

FLUSHING FINANCIAL CORP  
Form 10-Q  
November 08, 2018

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 **September 30, 2018**

Commission file number **001-33013**

**FLUSHING FINANCIAL CORPORATION**

*(Exact name of registrant as specified in its charter)*

**Delaware**

*(State or other jurisdiction of incorporation or organization)*

**11-3209278**

*(I.R.S. Employer Identification No.)*

**220 RXR Plaza, Uniondale, New York 11556**

*(Address of principal executive offices)*

**(718) 961-5400**

*(Registrant's telephone number, including area code)*

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 every Interactive Data File required to be submitted 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 such files).  Yes  No

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

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 Act).  Yes  No

The number of shares of the registrant's Common Stock outstanding as of October 31, 2018 was 28,001,422.

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**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Consolidated Statements of Financial Condition**

(Unaudited)

**Item 1. Financial Statements**

	September 30, 2018	December 31, 2017
	(Dollars in thousands, except per share data)	
Assets		
Cash and due from banks	\$45,094	\$51,546
Securities held-to-maturity:		
Mortgage-backed securities (including assets pledged of \$4,701 at September 30, 2018 and none pledged at December 31, 2017; fair value of \$7,221 and \$7,810 at September 30, 2018 and December 31, 2017, respectively)	7,958	7,973
Other securities (none pledged; fair value of \$20,996 and \$21,889 at September 30, 2018 and December 31, 2017, respectively)	23,207	22,913
Securities available for sale, at fair value:		
Mortgage-backed securities (including assets pledged of \$106,607 and \$148,505 at September 30, 2018 and December 31, 2017, respectively; \$1,330 and \$1,590 at fair value pursuant to the fair value option at September 30, 2018 and December 31, 2017, respectively)	528,119	509,650
Other securities (including assets pledged of \$24,575 and \$44,052 at September 30, 2018 and December 31, 2017, respectively; \$12,610 and \$12,685 at fair value pursuant to the fair value option at September 30, 2018 and December 31, 2017, respectively)	232,913	228,704
Loans:		
Multi-family residential	2,235,370	2,273,595
Commercial real estate	1,460,555	1,368,112
One-to-four family mixed-use property	565,302	564,206
One-to-four family residential	188,975	180,663
Co-operative apartments	7,771	6,895
Construction	40,239	8,479
Small Business Administration	14,322	18,479
Taxi medallion	6,078	6,834
Commercial business and other	846,224	732,973
Net unamortized premiums and unearned loan fees	15,226	16,763
Allowance for loan losses	(20,309 )	(20,351 )
Net loans	5,359,753	5,156,648
Interest and dividends receivable	24,673	21,405

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Bank premises and equipment, net	29,929	30,836
Federal Home Loan Bank of New York stock, at cost	54,942	60,089
Bank owned life insurance	131,009	131,856
Goodwill	16,127	16,127
Other assets	85,819	61,527
Total assets	\$6,539,543	\$6,299,274
Liabilities		
Due to depositors:		
Non-interest bearing	\$398,606	\$385,269
Interest-bearing	4,259,042	3,955,403
Mortgagors' escrow deposits	58,667	42,606
Borrowed funds:		
Federal Home Loan Bank advances	1,083,031	1,198,968
Subordinated debentures	73,919	73,699
Junior subordinated debentures, at fair value	40,151	36,986
Total borrowed funds	1,197,101	1,309,653
Other liabilities	84,371	73,735
Total liabilities	5,997,787	5,766,666
Stockholders' Equity		
Preferred stock (\$0.01 par value; 5,000,000 shares authorized; none issued)	-	-
Common stock (\$0.01 par value; 100,000,000 shares authorized; 31,530,595 shares issued at September 30, 2018 and December 31, 2017; 28,025,081 shares and 28,588,266 shares outstanding at September 30, 2018 and December 31, 2017, respectively)	315	315
Additional paid-in capital	221,622	217,906
Treasury stock, at average cost (3,505,514 shares and 2,942,329 shares at September 30, 2018 and December 31, 2017, respectively)	(74,222 )	(57,675 )
Retained earnings	407,590	381,048
Accumulated other comprehensive loss, net of taxes	(13,549 )	(8,986 )
Total stockholders' equity	541,756	532,608
Total liabilities and stockholders' equity	\$6,539,543	\$6,299,274

The accompanying notes are an integral part of these consolidated financial statements.

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Consolidated Statements of Income**

(Unaudited)

(Dollars in thousands, except per share data)	For the three months ended September 30,		For the nine months ended September 30,	
	2018	2017	2018	2017
Interest and dividend income				
Interest and fees on loans	\$59,658	\$53,318	\$171,997	\$155,834
Interest and dividends on securities:				
Interest	5,562	5,850	16,646	18,377
Dividends	18	30	49	274
Other interest income	248	121	873	403
Total interest and dividend income	65,486	59,319	189,565	174,888
Interest expense				
Deposits	17,425	10,655	44,323	29,145
Other interest expense	6,540	5,623	18,472	15,696
Total interest expense	23,965	16,278	62,795	44,841
Net interest income	41,521	43,041	126,770	130,047
Provision for loan losses	-	3,266	153	3,266
Net interest income after provision for loan losses	41,521	39,775	126,617	126,781
Non-interest income				
Banking services fee income	1,017	885	2,965	2,773
Net loss on sale of securities	-	(186 )	-	(186 )
Net gain on sale of loans	10	152	168	396
Net loss from fair value adjustments	(170 )	(1,297 )	(537 )	(2,834 )
Federal Home Loan Bank of New York stock dividends	873	740	2,630	2,206
Gain from life insurance proceeds	2,222	238	2,998	1,405
Bank owned life insurance	782	816	2,320	2,418
Other income	221	313	779	1,120
Total non-interest income	4,955	1,661	11,323	7,298
Non-interest expense				
Salaries and employee benefits	15,720	15,310	49,466	47,838
Occupancy and equipment	2,475	2,502	7,528	7,652

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Professional services	1,915	1,763	6,539	5,678
FDIC deposit insurance	596	499	1,643	1,328
Data processing	1,427	1,349	4,254	3,873
Depreciation and amortization	1,484	1,173	4,328	3,493
Other real estate owned/foreclosure expense (income)	(102 )	121	34	376
Net gain from sales of real estate owned	-	-	(27 )	(50 )
Other operating expenses	3,718	3,249	12,158	11,407
Total non-interest expense	27,233	25,966	85,923	81,595
Income before income taxes	19,243	15,470	52,017	52,484
Provision (benefit) for income taxes				
Federal	2,307	4,680	8,225	15,005
State and local	(397 )	611	1,124	2,315
Total taxes	1,910	5,291	9,349	17,320
Net income	\$17,333	\$10,179	\$42,668	\$35,164
Basic earnings per common share	\$0.61	\$0.35	\$1.48	\$1.21
Diluted earnings per common share	\$0.61	\$0.35	\$1.48	\$1.21
Dividends per common share	\$0.20	\$0.18	\$0.60	\$0.54

The accompanying notes are an integral part of these consolidated financial statements.



