30, 2015 and 2014, we incurred a noncash expense related to the provision for loan losses of $1.0 million and $950,000, respectively, resulting in an allowance for loan losses of $12.9 million and $11.1 million for the 2015 and 2014 periods, respectively. For the six months ended June 30, 2015 and 2014 our provision for loan losses was $1.6 million and $2.0 million, respectively. The $12.9 million allowance represented 1.34% of gross loans at June 30, 2015 while the $11.1 million allowance was 1.37% of gross loans at June 30, 2014. During the past 12 months, our loan balances increased by $150.7 million, while the amount of our nonperforming loans and classified loans declined. Factors such as these are also considered in determining the amount of loan loss provision necessary to maintain our allowance for loan losses at an adequate level.

Noninterest Income

The following table sets forth information related to our noninterest income.

	Three months ended June 30,		**Six months ended June 30,**	
(dollars in thousands)	**2015**	**2014**	**2015**	**2014**
Loan and mortgage fee income	$ 1,409	613	2,605	955
Service fees on deposit accounts	219	231	445	445
Income from bank owned life insurance	165	167	331	329
Gain on sale of investment securities	36	230	295	230
Other income	286	277	580	529
Total noninterest income	$ 2,115	1,518	4,256	2,488

Noninterest income increased $597,000, or 39.3%, for the second quarter of 2015 as compared to the same period in 2014. Excluding the gain on sale of investment securities in both the 2015 and 2014 periods, noninterest income increased $791,000, or 61.4%, during the 2015 period. The increase in total noninterest income during this 2015 period resulted primarily from the following:

Loan and mortgage fee income increased $796,000, or 129.9%, resulting primarily from an increase in mortgage fee income which was driven by an expansion of our mortgage operations. Mortgage origination fee income increased from $576,000 for the three months ended June 30, 2014 to $1.3 million for the three months ended June 30, 2015.

Partially offsetting the increase was a $12,000, or 5.2%, decrease in service fees on deposit accounts which was primarily related to an $11,000 decrease in non-sufficient funds (NSF) fee income.

Noninterest income increased $1.8 million, or 71.1%, during the six months ended June 30, 2015 as compared to the same period in 2014. Excluding the gain on sale of investment securities, noninterest income increased $1.7 million, or 75.4%, from the 2014 period. The increase in total noninterest income during the six months ended June 30, 2015 resulted primarily from a $1.7 million increase in loan fee income, a $65,000 increase in gain on sale of investment securities, and a $51,000 increase in other income which consists primarily of income from ATM and debit card transactions, wire transfer fees and rent income from tenants at our Columbia, South Carolina office.

In accordance with the requirement set forth under the Dodd-Frank Act, in June 2011, the Federal Reserve approved a final rule which caps an issuer's base interchange fee at 21 cents per transaction and allows an additional 5 basis point charge per transaction to help cover fraud losses. Although the rule does not apply to institutions with less than $10 billion in assets, such as our Bank, there is concern that the price controls may harm community banks, which could be pressured by the marketplace to lower their own interchange rates. Our ATM/Debit card fee income is included in other noninterest income and was $196,000 and $169,000 for the three months ended June 30, 2015 and 2014, respectively, and $372,000 and $311,000 for the six months ended June 30, 2015 and 2014, respectively, the majority of which related to interchange fee income.

Noninterest expenses

The following table sets forth information related to our noninterest expenses.

