

CBIZ, Inc.
Form 10-Q
August 03, 2017

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

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

For the quarterly period ended June 30, 2017

OR

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

For the transition period from _____ to _____

Commission File Number 1-32961

CBIZ, INC.

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of incorporation

or organization)

6050 Oak Tree Boulevard, South, Suite 500, Cleveland, Ohio
(Address of principal executive offices)

22-2769024
(I.R.S. Employer

Identification No.)

44131
(Zip Code)

(Registrant's telephone number, including area code) 216-447-9000

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(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 for such shorter period that the registrant was required to submit and post such files). Yes No

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

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

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

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

Class of Common Stock	Outstanding at July 31, 2017
Common Stock, par value \$0.01 per share	54,818,911

CBIZ, INC. AND SUBSIDIARIES

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PART I – FINANCIAL INFORMATION

Item 1. Financial Statements

CBIZ, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS (Unaudited)

(In thousands)

	June 30, 2017	December 31, 2016
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 1,161	\$ 3,494
Restricted cash	34,924	27,880
Accounts receivable, net	218,317	175,354
Other current assets	25,489	21,407
Current assets before funds held for clients	279,891	228,135
Funds held for clients	148,704	213,457
Total current assets	428,595	441,592
Non-current assets:		
Property and equipment, net	23,728	19,450
Goodwill and other intangible assets, net	618,846	584,401
Assets of deferred compensation plan	76,251	69,912
Notes receivable	1,198	1,227
Other non-current assets	2,048	2,006
Total non-current assets	722,071	676,996
Total assets	\$ 1,150,666	\$ 1,118,588
LIABILITIES		
Current liabilities:		
Accounts payable	\$ 62,013	\$ 45,772
Income taxes payable	6,946	1,048
Accrued personnel costs	36,265	45,221
Notes payable	1,210	1,060
Contingent purchase price liability	18,396	16,322
Other current liabilities	16,604	16,169
Current liabilities before client fund obligations	141,434	125,592
Client fund obligations	148,814	213,855
Total current liabilities	290,248	339,447
Non-current liabilities:		
Bank debt	210,600	191,400
Debt issuance costs	(1,090)	(1,351)
Total long-term debt	209,510	190,049
Notes payable	1,696	1,721
Income taxes payable	4,612	4,426
Deferred income taxes, net	4,464	3,545
Deferred compensation plan obligations	76,251	69,912
Contingent purchase price liability	24,830	17,387
Other non-current liabilities	15,693	12,080

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Total non-current liabilities	337,056	299,120
Total liabilities	627,304	638,567
STOCKHOLDERS' EQUITY		
Common stock	1,296	1,282
Additional paid in capital	668,542	655,629
Retained earnings	330,797	294,925
Treasury stock	(476,986)	(471,311)
Accumulated other comprehensive loss	(287)	(504)
Total stockholders' equity	523,362	480,021
Total liabilities and stockholders' equity	\$1,150,666	\$ 1,118,588

See the accompanying notes to the consolidated financial statements

CBIZ, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (Unaudited)

(In thousands, except per share data)

	Three Months Ended		Six Months Ended	
	June 30, 2017	2016	June 30, 2017	2016
Revenue	\$211,016	\$197,015	\$452,475	\$421,253
Operating expenses	188,120	173,996	380,886	352,113
Gross margin	22,896	23,019	71,589	69,140
Corporate general and administrative expenses	9,232	8,346	18,000	18,591
Operating income	13,664	14,673	53,589	50,549
Other (expense) income:				
Interest expense	(1,692)	(1,733)	(3,209)	(3,259)
Gain on sale of operations, net	23	50	45	151
Other income, net	3,764	703	6,501	2,850
Total other income (expense), net	2,095	(980)	3,337	(258)
Income from continuing operations before income tax				
expense	15,759	13,693	56,926	50,291
Income tax expense	4,343	5,306	20,484	20,106
Income from continuing operations	11,416	8,387	36,442	30,185
Loss from discontinued operations, net of tax	(418)	(258)	(570)	(288)
Net income	\$10,998	\$8,129	\$35,872	\$29,897
Earnings (loss) per share:				
Basic:				
Continuing operations	\$0.21	\$0.16	\$0.68	\$0.58
Discontinued operations	(0.01)	—	(0.01)	(0.01)
Net income	\$0.20	\$0.16	\$0.67	\$0.57
Diluted:				
Continuing operations	\$0.20	\$0.16	\$0.66	\$0.57
Discontinued operations	(0.01)	—	(0.01)	(0.01)
Net income	\$0.19	\$0.16	\$0.65	\$0.56
Basic weighted average shares outstanding	53,968	52,031	53,632	51,802
Diluted weighted average shares outstanding	55,831	53,079	55,530	52,901
Comprehensive Income:				
Net income	\$10,998	\$8,129	\$35,872	\$29,897
Other comprehensive income (loss), net of tax	37	(130)	217	(441)
Comprehensive income	\$11,035	\$7,999	\$36,089	\$29,456