**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Consolidated Statements of Comprehensive Income**

(Unaudited)

(In thousands)	For the three months ended September 30, 2018		For the nine months ended September 30, 2017	
Net income	\$17,333	\$10,179	\$42,668	\$35,164
Other comprehensive income (loss), net of tax:				
Amortization of actuarial losses, net of taxes of \$(41) and (\$64) for the three months ended September 30, 2018 and 2017, respectively and of (\$124) and (\$192) for nine months ended September 30, 2018 and 2017, respectively.	91	88	272	262
Amortization of prior service credits, net of taxes of \$3 and \$5 for the three months ended September 30, 2018 and 2017, respectively and of \$8 and \$14 for nine months ended September 30, 2018 and 2017, respectively.	(7 )	(7 )	(20 )	(20 )
Reclassification adjustment for net gains included in income, net of taxes of (\$78) for the three and nine months ended September 30, 2017.	-	108	-	108
Net unrealized (losses) gains on securities, net of taxes of \$1,612 and \$241 for three months ended September 30, 2018 and 2017, respectively and of \$6,055 and (\$1,006) for nine months ended September 30, 2018 and 2017, respectively.	(3,505 )	(333 )	(13,159 )	1,416
Net unrealized gains (losses) on cash flow hedges, net of taxes of (\$860) and (\$41) three months ended September 30, 2018 and 2017, respectively and of (\$4,425) and \$49 for nine months ended September 30, 2018 and 2017, respectively.	1,870	56	9,616	(68 )
Change in fair value of liabilities related to instrument-specific credit risk, net of taxes of (\$4) and (\$10) for the three and nine months ended September 30, 2018, respectively.	9	-	22	-
Total other comprehensive income (loss), net of tax	(1,542 )	(88 )	(3,269 )	1,698
Comprehensive income	\$15,791	\$10,091	\$39,399	\$36,862

The accompanying notes are an integral part of these consolidated financial statements.

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**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Consolidated Statements of Cash Flows**

(Unaudited)

(In thousands)	For the nine months ended September 30,	
	2018	2017
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Net income	\$42,668	\$35,164
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	153	3,266
Depreciation and amortization of bank premises and equipment	4,328	3,493
Amortization of premium, net of accretion of discount	6,462	5,716
Net loss from fair value adjustments	537	2,834
Net gain from sale of loans	(168 )	(396 )
Net loss from sale of securities	-	186
Net gain from sale of OREO	(27 )	(50 )
Income from bank owned life insurance	(2,320 )	(2,418 )
Gain from life insurance proceeds	(2,998 )	(1,405 )
Stock-based compensation expense	5,973	5,092
Deferred compensation	(2,450 )	(3,322 )
Deferred income tax benefit	(1,437 )	(1,806 )
Increase in other liabilities	6,580	6,810
Decrease (increase) in other assets	2,103	(68 )
Net cash provided by operating activities	59,404	53,096
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Purchases of bank premises and equipment	(3,421 )	(5,321 )
Net redemptions of Federal Home Loan Bank of New York shares	5,147	3,945
Purchases of securities held-to-maturity	(653 )	(8,030 )
Proceeds from maturities and prepayments of securities held-to-maturity	364	14,830
Purchases of securities available for sale	(102,756)	(152,121)
Proceeds from sales and calls of securities available for sale	10,000	155,999
Proceeds from maturities and prepayments of securities available for sale	57,839	60,573
Proceeds from bank owned life insurance	6,165	4,646
Net repayments (originations) of loans	3,605	(234,227)
Purchases of loans	(235,193)	(75,832 )
Proceeds from sale of real estate owned	665	583
Proceeds from sale of loans	14,410	54,990
Net cash used in investing activities	(243,828)	(179,965)

## CASH FLOWS FROM FINANCING ACTIVITIES

Net increase in non-interest bearing deposits	13,337	29,346
Net increase in interest-bearing deposits	303,288	195,552
Net increase in mortgagors' escrow deposits	16,061	13,455
Net proceeds (repayments) from short-term borrowed funds	115,250	(43,500 )
Proceeds from long-term borrowings	25,000	180,000
Repayment of long-term borrowings	(256,088)	(205,049)
Purchases of treasury stock	(21,638 )	(2,902 )
Proceeds from issuance of common stock upon exercise of stock options	6	-
Cash dividends paid	(17,244 )	(15,729 )
Net cash provided by financing activities	177,972	151,173
Net (decrease) increase in cash and cash equivalents	(6,452 )	24,304
Cash and cash equivalents, beginning of period	51,546	35,857
Cash and cash equivalents, end of period	\$45,094	\$60,161

## SUPPLEMENTAL CASH FLOW DISCLOSURE

Interest paid	\$57,811	\$42,543
Income taxes paid	5,116	16,906
Taxes paid if excess tax benefits were not tax deductible	5,753	16,906
Non-cash activities:		
Loans transferred to Other Real Estate Owned or Other Assets	673	-
Reclassification of the Income tax effects of Tax Cuts and Jobs Act from AOCI to Retained Earnings	2,073	-
Loans held for investment transferred to loans available for sale	-	30,565
Securities purchased not yet settled	10,000	-

The accompanying notes are an integral part of these consolidated financial statements.

