

Edgar Filing: First Internet Bancorp - Form 10-Q

First Internet Bancorp  
Form 10-Q  
May 04, 2016

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

FORM 10-Q

(Mark One)

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

For the Quarterly Period ended March 31, 2016

OR

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

For the Transition Period From \_\_\_\_\_ to \_\_\_\_\_.

Commission File Number 001-35750

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

Indiana 20-3489991  
(State or Other Jurisdiction of (I.R.S. Employer  
Incorporation or Organization) Identification No.)

11201 USA Parkway 46037  
Fishers, IN  
(Address of Principal Executive Offices) (Zip Code)  
(317) 532-7900  
(Registrant's Telephone Number, Including Area Code)

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

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

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

Yes  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 (as defined in Rule 12b-2 of the Exchange Act).

Large Accelerated Filer

Accelerated Filer

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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

As of May 2, 2016, the registrant had 4,497,284 shares of common stock issued and outstanding.

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Cautionary Note Regarding Forward-Looking Statements

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

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

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## PART I

## ITEM 1. FINANCIAL STATEMENTS

## First Internet Bancorp

## Condensed Consolidated Balance Sheets

(Amounts in thousands except share data)

|   | March 31,<br>2016<br>(Unaudited) | December 31,<br>2015 |
|---|----------------------------------|----------------------|
| Assets  |                                  |                      |
| Cash and due from banks   | \$2,411                          | \$ 1,063             |
| Interest-bearing demand deposits  | 98,533                           | 24,089               |
| Total cash and cash equivalents   | 100,944                          | 25,152               |
| Interest-bearing time deposits  | 1,000                            | 1,000                |
| Securities available-for-sale, at fair value (amortized cost of \$315,315 and \$215,576 in 2016 and 2015, respectively)                               | 315,311                          | 213,698              |
| Loans held-for-sale (includes \$26,688 and \$24,065 at fair value in 2016 and 2015, respectively)   | 29,491                           | 36,518               |
| Loans receivable  | 1,040,683                        | 953,859              |
| Allowance for loan losses   | (9,220 )                         | (8,351 )             |
| Net loans receivable  | 1,031,463                        | 945,508              |
| Accrued interest receivable   | 4,528                            | 4,105                |
| Federal Home Loan Bank of Indianapolis stock  | 8,595                            | 8,595                |
| Cash surrender value of bank-owned life insurance   | 12,826                           | 12,727               |
| Premises and equipment, net   | 8,485                            | 8,521                |
| Goodwill  | 4,687                            | 4,687                |
| Other real estate owned   | 4,488                            | 4,488                |
| Accrued income and other assets   | 5,901                            | 4,871                |
| Total assets  | \$1,527,719                      | \$ 1,269,870         |
| Liabilities and Shareholders' Equity  |                                  |                      |
| Liabilities   |                                  |                      |
| Noninterest-bearing deposits  | \$28,945                         | \$ 23,700            |
| Interest-bearing deposits   | 1,214,233                        | 932,354              |
| Total deposits  | 1,243,178                        | 956,054              |
| Advances from Federal Home Loan Bank  | 150,969                          | 190,957              |
| Subordinated debt, net of unamortized discounts and debt issuance costs of \$249 and \$276 in 2016 and 2015, respectively                             | 12,751                           | 12,724               |
| Accrued interest payable  | 108                              | 117                  |
| Accrued expenses and other liabilities  | 12,883                           | 5,688                |
| Total liabilities   | 1,419,889                        | 1,165,540            |
| Commitments and Contingencies   |                                  |                      |
| Shareholders' Equity  |                                  |                      |
| Preferred stock, no par value; 4,913,779 shares authorized; issued and outstanding - none   | —                                | —                    |
| Voting common stock, no par value; 45,000,000 shares authorized; 4,497,284 and 4,481,347 shares issued and outstanding in 2016 and 2015, respectively | 72,697                           | 72,559               |
| Nonvoting common stock, no par value; 86,221 shares authorized; issued and outstanding - none   | —                                | —                    |
| Retained earnings   | 35,135                           | 32,980               |

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|  |             |              |   |
|--|-------------|--------------|---|
| Accumulated other comprehensive loss       | (2          | ) (1,209     | ) |
| Total shareholders' equity                 | 107,830     | 104,330      |   |
| Total liabilities and shareholders' equity | \$1,527,719 | \$ 1,269,870 |   |

See Notes to Condensed Consolidated Financial Statements

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

|  | Three Months<br>Ended March 31, |           |
|--|---------------------------------|-----------|
|  | 2016                            | 2015      |
| Interest Income                                      |                                 |           |
| Loans  | \$11,189                        | \$ 8,390  |
| Securities – taxable                                 | 1,169                           | 722       |
| Securities – non-taxable                             | 165                             | —         |
| Other earning assets                                 | 170                             | 75        |
| Total interest income                                | 12,693                          | 9,187     |
| Interest Expense                                     |                                 |           |
| Deposits   | 2,888                           | 1,953     |
| Other borrowed funds                                 | 664                             | 460       |
| Total interest expense                               | 3,552                           | 2,413     |
| Net Interest Income                                  | 9,141                           | 6,774     |
| Provision for Loan Losses                            | 946                             | 442       |
| Net Interest Income After Provision for Loan Losses  | 8,195                           | 6,332     |
| Noninterest Income                                   |                                 |           |
| Service charges and fees                             | 200                             | 176       |
| Mortgage banking activities                          | 2,254                           | 2,886     |
| Loss on asset disposals                              | (16                             | ) (14     |
| Other  | 102                             | 100       |
| Total noninterest income                             | 2,540                           | 3,148     |
| Noninterest Expense                                  |                                 |           |
| Salaries and employee benefits                       | 3,898                           | 3,578     |
| Marketing, advertising, and promotion                | 464                             | 452       |
| Consulting and professional services                 | 638                             | 592       |
| Data processing                                      | 274                             | 248       |
| Loan expenses  | 184                             | 181       |
| Premises and equipment                               | 798                             | 642       |
| Deposit insurance premium                            | 180                             | 150       |
| Other  | 569                             | 414       |
| Total noninterest expense                            | 7,005                           | 6,257     |
| Income Before Income Taxes                           | 3,730                           | 3,223     |
| Income Tax Provision                                 | 1,298                           | 1,160     |
| Net Income   | \$2,432                         | \$ 2,063  |
| Income Per Share of Common Stock                     |                                 |           |
| Basic  | \$0.54                          | \$ 0.46   |
| Diluted  | \$0.53                          | \$ 0.46   |
| Weighted-Average Number of Common Shares Outstanding |                                 |           |
| Basic  | 4,541,728                       | 4,516,776 |
| Diluted  | 4,575,555                       | 4,523,246 |
| Dividends Declared Per Share                         | \$0.06                          | \$ 0.06   |

See Notes to Condensed Consolidated Financial Statements



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

|  | Three Months<br>Ended March<br>31, |         |
|--|------------------------------------|---------|
|  | 2016                               | 2015    |
| Net income   | \$2,432                            | \$2,063 |
| Net unrealized holding gains on securities available-for-sale recorded within other comprehensive income before income tax | 1,874                              | 818     |
| Income tax provision   | 667                                | 291     |
| Other comprehensive income   | 1,207                              | 527     |
| Comprehensive income   | \$3,639                            | \$2,590 |

See Notes to Condensed Consolidated Financial Statements



## First Internet Bancorp

## Condensed Consolidated Statement of Shareholders' Equity - Unaudited

Three Months Ended March 31, 2016

(Amounts in thousands except per share data)

|   | Voting and<br>Nonvoting<br>Common<br>Stock | Accumulated<br>Other<br>Comprehensive<br>Loss | Retained<br>Earnings | Total<br>Shareholders'<br>Equity |
|---|--|---|----------------------|----------------------------------|
| Balance, January 1, 2016  | \$ 72,559                                  | \$ (1,209 )                                   | \$ 32,980            | \$ 104,330                       |
| Net income  | —  | —   | 2,432                | 2,432                            |
| Other comprehensive income  | —  | 1,207   | —                    | 1,207                            |
| Dividends declared (\$0.06 per share)   | —  | —   | (277 )               | (277 )                           |
| Recognition of the fair value of share-based compensation   | 173  | —   | —                    | 173                              |
| Deferred stock rights and restricted stock units issued in lieu of cash dividends payable on outstanding deferred stock rights and restricted stock units | 7  | —   | —                    | 7                                |
| Excess tax benefit on share-based compensation  | 49   | —   | —                    | 49                               |
| Common stock redeemed for the net settlement of share-based awards  | (91 )                                      | —   | —                    | (91 )                            |
| Balance, March 31, 2016   | \$ 72,697                                  | \$ (2 )                                       | \$ 35,135            | \$ 107,830                       |

See Notes to Condensed Consolidated Financial Statements

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

|   | Three Months Ended<br>March 31, |            |
|---|---------------------------------|------------|
|   | 2016                            | 2015       |
| <b>Operating Activities</b>   |                                 |            |
| Net income  | \$2,432                         | \$2,063    |
| Adjustments to reconcile net income to net cash provided by operating activities: |                                 |            |
| Depreciation and amortization   | 575                             | 456        |
| Increase in cash surrender value of bank-owned life insurance                     | (99 )                           | (98 )      |
| Provision for loan losses   | 946                             | 442        |
| Share-based compensation expense  | 173                             | 282        |
| Loans originated for sale   | (107,984 )                      | (134,159 ) |
| Proceeds from sale of loans   | 116,965                         | 143,737    |
| Gain on loans sold  | (1,600 )                        | (2,314 )   |
| Increase in fair value of loans held-for-sale                                     | (354 )                          | (177 )     |
| Gain on derivatives   | (300 )                          | (395 )     |
| Net change in accrued income and other assets                                     | (1,449 )                        | 128        |
| Net change in accrued expenses and other liabilities                              | (1,319 )                        | (17 )      |
| Net cash provided by operating activities   | 7,986                           | 9,948      |
| <b>Investing Activities</b>   |                                 |            |
| Net loan activity, excluding sales and purchases                                  | (78,894 )                       | (35,120 )  |
| Maturities of securities available-for-sale                                       | 6,088                           | 5,092      |
| Purchase of securities available-for-sale   | (97,928 )                       | (30,598 )  |
| Purchase of premises and equipment  | (268 )                          | (316 )     |
| Loans purchased   | (8,007 )                        | —          |
| Net cash used in investing activities   | (179,009 )                      | (60,942 )  |
| <b>Financing Activities</b>   |                                 |            |
| Net increase in deposits  | 287,124                         | 62,571     |
| Cash dividends paid   | (267 )                          | (265 )     |
| Proceeds from advances from Federal Home Loan Bank                                | 40,000                          | 90,000     |
| Repayment of advances from Federal Home Loan Bank                                 | (80,000 )                       | (90,000 )  |
| Other, net  | (42 )                           | (29 )      |
| Net cash provided by financing activities   | 246,815                         | 62,277     |
| Net Increase in Cash and Cash Equivalents   | 75,792                          | 11,283     |
| Cash and Cash Equivalents, Beginning of Period                                    | 25,152                          | 28,289     |
| Cash and Cash Equivalents, End of Period  | \$100,944                       | \$39,572   |
| <b>Supplemental Disclosures of Cash Flows Information</b>                         |                                 |            |
| Cash paid during the period for interest  | \$3,561                         | \$2,406    |
| Cash paid during the period for taxes   | 1,521                           | —          |
| Cash dividends declared, not paid   | 269                             | 268        |
| See Notes to Condensed Consolidated Financial Statements                          |                                 |            |

First Internet Bancorp

Notes to Condensed Consolidated Financial Statements – Unaudited

(Table amounts in thousands except share and per share data)

Note 1: Basis of Presentation

The accompanying unaudited condensed consolidated financial statements have been prepared in conformity with U.S. generally accepted accounting principles (“GAAP”) for interim financial information and pursuant to the rules and regulations of the SEC. Accordingly, they do not include all of the information or footnotes necessary for a complete presentation of financial condition, results of operations, or cash flows in accordance with GAAP. In our opinion, all adjustments (consisting only of normal recurring adjustments) necessary for a fair presentation have been included. The results of operations for the three months ended March 31, 2016 are not necessarily indicative of the results expected for the year ending December 31, 2016 or any other period. The March 31, 2016 condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes included in the First Internet Bancorp Annual Report on Form 10-K for the year ended December 31, 2015.

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

The condensed consolidated financial statements include the accounts of First Internet Bancorp (the “Company”), its wholly-owned subsidiary, First Internet Bank of Indiana (the “Bank”), and the Bank’s wholly-owned subsidiary, JKH Realty Services, LLC. All significant intercompany accounts and transactions have been eliminated in consolidation.

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

Certain reclassifications have been made to the 2015 financial statements to conform to the presentation of the 2016 financial statements. These reclassifications had no effect on net income.