See the accompanying notes to the consolidated financial statements

CBIZ, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY (Unaudited)

(In thousands)

	Issued Common Shares	Treasury Shares	Common Stock	Additional Paid-In Capital	Retained Earnings	Treasury Stock	Accumulated Other Comprehensive Loss	Totals
December 31, 2016	128,191	74,147	\$ 1,282	\$ 655,629	\$ 294,925	\$(471,311)	\$ (504)	\$ 480,021
Net income	—	—	—	—	35,872	—	—	35,872
Other comprehensive income	—	—	—	—	—	—	217	217
Share repurchases	—	400	—	—	—	(5,675)	—	(5,675)
Restricted stock	294	—	3	(3)	—	—	—	—
Stock options								
exercised	805	—	8	5,641	—	—	—	5,649
Share-based compensation	—	—	—	2,790	—	—	—	2,790
Business acquisitions	312	—	3	4,485	—	—	—	4,488
June 30, 2017	129,602	74,547	\$ 1,296	\$ 668,542	\$ 330,797	\$(476,986)	\$ (287)	\$ 523,362

See the accompanying notes to the consolidated financial statements

CBIZ, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)

(In thousands)

	Six Months Ended June 30,	
	2017	2016
Cash flows from operating activities:		
Net income	\$35,872	\$29,897
Adjustments to reconcile net income to net cash provided by operating activities:		
Loss from discontinued operations, net of tax	570	288
Gain on sale of operations, net	(45)	(151)
Depreciation and amortization expense	11,279	10,682
Amortization of discount on notes and deferred financing costs	262	262
Amortization of discount on contingent earnout liability	276	106
Bad debt expense, net of recoveries	2,439	2,205
Adjustment to contingent earnout liability	(1,032)	(714)
Deferred income taxes	776	894
Employee stock awards	2,790	2,842
Excess tax benefits from share based payment arrangements	(2,678)	(673)
Changes in assets and liabilities, net of acquisitions and divestitures:		
Restricted cash	(7,044)	(6,998)
Accounts receivable, net	(40,997)	(36,439)
Other assets	(263)	(2,950)
Accounts payable	14,376	19,268
Income taxes payable	8,762	7,766
Accrued personnel costs	(9,598)	(6,616)
Other liabilities	1,989	2,163
Operating cash flows provided by continuing operations	17,734	21,832
Operating cash flows (used in) provided by discontinued operations	(540)	428
Net cash provided by operating activities	17,194	22,260
Cash flows from investing activities:		
Business acquisitions and purchases of client lists, net of cash acquired	(26,561)	(34,004)
Purchases of client fund investments	(11,788)	(4,963)
Proceeds from the sales and maturities of client fund investments	4,375	4,747
Proceeds from sales of divested operations	45	93
Increase in funds held for clients	72,417	3,649
Additions to property and equipment, net	(6,749)	(1,837)
Collection of notes receivable	18	119
Net cash provided by (used in) investing activities	31,757	(32,196)
Cash flows from financing activities:		
Proceeds from bank debt	308,000	278,000
Payment of bank debt	(288,800)	(248,300)
Payment on early extinguishment of convertible debt	—	(760)
Payment for acquisition of treasury stock	(5,675)	(7,828)
Decrease in client funds obligations	(65,041)	(3,504)
Proceeds from exercise of stock options	5,649	3,529