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Consolidated Statements of Changes in Stockholders' Equity****For the nine months ended September 30, 2018 and 2017**

(Unaudited)

(Dollars in thousands, except per share data)	Total	Common Stock	Additional Paid-in Capital	Retained Earnings	Treasury Stock	Accumulated Other Comprehensive Income (Loss)
Balance at December 31, 2017	\$532,608	\$ 315	\$217,906	\$381,048	\$(57,675)	\$ (8,986 )
Reclassification of the Income Tax Effects of the Tax Cuts and Jobs Act from Accumulated Other Comprehensive Income (Loss) to Retained Earnings	-	-	-	2,073	-	(2,073 )
Impact of adoption of Accounting Standard Update 2016-01	-	-	-	(779 )	-	779
Net income	42,668	-	-	42,668	-	-
Award of common shares released from Employee Benefit Trust (124,583 shares)	2,652	-	2,652	-	-	-
Vesting of restricted stock unit awards (257,597 shares)	-	-	(4,908 )	(176 )	5,084	-
Exercise of stock options (600 shares)	6	-	(1 )	-	7	-
Stock-based compensation expense	5,973	-	5,973	-	-	-
Purchase of treasury shares (744,953 shares)	(19,500 )	-	-	-	(19,500)	-
Repurchase of shares to satisfy tax obligation (76,212 shares)	(2,138 )	-	-	-	(2,138 )	-
Dividends on common stock (\$0.60 per share)	(17,244 )	-	-	(17,244 )	-	-
Other comprehensive loss	(3,269 )	-	-	-	-	(3,269 )
Balance at September 30, 2018	\$541,756	\$ 315	\$221,622	\$407,590	\$(74,222)	\$ (13,549 )
Balance at December 31, 2016	\$513,853	\$ 315	\$214,462	\$361,192	\$(53,754)	\$ (8,362 )
Net income	35,164	-	-	35,164	-	-
Award of common shares released from Employee Benefit Trust (114,754 shares)	2,433	-	2,433	-	-	-
Vesting of restricted stock unit awards (284,595 shares)	-	-	(5,052 )	(271 )	5,323	-
Exercise of stock options (4,400 shares)	-	-	(6 )	(40 )	46	-
Stock-based compensation expense	5,092	-	5,092	-	-	-

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Purchase of treasury shares (10,000 shares)	(278 )	-	-	-	(278 )	-
Repurchase of shares to satisfy tax obligation (90,779 shares)	(2,624 )	-	-	-	(2,624 )	-
Dividends on common stock (\$0.54 per share)	(15,729 )	-	-	(15,729 )	-	-
Other comprehensive income	1,698	-	-	-	-	1,698
Balance at September 30, 2017	\$539,609	\$ 315	\$216,929	\$380,316	\$(51,287)	\$ (6,664 )

The accompanying notes are an integral part of these consolidated financial statements.

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## **PART I – FINANCIAL INFORMATION**

### **FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES**

#### **Notes to Consolidated Financial Statements**

(Unaudited)

#### **1. Basis of Presentation**

The primary business of Flushing Financial Corporation (the “Holding Company”), a Delaware corporation, is the operation of its wholly owned subsidiary, Flushing Bank (the “Bank”).

The unaudited consolidated financial statements presented in this Quarterly Report on Form 10-Q (“Quarterly Report”) include the collective results of the Holding Company and its direct and indirect wholly-owned subsidiaries, including the Bank, Flushing Preferred Funding Corporation, Flushing Service Corporation, and FSB Properties Inc., which are collectively herein referred to as “we,” “us,” “our” and the “Company.”

The Holding Company also owns Flushing Financial Capital Trust II, Flushing Financial Capital Trust III, and Flushing Financial Capital Trust IV (the “Trusts”), which are special purpose business trusts. The Trusts are not included in the Company’s consolidated financial statements, as the Company would not absorb the losses of the Trusts if any losses were to occur.

The accompanying unaudited consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”) and general practices within the banking industry. The information furnished in these interim statements reflects all adjustments that are, in the opinion of management, necessary for a fair statement of the results for such presented periods of the Company. Such adjustments are of a normal recurring nature, unless otherwise disclosed in this Quarterly Report. All inter-company balances and transactions have been eliminated in consolidation. The results of operations in the interim statements are not necessarily indicative of the results that may be expected for the full year.

The accompanying unaudited consolidated financial statements have been prepared in conformity with the instructions to Quarterly Report on Form 10-Q and Article 10, Rule 10-01 of Regulation S-X for interim financial statements. Accordingly, certain information and footnote disclosures normally included in financial statements prepared in accordance with GAAP have been condensed or omitted pursuant to the rules and regulations of the Securities and Exchange Commission (“SEC”). The unaudited consolidated interim financial information should be read in conjunction with the Company’s Annual Report on Form 10-K for the year ended December 31, 2017.

When necessary, certain reclassifications were made to prior-year amounts to conform to the current-year presentation.

## 2. Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, and disclosure of contingent assets and liabilities at the date of the financial statements, and reported amounts of revenue and expenses during the reporting period. Estimates that are particularly susceptible to change in the near term are used in connection with the determination of the allowance for loan losses (“ALLL”), the evaluation of goodwill for impairment, the review of the need for a valuation allowance of the Company’s deferred tax assets, the fair value of financial instruments and the evaluation of other-than-temporary impairment (“OTTI”) on securities. Actual results could differ from these estimates.

## 3. Earnings Per Share

Earnings per common share have been computed based on the following:

	For the three months ended		For the nine months ended	
	September 30, 2018	September 30, 2017	September 30, 2018	September 30, 2017
	(Dollars in thousands, except per share data)			
Net income, as reported	\$17,333	\$10,179	\$42,668	\$35,164
Divided by:				
Weighted average common shares outstanding	28,604	29,120	28,806	29,092
Weighted average common stock equivalents	-	1	1	2
Total weighted average common shares outstanding and common stock equivalents	28,604	29,121	28,807	29,094
Basic earnings per common share	\$0.61	\$0.35	\$1.48	\$1.21
Diluted earnings per common share <sup>(1)</sup>	\$0.61	\$0.35	\$1.48	\$1.21
Dividend payout ratio	32.8 %	51.4 %	40.5 %	44.6 %

(1) For the three and nine months ended September 30, 2018 and 2017, there were no common stock equivalents that were anti-dilutive.