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Note 2: Earnings Per Share

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

The following is a reconciliation of the weighted-average common shares for the basic and diluted earnings per share computations for the three months ended March 31, 2016 and 2015.

|  | Three Months<br>Ended March 31, |           |
|--|---------------------------------|-----------|
|  | 2016                            | 2015      |
| Basic earnings per share   |                                 |           |
| Net income   | \$2,432                         | \$ 2,063  |
| Weighted-average common shares   | 4,541,728                       | 4,516,776 |
| Basic earnings per common share  | \$0.54                          | \$ 0.46   |
| Diluted earnings per share   |                                 |           |
| Net income   | \$2,432                         | \$ 2,063  |
| Weighted-average common shares   | 4,541,728                       | 4,516,776 |
| Dilutive effect of warrants  | 11,293                          | —         |
| Dilutive effect of equity compensation   | 22,534                          | 6,470     |
| Weighted-average common and incremental shares   | 4,575,555                       | 4,523,246 |
| Diluted earnings per common share  | \$0.53                          | \$ 0.46   |
| Number of warrants excluded from the calculation of diluted earnings per share as the exercise prices were greater than the average market price of the Company's common stock during the period | —                               | 48,750    |

Note 3: Securities

The following tables summarize securities available-for-sale as of March 31, 2016 and December 31, 2015.

|                                    | March 31, 2016    |                              |           |               |
|------------------------------------|-------------------|------------------------------|-----------|---------------|
|                                    | Amortized<br>Cost | Gross<br>Unrealized<br>Gains | Losses    | Fair<br>Value |
| Securities available-for-sale      |                   |                              |           |               |
| U.S. Government-sponsored agencies | \$60,511          | \$466                        | \$(185)   | \$60,792      |
| Municipal securities               | 35,016            | 626                          | (3)       | 35,639        |
| Mortgage-backed securities         | 177,337           | 771                          | (119)     | 177,989       |
| Asset-backed securities            | 19,451            | —                            | (559)     | 18,892        |
| Corporate securities               | 20,000            | —                            | (1,022)   | 18,978        |
| Other securities                   | 3,000             | 21                           | —         | 3,021         |
| Total available-for-sale           | \$315,315         | \$1,884                      | \$(1,888) | \$315,311     |

|                                    | December 31, 2015 |                              |         |               |
|------------------------------------|-------------------|------------------------------|---------|---------------|
|                                    | Amortized<br>Cost | Gross<br>Unrealized<br>Gains | Losses  | Fair<br>Value |
| Securities available-for-sale      |                   |                              |         |               |
| U.S. Government-sponsored agencies | \$38,093          | \$139                        | \$(482) | \$37,750      |
| Municipal securities               | 21,091            | 385                          | (7)     | 21,469        |
| Mortgage-backed securities         | 113,948           | 110                          | (1,006) | 113,052       |

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|                          |           |       |           |   |           |
|--------------------------|-----------|-------|-----------|---|-----------|
| Asset-backed securities  | 19,444    | —     | (83       | ) | 19,361    |
| Corporate securities     | 20,000    | —     | (913      | ) | 19,087    |
| Other securities         | 3,000     | —     | (21       | ) | 2,979     |
| Total available-for-sale | \$215,576 | \$634 | \$(2,512) |   | \$213,698 |

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The carrying value of securities at March 31, 2016 is shown below by their contractual maturity date. Actual maturities will differ because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

|                            | Available-for-Sale |            |
|----------------------------|--------------------|------------|
|                            | Amortized Cost     | Fair Value |
| Within one year            | \$—                | \$—        |
| One to five years          | 403                | 364        |
| Five to ten years          | 33,739             | 33,361     |
| After ten years            | 81,385             | 81,684     |
|                            | 115,527            | 115,409    |
| Mortgage-backed securities | 177,337            | 177,989    |
| Asset-backed securities    | 19,451             | 18,892     |
| Other securities           | 3,000              | 3,021      |
| Total                      | \$315,315          | \$315,311  |

The Company did not sell any available-for-sale securities during the three months ended March 31, 2016 and 2015, and therefore, did not recognize any gross realized gains or losses.

Certain investments in debt securities are reported in the condensed consolidated financial statements at an amount less than their historical cost. The total fair value of these investments at March 31, 2016 and December 31, 2015 was \$91.9 million and \$166.1 million, which was approximately 29% and 78%, respectively, of the Company's available-for-sale securities portfolio. These declines resulted primarily from fluctuations in market interest rates after purchase.

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

The following tables show the available-for-sale securities portfolio's gross unrealized losses and fair value, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position at March 31, 2016 and December 31, 2015.

|                                    | March 31, 2016      |                   |                     |                   |            |                   |
|------------------------------------|---------------------|-------------------|---------------------|-------------------|------------|-------------------|
|                                    | Less Than 12 Months |                   | 12 Months or Longer |                   | Total      |                   |
|                                    | Fair Value          | Unrealized Losses | Fair Value          | Unrealized Losses | Fair Value | Unrealized Losses |
| Securities available-for-sale      |                     |                   |                     |                   |            |                   |
| U.S. Government-sponsored agencies | \$12,548            | \$(116)           | \$8,307             | \$(69)            | \$20,855   | \$(185)           |
| Municipal securities               | 1,299               | (3)               | —                   | —                 | 1,299      | (3)               |
| Mortgage-backed securities         | 27,993              | (93)              | 3,906               | (26)              | 31,899     | (119)             |
| Asset-backed securities            | 14,003              | (365)             | 4,889               | (194)             | 18,892     | (559)             |
| Corporate securities               | 18,978              | (1,022)           | —                   | —                 | 18,978     | (1,022)           |
| Total                              | \$74,821            | \$(1,599)         | \$17,102            | \$(289)           | \$91,923   | \$(1,888)         |

|                                    | December 31, 2015   |                   |                     |                   |            |                   |
|------------------------------------|---------------------|-------------------|---------------------|-------------------|------------|-------------------|
|                                    | Less Than 12 Months |                   | 12 Months or Longer |                   | Total      |                   |
|                                    | Fair Value          | Unrealized Losses | Fair Value          | Unrealized Losses | Fair Value | Unrealized Losses |
| Securities available-for-sale      |                     |                   |                     |                   |            |                   |
| U.S. Government-sponsored agencies | \$18,289            | \$ (237 )         | \$8,537             | \$ (245 )         | \$26,826   | \$ (482 )         |
| Municipal securities               | 1,026               | (7 )              | —                   | —                 | 1,026      | (7 )              |
| Mortgage-backed securities         | 74,198              | (562 )            | 22,655              | (444 )            | 96,853     | (1,006 )          |
| Asset-backed securities            | 19,361              | (83 )             | —                   | —                 | 19,361     | (83 )             |
| Corporate securities               | 19,087              | (913 )            | —                   | —                 | 19,087     | (913 )            |
| Other securities                   | 2,979               | (21 )             | —                   | —                 | 2,979      | (21 )             |
| Total                              | \$134,940           | \$ (1,823 )       | \$31,192            | \$ (689 )         | \$166,132  | \$ (2,512 )       |

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

The unrealized losses on the Company's investments in securities issued by U.S. Government-sponsored agencies, municipal organizations and corporate entities were caused by interest rate changes. The contractual terms of those investments do not permit the issuer to settle the securities at a price less than the amortized cost bases of the investments. Because the Company does not intend to sell the investments and it is not likely that the Company will be required to sell the investments before recovery of their amortized cost bases, which may be maturity, the Company does not consider those investments to be other-than-temporarily impaired at March 31, 2016.

#### Mortgage-Backed and Asset-Backed Securities

The unrealized losses on the Company's investments in mortgage-backed and asset-backed securities were caused by interest rate changes. The Company expects to recover the amortized cost bases over the term of the securities. Because the Company does not intend to sell the investments and it is not likely that the Company will be required to sell the investments before recovery of their amortized cost bases, which may be maturity, the Company does not consider those investments to be other-than-temporarily impaired at March 31, 2016.

## Note 4: Loans Receivable

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

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

Categories of loans include:

|   | March 31,<br>2016 | December 31,<br>2015 |
|---|-------------------|----------------------|
| Commercial loans  |                   |                      |
| Commercial and industrial   | \$ 106,431        | \$ 102,000           |
| Owner-occupied commercial real estate   | 47,010            | 44,462               |
| Investor commercial real estate   | 14,756            | 16,184               |
| Construction  | 52,591            | 45,898               |
| Single tenant lease financing   | 445,534           | 374,344              |
| Total commercial loans  | 666,322           | 582,888              |
| Consumer loans  |                   |                      |
| Residential mortgage  | 208,636           | 214,559              |
| Home equity   | 40,000            | 43,279               |
| Other consumer  | 121,323           | 108,312              |
| Total consumer loans  | 369,959           | 366,150              |
| Total commercial and consumer loans   | 1,036,281         | 949,038              |
| Deferred loan origination costs and premiums and discounts on purchased loans | 4,402             | 4,821                |
| Total loans receivable  | 1,040,683         | 953,859              |
| Allowance for loan losses   | (9,220 )          | (8,351 )             |
| Net loans receivable  | \$ 1,031,463      | \$ 945,508           |

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

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

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

**Investor Commercial Real Estate:** These loans are underwritten primarily based on the cash flow expected to be generated from the property and are secondarily supported by the value of the real estate. These loans typically incorporate a personal guarantee. This portfolio segment typically involves higher loan principal amounts, and the repayment of these loans is generally dependent on the successful operation of the property securing the loan or the business conducted on the property securing the loan. Investor commercial real estate loans may be more adversely



affected by conditions in the real estate markets, changing industry dynamics, or the overall health of the general economy. The properties securing the Company's investor commercial real estate portfolio tend to be diverse in terms of property type and are typically located in the state of Indiana and markets adjacent to Indiana. Management monitors and evaluates commercial real estate loans based on property financial performance, collateral value, guarantor strength, and other risk grade criteria. As a general rule, the Company avoids financing special use projects or properties outside of its designated market areas unless other underwriting factors are present to help mitigate risk.

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

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

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

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

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

#### Allowance for Loan Losses Methodology

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

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

Provision for Loan Losses

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

Policy for Charging Off Loans

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

The following tables present changes in the balance of the ALLL during the three month periods ended March 31, 2016 and 2015.

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

|                                       | Three Months Ended March 31, 2015 |                              |                                 |              |                               |                      |             |                | Total   |
|---------------------------------------|-----------------------------------|------------------------------|---------------------------------|--------------|-------------------------------|----------------------|-------------|----------------|---------|
|                                       | Commercial and industrial         | Other-commercial real estate | Investor commercial real estate | Construction | Single tenant lease financing | Residential mortgage | Home equity | Other consumer |         |
| Allowance for loan losses:            |                                   |                              |                                 |              |                               |                      |             |                |         |
| Balance, beginning of period          | \$920                             | \$ 345                       | \$ 261                          | \$ 330       | \$ 2,061                      | \$ 985               | \$ 207      | \$ 691         | \$5,800 |
| Provision (credit) charged to expense | 90                                | 46                           | (43 )                           | 29           | 391                           | (194 )               | (4 )        | 127            | 442     |
| Losses charged off                    | —                                 | —                            | —                               | —            | —                             | (71 )                | —           | (157 )         | (228 )  |
| Recoveries                            | —                                 | —                            | —                               | —            | —                             | 268                  | —           | 96             | 364     |
| Balance, end of period                | \$1,010                           | \$ 391                       | \$ 218                          | \$ 359       | \$ 2,452                      | \$ 988               | \$ 203      | \$ 757         | \$6,378 |



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The following tables present the recorded investment in loans based on portfolio segment and impairment method as of March 31, 2016, and December 31, 2015.

March 31, 2016

|   | Commercial and industrial | Owner-occupied commercial real estate | Investor commercial real estate | Construction | Single tenant lease financing | Residential mortgage | Home equity | Other consumer | Total       |
|---|---------------------------|---------------------------------------|---------------------------------|--------------|-------------------------------|----------------------|-------------|----------------|-------------|
| Loans:  |                           |                                       |                                 |              |                               |                      |             |                |             |
| Ending balance: collectively evaluated for impairment | \$106,431                 | \$47,010                              | \$14,756                        | \$52,591     | \$445,534                     | \$207,515            | \$40,000    | \$121,171      | \$1,035,008 |
| Ending balance: individually evaluated for impairment | —                         | —                                     | —                               | —            | —                             | 1,121                | —           | 152            | 1,273       |
| Ending balance  | \$106,431                 | \$47,010                              | \$14,756                        | \$52,591     | \$445,534                     | \$208,636            | \$40,000    | \$121,323      | \$1,036,281 |
| Allowance for loan losses:                            |                           |                                       |                                 |              |                               |                      |             |                |             |
| Ending balance: collectively evaluated for impairment | \$1,383                   | \$475                                 | \$197                           | \$563        | \$4,678                       | \$871                | \$120       | \$933          | \$9,220     |
| Ending balance: individually evaluated for impairment | —                         | —                                     | —                               | —            | —                             | —                    | —           | —              | —           |
| Ending balance  | \$1,383                   | \$475                                 | \$197                           | \$563        | \$4,678                       | \$871                | \$120       | \$933          | \$9,220     |

December 31, 2015

|   | Commercial and industrial | Owner-occupied commercial real estate | Investor commercial real estate | Construction | Single tenant lease financing | Residential mortgage | Home equity | Other consumer | Total     |
|---|---------------------------|---------------------------------------|---------------------------------|--------------|-------------------------------|----------------------|-------------|----------------|-----------|
| Loans:  |                           |                                       |                                 |              |                               |                      |             |                |           |
| Ending balance: collectively evaluated for impairment | \$102,000                 | \$44,462                              | \$16,184                        | \$45,898     | \$374,344                     | \$213,426            | \$43,279    | \$108,163      | \$947,756 |
| Ending balance: individually evaluated for impairment | —                         | —                                     | —                               | —            | —                             | 1,133                | —           | 149            | 1,282     |
| Ending balance  | \$102,000                 | \$44,462                              | \$16,184                        | \$45,898     | \$374,344                     | \$214,559            | \$43,279    | \$108,312      | \$949,038 |
| Allowance for loan losses:                            |                           |                                       |                                 |              |                               |                      |             |                |           |
| Ending balance: collectively evaluated for            | \$1,367                   | \$476                                 | \$212                           | \$500        | \$3,931                       | \$896                | \$125       | \$844          | \$8,351   |

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|                 |          |        |        |        |          |        |        |        |          |
|-----------------|----------|--------|--------|--------|----------|--------|--------|--------|----------|
| impairment      |          |        |        |        |          |        |        |        |          |
| Ending balance: |          |        |        |        |          |        |        |        |          |
| individually    |          |        |        |        |          |        |        |        |          |
| evaluated for   | —        | —      | —      | —      | —        | —      | —      | —      | —        |
| impairment      |          |        |        |        |          |        |        |        |          |
| Ending balance  | \$ 1,367 | \$ 476 | \$ 212 | \$ 500 | \$ 3,931 | \$ 896 | \$ 125 | \$ 844 | \$ 8,351 |

The Company utilizes a risk grading matrix to assign a risk grade to each of its commercial loans. Loans are graded on a scale of 1 to 9. A description of the general characteristics of the nine risk grades is as follows:

•“Pass” (Grades 1-5) - Higher quality loans that do not fit any of the other categories described below.

•“Special Mention” (Grade 6) - Loans that possess some credit deficiency or potential weakness which deserve close attention.

“Substandard” (Grade 7) - Loans that possess a defined weakness or weaknesses that jeopardize the liquidation of the debt. Loans characterized by the distinct possibility that the institution will sustain some loss if the deficiencies are not corrected. Loans that are inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any.