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Payment of contingent consideration for acquisitions and client list purchases	(5,211)	(4,110)
Excess tax benefit from exercise of stock awards	—	673
Payment of notes payable	(206)	(116)
Deferred financing costs	—	(6)
Net cash (used In) provided by financing activities	(51,284)	17,578
Net (decrease) increase in cash and cash equivalents	(2,333)	7,642
Cash and cash equivalents at beginning of year	3,494	850
Cash and cash equivalents at end of period	\$1,161	\$8,492

See the accompanying notes to the consolidated financial statements

CBIZ, INC. AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

Note 1. Basis of Presentation

The accompanying unaudited condensed consolidated financial statements of CBIZ, Inc. and its subsidiaries (“CBIZ,” the “Company,” “we,” “us,” or “our”) have been prepared in accordance with the instructions to Form 10-Q and do not include all of the information and notes required by the accounting principles generally accepted in the United States (“GAAP”) for complete financial statements.

All intercompany accounts and transactions have been eliminated in consolidation. The accompanying unaudited consolidated financial statements do not reflect the operations or accounts of variable interest entities as the impact is not material to the financial condition, results of operations or cash flows of CBIZ.

These interim unaudited condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2016. In the opinion of management, all adjustments of a normal recurring nature considered necessary for a fair presentation have been included. Operating results for the three and six months ended June 30, 2017 are not necessarily indicative of the results that may be expected for the full year ending December 31, 2017.

The preparation of the consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Management’s estimates and assumptions include, but are not limited to, estimates of collectability of accounts receivable and unbilled revenue, the realizability of goodwill and other intangible assets, the fair value of certain assets, the valuation of stock options in determining compensation expense, estimates of accrued liabilities (such as incentive compensation, self-funded health insurance accruals, legal reserves, income tax uncertainties and contingent purchase price obligations), the provision for income taxes and the realizability of deferred tax assets. Management’s estimates and assumptions are derived from and are continually evaluated based upon available information, judgment and experience. Changes in circumstances could cause actual results to differ materially from those estimates.

Refer to Note 1, Organization and Summary of Significant Accounting Policies, in our Annual Report on Form 10-K for the year ended December 31, 2016 for a description of revenue recognition policies.

Note 2. Accounts Receivable, Net

Accounts receivable, net, at June 30, 2017 and December 31, 2016 were as follows (in thousands):

	June 30, 2017	December 31, 2016
Trade accounts receivable	\$153,156	\$ 132,880
Unbilled revenue, at net realizable value	77,987	55,982

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Total accounts receivable	231,143	188,862
Allowance for doubtful accounts	(12,826)	(13,508)
Accounts receivable, net	\$218,317	\$ 175,354

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CBIZ, INC. AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Unaudited) (Continued)

Note 3. Goodwill and Other Intangible Assets, Net

The components of goodwill and other intangible assets, net, at June 30, 2017 and December 31, 2016 were as follows (in thousands):

	June 30, 2017	December 31, 2016
Goodwill	\$526,984	\$ 487,484
Intangible assets:		
Client lists	175,397	172,343
Other intangible assets	8,703	7,994
Total intangible assets	184,100	180,337
Total goodwill and intangibles assets	711,084	667,821
Accumulated amortization:		
Client lists	(88,754)	(80,560)
Other intangible assets	(3,484)	(2,860)
Total accumulated amortization	(92,238)	(83,420)
Goodwill and other intangible assets, net	\$618,846	\$ 584,401

Note 4. Depreciation and Amortization

Depreciation and amortization expense for property and equipment and intangible assets for the three and six months ended June 30, 2017 and 2016 was as follows (in thousands):

	Three Months Ended		Six Months Ended	
	June 30, 2017	2016	June 30, 2017	2016
Operating expenses	\$5,546	\$5,322	\$11,089	\$10,452
Corporate general and administrative expenses	92	115	190	230
Total depreciation and amortization expense	\$5,638	\$5,437	\$11,279	\$10,682

Note 5. Debt and Financing Arrangements

At June 30, 2017, our primary financing arrangement was the \$400 million unsecured credit facility discussed below, which provides us with the capital necessary to meet our working capital needs as well as the flexibility to continue with our strategic initiatives, including business acquisitions and share repurchases. In addition to the discussion below, refer to our Annual Report on Form 10-K for the year ended December 31, 2016 for additional details of our debt and financing arrangements.

Bank Debt

We have a \$400 million unsecured credit facility with Bank of America as agent for a group of eight participating banks that matures in July 2019. The balance outstanding under the credit facility was \$210.6 million and \$191.4 million at June 30, 2017 and December 31, 2016, respectively.

