

CENTRAL VALLEY COMMUNITY BANCORP
Form 10-Q
November 06, 2014
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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 September 30, 2014

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

FOR THE TRANSITION PERIOD FROM _____ TO _____

COMMISSION FILE NUMBER: 000—31977

CENTRAL VALLEY COMMUNITY BANCORP
(Exact name of registrant as specified in its charter)

California
(State or other jurisdiction of incorporation or organization)

77-0539125
(I.R.S. Employer Identification No.)

7100 N. Financial Dr, Suite 101, Fresno, California
(Address of principal executive offices)

93720
(Zip code)

Registrant's telephone number (559) 298-1775

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 past 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

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

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

Large accelerated filer

Accelerated filer

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Non-accelerated filer

Smaller reporting company

(Do not check if a 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 November 1, 2014 there were 10,979,790 shares of the registrant's common stock outstanding.

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CENTRAL VALLEY COMMUNITY BANCORP AND SUBSIDIARY

2014 QUARTERLY REPORT ON FORM 10-Q

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PART 1: FINANCIAL INFORMATION

ITEM 1: FINANCIAL STATEMENTS

CENTRAL VALLEY COMMUNITY BANCORP AND SUBSIDIARY
CONSOLIDATED BALANCE SHEETS

(In thousands, except share amounts)	September 30, 2014 (Unaudited)	December 31, 2013
ASSETS		
Cash and due from banks	\$28,059	\$25,878
Interest-earning deposits in other banks	26,658	85,956
Federal funds sold	331	218
Total cash and cash equivalents	55,048	112,052
Available-for-sale investment securities (Amortized cost of \$439,576 at September 30, 2014 and \$447,108 at December 31, 2013)	447,016	443,224
Held-to-maturity investment securities (Fair value of \$34,523 at September 30, 2014)	31,837	—
Loans, less allowance for credit losses of \$7,489 at September 30, 2014 and \$9,208 at December 31, 2013	547,247	503,149
Bank premises and equipment, net	10,443	10,541
Other real estate owned	—	190
Bank owned life insurance	20,802	19,443
Federal Home Loan Bank stock	4,791	4,499
Goodwill	29,917	29,917
Core deposit intangibles	1,428	1,680
Accrued interest receivable and other assets	15,590	20,940
Total assets	\$1,164,119	\$1,145,635
LIABILITIES AND SHAREHOLDERS' EQUITY		
Deposits:		
Non-interest bearing	\$345,003	\$356,392
Interest bearing	663,860	647,751
Total deposits	1,008,863	1,004,143
Junior subordinated deferrable interest debentures	5,155	5,155
Accrued interest payable and other liabilities	17,088	16,294
Total liabilities	1,031,106	1,025,592
Commitments and contingencies (Note 9)		
Shareholders' equity:		
Preferred stock, no par value, \$1,000 per share liquidation preference; 10,000,000 shares authorized, none issued and outstanding	—	—
Common stock, no par value; 80,000,000 shares authorized; issued and outstanding: 10,979,370 at September 30, 2014 and 10,914,680 at December 31, 2013	54,125	53,981
Retained earnings	74,367	68,348
Accumulated other comprehensive income (loss), net of tax	4,521	(2,286)
Total shareholders' equity	133,013	120,043

Total liabilities and shareholders' equity	\$1,164,119	\$1,145,635
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See notes to unaudited consolidated financial statements.

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CONSOLIDATED STATEMENTS OF INCOME
(Unaudited)