“Doubtful” (Grade 8) - Such loans have been placed on nonaccrual status and may be heavily dependent upon collateral possessing a value that is difficult to determine or based upon some near-term event which lacks clear certainty. These loans have all of the weaknesses of those classified as Substandard; however, based on existing conditions, these weaknesses make full collection of the principal balance highly improbable.

“Loss” (Grade 9) - Loans that are considered uncollectible and of such little value that continuing to carry them as assets is not warranted.

#### Nonaccrual Loans

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

The following tables present the credit risk profile of the Company’s commercial loan portfolio based on rating category and payment activity as of March 31, 2016 and December 31, 2015.

#### March 31, 2016

|                   | Commercial and industrial | Owner-occupied commercial real estate | Investor commercial real estate | Construction | Single tenant lease financing | Total     |
|-------------------|---------------------------|---------------------------------------|---------------------------------|--------------|-------------------------------|-----------|
| Rating:           |                           |                                       |                                 |              |                               |           |
| 1-5 Pass          | \$96,712                  | \$ 46,469                             | \$ 14,756                       | \$ 52,294    | \$444,590                     | \$654,821 |
| 6 Special Mention | 4,766                     | 528                                   | —                               | 297          | 944                           | 6,535     |
| 7 Substandard     | 4,953                     | 13                                    | —                               | —            | —                             | 4,966     |
| 8 Doubtful        | —                         | —                                     | —                               | —            | —                             | —         |
| Total             | \$106,431                 | \$ 47,010                             | \$ 14,756                       | \$ 52,591    | \$445,534                     | \$666,322 |

#### March 31, 2016

|            | Residential mortgage | Home equity | Other consumer | Total     |
|------------|----------------------|-------------|----------------|-----------|
| Performing | \$208,533            | \$40,000    | \$121,254      | \$369,787 |
| Nonaccrual | 103                  | —           | 69             | 172       |
| Total      | \$208,636            | \$40,000    | \$121,323      | \$369,959 |

#### December 31, 2015

|                   | Commercial and industrial | Owner-occupied commercial real estate | Investor commercial real estate | Construction | Single tenant lease financing | Total     |
|-------------------|---------------------------|---------------------------------------|---------------------------------|--------------|-------------------------------|-----------|
| Rating:           |                           |                                       |                                 |              |                               |           |
| 1-5 Pass          | \$95,589                  | \$ 43,913                             | \$ 14,746                       | \$ 45,599    | \$374,344                     | \$574,191 |
| 6 Special Mention | 2,006                     | 535                                   | —                               | 299          | —                             | 2,840     |



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|               |            |           |           |           |            |            |
|---------------|------------|-----------|-----------|-----------|------------|------------|
| 7 Substandard | 4,405      | 14        | 1,438     | —         | —          | 5,857      |
| 8 Doubtful    | —          | —         | —         | —         | —          | —          |
| Total         | \$ 102,000 | \$ 44,462 | \$ 16,184 | \$ 45,898 | \$ 374,344 | \$ 582,888 |

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|            | December 31, 2015    |             |                | Total     |
|------------|----------------------|-------------|----------------|-----------|
|            | Residential mortgage | Home equity | Other consumer |           |
| Performing | \$214,456            | \$43,279    | \$108,248      | \$365,983 |
| Nonaccrual | 103                  | —           | 64             | 167       |
| Total      | \$214,559            | \$43,279    | \$108,312      | \$366,150 |

The following tables present the Company's loan portfolio delinquency analysis as of March 31, 2016 and December 31, 2015.

|                                       | March 31, 2016      |                     |                          |                |             | Total Commercial and Consumer Loans | Non-accrual Loans | Total Loans 90 Days or More Past Due and Accruing |
|---------------------------------------|---------------------|---------------------|--------------------------|----------------|-------------|-------------------------------------|-------------------|---|
|                                       | 30-59 Days Past Due | 60-89 Days Past Due | 90 Days or More Past Due | Total Past Due | Current     |                                     |                   |   |
| Commercial and industrial             | \$—                 | \$ —                | \$ —                     | \$ —           | \$106,431   | \$106,431                           | \$ —              | \$ —  |
| Owner-occupied commercial real estate | —                   | —                   | —                        | —              | 47,010      | 47,010                              | —                 | —   |
| Investor commercial real estate       | —                   | —                   | —                        | —              | 14,756      | 14,756                              | —                 | —   |
| Construction                          | —                   | —                   | —                        | —              | 52,591      | 52,591                              | —                 | —   |
| Single tenant lease financing         | —                   | —                   | —                        | —              | 445,534     | 445,534                             | —                 | —   |
| Residential mortgage                  | 871                 | —                   | 264                      | 1,135          | 207,501     | 208,636                             | 103               | 195   |
| Home equity                           | —                   | —                   | —                        | —              | 40,000      | 40,000                              | —                 | —   |
| Other consumer                        | 94                  | 29                  | 1                        | 124            | 121,199     | 121,323                             | 69                | —   |
| Total                                 | \$965               | \$ 29               | \$ 265                   | \$ 1,259       | \$1,035,022 | \$1,036,281                         | \$ 172            | \$ 195  |

|                                       | December 31, 2015   |                     |                          |                |           | Total Commercial and Consumer Loans | Non-accrual Loans | Total Loans 90 Days or More Past Due and Accruing |
|---------------------------------------|---------------------|---------------------|--------------------------|----------------|-----------|-------------------------------------|-------------------|---|
|                                       | 30-59 Days Past Due | 60-89 Days Past Due | 90 Days or More Past Due | Total Past Due | Current   |                                     |                   |   |
| Commercial and industrial             | \$29                | \$ —                | \$ —                     | \$ 29          | \$101,971 | \$102,000                           | \$ —              | \$ —  |
| Owner-occupied commercial real estate | —                   | —                   | —                        | —              | 44,462    | 44,462                              | —                 | —   |
| Investor commercial real estate       | —                   | —                   | —                        | —              | 16,184    | 16,184                              | —                 | —   |
| Construction                          | —                   | —                   | —                        | —              | 45,898    | 45,898                              | —                 | —   |
| Single tenant lease financing         | —                   | —                   | —                        | —              | 374,344   | 374,344                             | —                 | —   |
| Residential mortgage                  | 300                 | 23                  | 45                       | 368            | 214,191   | 214,559                             | 103               | —   |
| Home equity                           | 20                  | —                   | —                        | 20             | 43,259    | 43,279                              | —                 | —   |
| Other consumer                        | 116                 | 12                  | —                        | 128            | 108,184   | 108,312                             | 64                | —   |
| Total                                 | \$465               | \$ 35               | \$ 45                    | \$ 545         | \$948,493 | \$949,038                           | \$ 167            | \$ —  |

Impaired Loans

A loan is designated as impaired, in accordance with the impairment accounting guidance when, based on current information or events, it is probable that the Company will be unable to collect all amounts due (principal and interest) according to the contractual terms of the loan agreement. Payments with delays generally not exceeding 90 days outstanding are not considered impaired. Certain nonaccrual and substantially all delinquent loans more than 90 days

past due may be considered to be impaired. Generally, loans are placed on nonaccrual status at 90 days past due and accrued interest is reversed against earnings, unless the loan is well-secured and in the process of collection. The accrual of interest on impaired and nonaccrual loans is discontinued when, in management's opinion, the borrower may be unable to meet payments as they become due.

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

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

The following table presents the Company's impaired loans as of March 31, 2016 and December 31, 2015. The Company had no impaired loans with a specific valuation allowance as of March 31, 2016 or December 31, 2015.

|  | March 31, 2016      |                                |                       | December 31, 2015   |                                |                       |
|--|---------------------|--------------------------------|-----------------------|---------------------|--------------------------------|-----------------------|
|  | Recorded<br>Balance | Unpaid<br>Principal<br>Balance | Specific<br>Allowance | Recorded<br>Balance | Unpaid<br>Principal<br>Balance | Specific<br>Allowance |
| Loans without a specific valuation allowance |                     |                                |                       |                     |                                |                       |
| Residential mortgage                         | \$1,121             | \$ 1,121                       | \$ —                  | \$1,133             | \$ 1,154                       | \$ —                  |
| Other consumer                               | 152                 | 152                            | —                     | 149                 | 178                            | —                     |
| Total impaired loans                         | \$1,273             | \$ 1,273                       | \$ —                  | \$1,282             | \$ 1,332                       | \$ —                  |

The table below presents average balances and interest income recognized for impaired loans during the three month periods ended March 31, 2016 and March 31, 2015.

|  | Three Months Ended |                    |                    |                    |
|--|--------------------|--------------------|--------------------|--------------------|
|  | March 31, 2016     |                    | March 31, 2015     |                    |
|  | Average<br>Balance | Interest<br>Income | Average<br>Balance | Interest<br>Income |
| Loans without a specific valuation allowance |                    |                    |                    |                    |
| Investor commercial real estate              | \$—                | \$ —               | \$85               | \$ 2               |
| Residential mortgage                         | 1,068              | 3                  | 1,060              | 2                  |
| Other consumer                               | 155                | 2                  | 121                | 3                  |
| Total  | 1,223              | 5                  | 1,266              | 7                  |
| Loans with a specific valuation allowance    |                    |                    |                    |                    |
| Other consumer                               | —                  | —                  | 53                 | 1                  |
| Total  | —                  | —                  | 53                 | 1                  |
| Total impaired loans                         | \$1,223            | \$ 5               | \$1,319            | \$ 8               |

There were no residential mortgage loans in other real estate owned at March 31, 2016 or December 31, 2015 and there were less than \$0.1 million of loans at March 31, 2016 and December 31, 2015 in the process of foreclosure.

Note 5: Premises and Equipment

The following table summarizes premises and equipment at March 31, 2016 and December 31, 2015.

|                                | March 31, December 31, |          |
|--------------------------------|------------------------|----------|
|                                | 2016                   | 2015     |
| Land                           | \$ 2,500               | \$ 2,500 |
| Building and improvements      | 4,853                  | 4,636    |
| Furniture and equipment        | 6,215                  | 6,164    |
| Less: accumulated depreciation | (5,083 )               | (4,779 ) |
|                                | \$ 8,485               | \$ 8,521 |



## Note 6: Goodwill

The following table shows the changes in the carrying amount of goodwill for the three month period ended March 31, 2016 and the year ended December 31, 2015.

|                                       |         |
|---------------------------------------|---------|
| Balance as of January 1, 2015         | \$4,687 |
| Changes in goodwill during the year   | —       |
| Balance as of December 31, 2015       | 4,687   |
| Changes in goodwill during the period | —       |
| Balance as of March 31, 2016          | \$4,687 |

Goodwill is tested for impairment on an annual basis as of August 31, or whenever events or changes in circumstances indicate the carrying amount of goodwill exceeds its implied fair value. No events or changes in circumstances have occurred since the August 31, 2015 annual impairment test that would suggest it was more likely than not goodwill impairment existed.

## Note 7: Subordinated Debt

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

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

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

In October 2015, the Company issued subordinated notes (the “Notes”) in the principal amount of \$10.0 million. The Notes bear a fixed interest rate of 6.4375% per year, payable quarterly, and are scheduled to mature on October 1, 2025. The Notes may be repaid, without penalty, on any interest payment date on or after October 15, 2020. The Notes are intended to qualify as Tier 2 capital under regulatory guidelines.

The following table presents the principal balance and unamortized discount and debt issuance costs for the Debenture and the Notes as of March 31, 2016 and December 31, 2015.

|  | March 31, 2016                    |        | December 31, 2015                 |        |
|--|-----------------------------------|--------|-----------------------------------|--------|
|  | Unamortized Discount              |        | Unamortized Discount              |        |
|  | Principal and Debt Issuance Costs |        | Principal and Debt Issuance Costs |        |
| 8.00% subordinated debenture, due 2021 | \$3,000                           | (21 )  | 3,000                             | (42 )  |
| 6.4375% subordinated notes, due 2025   | 10,000                            | (228 ) | 10,000                            | (234 ) |

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Total \$13,000 (249 ) 13,000 (276 )

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Note 8: Benefit Plans

Employment Agreement

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

2013 Equity Incentive Plan

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

The Company recorded \$0.2 million and \$0.3 million of share-based compensation expense for the three month periods ended March 31, 2016 and 2015, respectively, related to awards made under the 2013 Plan.

The following table summarizes the status of the 2013 Plan awards as of March 31, 2016, and activity for the three months ended March 31, 2016.

|                                | Restricted Stock Units | Weighted-Average Grant Date Fair Value Per Share | Restricted Stock Awards | Weighted-Average Grant Date Fair Value Per Share | Deferred Stock Units | Weighted-Average Grant Date Fair Value Per Share |
|--------------------------------|------------------------|--|-------------------------|--|----------------------|--|
| Nonvested at December 31, 2015 | 28,302                 | \$ 18.90   | 27,529                  | \$ 18.17   | —                    | \$ —   |
| Granted                        | 30,583                 | 25.64  | 10,232                  | 24.44  | 3                    | 24.44  |
| Vested                         | (9,470 )               | 18.86  | (17,507 )               | 19.60  | (3 )                 | 24.44  |
| Nonvested at March 31, 2016    | 49,415                 | \$ 23.07   | 20,254                  | \$ 20.10   | —                    | \$ —   |

At March 31, 2016, the total unrecognized compensation cost related to nonvested awards was \$1.3 million with a weighted-average expense recognition period of 2.3 years.

Directors Deferred Stock Plan

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

The following table summarizes the status of deferred stock rights related to the Directors Deferred Stock Plan for the three months ended March 31, 2016.

Deferred  
Stock  
Rights



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|                                  |        |
|----------------------------------|--------|
| Outstanding, beginning of period | 81,693 |
| Granted                          | 171    |
| Exercised                        | —      |
| Outstanding, end of period       | 81,864 |

All deferred stock rights granted during the 2016 period were additional rights issued in lieu of cash dividends payable on outstanding deferred stock rights.

Note 9: Fair Value of Financial Instruments

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

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

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

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

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

Securities

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

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

In certain cases where Level 1 or Level 2 inputs are not available, securities are classified within Level 3 of the hierarchy. Fair values are calculated using discounted cash flows. Discounted cash flows are calculated based off of the anticipated future cash flows updated to incorporate loss severities. Rating agency and industry research reports as well as default and deferral activity are reviewed and incorporated into the calculation. The Company did not own any securities classified within Level 3 of the hierarchy as of March 31, 2016 or December 31, 2015.