**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

**4. Securities**

The Company did not hold any trading securities at September 30, 2018 and December 31, 2017. Securities available for sale are recorded at fair value. Securities held-to-maturity are recorded at amortized cost.

The following table summarizes the Company's portfolio of securities held-to-maturity at September 30, 2018:

	Amortized Cost	Fair Value	Gross Unrealized Gains	Gross Unrealized Losses
(In thousands)				
Securities held-to-maturity:				
Municipals	\$23,207	\$20,996	\$ -	\$ 2,211
Total other securities	23,207	20,996	-	2,211
FNMA	7,958	7,221	-	737
Total mortgage-backed securities	7,958	7,221	-	737
Total	\$31,165	\$28,217	\$ -	\$ 2,948

The following table summarizes the Company's portfolio of securities held-to-maturity at December 31, 2017:

	Amortized Cost	Fair Value	Gross Unrealized Gains	Gross Unrealized Losses
(In thousands)				
Securities held-to-maturity:				
Municipals	\$22,913	\$21,889	\$ -	\$ 1,024
Total other securities	22,913	21,889	-	1,024
FNMA	7,973	7,810	-	163
Total mortgage-backed securities	7,973	7,810	-	163

Total	\$30,886	\$29,699	\$ -	\$ 1,187
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**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

The following table summarizes the Company's portfolio of securities available for sale at September 30, 2018:

	Amortized Cost	Fair Value	Gross Unrealized Gains	Gross Unrealized Losses
(In thousands)				
Corporate	\$ 120,000	\$ 109,757	\$ -	\$ 10,243
Municipals	100,018	100,546	589	61
Mutual funds	11,405	11,405	-	-
Collateralized loan obligations	10,000	10,000	-	-
Other	1,205	1,205	-	-
Total other securities	242,628	232,913	589	10,304
REMIC and CMO	372,472	360,119	17	12,370
GNMA	805	848	43	-
FNMA	130,397	125,168	47	5,276
FHLMC	43,939	41,984	9	1,964
Total mortgage-backed securities	547,613	528,119	116	19,610
Total securities available for sale	\$ 790,241	\$ 761,032	\$ 705	\$ 29,914

The following table summarizes the Company's portfolio of securities available for sale at December 31, 2017:

	Amortized Cost	Fair Value	Gross Unrealized Gains	Gross Unrealized Losses
(In thousands)				
Corporate	\$ 110,000	\$ 102,767	\$ -	\$ 7,233
Municipals	101,680	103,199	1,519	-
Mutual funds	11,575	11,575	-	-
Collateralized loan obligations	10,000	10,053	53	-
Other	1,110	1,110	-	-
Total other securities	234,365	228,704	1,572	7,233
REMIC and CMO	328,668	325,302	595	3,961
GNMA	1,016	1,088	72	-
FNMA	136,198	135,474	330	1,054
FHLMC	48,103	47,786	18	335

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Total mortgage-backed securities	513,985	509,650	1,015	5,350
Total securities available for sale	\$748,350	\$738,354	\$ 2,587	\$ 12,583

Mortgage-backed securities shown in the table above include one private issue collateralized mortgage obligation (“CMO”) that is collateralized by commercial real estate mortgages with an amortized cost and market value of \$21,000 at December 31, 2017. We did not hold any private issue CMO’s that are collateralized by commercial real estate mortgages at September 30, 2018.

The corporate securities held by the Company at September 30, 2018 and December 31, 2017 are issued by U.S. banking institutions.

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

The following tables detail the amortized cost and fair value of the Company's securities classified as held-to-maturity and available for sale at September 30, 2018, by contractual maturity. Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

Securities held-to-maturity:	Amortized Cost	Fair Value
	(In thousands)	
Due in one year or less	\$1,568	\$1,568
Due after ten years	21,639	19,428
Total other securities	23,207	20,996
Mortgage-backed securities	7,958	7,221
Total	\$31,165	\$28,217

Securities available for sale:	Amortized Cost	Fair Value
	(In thousands)	
Due in one year or less	\$-	\$-
Due after one year through five years	4,219	4,215
Due after five years through ten years	135,466	125,245
Due after ten years	91,538	92,048
Total other securities	231,223	221,508
Mutual funds	11,405	11,405
Mortgage-backed securities	547,613	528,119
Total	\$790,241	\$761,032



**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

The following tables show the Company's securities with gross unrealized losses and their fair value, aggregated by category and length of time that individual securities have been in a continuous unrealized loss position, at the dates indicated:

	At September 30, 2018						
	Total			Less than 12 months		12 months or more	
	Count	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
	(Dollars in thousands)						
<b>Held-to-maturity securities</b>							
Municipals	1	\$19,427	\$2,211	\$-	\$-	\$19,427	\$2,211
Total other securities	1	19,427	2,211	-	-	19,427	2,211
<b>FNMA</b>							
Total mortgage-backed securities	1	7,221	737	-	-	7,221	737
Total	2	\$26,648	\$2,948	\$-	\$-	\$26,648	\$2,948
<b>Available for sale securities</b>							
Corporate	14	\$99,756	\$10,243	\$-	\$-	\$99,756	\$10,243
Municipals	11	28,686	61	28,686	61	-	-
Total other securities	25	128,442	10,304	28,686	61	99,756	10,243
<b>REMIC and CMO</b>							
FNMA	23	123,654	5,276	38,461	904	85,193	4,372
FHLMC	2	41,274	1,964	-	-	41,274	1,964
Total mortgage-backed securities	81	502,112	19,610	227,489	5,562	274,623	14,048
Total	106	\$630,554	\$29,914	\$256,175	\$5,623	\$374,379	\$24,291

	At December 31, 2017						
	Total			Less than 12 months		12 months or more	
	Count	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
	(Dollars in thousands)						
<b>Held-to-maturity securities</b>							
Municipals	1	\$20,844	\$1,024	\$20,844	\$1,024	\$-	\$-