(In thousands, except share and per share amounts)	For the Three Months		For the Nine Months	
	Ended September 30, 2014	2013	Ended September 30, 2014	2013
INTEREST INCOME:				
Interest and fees on loans	\$7,301	\$8,677	\$22,197	\$19,523
Interest on deposits in other banks	37	45	134	104
Interest on Federal funds sold	—	—	1	—
Interest and dividends on investment securities:				
Taxable	1,341	588	4,127	1,341
Exempt from Federal income taxes	1,469	1,593	4,305	4,329
Total interest income	10,148	10,903	30,764	25,297
INTEREST EXPENSE:				
Interest on deposits	249	342	813	947
Interest on junior subordinated deferrable interest debentures	23	25	72	74
Other	—	—	—	17
Total interest expense	272	367	885	1,038
Net interest income before provision for credit losses	9,876	10,536	29,879	24,259
PROVISION FOR CREDIT LOSSES	—	—	(400)	—
Net interest income after provision for credit losses	9,876	10,536	30,279	24,259
NON-INTEREST INCOME:				
Service charges	811	911	2,441	2,282
Appreciation in cash surrender value of bank owned life insurance	156	149	459	342
Interchange fees	295	268	924	678
Net gain on disposal of other real estate owned	—	—	63	—
Net realized gains on sales of investment securities	240	—	573	1,133
Federal Home Loan Bank dividends	86	59	237	113
Loan placement fees	212	128	401	507
Other income	261	298	983	811
Total non-interest income	2,061	1,813	6,081	5,866
NON-INTEREST EXPENSES:				
Salaries and employee benefits	5,076	5,048	14,833	12,916
Occupancy and equipment	1,222	1,134	3,671	2,936
Data processing	448	357	1,362	949
Regulatory assessments	177	220	569	517
ATM/Debit card expenses	166	170	476	388
License and maintenance contracts	128	139	384	338
Advertising	155	124	462	346
Audit and accounting fees	185	135	492	406
Internet banking expense	134	109	359	257
Acquisition and integration	—	271	—	784
Amortization of core deposit intangibles	84	84	252	184
Other	1,276	1,200	3,660	3,126
Total non-interest expenses	9,051	8,991	26,520	23,147

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Income before provision for income taxes	2,886	3,358	9,840	6,978
Provision for income taxes	535	389	2,180	939
Net income	\$2,351	\$2,969	\$7,660	\$6,039
Preferred stock dividends and accretion	—	87	—	262
Net income available to common shareholders	\$2,351	\$2,882	\$7,660	\$5,777
Earnings per common share:				
Basic earnings per share	\$0.22	\$0.26	\$0.70	\$0.58
Weighted average common shares used in basic computation	10,919,630	10,899,086	10,917,892	10,020,057
Diluted earnings per share	\$0.21	\$0.26	\$0.70	\$0.57
Weighted average common shares used in diluted computation	11,014,907	10,958,811	11,005,553	10,080,034
Cash dividend per common share	\$0.05	\$0.05	\$0.15	\$0.15

See notes to unaudited consolidated financial statements.

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CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)
(Unaudited)

(In thousands)	For the Three Months		For the Nine Months	
	Ended September 30,		Ended September 30,	
	2014	2013	2014	2013
Net income	\$2,351	\$2,969	\$7,660	\$6,039
Other Comprehensive Income (Loss):				
Unrealized gains (losses) on securities:				
Unrealized holdings gains (losses) arising and transferred during the period	619	797	12,060	(13,195)
Less: reclassification for net gains included in net income	240	—	573	1,133
Amortization of net unrealized gains transferred during the period	(2)		(20)	
Other comprehensive income (loss), before tax	377	797	11,467	(14,328)
Tax (expense) benefit related to items of other comprehensive income	(156)	(328)	(4,660)	5,896
Total other comprehensive income (loss)	221	469	6,807	(8,432)
Comprehensive income (loss)	\$2,572	\$3,438	\$14,467	\$(2,393)

See notes to unaudited consolidated financial statements.

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CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

(In thousands)	For the Nine Months Ended September 30,	
	2014	2013
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	\$7,660	\$6,039
Adjustments to reconcile net income to net cash provided by operating activities:		
Net decrease in deferred loan fees	(336)	(217)
Depreciation	1,019	801
Accretion	(730)	(614)
Amortization	5,841	7,031
Stock-based compensation	93	73
Tax benefit from exercise of stock options	(6)	(16)
Provision for credit losses	(400)	—
Net realized gains on sales of available-for-sale investment securities	(573)	(1,133)
Net gain (loss) on disposal of premises and equipment	191	(1)
Net gain on sale of other real estate owned	(63)	—
Increase in bank owned life insurance, net of expenses	(459)	(342)
Net (increase) decrease in accrued interest receivable and other assets	(505)	873
Net decrease in prepaid FDIC assessments	—	1,542
Net increase in accrued interest payable and other liabilities	(409)	(1,741)
Provision for (benefit from) deferred income taxes	1,201	(1,191)
Net cash provided by operating activities	12,524	11,104
CASH FLOWS FROM INVESTING ACTIVITIES:		
Net cash and cash equivalents acquired in acquisition	—	40,729
Purchases of available-for-sale investment securities	(137,360)	(129,572)
Proceeds from sales or calls of available-for-sale investment securities	73,982	37,428
Proceeds from maturity and principal repayments of available-for-sale investment securities	36,133	63,666
Net increase in loans	(43,598)	(6,633)
Proceeds from sale of other real estate owned	488	139
Purchases of premises and equipment	(1,112)	(852)
Purchases of bank owned life insurance	(900)	—
FHLB stock (purchased) redeemed	(292)	48
Proceeds from sale of premises and equipment	1	1
Net cash (used in) provided by investing activities	(72,658)	4,954
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net increase in demand, interest bearing and savings deposits	12,745	11,334
Net (decrease) increase in time deposits	(8,025)	6,816
Repayments of short-term borrowings to Federal Home Loan Bank	—	(4,000)
Proceeds from exercise of stock options	45	782
Excess tax benefit from exercise of stock options	6	16
Cash dividend payments on common stock	(1,641)	(1,502)
Cash dividend payments on preferred stock	—	(262)
Net cash provided by financing activities	3,130	13,184
(Decrease) increase in cash and cash equivalents	(57,004)	29,242