	Three months ended June 30,		Six months ended June 30,	
(dollars in thousands)	**2015**	**2014**	**2015**	**2014**
Compensation and benefits	$ 4,106	3,514	8,382	6,925
Occupancy	842	730	1,579	1,457
Real estate owned expenses	93	12	855	25
Data processing and related costs	573	622	1,158	1,216
Insurance	213	203	415	395
Professional fees	233	294	466	517
Marketing	222	197	460	398
Other	364	743	791	1,152
Total noninterest expense	$ 6,646	6,315	14,106	12,085

Noninterest expense was $6.7 million for the three months ended June 30, 2015, a $331,000, or 5.2%, increase from noninterest expense of $6.3 million for the three months ended June 30, 2014. The increase in total noninterest expenses resulted primarily from the following:

- Compensation and benefits expense increased $592,000, or 16.8%, relating primarily to increases in base compensation and benefits expenses. Base compensation increased by $587,000 driven by the cost of 18 additional employees, five of which were hired to support our Mount Pleasant, South Carolina office, two of which were hired in relation to the expansion of our mortgage operations, and the remainder of which were hired to support our loan and deposit growth, combined with annual company-wide salary increases.
- Occupancy expenses increased by $112,000, or 15.3%, driven by increased depreciation and maintenance costs on the properties we own.
- Real estate owned expenses increased $81,000, due primarily to expenses associated with one commercial property.

Partially offsetting these increases in noninterest expenses were decreases in data processing and related costs, professional fees, and other noninterest expense. The $61,000 decrease in professional fees and the $379,000 decrease in other noninterest expense related primarily to costs associated with a specific litigation issue during the second quarter of 2014. In addition, our collection costs, which are included in other noninterest expense, decreased by $106,000 during the three months ended June 30, 2015.

Our efficiency ratio was 57.3% for the second quarter of 2015 compared to 65.9% for the same period in 2014. The efficiency ratio represents the percentage of one dollar of expense required to be incurred to earn a full dollar of revenue and is computed by dividing noninterest expense by the sum of net interest income and noninterest income. The improved efficiency ratio for 2015 was driven primarily by an increase in net interest income and noninterest income during the three months ended June 30, 2015, as compared to the same period in 2014.

Noninterest expense for the six months ended June 30, 2015 increased 16.7%, or $2.0 million, as compared to the six months ended June 30, 2014. The increase relates primarily to the $1.5 million increase in compensation and benefits expense, $122,000 in occupancy expense, $830,000 in real estate owned expenses and $62,000 in marketing expenses. Partially offsetting the increases in noninterest expense was a decrease of $58,000 in data processing and related costs, $51,000 in professional fees, and $361,000 in other noninterest expenses.

We incurred income tax expense of $1.4 million for the three months ended June 30, 2015 as compared to $757,000 during the same period in 2014. Income tax expense for the six months ended June 30, 2015 was $2.5 million as compared to $1.4 million for the same period of 2014. Our effective tax rate was 35.3% and 32.4% for the six months ended June 30, 2015 and 2014, respectively. The increase in the effective tax rate during the 2015 period is primarily a result of the lesser impact of tax-exempt income.

BALANCE SHEET REVIEW

Investment Securities

At June 30, 2015, the $57.0 million in our investment securities portfolio represented approximately 5.1% of our total assets. Our available for sale investment portfolio included US government agency securities, SBA securities, state and political subdivisions, and mortgage-backed securities with a fair value of $51.5 million and an amortized cost of $51.6 million resulting in an unrealized loss of $169,000. At December 31, 2014, the $61.5 million in our investment securities portfolio represented approximately 6.0% of our total assets. At December 31, 2014, we held investment securities available for sale with a fair value of $55.0 million and an amortized cost of $54.6 million for an unrealized gain of $458,000.

Loans

Since loans typically provide higher interest yields than other types of interest earning assets, a substantial percentage of our earning assets are invested in our loan portfolio. Average loans, excluding loans held for sale, for the six months ended June 30, 2015 and 2014 were $912.8 million and $773.1 million, respectively. Before the allowance for loan losses, total loans outstanding at June 30, 2015 and December 31, 2014 were $963.5 million and $871.4 million, respectively.