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Total other securities	1	20,844	1,024	20,844	1,024	-	-
FNMA	1	7,810	163	7,810	163	-	-
Total mortgage-backed securities	1	7,810	163	7,810	163	-	-
Total securities held-to-maturity	2	\$28,654	\$ 1,187	\$28,654	\$ 1,187	\$-	\$ -
Available for sale securities							
Corporate	14	\$102,767	\$ 7,233	\$9,723	\$ 277	\$93,044	\$ 6,956
Total other securities	14	102,767	7,233	9,723	277	93,044	6,956
REMIC and CMO	36	249,596	3,961	162,781	1,406	86,815	2,555
FNMA	17	120,510	1,054	109,258	850	11,252	204
FHLMC	2	46,829	335	43,258	294	3,571	41
Total mortgage-backed securities	55	416,935	5,350	315,297	2,550	101,638	2,800
Total securities available for sale	69	\$519,702	\$ 12,583	\$325,020	\$ 2,827	\$194,682	\$ 9,756

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**PART I – FINANCIAL INFORMATION**

**FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES**

**Notes to Consolidated Financial Statements**

(Unaudited)

OTTI losses on impaired securities must be fully recognized in earnings if an investor has the intent to sell the debt security or if it is more likely than not that the investor will be required to sell the debt security before recovery of its amortized cost. However, even if an investor does not expect to sell a debt security in an unrealized loss position, the investor must evaluate the expected cash flows to be received and determine if a credit loss has occurred. In the event that a credit loss has occurred, only the amount of impairment associated with the credit loss is recognized in earnings in the Consolidated Statements of Income. Amounts relating to factors other than credit losses are recorded in accumulated other comprehensive loss (“AOCL”) within Stockholders’ Equity. Unrealized losses on available for sale securities, that are deemed to be temporary, are recorded in AOCL, net of tax.

The Company reviewed each investment that had an unrealized loss at September 30, 2018 and December 31, 2017. The unrealized losses in held-to-maturity municipal securities at September 30, 2018 and December 31, 2017 were caused by illiquidity in the market and movements in interest rates. The unrealized losses in held-to-maturity FNMA securities at September 30, 2018 and December 31, 2017 were caused by movements in interest rates. The unrealized losses in securities available for sale at September 30, 2018 and December 31, 2017 were caused by movements in interest rates.

It is not anticipated that these securities would be settled at a price that is less than the amortized cost of the Company’s investment. Each of these securities is performing according to its terms and, in the opinion of management, will continue to perform according to its terms. The Company does not have the intent to sell these securities and it is more likely than not the Company will not be required to sell the securities before recovery of the securities’ amortized cost basis. This conclusion is based upon considering the Company’s cash and working capital requirements and contractual and regulatory obligations, none of which the Company believes would cause the sale of the securities. Therefore, the Company did not consider these investments to be other-than-temporarily impaired at September 30, 2018 and December 31, 2017.

Realized gains and losses on the sales of securities are determined using the specific identification method. The Company did not sell any securities during the three and nine months ended September 30, 2018. The Company sold available for sale securities totaling \$112.4 million during the three and nine months ended September 30, 2017.

The following table represents the gross gains and gross losses realized from the sale of securities available for sale for the periods indicated:

	For the three months ended September 30, 2017	For the nine months ended September 30, 2017
	(In thousands)	
Gross gains from the sale of securities	\$- \$401	\$- \$401
Gross losses from the sale of securities	- (587)	- (587)
Net losses from the sale of securities	\$- \$(186)	\$- \$(186)

## 5. Loans

Loans are reported at their outstanding principal balance net of any unearned income, charge-offs, deferred loan fees and costs on originated loans and unamortized premiums or discounts on purchased loans. Loan fees and certain loan origination costs are deferred. Net loan origination costs and premiums or discounts on loans purchased are amortized into interest income over the contractual life of the loans using the level-yield method. Prepayment penalties received on loans which pay in full prior to their scheduled maturity are included in interest income in the period they are collected.

Interest on loans is recognized on the accrual basis. The accrual of income on loans is generally discontinued when certain factors, such as contractual delinquency of 90 days or more, indicate reasonable doubt as to the timely collectability of such income. Uncollected interest previously recognized on non-accrual loans is reversed from interest income at the time the loan is placed on non-accrual status. A non-accrual loan can be returned to accrual status when contractual delinquency returns to less than 90 days delinquent. Payments received on non-accrual loans that do not bring the loan to less than 90 days delinquent are recorded on a cash basis. Payments can also be applied first as a reduction of principal until all principal is recovered and then subsequently to interest, if in management's opinion, it is evident that recovery of all principal due is likely to occur.

## **PART I – FINANCIAL INFORMATION**

### **FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES**

#### **Notes to Consolidated Financial Statements**

(Unaudited)

The Company recognizes a loan as non-performing when the borrower has demonstrated the inability to bring the loan current, or due to other circumstances which, in management's opinion, indicate the borrower will be unable to bring the loan current within a reasonable time. All loans classified as non-performing, which includes all loans past due 90 days or more, are classified as non-accrual unless there is, in our opinion, compelling evidence the borrower will bring the loan current in the immediate future. Prior to a loan becoming 90 days delinquent, an updated appraisal is ordered and/or an internal evaluation is prepared.

A loan is considered impaired when, based upon current information, the Company believes it is probable that it will be unable to collect all amounts due, both principal and interest, in accordance with the original terms of the loan. Impaired loans are measured based on the present value of the expected future cash flows discounted at the loan's effective interest rate or at the loan's observable market price or, as a practical expedient, the fair value of the collateral if the loan is collateral dependent. All non-accrual loans are considered impaired.

The Company maintains an allowance for loan losses at an amount, which, in management's judgment, is adequate to absorb probable estimated losses inherent in the loan portfolio. Management's judgment in determining the adequacy of the allowance is based on evaluations of the collectability of loans. This evaluation is inherently subjective, as it requires estimates that are susceptible to significant revisions as more information becomes available. An unallocated component may at times be maintained to cover uncertainties that could affect management's estimate of probable losses. When necessary an unallocated component of the allowance will reflect the margin of imprecision inherent in the underlying assumptions used in the methodologies for estimating specific and general losses in the portfolio. The allowance is established through charges to earnings in the form of a provision for loan losses based on management's evaluation of the risk inherent in the various components of the loan portfolio and other factors, including historical loan loss experience (which is updated quarterly), current economic conditions, delinquency and non-accrual trends, classified loan levels, risk in the portfolio and volumes and trends in loan types, recent trends in charge-offs, changes in underwriting standards, experience, ability and depth of the Company's lenders, collection policies and experience, internal loan review function and other external factors. Increases and decreases in the allowance other than charge-offs and recoveries are included in the provision for loan losses. When a loan or a portion of a loan is determined to be uncollectible, the portion deemed uncollectible is charged against the allowance, and subsequent recoveries, if any, are credited to the allowance.