Loans Held-for-Sale (mandatory pricing agreements)

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

Forward Contracts

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

Interest Rate Lock Commitments

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

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The following tables present the fair value measurements of assets and liabilities recognized in the accompanying condensed consolidated balance sheets measured at fair value on a recurring basis and the level within the fair value hierarchy in which the fair value measurements fall at March 31, 2016 and December 31, 2015.

|  | March 31, 2016 |  |   |   |
|--|----------------|--|---|---|
|  | Fair Value     | Fair Value Measurements Using                                  |   |   |
|  |                | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
| U.S. Government-sponsored agencies                 | \$60,792       | \$ —   | \$ 60,792                                     | \$ —                                      |
| Municipal securities                               | 35,639         | —  | 35,639  | —   |
| Mortgage-backed securities                         | 177,989        | —  | 177,989                                       | —   |
| Asset-backed securities                            | 18,892         | —  | 18,892  | —   |
| Corporate securities                               | 18,978         | —  | 18,978  | —   |
| Other securities                                   | 3,021          | 3,021  | —   | —   |
| Total available-for-sale securities                | 315,311        | 3,021  | 312,290                                       | —   |
| Loans held-for-sale (mandatory pricing agreements) | 26,688         | —  | 26,688  | —   |
| Forward contracts                                  | (371)          | (371)  | —   | —   |
| IRLCs  | 1,283          | —  | —   | 1,283                                     |

|  | December 31, 2015 |  |   |   |
|--|-------------------|--|---|---|
|  | Fair Value        | Fair Value Measurements Using                                  |   |   |
|  |                   | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
| U.S. Government-sponsored agencies                 | \$37,750          | \$ —   | \$ 37,750                                     | \$ —                                      |
| Municipal securities                               | 21,469            | —  | 21,469  | —   |
| Mortgage-backed securities                         | 113,052           | —  | 113,052                                       | —   |
| Asset-backed securities                            | 19,361            | —  | 19,361  | —   |
| Corporate securities                               | 19,087            | —  | 19,087  | —   |
| Other securities                                   | 2,979             | 2,979  | —   | —   |
| Total available-for-sale securities                | 213,698           | 2,979  | 210,719                                       | —   |
| Loans held-for-sale (mandatory pricing agreements) | 24,065            | —  | 24,065  | —   |
| Forward contracts                                  | 30                | 30   | —   | —   |
| IRLCs  | 582               | —  | —   | 582                                       |

The following tables reconcile the beginning and ending balances of recurring fair value measurements recognized in the accompanying condensed consolidated balance sheets using significant unobservable (Level 3) inputs for the three month periods ended March 31, 2016 and March 31, 2015.

|  | Three Months<br>Ended<br>Interest Rate<br>Lock<br>Commitments |
|--|---|
| Balance, January 1, 2016                       | \$ 582  |
| Total realized gains<br>Included in net income | 701   |
| Balance, March 31, 2016                        | \$ 1,283  |
| Balance as of January 1, 2015                  | \$ 521  |
| Total realized gains<br>Included in net income | 392   |
| Balance, March 31, 2015                        | \$ 913  |

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

#### Impaired Loans (Collateral Dependent)

Loans for which it is probable that the Company will not collect all principal and interest due according to contractual terms are measured for impairment. Allowable methods for determining the amount of impairment include estimating fair value using the fair value of the collateral, less costs to sell, for collateral dependent loans.

If the impaired loan is identified as collateral dependent, then the fair value method of measuring the amount of impairment is utilized. This method requires obtaining a current independent appraisal of the collateral and applying a discount factor to the value.

Impaired loans that are collateral dependent are classified within Level 3 of the fair value hierarchy when impairment is determined using the fair value method.

There were no impaired loans that were measured at fair value on a nonrecurring basis at March 31, 2016 or December 31, 2015.

#### Significant Unobservable (Level 3) Inputs

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

| Fair Value         | Valuation Technique | Significant Unobservable Inputs | Range |
|--------------------|---------------------|---------------------------------|-------|
| at<br>March<br>31, |                     |                                 |       |

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|       |               |                      |                          |            |
|-------|---------------|----------------------|--------------------------|------------|
|       | 2016          |                      |                          |            |
| IRLCs | 1,283         | Discounted cash flow | Loan closing rates       | 40% - 99%  |
|       | Fair Value at | Valuation            | Significant Unobservable |            |
|       | December 31,  | Technique            | Inputs                   | Range      |
|       | 2015          |                      |                          |            |
| IRLCs | \$ 582        | Discounted cash flow | Loan closing rates       | 43% - 100% |

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

Cash and Cash Equivalents

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

#### Interest-Bearing Time Deposits

The fair value of these financial instruments approximates carrying value.

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

The fair value of these loans approximates carrying value.

#### Loans Receivable

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

#### Accrued Interest Receivable

The fair value of these financial instruments approximates carrying value.

#### Federal Home Loan Bank of Indianapolis Stock

The fair value approximates carrying value.

#### Deposits

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

#### Advances from Federal Home Loan Bank

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

#### Subordinated Debt

The fair value of the Company's subordinated debt is estimated using discounted cash flow analysis, based on current borrowing rates for similar types of debt instruments.

#### Accrued Interest Payable

The fair value of these financial instruments approximates carrying value.

#### Commitments

The fair value of commitments to extend credit are based on fees currently charged to enter into similar agreements with similar maturities and interest rates. The Company determined that the fair value of commitments was zero based on the contractual value of outstanding commitments at each of March 31, 2016 and December 31, 2015.

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The following tables summarize the carrying value and estimated fair value of all financial assets and liabilities at March 31, 2016 and December 31, 2015.

|   | March 31, 2016    |   |   |   |
|---|-------------------|---|---|---|
|   | Carrying Amount   | Fair Value Measurements Using                                 |   |   |
|   |                   | Quoted Prices In Active Market for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
| Cash and cash equivalents                             | \$ 100,944        | \$ 100,944  | \$ —  | \$ —                                      |
| Interest-bearing time deposits                        | 1,000             | 1,000   | —   | —   |
| Loans held-for-sale (best efforts pricing agreements) | 2,803             | —   | 2,803   | —   |
| Loans receivable                                      | 1,040,683         | —   | —   | 1,061,086                                 |
| Accrued interest receivable                           | 4,528             | 4,528   | —   | —   |
| Federal Home Loan Bank of Indianapolis stock          | 8,595             | —   | 8,595   | —   |
| Deposits  | 1,243,178         | 511,599   | —   | 722,428                                   |
| Advances from Federal Home Loan Bank                  | 150,969           | —   | 148,568                                       | —   |
| Subordinated debt                                     | 12,751            | —   | 13,027  | —   |
| Accrued interest payable                              | 108               | 108   | —   | —   |
|   | December 31, 2015 |   |   |   |
|   | Carrying Amount   | Fair Value Measurements Using                                 |   |   |
|   |                   | Quoted Prices In Active Market for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
| Cash and cash equivalents                             | \$ 25,152         | \$ 25,152   | \$ —  | \$ —                                      |
| Interest-bearing time deposits                        | 1,000             | 1,000   | —   | —   |
| Loans held-for-sale (best efforts pricing agreements) | 12,453            | —   | 12,453  | —   |
| Loans receivable                                      | 953,859           | —   | —   | 967,303                                   |
| Accrued interest receivable                           | 4,105             | 4,105   | —   | —   |
| Federal Home Loan Bank of Indianapolis stock          | 8,595             | —   | 8,595   | —   |
| Deposits  | 956,054           | 472,481   | —   | 478,360                                   |
| Advances from Federal Home Loan Bank                  | 190,957           | —   | 188,126                                       | —   |
| Subordinated debt                                     | 12,724            | —   | 13,212  | —   |
| Accrued interest payable                              | 117               | 117   | —   | —   |

Note 10: Mortgage Banking Activities

The Company's residential real estate lending business originates mortgage loans for customers and sells a majority of the originated loans into the secondary market. The Company hedges its mortgage banking pipeline by entering into forward contracts for the future delivery of mortgage loans to third party investors and entering into interest rate lock commitments with potential borrowers to fund specific mortgage loans that will be sold into the secondary market. To facilitate the hedging of the loans, the Company has elected the fair value option for loans originated and intended for sale in the secondary market under mandatory pricing agreements. Changes in the fair value of loans held-for-sale,



interest rate lock commitments and forward contracts are recorded in the mortgage banking activities line item within noninterest income. Refer to Note 11 for further information on derivative financial instruments.

During the three months ended March 31, 2016 and 2015, the Company originated mortgage loans held-for-sale of \$108.0 million and \$134.2 million, respectively, and sold \$117.0 million and \$143.7 million of mortgage loans, respectively, into the secondary market.

The following table provides the components of income from mortgage banking activities for the three months ended March 31, 2016 and 2015.

|   | Three Months<br>Ended March<br>31, |         |
|---|------------------------------------|---------|
|   | 2016                               | 2015    |
| Gain on loans sold  | \$1,600                            | \$2,314 |
| Gain resulting from the change in fair value of loans held-for-sale | 354                                | 177     |
| Gain resulting from the change in fair value of derivatives         | 300                                | 395     |
| Net revenue from mortgage banking activities                        | \$2,254                            | \$2,886 |

Note 11: Derivative Financial Instruments

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

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

The following table presents the notional amount and fair value of IRLCs and forward contracts utilized by the Company at March 31, 2016 and December 31, 2015.

|   | March 31, 2016     |               | December 31,<br>2015 |               |
|---|--------------------|---------------|----------------------|---------------|
|   | Notional<br>Amount | Fair<br>Value | Notional<br>Amount   | Fair<br>Value |
| Asset Derivatives                                 |                    |               |                      |               |
| Derivatives not designated as hedging instruments |                    |               |                      |               |
| IRLCs   | \$55,004           | \$1,283       | \$28,444             | \$ 582        |
| Forward contracts                                 | —                  | —             | 42,743               | 30            |
| Liability Derivatives                             |                    |               |                      |               |
| Derivatives not designated as hedging instruments |                    |               |                      |               |
| Forward contracts                                 | 83,000             | (371 )        | —                    | —             |

Fair values of derivative financial instruments were estimated using changes in mortgage interest rates from the date the Company entered into the IRLC and the balance sheet date. The following table summarizes the periodic changes in the fair value of the derivative financial instruments on the condensed consolidated statements of income for the three month periods ended March 31, 2016 and 2015.

|   | Amount of gain<br>/ (loss)<br>recognized in<br>the three<br>months ended |                      |
|---|--|----------------------|
|   | March<br>31,<br>2016   | March<br>31,<br>2015 |
| <b>Asset Derivatives</b>                          |  |                      |
| Derivatives not designated as hedging instruments |  |                      |
| IRLCs   | \$ 701   | \$ 392               |
| <b>Liability Derivatives</b>                      |  |                      |
| Derivatives not designated as hedging instruments |  |                      |
| Forward contracts                                 | (401   | ) 3                  |

Note 12: Recent Accounting Pronouncements

Accounting Standards Update (“Update”) 2016-06, Derivatives and Hedging (Topic 815): Contingent Put and Call Options in Debt Instruments (March 2016)

The amendments in this Update clarify the requirements for assessing whether contingent call (put) options that can accelerate the payment of principal on debt instruments are clearly and closely related to their debt hosts. An entity performing the assessment under the amendments in this Update is required to assess the embedded call (put) options solely in accordance with the four-step decision sequence. The amendments in this Update clarify what steps are required when assessing whether the economic characteristics and risks of call (put) options are clearly and closely related to the economic characteristics and risks of their debt hosts, which is one of the criteria for bifurcating an embedded derivative. Consequently, when a call (put) option is contingently exercisable, an entity does not have to assess whether the event that triggers the ability to exercise a call (put) option is related to interest rates or credit risks. For public business entities, the amendments in this Update are effective for fiscal years beginning after December 15, 2016, including interim periods within those fiscal years, and should be implemented using a modified retrospective method. Adoption of this Update is not expected to have a significant effect on the Company’s consolidated financial statements.

Accounting Standards Update 2016-07, Investments - Equity Method and Joint Ventures (Topic 323): Simplifying the Transition to the Equity Method of Accounting (March 2016)

The amendments in this Update eliminate the requirement that when an investment qualifies for use of the equity method as a result of an increase in the level of ownership interest or degree of influence, an investor must adjust the investment, results of operations, and retained earnings retroactively on a step-by-step basis as if the equity method had been in effect during all previous periods that the investment had been held. The amendments require that the equity method investor add the cost of acquiring the additional interest in the investee to the current basis of the investor’s previously held interest and adopt the equity method of accounting as of the date the investment becomes qualified for equity method accounting. Therefore, upon qualifying for the equity method of accounting, no retroactive adjustment of the investment is required.

The amendments in this Update require that an entity that has an available-for-sale equity security that becomes qualified for the equity method of accounting recognize through earnings the unrealized holding gain or loss in accumulated other comprehensive income at the date the investment becomes qualified for use of the equity method.

For all business entities, the amendments in this Update are effective for fiscal years beginning after December 15, 2016, including interim periods within those fiscal years, and should be implemented using the prospective method. Adoption of this Update is not expected to have a significant effect on the Company's consolidated financial statements.

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

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

- Accounting for Income Taxes:** All excess tax benefits and tax deficiencies (including tax benefits of dividends on share-based payment awards) should be recognized as income tax expense or benefit in the income statement. The tax effects of exercised or vested awards should be treated as discrete items in the reporting period in which they occur. An entity also should recognize excess tax benefits regardless of whether the benefit reduces taxes payable in the current period.
- Classification of Excess Tax Benefits on the Statement of Cash Flows:** Excess tax benefits should be classified along with other income tax cash flows as an operating activity.
- Forfeitures:** An entity can make an entity-wide accounting policy election to either estimate the number of awards that are expected to vest (current GAAP) or account for forfeitures when they occur.
- Minimum Statutory Tax Withholding Requirements:** The threshold to qualify for equity classification permits withholding up to the maximum statutory tax rates in the applicable jurisdictions.
- Classification of Employee Taxes Paid on the Statement of Cash Flows When an Employer Withholds Shares for Tax-Withholding Purposes:** Cash paid by an employer when directly withholding shares for tax-withholding purposes should be classified as a financing activity.