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CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	112,052	52,956
CASH AND CASH EQUIVALENTS AT END OF PERIOD	\$55,048	\$82,198

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(In thousands)	For the Nine Months Ended September 30,	
	2014	2013
SUPPLEMENTAL DISCLOSURE OF CASH FLOWS INFORMATION:		
Cash paid during the period for:		
Interest	\$904	\$1,078
Income taxes	\$1,030	\$1,340
Non-cash investing and financing activities:		
Foreclosure of loan collateral and recognition of other real estate owned	\$235	\$—
Transfer of securities from available-for-sale to held-to-maturity	\$31,346	
Unrealized gain on transfer of securities from available-for-sale to held-to-maturity	\$163	
Accrued preferred stock dividends	\$—	\$87
Purchases of available-for-sale investment securities, not yet settled	\$1,203	\$—
Common stock issued in Visalia Community Bank acquisition	\$—	\$12,494

See notes to unaudited consolidated financial statements.

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Note 1. Basis of Presentation

The interim unaudited condensed consolidated financial statements of Central Valley Community Bancorp and subsidiary have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission (the SEC). These interim condensed consolidated financial statements include the accounts of Central Valley Community Bancorp and its wholly owned subsidiary Central Valley Community Bank (the Bank) (collectively, the Company). All significant intercompany accounts and transactions have been eliminated in consolidation. As discussed in Note 2, on July 1, 2013, the Company completed an acquisition under which Visalia Community Bank merged with and into Central Valley Community Bancorp's subsidiary, Central Valley Community Bank. Certain information and footnote disclosures normally included in the annual consolidated financial statements prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) have been omitted. The Company believes that the disclosures are adequate to make the information presented not misleading. These interim consolidated financial statements should be read in conjunction with the audited financial statements and notes thereto included in the Company's 2013 Annual Report to Shareholders on Form 10-K. In the opinion of management, all adjustments, consisting only of normal recurring adjustments, necessary to present fairly the Company's financial position at September 30, 2014, and the results of its operations and its cash flows for the three and nine month interim periods ended September 30, 2014 and 2013 have been included. Certain reclassifications have been made to prior year amounts to conform to the 2014 presentation. Reclassifications had no effect on prior period net income or shareholders' equity. The results of operations for interim periods are not necessarily indicative of results for the full year.

The preparation of these consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions. These estimates and assumptions affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Management has determined that since all of the banking products and services offered by the Company are available in each branch of the Bank, all branches are located within the same economic environment, and management does not allocate resources based on the performance of different lending or transaction activities, it is appropriate to aggregate the Bank branches and report them as a single operating segment. No customer accounts for more than 10 percent of revenues for the Company or the Bank.

Note 2. Acquisition of Visalia Community Bank

Effective July 1, 2013, the Company acquired Visalia Community Bank, headquartered in Visalia, California, wherein Visalia Community Bank, with three full-service offices in Visalia and one in Exeter, merged with and into Central Valley Community Bancorp's subsidiary, Central Valley Community Bank. Visalia Community Bank's assets (unaudited) as of July 1, 2013 totaled approximately \$197 million. The acquired assets and liabilities were recorded at fair value at the date of acquisition.

Under the terms of the merger agreement, the Company issued an aggregate of approximately 1.263 million shares of its common stock and cash totaling approximately \$11.05 million to the former shareholders of Visalia Community Bank. Each Visalia Community Bank common shareholder of record at the effective time of the merger became entitled to receive 2.971 shares of common stock of the Company for each of their former shares of Visalia Community Bank common stock.