Interest rates for the six months ended June 30, 2017 and 2016 were as follows:

	Six Months	
	Ended	
	June 30,	
	2017	2016
Weighted average rates	2.60%	2.38%
Range of effective rates	2.19% - 4.75%	3.50%

CBIZ, INC. AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Unaudited) (Continued)

We have approximately \$140 million of available funds under the credit facility at June 30, 2017, net of outstanding letters of credit of \$2.3 million. The credit facility provides us with operating flexibility and funding to support seasonal working capital needs and other strategic initiatives such as acquisitions and share repurchases. As of June 30, 2017, we were in compliance with our debt covenants.

Available funds under the credit facility are based on a multiple of earnings before interest, taxes, depreciation and amortization as defined in the credit facility, and are reduced by letters of credit, license bonds, other indebtedness and outstanding borrowings under the credit facility.

Under the credit facility, loans are charged an interest rate consisting of a base rate or Eurodollar rate plus an applicable margin, letters of credit are charged based on the same applicable margin, and a commitment fee is charged on the unused portion of the credit facility.

Interest Expense

During the three and six months ended June 30, 2017 and 2016, we recognized interest expense as follows (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
Credit facility (1)	\$ 1,692	\$ 1,731	\$ 3,209	\$ 3,251
2006 Notes (2)	—	2	—	8
Total interest expense	\$ 1,692	\$ 1,733	\$ 3,209	\$ 3,259

(1) Components of interest expense related to the credit facility include amortization of deferred financing costs, commitment fees and line of credit fees.

(2) During the second quarter of 2016, we redeemed the remaining 3.125% Convertible Senior Subordinated Notes (the "2006 Notes") for \$750 thousand in cash plus accrued interest under an optional early redemption provision.

Note 6. Commitments and Contingencies

Letters of Credit and Guarantees

We provide letters of credit to landlords (lessors) of our leased premises in lieu of cash security deposits, which totaled \$2.3 million at both June 30, 2017 and December 31, 2016. In addition, we provide license bonds to various state agencies to meet certain licensing requirements. The amount of license bonds outstanding was \$2.5 million and \$2.3 million at June 30, 2017 and December 31, 2016, respectively.

Legal Proceedings

In 2010, CBIZ, Inc. and its subsidiary, CBIZ MHM, LLC (fka CBIZ Accounting, Tax & Advisory Services, LLC) (the “CBIZ Parties”), were named as defendants in lawsuits filed in the U.S. District Court for the District of Arizona and the Superior Court for Maricopa County, Arizona. The federal court case is captioned Robert Facciola, et al v. Greenberg Traurig LLP, et al, and the state court cases are captioned Victims Recovery, LLC v. Greenberg Traurig LLP, et al, Roger Ashkenazi, et al v. Greenberg Traurig LLP, et al, Mary Marsh, et al v. Greenberg Traurig LLP, et al; and ML Liquidating Trust v. Mayer Hoffman McCann PC, et al. Prior to these suits CBIZ MHM, LLC was named as a defendant in Jeffrey C. Stone v. Greenberg Traurig LLP, et al.

These lawsuits arose out of the bankruptcy of Mortgages Ltd., a mortgage lender to developers in the Phoenix, Arizona area. Various other professional firms and individuals not related to the Company were also named defendants in these lawsuits. The lawsuits asserted claims for, among others things, violations of the Arizona Securities Act, common law fraud, and negligent misrepresentation, and sought to hold the CBIZ Parties vicariously liable for Mayer Hoffman’s conduct as Mortgage Ltd.’s auditor, as either a statutory control person under the Arizona Securities Act or a joint venturer under Arizona common law.

CBIZ, INC. AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Unaudited) (Continued)

With the exception of claims being pursued by two plaintiffs from the Ashkenazi lawsuit (“Baldino Group”), all other related matters have been dismissed or settled without payment by the CBIZ Parties. The Baldino Group’s claims, which allege damages of approximately \$16 million, are currently stayed as to the CBIZ Parties and Mayer Hoffman, and no trial date has been set.