The determination of the amount of the allowance for loan losses includes estimates that are susceptible to significant changes due to changes in appraisal values of collateral, national and local economic conditions and other factors. We review our loan portfolio by separate categories with similar risk and collateral characteristics. Impaired loans are segregated and reviewed separately.

The Company reviews each impaired loan on an individual basis to determine if either a charge-off or a valuation allowance needs to be allocated to the loan. The Company does not charge-off or allocate a valuation allowance to loans for which management has concluded the current value of the underlying collateral will allow for recovery of the loan balance through the sale of the loan or by foreclosure and sale of the property.

The Company considers fair value of collateral dependent loans to be 85% of the appraised or internally estimated value of the property. The 85% is based on the actual net proceeds the Bank has received from the sale of other real estate owned ("OREO") as a percentage of OREO's appraised value. For collateral dependent taxi medallion loans, the Company considers fair value to be the value of the underlying medallion based upon the most recently reported arm's length sales transaction. When there is no recent sale activity, the fair value is calculated using capitalization rates. For both collateral dependent mortgage loans and taxi medallion loans, the amount by which the loan's book value exceeds fair value is charged-off.

Prior to the quarter ended September 30, 2018, we have segregated our loans into two portfolios based on year of origination. One portfolio was reviewed for loans originated after December 31, 2009 and a second portfolio for loans originated prior to January 1, 2010. Our decision to segregate the portfolio based upon origination dates was based on changes made in our underwriting standards during 2009. For the September 30, 2018 ALLL calculation, the decision was made to no longer segregate the loans by origination year and collapse the two portfolios. Management concluded this revision was appropriate due to the loan balance of loans originated before January 1, 2010 represents approximately 11% of the total loan portfolio and these loans are seasoned, therefore most losses in the pre January 1, 2010 originations have already been identified and incurred. Additionally, in connection with this change in methodology we also combined the economic factors used to calculate the qualitative component of the ALLL. The combined impact of these changes in methodology reduced the ALLL by approximately \$0.2 million from what would have been recorded if we did not change our methodology. The Loss Emergence Period ("LEP") used was 1.33 years for the Residential portfolio and 1.58 years for the Commercial portfolio. The Company's Board of Directors reviews and approves management's evaluation of the adequacy of the allowance for loan losses on a quarterly basis.

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(Unaudited)

The Company evaluates the underlying collateral through a third party appraisal, or when a third party appraisal is not available, the Company will use an internal evaluation. The internal evaluations are prepared using an income approach or a sales approach. The income approach is used for income producing properties and uses current revenues less operating expenses to determine the net cash flow of the property. Once the net cash flow is determined, the value of the property is calculated using an appropriate capitalization rate for the property. The sales approach uses comparable sales prices in the market. When an internal evaluation is used, we place greater reliance on the income approach to value the collateral.

The Company may restructure a loan to enable a borrower experiencing financial difficulties to continue making payments when it is deemed to be in the Company's best long-term interest. This restructure may include reducing the interest rate or amount of the monthly payment for a specified period of time, after which the interest rate and repayment terms revert to the original terms of the loan. We classify these loans as Troubled Debt Restructured ("TDR").

These restructurings have not included a reduction of principal balance. The Company believes that restructuring these loans in this manner will allow certain borrowers to become and remain current on their loans. All loans classified as TDR are considered impaired, however TDR loans which have been current for six consecutive months at the time they are restructured as TDR remain on accrual status and are not included as part of non-performing loans. Loans which were delinquent at the time they are restructured as a TDR are placed on non-accrual status and reported as non-accrual performing TDR loans until they have made timely payments for six consecutive months.

The allocation of a portion of the allowance for loan losses for a performing TDR loan is based upon the present value of the future expected cash flows discounted at the loan's original effective rate, or for a non-performing TDR loan which is collateral dependent, the fair value of the collateral. At September 30, 2018, there were no commitments to lend additional funds to borrowers whose loans were modified to a TDR. The modification of loans to a TDR did not have a significant effect on our operating results, nor did it require a significant allocation of the allowance for loan losses.

The following tables shows loans modified and classified as TDR during the periods indicated:

(Dollars in thousands)	For the three months ended	
	September 30, 2018	September 30, 2017
	Number	Number
	Balance	Balance
	Modification description	Modification description

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Taxi medallion	-	\$-		4	\$1,306	Loan amortization extension
Commercial business and other	1	1,620	Loan amortization extension	-	-	
Total	1	\$1,620		4	\$1,306	

(Dollars in thousands)	For the nine months ended September 30, 2018		September 30, 2017		Modification description
	Number	Balance	Number	Balance	
Taxi medallion	-	\$-	9	\$5,595	All Loan amortization extension, with three loans also receiving a below market rate
Commercial business and other	1	1,620	-	-	Loan amortization extension
Total	1	\$1,620	9	\$5,595	

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The recorded investment of the loans modified and classified as TDR presented in the table above, were unchanged as there was no principal forgiven in this modification.

The following table shows our recorded investment for loans classified as TDR that are performing according to their restructured terms at the periods indicated:

(Dollars in thousands)	September 30, 2018		December 31, 2017	
	Number of contracts	Recorded investment	Number of contracts	Recorded investment
Multi-family residential	7	\$ 1,927	9	\$ 2,518
Commercial real estate	-	-	2	1,986
One-to-four family - mixed-use property	5	1,713	5	1,753
One-to-four family - residential	3	557	3	572
Taxi medallion	19	5,366	20	5,916
Commercial business and other	3	1,885	2	462
Total performing troubled debt restructured	37	\$ 11,448	41	\$ 13,207

During the nine months ended September 30, 2018, we sold one commercial real estate TDR loan totaling \$1.8 million, for a loss of \$0.3 million and foreclosed on one taxi medallion TDR loan of \$35,000, which is included in “Other Assets”. There were no TDR loans that defaulted during the period, which were within 12 months of their modification date.