The Company recorded \$6.2 million of goodwill and \$1.4 million of other intangible assets at the date of acquisition. The other intangible assets are primarily related to core deposits and are being amortized using a straight-line method over a period of ten years with no significant residual value. For tax purposes purchase accounting adjustments, including goodwill are all non-taxable and/or non-deductible.

The acquisition was consistent with the Company's strategy to build a regional presence in Central California. The acquisition offers the Company the opportunity to increase profitability by introducing existing products and services to the acquired customer base as well as add new customers in the expanded region.

Pro Forma Results of Operations

The following table presents pro forma results of operations information for the periods presented as if the acquisition had occurred as of January 1, 2013. The pro forma results of operations for the nine months ended September 30, 2013 include the historical accounts of the Company and Visalia Community Bank and pro forma adjustments as may be required, including the amortization of intangibles with definite lives and the amortization or accretion of any premiums or discounts arising from fair

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value adjustments for assets acquired and liabilities assumed. The pro forma information is intended for informational purposes only and is not necessarily indicative of the Company's future operating results or operating results that would have occurred had the acquisition been completed at the beginning of 2013. No assumptions have been applied to the pro forma results of operations regarding possible revenue enhancements, expense efficiencies or asset dispositions.

Pro Forma Results of Operations	For the Nine Months Ended September 30, 2013
(In thousands, except per share amounts)	
Net interest income	\$27,581
Provision for credit losses	298
Non-interest income	6,611
Non-interest expense	28,619
Income before provision for income taxes	5,275
Provision for income taxes	375
Net income	\$4,900
Basic earnings per share	\$0.46
Diluted earnings per share	\$0.46

Note 3. Fair Value Measurements

Fair Value Hierarchy

Fair value is the exchange price that would be received for an asset or paid to transfer a liability (exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. In accordance with applicable guidance, the Company groups its assets and liabilities measured at fair value in three levels, based on the markets in which the assets and liabilities are traded and the reliability of the assumptions used to determine fair value. Valuations within these levels are based upon:

Level 1 — Quoted market prices (unadjusted) for identical instruments traded in active exchange markets that the Company has the ability to access as of the measurement date.

Level 2 — Quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable or can be corroborated by observable market data.

Level 3 — Model-based techniques that use at least one significant assumption not observable in the market. These unobservable assumptions reflect the Company's estimates of assumptions that market participants would use on pricing the asset or liability. Valuation techniques include management judgment and estimation which may be significant.

Management monitors the availability of observable market data to assess the appropriate classification of financial instruments within the fair value hierarchy. Changes in economic conditions or model-based valuation techniques may require the transfer of financial instruments from one fair value level to another. In such instances, we report the transfer at the beginning of the reporting period. The estimated carrying and fair values of the Company's financial instruments are as follows (in thousands):

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(In thousands)	September 30, 2014				
	Carrying Amount	Fair Value Level 1	Level 2	Level 3	Total
Financial assets:					
Cash and due from banks	\$28,059	\$28,059	\$—	\$—	\$28,059
Interest-earning deposits in other banks	26,658	26,658	—	—	26,658
Federal funds sold	331	331	—	—	331
Available-for-sale investment securities	447,016	7,529	439,487	—	447,016
Held-to-maturity investment securities	31,837	—	34,523	—	34,523
Loans, net	547,247	—	—	550,002	550,002
Federal Home Loan Bank stock	4,791	N/A	N/A	N/A	N/A
Accrued interest receivable	5,223	22	2,819	2,382	5,223
Financial liabilities:					
Deposits	1,008,863	847,644	161,213	—	1,008,857
Junior subordinated deferrable interest debentures	5,155	—	—	3,175	3,175
Accrued interest payable	110	—	86	24	110
(In thousands)	December 31, 2013				
	Carrying Amount	Fair Value Level 1	Level 2	Level 3	Total
Financial assets:					
Cash and due from banks	\$25,878	\$25,878	\$—	\$—	\$25,878
Interest-earning deposits in other banks	85,956	85,956	—	—	85,956
Federal funds sold	218	218	—	—	218
Available-for-sale investment securities	443,224	7,514	435,710	—	443,224
Loans, net	503,149	—	—	507,361	507,361
Federal Home Loan Bank stock	4,499	N/A	N/A	N/A	N/A
Accrued interest receivable	5,026	21	2,976	2,029	5,026
Financial liabilities:					
Deposits	1,004,143	834,864	169,065	—	1,003,929
Junior subordinated deferrable interest debentures	5,155	—	—	2,750	2,750
Accrued interest payable	129	—	105	24	129

These estimates do not reflect any premium or discount that could result from offering the Company's entire holdings of a particular financial instrument for sale at one time, nor do they attempt to estimate the value of anticipated future business related to the instruments. In addition, the tax ramifications related to the realization of unrealized gains and losses can have a significant effect on fair value estimates and have not been considered in any of these estimates. These estimates are made at a specific point in time based on relevant market data and information about the financial instruments. Because no market exists for a significant portion of the Company's financial instruments, fair value estimates are based on judgments regarding current economic conditions, risk characteristics of various financial instruments and other factors. These estimates are subjective in nature and involve uncertainties and matters of significant judgment and therefore cannot be determined with precision. Changes in assumptions could significantly affect the fair values presented.