The principal component of our loan portfolio is loans secured by real estate mortgages. As of June 30, 2015, our loan portfolio included $786.8 million, or 81.7%, of real estate loans. As of December 31, 2014, real estate loans made up 81.2% of our loan portfolio and totaled $707.2 million. Most of our real estate loans are secured by residential or commercial property. We obtain a security interest in real estate, in addition to any other available collateral. This collateral is taken to increase the likelihood of the ultimate repayment of the loan. Generally, we limit the loan-to-value ratio on loans to coincide with the appropriate regulatory guidelines. We attempt to maintain a relatively diversified loan portfolio to help reduce the risk inherent in concentration in certain types of collateral and business types. We do not generally originate traditional long term residential mortgages to hold in our loan portfolio, but we do issue traditional second mortgage residential real estate loans and home equity lines of credit. Home equity lines of credit totaled $105.2 million as of June 30, 2015, of which approximately 32% were in a first lien position, while the remaining balance was second liens, compared to $95.6 million as of December 31, 2014, with approximately 35% in first lien positions and the remaining balance was in second liens. The average loan had a balance of approximately $88,000 and a loan to value of 72% as of June 30, 2015, compared to an average loan balance of $87,000 and a loan to value of approximately 72% as of December 31, 2014. Further, 0.4% and 0.3% of our total home equity lines of credit were over 30 days past due as of June 30, 2015 and December 31, 2014, respectively.

Following is a summary of our loan composition at June 30, 2015 and December 31, 2014. Of the $92.1 million in loan growth during the first half of 2015, $31.4 million was originated in the Greenville market, $24.8 million was originated in the Columbia market, and $35.9 million was originated in the Charleston market. In addition, $79.6 million of the increase was in loans secured by real estate, and $12.0 million in commercial business loans. The $19.5 million increase in consumer real estate loans is related to our focus to continue to originate high quality 1-4 family consumer real estate loans. Our average consumer real estate loan currently has a principal balance of $299,000, a term of eight years, and an average rate of 4.46%.

	June 30, 2015		December 31, 2014	
(dollars in thousands)	Amount	% of Total	Amount	% of Total
Commercial				
Owner occupied RE	$ 232,997	24.2%	$ 191,061	21.9%
Non-owner occupied RE	207,623	21.6%	183,440	21.1%
Construction	33,570	3.5%	50,995	5.8%
Business	162,017	16.8%	149,986	17.2%
Total commercial loans	636,207	66.1%	575,482	66.0%
Consumer				
Real estate	166,404	17.3%	146,859	16.9%
Home equity	105,241	10.9%	95,629	11.0%
Construction	40,957	4.2%	39,226	4.5%
Other	14,687	1.5%	14,250	1.6%
Total consumer loans	327,289	33.9%	295,964	34.0%
Total gross loans, net of deferred fees	963,496	100.0%	871,446	100.0%
Less allowance for loan losses	(12,927)		(11,752)	
Total loans, net	$ 950,569		$ 859,694	

Nonperforming assets

Nonperforming assets include real estate acquired through foreclosure or deed taken in lieu of foreclosure and loans on nonaccrual status. Generally, a loan is placed on nonaccrual status when it becomes 90 days past due as to principal or interest, or when we believe, after considering economic and business conditions and collection efforts, that the borrower s financial condition is such that collection of the contractual principal or interest on the loan is doubtful. A payment of interest on a loan that is classified as nonaccrual is recognized as a reduction in principal when received. Our policy with respect to nonperforming loans requires the borrower to make a minimum of six consecutive payments in accordance with the loan terms and to show capacity to continue performing into the future before that loan can be placed back on accrual status. As of June 30, 2015 and December 31, 2014, we had no loans 90 days past due and still accruing.

Following is a summary of our nonperforming assets, including nonaccruing TDRs.

(dollars in thousands)	June 30, 2015	December 31, 2014
Commercial	$ 4,916	4,857
Consumer	670	646
Nonaccruing troubled debt restructurings	1,087	1,147
Total nonaccrual loans	6,673	6,650