For public business entities, the amendments in this Update are effective for fiscal years beginning after December 15, 2016, including interim periods within those fiscal years. Amendments related to the timing of when excess tax benefits are recognized, minimum statutory withholding requirements and forfeitures should be applied using a modified retrospective transition method by means of a cumulative-effect adjustment to equity as of the beginning of the period in which the guidance is adopted. Amendments related to the presentation of employee taxes paid on the statement of cash flows when an employer withholds shares to meet the minimum statutory withholding requirement should be applied retrospectively. Amendments requiring recognition of excess tax benefits and tax deficiencies in the income statement should be applied prospectively. An entity may elect to apply the amendments related to the presentation of excess tax benefits on the statement of cash flows using either a prospective transition method or a retrospective transition method. Adoption of this Update is not expected to have a significant effect on the Company’s consolidated financial statements.

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

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our condensed consolidated financial statements and related notes appearing elsewhere in this report. This discussion and analysis includes certain forward-looking statements that involve risks, uncertainties, and assumptions. You should review the "Risk Factors" section of our Annual Report on Form 10-K for the year ended December 31, 2015 for a discussion of important factors that could cause actual results to differ materially from the results described in or implied by such forward-looking statements. See also "Cautionary Note Regarding Forward-Looking Statements" at the beginning of this report.

Overview

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

We offer a full complement of products and services on a nationwide basis. We conduct our deposit operations primarily over the Internet and have no traditional branch offices. We have diversified our operations by adding commercial real estate ("CRE") lending, including nationwide single tenant lease financing, and commercial and industrial ("C&I") lending, including business banking/treasury management services to meet the needs of high-quality commercial borrowers and depositors.

Our business model differs from that of a typical community bank. We do not have a conventional brick and mortar branch system; but instead operate through our scalable Internet banking platform. The market area for our residential real estate lending, consumer lending, and deposit gathering activities is the entire United States. We also offer single tenant lease financing on a nationwide basis. Our other commercial banking activities, including CRE and C&I loans, corporate credit cards, and corporate treasury management services, are offered by our commercial banking team to businesses primarily within Central Indiana, Phoenix, Arizona, and adjacent markets. We have no significant customer concentrations within our loan portfolio.

## Results of Operations

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

| (dollars in thousands except for share and per share data) | Three Months Ended |                   |                    |               |                |   |
|--|--------------------|-------------------|--------------------|---------------|----------------|---|
|  | March 31, 2016     | December 31, 2015 | September 30, 2015 | June 30, 2015 | March 31, 2015 |   |
| <b>Income Statement Summary:</b>                           |                    |                   |                    |               |                |   |
| Net interest income  | \$9,141            | \$ 8,568          | \$ 7,839           | \$7,572       | \$ 6,774       |   |
| Provision for loan losses                                  | 946                | 746               | 454                | 304           | 442            |   |
| Noninterest income   | 2,540              | 2,143             | 2,374              | 2,476         | 3,148          |   |
| Noninterest expense  | 7,005              | 6,492             | 6,207              | 6,327         | 6,257          |   |
| Income tax provision                                       | 1,298              | 1,195             | 1,229              | 1,152         | 1,160          |   |
| Net income   | \$2,432            | \$ 2,278          | \$ 2,323           | \$2,265       | \$ 2,063       |   |
| <b>Per Share Data:</b>                                     |                    |                   |                    |               |                |   |
| Earnings per share - basic                                 | \$0.54             | \$ 0.50           | \$ 0.51            | \$0.50        | \$0.46         |   |
| Earnings per share - diluted                               | \$0.53             | \$ 0.50           | \$ 0.51            | \$0.50        | \$0.46         |   |
| Dividends declared per share                               | \$0.06             | \$ 0.06           | \$ 0.06            | \$0.06        | \$0.06         |   |
| Book value per common share                                | \$23.98            | \$ 23.28          | \$ 22.95           | \$22.28       | \$ 22.16       |   |
| Tangible book value per common share <sup>1</sup>          | \$22.93            | \$ 22.24          | \$ 21.90           | \$21.23       | \$ 21.11       |   |
| Common shares outstanding                                  | 4,497,284          | 4,481,347         | 4,484,513          | 4,484,513     | 4,484,513      |   |
| <b>Average common shares outstanding:</b>                  |                    |                   |                    |               |                |   |
| Basic  | 4,541,728          | 4,534,910         | 4,532,360          | 4,529,823     | 4,516,776      |   |
| Diluted  | 4,575,555          | 4,580,353         | 4,574,455          | 4,550,034     | 4,523,246      |   |
| <b>Performance Ratios:</b>                                 |                    |                   |                    |               |                |   |
| Return on average assets                                   | 0.72               | % 0.74            | % 0.82             | % 0.84        | % 0.84         | % |
| Return on average shareholders' equity                     | 9.20               | % 8.73            | % 9.14             | % 9.15        | % 8.55         | % |
| Return on average tangible common equity <sup>1</sup>      | 9.63               | % 9.14            | % 9.58             | % 9.60        | % 8.98         | % |
| Net interest margin  | 2.78               | % 2.85            | % 2.84             | % 2.87        | % 2.84         | % |
| <b>Capital Ratios:</b>                                     |                    |                   |                    |               |                |   |
| Tangible common equity to tangible assets <sup>1</sup>     | 6.77               | % 7.88            | % 8.46             | % 8.66        | % 9.18         | % |
| Tier 1 leverage ratio                                      | 7.65               | % 8.28            | % 8.81             | % 8.93        | % 9.52         | % |
| Common equity tier 1 capital ratio                         | 9.38               | % 10.11           | % 10.74            | % 11.12       | % 11.99        | % |
| Tier 1 capital ratio                                       | 9.38               | % 10.11           | % 10.74            | % 11.12       | % 11.99        | % |
| Total risk-based capital ratio                             | 11.38              | % 12.25           | % 11.90            | % 12.28       | % 13.18        | % |

<sup>1</sup> This information represents a non-GAAP financial measure. See the "Reconciliation of Non-GAAP Financial Measures" for a reconciliation of these measures to their most directly comparable GAAP measures.

During the first quarter 2016, net income was \$2.4 million, or \$0.53 per diluted share, compared to the first quarter 2015 net income of \$2.1 million, or \$0.46 per diluted share, resulting in an increase in net income of \$0.4 million, or 17.9%.

The increase in net income in the first quarter 2016 compared to the first quarter 2015 was primarily due to a \$2.4 million, or 34.9%, increase in net interest income, partially offset by a \$0.7 million, or 12.0%, increase in noninterest expense, a \$0.6 million, or 19.3%, decrease in noninterest income, a \$0.5 million, or 114.0%, increase in provision for loan losses and a \$0.1 million, or 11.9%, increase in income tax expense.

During the first quarter 2016, return on average assets and return on average shareholders' equity were 0.72% and 9.20%, respectively, compared to 0.84% and 8.55%, respectively, for the first quarter 2015.





## Consolidated Average Balance Sheets and Net Interest Income Analyses

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

(dollars in thousands)

|  | Three Months Ended |            |                   |            |                 |            |
|--|--------------------|------------|-------------------|------------|-----------------|------------|
|  | March 31, 2016     |            | December 31, 2015 |            | March 31, 2015  |            |
|  | Average Balance    | Yield/Cost | Average Balance   | Yield/Cost | Average Balance | Yield/Cost |
| <b>Assets</b>                              |                    |            |                   |            |                 |            |
| <b>Interest-earning assets</b>             |                    |            |                   |            |                 |            |
| Loans, including loans held-for-sale       | \$1,020,168        | 4.41 %     | \$942,801         | 4.33 %     | \$780,302       | 4.36 %     |
| Securities - taxable                       | 202,898            | 2.32 %     | 189,447           | 2.23 %     | 145,241         | 2.02 %     |
| Securities - non-taxable                   | 22,179             | 2.99 %     | 18,401            | 2.95 %     | —               | 0.00 %     |
| Other earning assets                       | 78,291             | 0.87 %     | 41,274            | 0.96 %     | 41,643          | 0.73 %     |
| Total interest-earning assets              | 1,323,536          | 3.86 %     | 1,191,923         | 3.86 %     | 967,186         | 3.85 %     |
| Allowance for loan losses                  | (8,655 )           |            | (7,947 )          |            | (5,883 )        |            |
| Noninterest-earning assets                 | 37,951             |            | 37,541            |            | 34,548          |            |
| Total assets                               | \$1,352,832        |            | \$1,221,517       |            | \$995,851       |            |
| <b>Liabilities</b>                         |                    |            |                   |            |                 |            |
| <b>Interest-bearing liabilities</b>        |                    |            |                   |            |                 |            |
| Interest-bearing demand deposits           | \$81,338           | 0.55 %     | \$77,096          | 0.55 %     | \$75,405        | 0.55 %     |
| Regular savings accounts                   | 25,021             | 0.58 %     | 26,239            | 0.57 %     | 22,099          | 0.59 %     |
| Money market accounts                      | 350,809            | 0.71 %     | 345,337           | 0.70 %     | 274,312         | 0.73 %     |
| Certificates and brokered deposits         | 575,976            | 1.48 %     | 467,334           | 1.40 %     | 390,101         | 1.38 %     |
| Total interest-bearing deposits            | 1,033,144          | 1.12 %     | 916,006           | 1.04 %     | 761,917         | 1.04 %     |
| Other borrowed funds                       | 185,618            | 1.44 %     | 171,169           | 1.44 %     | 109,787         | 1.70 %     |
| Total interest-bearing liabilities         | 1,218,762          | 1.17 %     | 1,087,175         | 1.10 %     | 871,704         | 1.12 %     |
| Noninterest-bearing deposits               | 22,899             |            | 25,198            |            | 22,265          |            |
| Other noninterest-bearing liabilities      | 4,893              |            | 5,561             |            | 4,038           |            |
| Total liabilities                          | 1,246,554          |            | 1,117,934         |            | 898,007         |            |
| Shareholders' equity                       | 106,278            |            | 103,583           |            | 97,844          |            |
| Total liabilities and shareholders' equity | \$1,352,832        |            | \$1,221,517       |            | \$995,851       |            |
| Interest rate spread <sup>1</sup>          |                    | 2.69 %     |                   | 2.76 %     |                 | 2.73 %     |
| Net interest margin <sup>2</sup>           |                    | 2.78 %     |                   | 2.85 %     |                 | 2.84 %     |

<sup>1</sup> Yield on total interest-earning assets minus cost of total interest-bearing liabilities

<sup>2</sup> Net interest income divided by total interest-earning assets (annualized)

## Rate/Volume Analysis

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

| (dollars in thousands)                 | Rate/Volume Analysis of Net Interest Income                   |                |               |  |               |                 |
|--|---|----------------|---------------|--|---------------|-----------------|
|  | Three Months Ended<br>March 31, 2016 vs.<br>December 31, 2015 |                |               | Three Months Ended<br>March 31, 2016 vs.<br>March 31, 2015 |               |                 |
|  | Due to Changes in<br>Volume                                   |                | Rate          | Due to Changes in<br>Volume                                |               | Rate            |
|  | Net   | Rate           | Net           | Rate   | Net           | Rate            |
| <b>Interest income</b>                 |   |                |               |  |               |                 |
| Loans, including loans held-for-sale   | \$ 734  | \$ 165         | \$ 899        | \$ 2,698   | \$ 101        | \$ 2,799        |
| Securities – taxable                   | 65  | 37             | 102           | 325  | 122           | 447             |
| Securities – non-taxable               | 26  | 2              | 28            | 165  | —             | 165             |
| Other earning assets                   | 130   | (60 )          | 70            | 78   | 17            | 95              |
| <b>Total</b>                           | <b>955</b>  | <b>144</b>     | <b>1,099</b>  | <b>3,266</b>   | <b>240</b>    | <b>3,506</b>    |
| <b>Interest expense</b>                |   |                |               |  |               |                 |
| Interest-bearing deposits              | 302   | 181            | 483           | 769  | 166           | 935             |
| Other borrowed funds                   | 43  | —              | 43            | 634  | (430 )        | 204             |
| <b>Total</b>                           | <b>345</b>  | <b>181</b>     | <b>526</b>    | <b>1,403</b>   | <b>(264 )</b> | <b>1,139</b>    |
| <b>Increase in net interest income</b> | <b>\$ 610</b>   | <b>\$(37 )</b> | <b>\$ 573</b> | <b>\$ 1,863</b>  | <b>\$ 504</b> | <b>\$ 2,367</b> |

Net interest income for the first quarter 2016 was \$9.1 million, increasing \$2.4 million, or 34.9%, compared to \$6.8 million for the first quarter 2015. Net interest margin was 2.78% for the first quarter 2016 compared to 2.84% for the first quarter 2015. The increase in net interest income was primarily driven by an increase of \$356.4 million, or 36.8%, in the balance of average interest-earning assets for the first quarter 2016 compared to the first quarter 2015. The decline in net interest margin for the first quarter 2016 compared to the first quarter 2015, was driven primarily by an increase of 8 basis points (“bps”) in the cost of interest-bearing deposits.

The increase in net interest income for the first quarter 2016, as compared to the first quarter 2015, was the result of a \$3.5 million, or 38.2%, increase in total interest income to \$12.7 million for the first quarter 2016 from \$9.2 million for the first quarter 2015. The increase in total interest income was partially offset by a \$1.1 million, or 47.2%, increase in total interest expense to \$3.6 million for the first quarter 2016 from \$2.4 million for the first quarter 2015.

The increase in total interest income was due primarily to an increase in interest earned on loans resulting from an increase of \$239.9 million, or 30.7%, in the average balance of loans, including loans held-for-sale, as well as an increase in interest earned on securities resulting from an increase of \$79.8 million, or 55.0%, in the average balance of securities for the first quarter 2016 compared to the first quarter 2015. The increase in total interest income was also due to a 36 bps increase in the yield earned on the securities portfolio and a 5 bps increase in the yield earned on loans, including loans held-for-sale.