The methods and assumptions used to estimate fair values are described as follows:

(a) Cash and Cash Equivalents — The carrying amounts of cash and due from banks, interest-earning deposits in other banks, and Federal funds sold approximate fair values and are classified as Level 1.

(b) Investment Securities — Investment securities in Level 1 are mutual funds and fair values are based on quoted market prices for identical instruments traded in active markets. Fair values for investment securities classified in Level 2 are based on quoted market prices for similar securities in active markets. For securities where quoted prices or market prices of similar securities are not available, fair values are calculated using discounted cash flows or other market indicators.

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(c) Loans — Fair values of loans are estimated as follows: For variable rate loans that reprice frequently and with no significant change in credit risk, fair values are based on carrying values resulting in a Level 3 classification. Purchased credit impaired (PCI) loans are measured at estimated fair value on the date of acquisition. Carrying value is calculated as the present value of expected cash flows and approximates fair value. Fair values for other loans are estimated using discounted cash flow analyses, using interest rates currently being offered for loans with similar terms to borrowers of similar credit quality resulting in a Level 3 classification. Impaired loans are initially valued at the lower of cost or fair value. Impaired loans carried at fair value generally receive specific allocations of the allowance for credit losses. For collateral dependent loans, fair value is commonly based on recent real estate appraisals. These appraisals may utilize a single valuation approach or a combination of approaches including comparable sales and the income approach. Adjustments are routinely made in the appraisal process by the independent appraisers to adjust for differences between the comparable sales and income data available. Such adjustments are usually significant and typically result in a Level 3 classification of the inputs for determining fair value. Non-real estate collateral may be valued using an appraisal, net book value per the borrower's financial statements, or aging reports, adjusted or discounted based on management's historical knowledge, changes in market conditions from the time of the valuation, and management's expertise and knowledge of the client and client's business, resulting in a Level 3 fair value classification. Impaired loans are evaluated on a quarterly basis for additional impairment and adjusted accordingly. The methods utilized to estimate the fair value of loans do not necessarily represent an exit price.

(d) FHLB Stock — It is not practicable to determine the fair value of FHLB stock due to restrictions placed on its transferability.

(e) Other real estate owned — OREO is measured at fair value less estimated costs to sell when acquired, establishing a new cost basis. Fair value is commonly based on recent real estate appraisals. These appraisals may utilize a single valuation approach or a combination of approaches including comparable sales and the income approach. Adjustments are routinely made in the appraisal process to adjust for differences between the comparable sales and income data available. The Company records OREO as non-recurring with level 3 measurement inputs.

(f) Deposits — Fair value of demand deposit, savings, and money market accounts are, by definition, equal to the amount payable on demand at the reporting date (i.e., their carrying amount), resulting in a Level 1 classification. Fair value for fixed and variable rate certificates of deposit are estimated using discounted cash flow analyses using interest rates offered at each reporting date by the Company for certificates with similar remaining maturities resulting in a Level 2 classification.

(g) Short-Term Borrowings — The fair values of the Company's federal funds purchased, borrowings under repurchase agreements, and other short-term borrowings, generally maturing within ninety days, are based on the market rates for similar types of borrowing arrangements resulting in a Level 2 classification.

(h) Other Borrowings — The fair values of the Company's long-term borrowings are estimated using discounted cash flow analyses based on the current borrowing rates for similar types of borrowing arrangements resulting in a Level 2 classification.

The fair values of the Company's Subordinated Debentures are estimated using discounted cash flow analyses based on the current borrowing rates for similar types of borrowing arrangements resulting in a Level 3 classification.

(i) Accrued Interest Receivable/Payable — The fair value of accrued interest receivable and payable is based on the fair value hierarchy of the related asset or liability.

(j) Off-Balance Sheet Instruments — Fair values for off-balance sheet, credit-related financial instruments are based on fees currently charged to enter into similar agreements, taking into account