On September 16, 2016, CBIZ, Inc. and its subsidiary CBIZ Benefits & Insurance Services, Inc. (“CBIZ Benefits”) were named as defendants in a lawsuit filed in the U.S. District Court for the Western District of Pennsylvania. The federal court case is brought by UPMC, d/b/a University of Pittsburgh Medical Center, and a health system it acquired, UPMC Altoona (formerly, Altoona Regional Health System). The lawsuit asserts professional negligence, breach of contract, and negligent misrepresentation claims against CBIZ, CBIZ Benefits and a former employee of CBIZ Benefits in connection with actuarial services provided by CBIZ Benefits to Altoona Regional Health System. The complaint seeks damages in an amount of no less than \$142 million.

We cannot predict the outcome of the above matters or estimate the possible loss or range of possible loss, if any. Although the proceedings are subject to uncertainties inherent in the litigation process and the ultimate disposition of these proceedings is not presently determinable, we intend to vigorously defend these cases.

In addition to those items disclosed above, we are, from time to time, subject to claims and suits arising in the ordinary course of business.

Note 7. Financial Instruments

Bonds

We held corporate and municipal bonds with par values totaling \$50 million and \$42.4 million at June 30, 2017 and December 31, 2016, respectively. All bonds are investment grade and are classified as available-for-sale. These bonds have maturity or callable dates ranging from July 2017 through May 2022, and are included in “Funds held for clients – current” in the accompanying Consolidated Balance Sheets based on our intent and ability to sell these investments at any time under favorable conditions. The following table summarizes our bond activity for the six months ended June 30, 2017 and the twelve months ended December 31, 2016 (in thousands):

	Six Months	Twelve Months
	Ended June 30,	Ended December 31,
	2017	2016
Fair value at beginning of period	\$44,573	\$ 43,142

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Purchases	11,788	11,355
Redemptions	(940)	(2,900)
Maturities	(3,435)	(6,878)
Increase (decrease) in bond premium	204	(106)
Fair market value adjustment	251	(40)
Fair value at end of period	\$52,441	\$ 44,573

Interest Rate Swaps

We do not purchase or hold any derivative instruments for trading or speculative purposes. We utilize interest rate swaps to manage interest rate risk exposure associated with our floating-rate debt under the credit facility. Under these interest rate swap contracts, we receive cash flows from counterparties at variable rates based on the London Interbank Offered Rate (“LIBOR”) and pay the counterparties a fixed rate. See our Annual Report on Form 10-K for the year ended December 31, 2016 for further discussion on our interest rate swaps.

During the second quarter of 2017, we entered into an additional interest rate swap with a notional value of \$20 million at a fixed interest rate of 1.77% maturing in 5 years.

CBIZ, INC. AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Unaudited) (Continued)

The following table summarizes our outstanding interest rate swaps and their classification in the accompanying Consolidated Balance Sheets at June 30, 2017 and December 31, 2016 (in thousands):

	June 30, 2017		
	Notional	Fair	
		Value	
	Amount	(1)	Balance Sheet Location
Interest rate swaps (2)	\$70,000	\$629	Other non-current assets
Interest rate swaps (2)	\$10,000	\$13	Other current assets

	December 31, 2016		
	Notional	Fair	
		Value	
	Amount	(1)	Balance Sheet Location
Interest rate swaps (2)	\$50,000	\$525	Other non-current assets
Interest rate swaps (2)	\$10,000	\$4	Other current assets

(1) Refer to Note 8, Fair Value Measurements, for additional disclosures regarding fair value measurements.

(2) Under the terms of the interest rate swaps, we pay interest at a fixed rate of interest plus applicable margin as stated in the agreement, and receive interest that varies with the one-month LIBOR. The notional value, fixed rate of interest and maturity date of each interest rate swap is (i) \$10 million – 0.885% - November 2017, (ii) \$15 million – 1.155% - November 2018, (iii) \$25 million – 1.300% - October 2020, (iv) \$10 million – 1.120% - February 2021 and (v) \$20 million – 1.770% - May 2022.

The following table summarizes the effects of the interest rate swaps on the accompanying Consolidated Statements of Comprehensive Income for the three and six months ended June 30, 2017 and 2016 (in thousands):

(Loss) Gain Recognized	Gain (Loss) Reclassified
in AOCL, net of tax	from AOCL into Expense
Three Months Ended	Three Months Ended
June 30, 2017	June 30, 2016
2016	2017