The increase in total interest expense was driven primarily by an increase in interest expense related to interest-bearing deposits as a result of a \$271.2 million, or 35.6%, increase in the average balance of interest-bearing deposits for the first quarter 2016 compared to the first quarter 2015, as well as an increase in the cost of funds relating to interest-bearing deposits of 8 bps. The increase in the cost of interest-bearing deposits was primarily due to

a 10 bps increase in the cost of certificates and brokered deposits as new certificates of deposits production in the first quarter 2016 was predominately in longer duration products with higher costs of funds. Interest expense related to other borrowed funds also contributed to the increase in total interest expense due to a \$75.8 million, or 69.1%, increase in the average balance of other borrowed funds for the first quarter 2016 compared to the first quarter 2015, partially offset by a decline of 26 bps in the cost of other borrowed funds. The increase in the average balance of other borrowed funds was primarily due to the Company's issuance of subordinated debt in 2015 as well as the increase in Federal Home Loan Bank advances since the first quarter 2015.

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Noninterest Income

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

| (dollars in thousands)         | Three Months Ended |                   |                    |               |                |
|--------------------------------|--------------------|-------------------|--------------------|---------------|----------------|
|                                | March 31, 2016     | December 31, 2015 | September 30, 2015 | June 30, 2015 | March 31, 2015 |
| Service charges and fees       | \$200              | \$ 193            | \$ 202             | \$193         | \$ 176         |
| Mortgage banking activities    | 2,254              | 1,805             | 2,095              | 2,214         | 2,886          |
| (Loss) gain on asset disposals | (16 )              | 40                | (27 )              | (33 )         | (14 )          |
| Other                          | 102                | 105               | 104                | 102           | 100            |
| Total noninterest income       | \$2,540            | \$ 2,143          | \$ 2,374           | \$2,476       | \$ 3,148       |

During the first quarter 2016, noninterest income totaled \$2.5 million, representing a decrease of \$0.6 million, or 19.3%, compared to \$3.1 million for the first quarter 2015. The decrease in noninterest income was driven by a decrease of \$0.6 million, or 21.9%, in mortgage banking activities resulting primarily from lower origination volumes.

Noninterest Expense

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

| (dollars in thousands)               | Three Months Ended |                   |                    |               |                |
|--------------------------------------|--------------------|-------------------|--------------------|---------------|----------------|
|                                      | March 31, 2016     | December 31, 2015 | September 30, 2015 | June 30, 2015 | March 31, 2015 |
| Salaries and employee benefits       | \$3,898            | \$ 3,460          | \$ 3,446           | \$ 3,787      | \$ 3,578       |
| Marketing, advertising and promotion | 464                | 426               | 544                | 334           | 452            |
| Consulting and professional services | 638                | 674               | 544                | 564           | 592            |
| Data processing                      | 274                | 287               | 248                | 233           | 248            |
| Loan expenses                        | 184                | 172               | 97                 | 181           | 181            |
| Premises and equipment               | 798                | 759               | 676                | 691           | 642            |
| Deposit insurance premium            | 180                | 170               | 163                | 160           | 150            |
| Other                                | 569                | 544               | 489                | 377           | 414            |
| Total noninterest expense            | \$7,005            | \$ 6,492          | \$ 6,207           | \$ 6,327      | \$ 6,257       |

Noninterest expense for the first quarter 2016 was \$7.0 million, compared to \$6.3 million for the first quarter 2015. The increase of 0.7 million, or 12.0%, compared to the first quarter 2015 was primarily due to an increase of \$0.3 million in salaries and employee benefits, an increase of \$0.2 million in premises and equipment and an increase of \$0.2 million in other expenses. The increase in salaries and employee benefits was attributable to increased staffing, including the hiring of seasoned operations, credit and lending personnel to assist in managing the Company's strong balance sheet growth. The increase in premises and equipment was due to the Company's build out of its corporate headquarters facility and further investments in software.

Financial Condition

The following table presents summary balance sheet data for the last five quarters.

| (dollars in thousands)        | March 31, 2016 | December 31, 2015 | September 30, 2015 | June 30, 2015 | March 31, 2015 |
|-------------------------------|----------------|-------------------|--------------------|---------------|----------------|
| Balance Sheet Data:           |                |                   |                    |               |                |
| Total assets                  | \$1,527,719    | \$ 1,269,870      | \$ 1,166,170       | \$ 1,104,645  | \$ 1,035,677   |
| Loans receivable              | 1,040,683      | 953,859           | 876,578            | 814,243       | 767,682        |
| Securities available-for-sale | 315,311        | 213,698           | 202,565            | 190,767       | 163,676        |

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|                              |           |         |         |         |         |
|------------------------------|-----------|---------|---------|---------|---------|
| Loans held-for-sale          | 29,491    | 36,518  | 27,773  | 29,872  | 27,584  |
| Noninterest-bearing deposits | 28,945    | 23,700  | 22,338  | 20,994  | 19,178  |
| Interest-bearing deposits    | 1,214,233 | 932,354 | 877,412 | 835,509 | 801,991 |
| Total deposits               | 1,243,178 | 956,054 | 899,750 | 856,503 | 821,169 |
| Total shareholders' equity   | 107,830   | 104,330 | 102,912 | 99,908  | 99,362  |

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Total assets were \$1.5 billion at March 31, 2016, compared to \$1.3 billion at December 31, 2015, representing an increase of \$257.8 million, or 20.3%. The increase in total assets was due primarily to increases of \$101.6 million, or 47.5%, in securities available-for-sale, \$86.8 million, or 9.1%, in loans receivable and \$75.8 million, or 301.3%, in cash and cash equivalents, partially offset by a \$7.0 million, or 19.2%, decrease in loans held-for-sale.

Loan Portfolio Analysis

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

| (dollars in thousands)  | March 31, 2016 |        | December 31, 2015 |        | September 30, 2015 |        | June 30, 2015 |        | March 31, 2015 |        |
|---|----------------|--------|-------------------|--------|--------------------|--------|---------------|--------|----------------|--------|
| Commercial loans  |                |        |                   |        |                    |        |               |        |                |        |
| Commercial and industrial   | \$106,431      | 10.2 % | \$102,000         | 10.7 % | \$89,762           | 10.2 % | \$89,316      | 11.0 % | \$83,849       | 11.0 % |
| Owner-occupied commercial real estate   | 47,010         | 4.5 %  | 44,462            | 4.7 %  | 42,117             | 4.8 %  | 39,405        | 4.8 %  | 38,536         | 5.0 %  |
| Investor commercial real estate   | 14,756         | 1.4 %  | 16,184            | 1.7 %  | 17,483             | 2.0 %  | 20,163        | 2.5 %  | 18,491         | 2.4 %  |
| Construction  | 52,591         | 5.1 %  | 45,898            | 4.8 %  | 30,196             | 3.4 %  | 20,155        | 2.5 %  | 26,847         | 3.5 %  |
| Single tenant lease financing   | 445,534        | 42.8 % | 374,344           | 39.2 % | 329,149            | 37.6 % | 279,891       | 34.4 % | 227,229        | 29.6 % |
| Total commercial loans  | 666,322        | 64.0 % | 582,888           | 61.1 % | 508,707            | 58.0 % | 448,930       | 55.2 % | 394,952        | 51.5 % |
| Consumer loans  |                |        |                   |        |                    |        |               |        |                |        |
| Residential mortgage  | 208,636        | 20.1 % | 214,559           | 22.5 % | 209,507            | 23.9 % | 207,703       | 25.5 % | 215,910        | 28.1 % |
| Home equity   | 40,000         | 3.8 %  | 43,279            | 4.5 %  | 47,319             | 5.4 %  | 49,662        | 6.1 %  | 54,838         | 7.2 %  |
| Other consumer  | 121,323        | 11.7 % | 108,312           | 11.4 % | 106,187            | 12.1 % | 103,157       | 12.6 % | 97,192         | 12.6 % |
| Total consumer loans  | 369,959        | 35.6 % | 366,150           | 38.4 % | 363,013            | 41.4 % | 360,522       | 44.2 % | 367,940        | 47.9 % |
| Deferred loan origination costs and premiums and discounts on purchased loans | 4,402          | 0.4 %  | 4,821             | 0.5 %  | 4,858              | 0.6 %  | 4,791         | 0.6 %  | 4,790          | 0.6 %  |
| Total loans receivable  | 1,040,683      | 100.0% | 953,859           | 100.0% | 876,578            | 100.0% | 814,243       | 100.0% | 767,682        | 100.0% |
| Allowance for loan losses   | (9,220 )       |        | (8,351 )          |        | (7,671 )           |        | (7,073 )      |        | (6,378 )       |        |
| Net loans receivable  | \$1,031,463    |        | \$945,508         |        | \$868,907          |        | \$807,170     |        | \$761,304      |        |

Total loans receivable as of March 31, 2016 were \$1.0 billion, increasing \$86.8 million, or 9.1%, compared to \$953.9 million as of December 31, 2015.

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Total commercial loans increased \$83.4 million, or 14.3%, as of March 31, 2016, compared to December 31, 2015, due to increases of \$71.2 million, or 19.0%, in single tenant lease financing, \$6.7 million, or 14.6%, in construction, \$4.4 million, or 4.3%, in commercial and industrial and \$2.5 million, or 5.7%, in owner-occupied commercial real estate. These increases were partially offset by a decline of \$1.4 million, or 8.8%, in investor commercial real estate.

Total consumer loans increased \$3.8 million, or 1.0%, as of March 31, 2016, compared to December 31, 2015, due primarily to an increase of \$13.0 million, or 12.0%, in other consumer loans. This increase was partially offset by decreases of \$5.9 million, or 2.8%, in residential mortgages and \$3.3 million, or 7.6%, in home equity loans.

## Asset Quality

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

(dollars in thousands)

|   | March 31,<br>2016 | December 31,<br>2015 | September 30,<br>2015 | June 30,<br>2015 | March 31,<br>2015 |
|---|-------------------|----------------------|-----------------------|------------------|-------------------|
| Nonaccrual loans                                    |                   |                      |                       |                  |                   |
| Investor commercial real estate                     | \$—               | \$ —                 | \$ —                  | \$—              | \$ 83             |
| Total commercial loans                              | —                 | —                    | —                     | —                | 83                |
| Consumer loans:                                     |                   |                      |                       |                  |                   |
| Residential mortgage                                | 103               | 103                  | 104                   | 119              | 61                |
| Other consumer                                      | 69                | 64                   | 92                    | 69               | 102               |
| Total consumer loans                                | 172               | 167                  | 196                   | 188              | 163               |
| Total nonaccrual loans                              | 172               | 167                  | 196                   | 188              | 246               |
| Past Due 90 days and accruing loans                 |                   |                      |                       |                  |                   |
| Commercial loans                                    |                   |                      |                       |                  |                   |
| Commercial and industrial                           | —                 | —                    | 10                    | —                | —                 |
| Total commercial loans                              | —                 | —                    | 10                    | —                | —                 |
| Consumer loans:                                     |                   |                      |                       |                  |                   |
| Residential mortgage                                | 195               | —                    | —                     | —                | —                 |
| Total consumer loans                                | 195               | —                    | —                     | —                | —                 |
| Total past due 90 days and accruing loans           | 195               | —                    | 10                    | —                | —                 |
| Total nonperforming loans                           | 367               | 167                  | 206                   | 188              | 246               |
| Other real estate owned                             |                   |                      |                       |                  |                   |
| Investor commercial real estate                     | 4,488             | 4,488                | 4,488                 | 4,488            | 4,488             |
| Total other real estate owned                       | 4,488             | 4,488                | 4,488                 | 4,488            | 4,488             |
| Other nonperforming assets                          | 75                | 85                   | 30                    | 89               | 84                |
| Total nonperforming assets                          | \$4,930           | \$ 4,740             | \$ 4,724              | \$4,765          | \$4,818           |
| Total nonperforming loans to total loans receivable | 0.04              | % 0.02               | % 0.02                | % 0.02           | % 0.03            |
| Total nonperforming assets to total assets          | 0.32              | % 0.37               | % 0.41                | % 0.43           | % 0.47            |

## Troubled Debt Restructurings

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

| (dollars in thousands)                    | March 31,<br>2016 | December 31,<br>2015 | September 30,<br>2015 | June 30,<br>2015 | March 31,<br>2015 |
|---|-------------------|----------------------|-----------------------|------------------|-------------------|
| Troubled debt restructurings – nonaccrual | \$ —              | \$ —                 | \$ —                  | \$—              | \$ 5              |
| Troubled debt restructurings – performing | 1,100             | 1,115                | 1,134                 | 1,150            | 1,164             |
| Total troubled debt restructurings        | \$ 1,100          | \$ 1,115             | \$ 1,134              | \$ 1,150         | \$ 1,169          |





The increase of \$0.2 million, or 4.0%, in total nonperforming assets as of March 31, 2016 compared to December 31, 2015 was due primarily to increases in loans 90 days past due and accruing and nonaccrual loans, slightly offset by a decrease in other nonperforming assets. Total nonperforming loans increased \$0.2 million, or 119.8%, to \$0.4 million as of March 31, 2016 compared to \$0.2 million as of December 31, 2015. Other nonperforming assets declined less than \$0.1 million, or 11.8%, as of March 31, 2016 compared to December 31, 2015. As a result, the ratio of nonperforming loans to total loans receivable increased slightly to 0.04% as of March 31, 2016 compared to 0.02% as of December 31, 2015, while the ratio of nonperforming assets to total assets improved to 0.32% as of March 31, 2016 compared to 0.37% as of December 31, 2015.

As of March 31, 2016 and December 31, 2015, the Company had one commercial property in other real estate owned with a carrying value of \$4.5 million. This property consists of two buildings which are residential units adjacent to a university campus. Improvements to the property have been made in collaboration with the university and the property continues to be occupied.

#### Allowance for Loan Losses

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

| (dollars in thousands)       | Three Months Ended |                   |                    |               |                |
|------------------------------|--------------------|-------------------|--------------------|---------------|----------------|
|                              | March 31, 2016     | December 31, 2015 | September 30, 2015 | June 30, 2015 | March 31, 2015 |
| Balance, beginning of period | \$8,351            | \$ 7,671          | \$ 7,073           | \$6,378       | \$ 5,800       |
| Provision charged to expense | 946                | 746               | 454                | 304           | 442            |
| Losses charged off           | (149 )             | (100 )            | (76 )              | (232 )        | (228 )         |
| Recoveries                   | 72                 | 34                | 220                | 623           | 364            |
| Balance, end of period       | \$9,220            | \$ 8,351          | \$ 7,671           | \$7,073       | \$ 6,378       |

The allowance for loan losses was \$9.2 million as of March 31, 2016, compared to \$8.4 million as of December 31, 2015. The increase of \$0.9 million, or 10.4%, was due primarily to the continued growth in commercial loan balances. During the first quarter 2016, the Company recorded net charge-offs of \$0.1 million, compared to net recoveries of \$0.1 million during the first quarter 2015. During the three months ended March 31, 2016, the net charge-offs were driven primarily by charge-offs of \$0.1 million in other consumer loans.

The allowance for loan losses as a percentage of total loans receivable increased to 0.89% as of March 31, 2016, compared to 0.88% as of December 31, 2015, and as a percentage of nonperforming loans decreased to 2,512.3% as of March 31, 2016, compared to 5,000.6% as of December 31, 2015. The increase in the allowance for loan losses as a percentage of total loans receivable was primarily driven by a \$0.8 million increase in the allowance related to total commercial loans at March 31, 2016 compared to December 31, 2015. Under the Company's allowance for loan losses methodology, commercial loans are assigned higher reserve factors than consumer loans. Commercial loan growth has continued to outpace consumer loan growth, and as of March 31, 2016, total commercial loans represented 64.0% of total loans receivable compared to 61.1% as of December 31, 2015. The combination of higher growth and higher reserve factors related to commercial loans resulted in the increased percentage of allowance for loan losses to total loans receivable.

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Investment Securities

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

(dollars in thousands)

| Amortized Cost                      | March 31,<br>2016 | December 31,<br>2015 | September 30,<br>2015 | June 30,<br>2015 | March 31,<br>2015 |
|-------------------------------------|-------------------|----------------------|-----------------------|------------------|-------------------|
| Securities available-for-sale       |                   |                      |                       |                  |                   |
| U.S. Government-sponsored agencies  | \$ 60,511         | \$ 38,093            | \$ 36,006             | \$ 27,993        | \$ 28,238         |
| Municipal securities                | 35,016            | 21,091               | 15,213                | 15,219           | —                 |
| Mortgage-backed securities          | 177,337           | 113,948              | 109,645               | 107,055          | 112,401           |
| Asset-backed securities             | 19,451            | 19,444               | 19,438                | 19,430           | 19,428            |
| Corporate securities                | 20,000            | 20,000               | 20,000                | 20,000           | —                 |
| Other securities                    | 3,000             | 3,000                | 3,000                 | 3,000            | 3,000             |
| Total securities available-for-sale | \$ 315,315        | \$ 215,576           | \$ 203,302            | \$ 192,697       | \$ 163,067        |

| Approximate Fair Value              | March 31,<br>2016 | December 31,<br>2015 | September 30,<br>2015 | June 30,<br>2015 | March 31,<br>2015 |
|-------------------------------------|-------------------|----------------------|-----------------------|------------------|-------------------|
| Securities available-for-sale       |                   |                      |                       |                  |                   |
| U.S. Government-sponsored agencies  | \$ 60,792         | \$ 37,750            | \$ 35,624             | \$ 27,572        | \$ 28,063         |
| Municipal securities                | 35,639            | 21,469               | 15,224                | 14,779           | —                 |
| Mortgage-backed securities          | 177,989           | 113,052              | 110,052               | 106,674          | 113,132           |
| Asset-backed securities             | 18,892            | 19,361               | 19,423                | 19,452           | 19,457            |
| Corporate securities                | 18,978            | 19,087               | 19,229                | 19,305           | —                 |
| Other securities                    | 3,021             | 2,979                | 3,013                 | 2,985            | 3,024             |
| Total securities available-for-sale | \$ 315,311        | \$ 213,698           | \$ 202,565            | \$ 190,767       | \$ 163,676        |

The approximate fair value of investment securities available-for-sale increased \$101.6 million, or 47.5%, to \$315.3 million as of March 31, 2016 compared to \$213.7 million as of December 31, 2015. The increase was due primarily to increases of \$64.9 million in mortgage-backed securities, \$23.0 million in U.S. Government-sponsored agencies and \$14.2 million in municipal securities. During the three month period ended March 31, 2016, the Company deployed funds generated through deposit growth to purchase additional securities to further diversify the securities portfolio and enhance net interest income while supporting liquidity and interest rate risk management. At March 31, 2016, the Company had \$8.1 million of municipal securities available-for-sale that were traded but had not settled. This obligation is recorded within accrued expenses and other liabilities on the condensed consolidated balance sheet.

Deposits

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

| (dollars in thousands)           | March 31,<br>2016 | December 31,<br>2015 | September 30,<br>2015 | June 30,<br>2015 | March 31,<br>2015 |
|----------------------------------|-------------------|----------------------|-----------------------|------------------|-------------------|
| Noninterest-bearing deposits     | \$28,945 2.3 %    | \$23,700 2.5 %       | \$22,338 2.5 %        | \$20,994 2.5 %   | \$19,178 2.3 %    |
| Interest-bearing demand deposits | 89,180 7.2 %      | 84,241 8.8 %         | 79,031 8.8 %          | 77,822 9.1 %     | 82,982 10.1 %     |
| Regular savings accounts         | 27,279 2.2 %      | 22,808 2.4 %         | 26,316 2.9 %          | 24,405 2.8 %     | 23,367 2.8 %      |
| Money market accounts            | 366,195 29.5 %    | 341,732 35.7 %       | 314,105 34.9 %        | 278,791 32.5 %   | 280,740 34.2 %    |

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|                          |             |        |           |        |           |        |           |        |           |        |
|--------------------------|-------------|--------|-----------|--------|-----------|--------|-----------|--------|-----------|--------|
| Certificates of deposits | 718,733     | 57.8 % | 470,736   | 49.2 % | 444,396   | 49.4 % | 440,936   | 51.5 % | 401,347   | 48.9 % |
| Brokered deposits        | 12,846      | 1.0 %  | 12,837    | 1.4 %  | 13,564    | 1.5 %  | 13,555    | 1.6 %  | 13,555    | 1.7 %  |
| Total                    | \$1,243,178 | 100.0% | \$956,054 | 100.0% | \$899,750 | 100.0% | \$856,503 | 100.0% | \$821,169 | 100.0% |

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Total deposits increased \$287.1 million, or 30.0%, to \$1.2 billion as of March 31, 2016 as compared to \$956.1 million as of December 31, 2015. This increase was due primarily to increases of \$248.0 million, or 52.7%, in certificates of deposit, \$24.5 million, or 7.2%, in money market accounts, \$5.2 million, or 22.1%, in noninterest-bearing deposits, \$4.9 million, or 5.9%, in interest-bearing demand deposits and \$4.5 million, or 19.6%, in regular savings accounts. The increase in the balance of certificates of deposits during the first quarter 2016 was primarily due to the Company's concentrated efforts to capitalize on consumer demand for longer duration deposit products and to enhance liquidity and asset/liability management.

## Capital

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

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

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

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

The following tables present actual and required capital ratios as of March 31, 2016 and December 31, 2015 for the Company and the Bank under the Basel III Capital Rules. The minimum required capital amounts presented include the minimum required capital levels as of March 31, 2016 and December 31, 2015 based on the phase-in provisions of the Basel III Capital Rules and the minimum required capital levels as of January 1, 2019 when the Basel III Capital Rules have been fully phased-in. Capital levels required to be considered well capitalized are based upon prompt corrective action regulations, as amended to reflect the changes under the Basel III Capital Rules.

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|  | Actual         |         | Minimum Capital Required - Basel III Phase-In Schedule |        | Minimum Capital Required - Basel III Fully Phased-In |         | Required to be Considered Well Capitalized |         |
|--|----------------|---------|--|--------|--|---------|--|---------|
|  | Capital Amount | Ratio   | Capital Amount   | Ratio  | Capital Amount                                       | Ratio   | Capital Amount                             | Ratio   |
| (dollars in thousands)                               |                |         |  |        |  |         |  |         |
| As of March 31, 2016:                                |                |         |  |        |  |         |  |         |
| Common equity tier 1 capital to risk-weighted assets |                |         |  |        |  |         |  |         |
| Consolidated   | \$ 103,145     | 9.38 %  | \$ 56,351  | 5.13 % | \$ 76,967  | 7.00 %  | N/A  | N/A     |
| Bank   | 107,464        | 9.80 %  | 56,204   | 5.13 % | 76,766   | 7.00 %  | 71,283                                     | 6.50 %  |
| Tier 1 capital to risk-weighted assets               |                |         |  |        |  |         |  |         |
| Consolidated   | 103,145        | 9.38 %  | 72,844   | 6.63 % | 93,460   | 8.50 %  | N/A  | N/A     |
| Bank   | 107,464        | 9.80 %  | 72,654   | 6.63 % | 93,216   | 8.50 %  | 87,733                                     | 8.00 %  |
| Total capital to risk-weighted assets                |                |         |  |        |  |         |  |         |
| Consolidated   | 125,116        | 11.38 % | 94,834   | 8.63 % | 115,450  | 10.50 % | N/A  | N/A     |
| Bank   | 116,693        | 10.64 % | 94,587   | 8.63 % | 115,150  | 10.50 % | 109,666                                    | 10.00 % |
| Leverage ratio                                       |                |         |  |        |  |         |  |         |
| Consolidated   | 103,145        | 7.65 %  | 53,942   | 4.00 % | 53,942   | 4.00 %  | N/A  | N/A     |
| Bank   | 107,464        | 7.98 %  | 53,847   | 4.00 % | 53,847   | 4.00 %  | 67,309                                     | 5.00 %  |

|  | Actual         |         | Minimum Capital Required - Basel III Phase-In Schedule |        | Minimum Capital Required - Basel III Fully Phased-In |         | Minimum Required to be Considered Well Capitalized |         |
|--|----------------|---------|--|--------|--|---------|--|---------|
|  | Capital Amount | Ratio   | Capital Amount   | Ratio  | Capital Amount                                       | Ratio   | Capital Amount                                     | Ratio   |
| (dollars in thousands)                               |                |         |  |        |  |         |  |         |
| As of December 31, 2015:                             |                |         |  |        |  |         |  |         |
| Common equity tier 1 capital to risk-weighted assets |                |         |  |        |  |         |  |         |
| Consolidated   | \$ 100,839     | 10.11 % | \$ 44,881  | 4.50 % | \$ 69,815  | 7.00 %  | N/A  | N/A     |
| Bank   | 104,434        | 10.50 % | 44,768   | 4.50 % | 69,639   | 7.00 %  | 64,664   | 6.50 %  |
| Tier 1 capital to risk-weighted assets               |                |         |  |        |  |         |  |         |
| Consolidated   | 100,839        | 10.11 % | 59,842   | 6.00 % | 84,776   | 8.50 %  | N/A  | N/A     |
| Bank   | 104,434        | 10.50 % | 59,690   | 6.00 % | 84,561   | 8.50 %  | 79,587   | 8.00 %  |
| Total capital to risk-weighted assets                |                |         |  |        |  |         |  |         |
| Consolidated   | 122,190        | 12.25 % | 79,789   | 8.00 % | 104,723  | 10.50 % | N/A  | N/A     |
| Bank   | 112,785        | 11.34 % | 79,587   | 8.00 % | 104,458  | 10.50 % | 99,484   | 10.00 % |
| Leverage ratio                                       |                |         |  |        |  |         |  |         |
| Consolidated   | 100,839        | 8.28 %  | 48,713   | 4.00 % | 48,713   | 4.00 %  | N/A  | N/A     |
| Bank   | 104,434        | 8.59 %  | 48,636   | 4.00 % | 48,636   | 4.00 %  | 60,796   | 5.00 %  |

## Shareholders' Dividends

The Company's Board of Directors declared a cash dividend for the first quarter 2016 of \$0.06 per share of common stock payable April 15, 2016 to shareholders of record as of March 31, 2016. The Company expects to continue to pay cash dividends on a quarterly basis; however, the declaration and amount of any future cash dividends will be subject to the sole discretion of the Board of Directors and will depend upon many factors, including its results of operations, financial condition, capital requirements, regulatory and contractual restrictions (including with respect to the Company's outstanding subordinated debt), business strategy and other factors deemed relevant by the Board of Directors.

During 2013, the Company issued a \$3.0 million subordinated debenture to a third party, and during 2015, the Company issued \$10.0 million in subordinated notes to a third party. The agreements under which the subordinated debenture and subordinated notes were issued prohibit the Company from paying any dividends on its common stock or making any other distributions to shareholders at any time when there shall have occurred and be continuing an event of default under the applicable agreement. If an event of default were to occur and the Company did not cure it, the Company would be prohibited from paying any dividends or making any other distributions to shareholders or from redeeming or repurchasing any common stock.

## Capital Resources

While the Company believes it has sufficient liquidity and capital resources to meet its cash and capital expenditure requirements for at least the next twelve months, including any cash dividends it may pay, the Company intends to continue pursuing its growth strategy, which may require additional capital. If the Company is unable to secure such capital at favorable terms, its ability to execute its growth strategy could be adversely affected.

## Liquidity

Liquidity management is the process used by the Company to manage the continuing flow of funds necessary to meet its financial commitments on a timely basis and at a reasonable cost while also maintaining safe and sound operations. Liquidity, represented by cash and investment securities, is a product of the Company's operating, investing and financing activities. The primary sources of funds are deposits, principal and interest payments on loans and investment securities, maturing loans and investment securities, access to wholesale funding sources and collateralized borrowings. While scheduled payments and maturities of loans and investment securities are relatively predictable sources of funds, deposit flows are greatly influenced by interest rates, general economic conditions and competition. Therefore, the Company supplements deposit growth and enhances interest rate risk management through borrowings, which are generally advances from the Federal Home Loan Bank.

The Company maintains cash and investment securities that qualify as liquid assets to maintain adequate liquidity to ensure safe and sound operations and meet our financial commitments. At March 31, 2016, on a consolidated basis, the Company had \$417.3 million in cash and cash equivalents, interest-bearing time deposits and investment securities available-for-sale and \$29.5 million in loans held-for-sale that were generally available for our cash needs. The Company can also generate funds from wholesale funding sources and collateralized borrowings. At March 31, 2016, the Bank had the ability to borrow an additional \$167.0 million in advances from the Federal Home Loan Bank and correspondent bank Fed Funds lines of credit.

The Company is a separate legal entity from the Bank and must provide for its own liquidity. In addition to its operating expenses, the Company is responsible for paying any dividends declared to its common stockholders and interest and principal on outstanding debt. The Company's primary sources of funds are cash maintained at the holding company level and dividends from the Bank, the payment of which is subject to regulatory limits. At March 31, 2016,

the Company, on an unconsolidated basis, had \$5.3 million in cash generally available for its cash needs, which is in excess of its current annual regular shareholder dividend and operating expenses.

The Company uses its sources of funds primarily to meet ongoing financial commitments, including withdrawals by depositors, credit commitments to borrowers, operating expenses and capital expenditures. At March 31, 2016, approved outstanding loan commitments, including unused lines of credit and standby letters of credit, amounted to \$129.3 million. Certificates of deposit scheduled to mature in one year or less at March 31, 2016 totaled \$341.7 million. Generally, the Company believes that a majority of maturing deposits will remain with the Bank.

Management is not aware of any other events or regulatory requirements that, if implemented, are likely to have a material effect on either the Company's or the Bank's liquidity.



## Reconciliation of Non-GAAP Financial Measures

This Management's Discussion and Analysis contains financial information determined by methods other than in accordance with U.S. generally accepted accounting principles ("GAAP"). Non-GAAP financial measures, specifically tangible common equity, tangible assets, average tangible common equity, tangible book value per common share, return on average tangible common equity and tangible common equity to tangible assets are used by the Company's management to measure the strength of its capital and its ability to generate earnings on tangible capital invested by its shareholders. Although the Company believes these non-GAAP measures provide a greater understanding of its business, they should not be considered a substitute for financial measures determined in accordance with GAAP, nor are they necessarily comparable to non-GAAP performance measures that may be presented by other companies. Reconciliations of these non-GAAP financial measures to the most directly comparable GAAP financial measures are included in the following table for the past five quarters.

| (dollars in thousands, except share and per share data) | Three Months Ended |                      |                       |                  |                   |   |
|---|--------------------|----------------------|-----------------------|------------------|-------------------|---|
|   | March 31,<br>2016  | December 31,<br>2015 | September 30,<br>2015 | June 30,<br>2015 | March 31,<br>2015 |   |
| Total equity - GAAP                                     | \$107,830          | \$104,330            | \$102,912             | \$99,908         | \$99,362          |   |
| Adjustments:  |                    |                      |                       |                  |                   |   |
| Goodwill  | (4,687 )           | (4,687 )             | (4,687 )              | (4,687 )         | (4,687 )          |   |
| Tangible common equity                                  | \$103,143          | \$99,643             | \$98,225              | \$95,221         | \$94,675          |   |
| Total assets - GAAP                                     | \$1,527,719        | \$1,269,870          | \$1,166,170           | \$1,104,645      | \$1,035,677       |   |
| Adjustments:  |                    |                      |                       |                  |                   |   |
| Goodwill  | (4,687 )           | (4,687 )             | (4,687 )              | (4,687 )         | (4,687 )          |   |
| Tangible assets   | \$1,523,032        | \$1,265,183          | \$1,161,483           | \$1,099,958      | \$1,030,990       |   |
| Total common shares outstanding                         | 4,497,284          | 4,481,347            | 4,484,513             | 4,484,513        | 4,484,513         |   |
| Book value per common share                             | \$23.98            | \$23.28              | \$22.95               | \$22.28          | \$22.16           |   |
| Effect of goodwill                                      | (1.05 )            | (1.04 )              | (1.05 )               | (1.05 )          | (1.05 )           |   |
| Tangible book value per common share                    | \$22.93            | \$22.24              | \$21.90               | \$21.23          | \$21.11           |   |
| Total shareholders' equity to assets ratio              | 7.06               | % 8.22               | % 8.82                | % 9.04           | % 9.59            | % |
| Effect of goodwill                                      | (0.29 )            | (0.34 )              | (0.36 )               | (0.38 )          | (0.41 )           |   |
| Tangible common equity to tangible assets ratio         | 6.77               | % 7.88               | % 8.46                | % 8.66           | % 9.18            | % |
| Total average equity - GAAP                             | \$106,278          | \$103,583            | \$100,885             | \$99,333         | \$97,844          |   |
| Adjustments:  |                    |                      |                       |                  |                   |   |
| Average goodwill  | (4,687 )           | (4,687 )             | (4,687 )              | (4,687 )         | (4,687 )          |   |
| Average tangible common equity                          | \$101,591          | \$98,896             | \$96,198              | \$94,646         | \$93,157          |   |
| Return on average shareholders' equity                  | 9.20               | % 8.73               | % 9.14                | % 9.15           | % 8.55            | % |
| Effect of goodwill                                      | 0.43               | % 0.41               | % 0.44                | % 0.45           | % 0.43            | % |
| Return on average tangible common equity                | 9.63               | % 9.14               | % 9.58                | % 9.60           | % 8.98            | % |

## Critical Accounting Policies and Estimates

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There have been no material changes in the Company's critical accounting policies or estimates from those disclosed in its Annual Report on Form 10-K for the year ended December 31, 2015.

Recent Accounting Pronouncements

Refer to Note 12 of the condensed consolidated financial statements.

## Off-Balance Sheet Arrangements

In the ordinary course of business, the Company enters into financial transactions to extend credit and forms of commitments that may be considered off-balance sheet arrangements. The Company enters into forward contracts related to its mortgage banking business to hedge the exposures from commitments to extend new residential mortgage loans to customers and from our mortgage loans held-for-sale. At March 31, 2016 and December 31, 2015, the Company had commitments to sell residential real estate loans of \$83.0 million and \$42.7 million, respectively. These contracts mature in less than one year. The Company does not believe that off-balance sheet arrangements have had or are reasonably likely to have a material effect on its financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources.

## ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Market risk is the risk of loss arising from adverse changes in the fair value of financial instruments due to changes in interest rates, foreign exchange rates and equity prices. The primary source of market risk for the Company is interest rate risk. Interest rate risk is the risk to earnings and the value of the Company's equity resulting from changes in market interest rates and arises in the normal course of business to the extent that there are timing and volume differences between the amount of interest-earning assets and the amount of interest-bearing liabilities that are prepaid, withdrawn, re-priced or mature in specified periods. The Company seeks to achieve consistent growth in net interest income and equity while managing volatility arising from shifts in market interest rates.

The Company monitors its interest rate risk position using income simulation models and economic value of equity ("EVE") sensitivity analysis that capture both short-term and long-term interest rate risk exposure. Income simulation involves forecasting net interest income ("NII") under a variety of interest rate scenarios. The Company uses EVE sensitivity analysis to understand the impact of changes in interest rates on long-term cash flows, income and capital. EVE is calculated by discounting the cash flows for all balance sheet instruments under different interest-rate scenarios. Modeling the sensitivity of NII and EVE to changes in market interest rates is highly dependent on the assumptions incorporated into the modeling process. The Company continually reviews and refines the assumptions used in its interest rate risk modeling.

Presented below is the estimated impact on the Company's NII and EVE position as of March 31, 2016, assuming parallel shifts in interest rates:

|                          | % Change from Base Case<br>for Parallel Changes in<br>Rates |                         |                         |
|--------------------------|---|-------------------------|-------------------------|
|                          | -100<br>Basis<br>Points <sup>1</sup>                        | +100<br>Basis<br>Points | +200<br>Basis<br>Points |
| NII - next twelve months | (1.40)%   | 3.35 %                  | 7.18 %                  |
| EVE                      | (2.67)%   | (3.94)%                 | (5.84)%                 |

<sup>1</sup> Because certain current interest rates are at or below 1.00%, the 100 basis point downward shock assumes that certain corresponding interest rates approach an implied floor that, in effect, reflects a decrease of less than the full 100 basis point downward shock.

The Company's objective is to manage the balance sheet with a bias toward asset sensitivity while simultaneously balancing the potential earnings impact of this strategy. A "risk-neutral" position refers to the absence of a strong bias toward either asset or liability sensitivity. An "asset sensitive" position refers to when the characteristics of the balance sheet are expected to generate higher net interest income when interest rates, primarily short-term rates, increase as rates earned on interest-earning assets would reprice upward more quickly or in greater quantities than rates paid on interest-bearing liabilities would reprice. A "liability sensitive" position refers to when the characteristics of the balance sheet are expected to generate lower net interest income when short-term interest rates increase as rates paid on interest-bearing liabilities would reprice upward more quickly or in greater quantities than rates earned on

interest-earning assets.

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#### ITEM 4. CONTROLS AND PROCEDURES

##### Evaluation of Disclosure Controls and Procedures

The Company maintains disclosure controls and procedures that are designed to ensure that information it is required to disclose in reports that it files or submits under the Securities Exchange Act of 1934, as amended (the “Exchange Act”), is recorded, processed, summarized, and reported within the time period specified in SEC rules and forms. These controls and procedures are also designed to ensure that such information is accumulated and communicated to management, including the principal executive and principal financial officers, as appropriate, to allow timely decisions regarding required disclosure. In designing and evaluating disclosure controls and procedures, the Company has recognized that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives. Management is required to apply judgment in evaluating its controls and procedures.

The Company performed an evaluation under the supervision and with the participation of management, including the principal executive and principal financial officers, to assess the effectiveness of the design and operation of its disclosure controls and procedures under the Exchange Act. Based on that evaluation, the principal executive and principal financial officers concluded that the disclosure controls and procedures were effective as of March 31, 2016.

##### Changes in Internal Control Over Financial Reporting

There has been no change in the Company’s internal control over financial reporting during the three months ended March 31, 2016 that has materially affected, or is reasonably likely to materially affect, its internal control over financial reporting.

## PART II

## ITEM 1. LEGAL PROCEEDINGS

The Company is not party to any material legal proceedings. From time to time, the Bank is a party to legal actions arising from its normal business activities.

## ITEM 1A. RISK FACTORS

There have been no material changes to the risk factors previously disclosed in Part I, Item 1A, of the Company's Annual Report on Form 10-K for the year ended December 31, 2015.

## ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

Under our 2013 Equity Plan, employees may elect for the Company to withhold shares to satisfy minimum statutory federal, state, and local tax withholding obligations arising from the vesting of equity awards, including restricted stock awards. The following table provides information with respect to shares withheld by the Company to satisfy these obligations to the extent employees elected for the Company to withhold such shares. These repurchases were not part of any publicly announced stock repurchase program.

| Period                          | Total Number of Shares Purchased | Average Price Paid Per Share |
|---------------------------------|----------------------------------|------------------------------|
| January 1 to January 31, 2016   | 555                              | \$28.69                      |
| February 1 to February 29, 2016 | —                                | —                            |
| March 1 to March 31, 2016       | 1,760                            | 23.37                        |
| Total                           | 2,315                            | \$24.65                      |

## ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

## ITEM 4. MINE SAFETY DISCLOSURES

Not Applicable.

## ITEM 5. OTHER INFORMATION

None.

ITEM 6. EXHIBITS

Unless otherwise indicated, all documents incorporated into this quarterly report on Form 10-Q by reference to a document filed with the SEC pursuant to the Exchange Act are located under SEC file number 1-35750.

| Exhibit<br>No. | Description  |
|----------------|--|
| 3.1            | Articles of Incorporation of First Internet Bancorp (incorporated by reference to Exhibit 3.1 to registration statement on Form 10 filed November 30, 2012)                                    |
| 3.2            | Amended and Restated Bylaws of First Internet Bancorp, as amended March 18, 2013 (incorporated by reference to Exhibit 3.2 to annual report on Form 10-K for the year ended December 31, 2012) |
| 10.1           | 2016 Senior Executive Cash Incentive Plan  |
| 10.2           | Form of Director Restricted Stock Award Agreement under 2013 Equity Incentive Plan   |
| 31.1           | Rule 13a-14(a)/15d-14(a) Certification of Chief Executive Officer  |
| 31.2           | Rule 13a-14(a)/15d-14(a) Certification of Chief Financial Officer  |
| 32.1           | Section 1350 Certifications  |
| 101.INS        | XBRL Instance Document   |
| 101.SCH        | XBRL Taxonomy Extension Schema   |
| 101.CAL        | XBRL Taxonomy Extension Calculation Linkbase   |
| 101.DEF        | XBRL Taxonomy Extension Definition Linkbase  |
| 101.LAB        | XBRL Taxonomy Extension Label Linkbase   |
| 101.PRE        | XBRL Taxonomy Extension Presentation Linkbase  |

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

FIRST INTERNET BANCORP

Date: 5/4/2016    By    /s/ David B. Becker  
David B. Becker,  
Chairman, President and Chief Executive Officer

Date: 5/4/2016    By    /s/ Kenneth J. Lovik  
Kenneth J. Lovik,  
Senior Vice President and Chief Financial Officer (Principal Financial  
Officer)



EXHIBIT INDEX

| Exhibit No. | Description  | Method of Filing          |
|-------------|--|---------------------------|
| 3.1         | Articles of Incorporation of First Internet Bancorp                                | Incorporated by Reference |
| 3.2         | Amended and Restated Bylaws of First Internet Bancorp, as amended March 18, 2013   | Incorporated by Reference |
| 10.1        | 2016 Senior Executive Cash Incentive Plan  | Filed Electronically      |
| 10.2        | Form of Director Restricted Stock Award Agreement under 2013 Equity Incentive Plan | Filed Electronically      |
| 31.1        | Rule 13a-14(a)/15d-14(a) Certification of Chief Executive Officer                  | Filed Electronically      |
| 31.2        | Rule 13a-14(a)/15d-14(a) Certification of Chief Financial Officer                  | Filed Electronically      |
| 32.1        | Section 1350 Certifications  | Filed Electronically      |
| 101.INS     | XBRL Instance Document   | Filed Electronically      |
| 101.SCH     | XBRL Taxonomy Extension Schema   | Filed Electronically      |
| 101.CAL     | XBRL Taxonomy Extension Calculation Linkbase                                       | Filed Electronically      |
| 101.DEF     | XBRL Taxonomy Extension Definition Linkbase  | Filed Electronically      |
| 101.LAB     | XBRL Taxonomy Extension Label Linkbase   | Filed Electronically      |
| 101.PRE     | XBRL Taxonomy Extension Presentation Linkbase                                      | Filed Electronically      |