The following table shows our recorded investment for loans classified as TDR that are not performing according to their restructured terms at the periods indicated:

September 30, 2018	December 31, 2017
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(Dollars in thousands)	Number of investment contracts	Recorded of investment contracts	Number of investment contracts	Recorded of investment contracts
Multi-family residential	1	\$ 383	1	\$ 383
Total troubled debt restructurings that subsequently defaulted	1	\$ 383	1	\$ 383

There were no TDR loans transferred to non-performing status during the three and nine months ended September 30, 2018 and 2017.



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(Unaudited)

The following table shows our non-performing loans at the periods indicated:

(In thousands)	September 30, 2018	December 31, 2017
Loans ninety days or more past due and still accruing:		
Commercial real estate	\$ 111	\$ 2,424
Total	111	2,424
Non-accrual mortgage loans:		
Multi-family residential	862	3,598
Commercial real estate	1,398	1,473
One-to-four family - mixed-use property	795	1,867
One-to-four family - residential	6,610	7,808
Total	9,665	14,746
Non-accrual non-mortgage loans:		
Small Business Administration	1,395	46
Taxi medallion	712	918
Commercial business and other	761	-
Total	2,868	964
Total non-accrual loans	12,533	15,710
Total non-performing loans	\$ 12,644	\$ 18,134

The following is a summary of interest foregone on non-accrual loans and loans classified as TDR for the periods indicated:

For the three months ended September 30,	For the nine months ended September 30,
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	2018	2017	2018	2017
	(In thousands)			
Interest income that would have been recognized had the loans performed in accordance with their original terms	\$398	\$401	\$1,194	\$1,249
Less: Interest income included in the results of operations	173	166	487	434
Total foregone interest	\$225	\$235	\$707	\$815

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(Unaudited)

The following tables show an age analysis of our recorded investment in loans, including loans past maturity, at the periods indicated:

<i>(In thousands)</i>	September 30, 2018				Current	Total Loans
	30 - 59 Days Past Due	60 - 89 Days Past Due	Greater than 90 Days	Total Past Due		
Multi-family residential	\$3,233	\$486	\$863	\$4,582	\$2,230,788	\$2,235,370
Commercial real estate	562	2,025	1,509	4,096	1,456,459	1,460,555
One-to-four family - mixed-use property	1,657	362	796	2,815	562,487	565,302
One-to-four family - residential	1,382	266	6,610	8,258	180,717	188,975
Co-operative apartments	-	-	-	-	7,771	7,771
Construction loans	-	-	-	-	40,239	40,239
Small Business Administration	145	-	1,395	1,540	12,782	14,322
Taxi medallion	-	-	-	-	6,078	6,078
Commercial business and other	5	-	760	765	845,459	846,224
Total	\$6,984	\$3,139	\$11,933	\$22,056	\$5,342,780	\$5,364,836

<i>(In thousands)</i>	December 31, 2017				Current	Total Loans
	30 - 59 Days Past Due	60 - 89 Days Past Due	Greater than 90 Days	Total Past Due		
Multi-family residential	\$2,533	\$279	\$3,598	\$6,410	\$2,267,185	\$2,273,595
Commercial real estate	1,680	2,197	3,897	7,774	1,360,338	1,368,112
One-to-four family - mixed-use property	1,570	860	1,867	4,297	559,909	564,206
One-to-four family - residential	1,921	680	7,623	10,224	170,439	180,663
Co-operative apartments	-	-	-	-	6,895	6,895
Construction loans	-	-	-	-	8,479	8,479
Small Business Administration	-	-	-	-	18,479	18,479
Taxi medallion	-	108	-	108	6,726	6,834

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Commercial business and other	2	-	-	2	732,971	732,973
Total	\$7,706	\$4,124	\$16,985	\$28,815	\$5,131,421	\$5,160,236

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**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

The following tables show the activity in the allowance for loan losses for the three month periods indicated:

September 30, 2018

(In thousands)	Multi-family residential	Commercial real estate	One-to-four family - mixed-use property	One-to-four family - residential	Construction loans	Small Business Administration	Taxi medallion	Commercial business and other	Unallocated	Total
Allowance for credit losses:										
Beginning balance	\$ 5,538	\$ 4,726	\$ 2,297	\$ 1,003	\$ 264	\$ 549	\$ -	\$ 5,832	\$ 11	\$ 20,220
Charge-off's	(18 )	-	(3 )	-	-	(144 )	(40 )	(15 )	-	(220 )
Recoveries	-	-	39	258	-	10	-	2	-	309
Provision (Benefit)	37	(650 )	(407 )	(382 )	(2 )	138	40	1,186	40	-
Ending balance	\$ 5,557	\$ 4,076	\$ 1,926	\$ 879	\$ 262	\$ 553	\$ -	\$ 7,005	\$ 51	\$ 20,309

September 30, 2017

(In thousands)	Multi-family residential	Commercial real estate	One-to-four family - mixed-use property	One-to-four family - residential	Construction loans	Small Business Administration	Taxi medallion	Commercial business and other	Unallocated	Total
Allowance for credit losses:										
Beginning balance	\$ 5,917	\$ 4,688	\$ 2,568	\$ 990	\$ 130	\$ 306	\$ 2,330	\$ 4,668	\$ 560	\$ 22,157
Charge-off's	(290 )	-	(1 )	-	-	-	-	(33 )	-	(324 )
Recoveries	66	25	-	58	-	17	-	4	-	170
Provision (Benefit)	43	(86 )	(49 )	(90 )	(13 )	70	3,661	290	(560 )	3,266
Ending balance	\$ 5,736	\$ 4,627	\$ 2,518	\$ 958	\$ 117	\$ 393	\$ 5,991	\$ 4,929	\$ -	\$ 25,269



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(Unaudited)

The following tables show the activity in the allowance for loan losses for the nine month periods indicated:

September 30, 2018

(In thousands)	Multi-family residential	Commercial real estate	One-to-four family - mixed-use property	One-to-four family - residential	Construction loans	Small Business Administration	Taxi medallion	Commercial business and other	Unallocated	Total
Allowance for credit losses:										
Beginning balance	\$ 5,823	\$ 4,643	\$ 2,545	\$ 1,082	\$ 68	\$ 669	\$ -	\$ 5,521	\$ -	\$ 20,351
Charge-off's	(99 )	-	(3 )	(1 )	-	(196 )	(393 )	(29 )	-	(721 )
Recoveries	2	-	118	370	-	25	-	11	-	526
Provision (Benefit)	(169 )	(567 )	(734 )	(572 )	194	55	393	1,502	51	153
Ending balance	\$ 5,557	\$ 4,076	\$ 1,926	\$ 879	\$ 262	\$ 553	\$ -	\$ 7,005	\$ 51	\$ 20,309

September 30, 2017

(In thousands)	Multi-family residential	Commercial real estate	One-to-four family - mixed-use property	One-to-four family - residential	Construction loans	Small Business Administration	Taxi medallion	Commercial business and other	Unallocated	Total
Allowance for credit losses:										
Beginning balance	\$ 5,923	\$ 4,487	\$ 2,903	\$ 1,015	\$ 92	\$ 481	\$ 2,243	\$ 4,492	\$ 593	\$ 22,229
Charge-off's	(452 )	(4 )	(36 )	(170 )	-	(89 )	(54 )	(48 )	-	(853 )
Recoveries	297	93	68	58	-	66	-	45	-	627
Provision (Benefit)	(32 )	51	(417 )	55	25	(65 )	3,802	440	(593 )	3,266
Ending balance	\$ 5,736	\$ 4,627	\$ 2,518	\$ 958	\$ 117	\$ 393	\$ 5,991	\$ 4,929	\$ -	\$ 25,269





**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

The following tables show the manner in which loans were evaluated for impairment at the periods indicated:

September 30, 2018

(In thousands)	Multi-family residential	Commercial real estate	One-to-four family - mixed-use property	One-to-four family-residential	Co-operative apartments	Construction loans	Small Business Administration
Financing Receivables:							
Ending Balance	\$2,235,370	\$1,460,555	\$565,302	\$188,975	\$7,771	\$40,239	\$14,322
Ending balance: individually evaluated for impairment	\$5,023	\$4,206	\$3,680	\$7,561	\$-	\$-	\$1,429
Ending balance: collectively evaluated for impairment	\$2,230,347	\$1,456,349	\$561,622	\$181,414	\$7,771	\$40,239	\$12,893
Allowance for credit losses:							
Ending balance: individually evaluated for impairment	\$102	\$-	\$151	\$53	\$-	\$-	\$-
Ending balance: collectively evaluated for impairment	\$5,455	\$4,076	\$1,775	\$826	\$-	\$262	\$553

December 31, 2017

(In thousands)	Multi-family residential	Commercial real estate	One-to-four family - mixed-use	One-to-four family-residential	Co-operative apartments	Construction loans	Small Business Administration
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## property

Financing Receivables:							
Ending Balance	\$2,273,595	\$1,368,112	\$564,206	\$180,663	\$6,895	\$8,479	\$18,479
Ending balance:							
individually evaluated for impairment	\$7,311	\$9,089	\$5,445	\$9,686	\$-	\$-	\$137
Ending balance:							
collectively evaluated for impairment	\$2,266,284	\$1,359,023	\$558,761	\$170,977	\$6,895	\$8,479	\$18,342
Allowance for credit losses:							
Ending balance:							
individually evaluated for impairment	\$205	\$177	\$198	\$56	\$-	\$-	\$-
Ending balance:							
collectively evaluated for impairment	\$5,618	\$4,466	\$2,347	\$1,026	\$-	\$68	\$669

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

The following table shows our recorded investment, unpaid principal balance and allocated allowance for loan losses for impaired loans at the periods indicated:

	September 30, 2018			December 31, 2017		
	Recorded Investment	Unpaid Principal Balance	Related Allowance	Recorded Investment	Unpaid Principal Balance	Related Allowance
(In thousands)						
With no related allowance recorded:						
Mortgage loans:						
Multi-family residential	\$3,741	\$4,288	\$ -	\$5,091	\$5,539	\$ -
Commercial real estate	4,206	4,206	-	7,103	7,103	-
One-to-four family mixed-use property	2,484	2,703	-	4,218	4,556	-
One-to-four family residential	7,158	7,792	-	9,272	10,489	-
Non-mortgage loans:						
Small Business Administration	1,429	1,577	-	137	151	-
Taxi medallion	6,078	17,343	-	6,834	18,063	-
Commercial business and other	24,773	25,142	-	313	682	-
Total loans with no related allowance recorded	49,869	63,051	-	32,968	46,583	-
With an allowance recorded:						
Mortgage loans:						
Multi-family residential	1,282	1,282	102	2,220	2,220	205
Commercial real estate	-	-	-	1,986	1,986	177
One-to-four family mixed-use property	1,196	1,196	151	1,227	1,227	198
One-to-four family residential	403	403	53	414	414	56
Non-mortgage loans:						
Commercial business and other	286	286	2	348	348	6
Total loans with an allowance recorded	3,167	3,167	308	6,195	6,195	642
Total Impaired Loans:						
Total mortgage loans	\$20,470	\$21,870	\$ 306	\$31,531	\$33,534	\$ 636
Total non-mortgage loans	\$32,566	\$44,348	\$ 2	\$7,632	\$19,244	\$ 6



**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

The following table shows our average recorded investment and interest income recognized for impaired loans for the three months ended:

	September 30, 2018		September 30, 2017	
	Average	Interest	Average	Interest
	Recorded	Recognized	Recorded	Recognized
	Investment	Investment	Investment	Investment
	(In thousands)			
With no related allowance recorded:				
Mortgage loans:				
Multi-family residential	\$4,013	\$ 31	\$2,451	\$ 12
Commercial real estate	4,587	50	5,142	60
One-to-four family mixed-use property	3,452	28	5,269	45
One-to-four family residential	7,742	7	10,023	29
Construction	365	-	890	15
Non-mortgage loans:				
Small Business Administration	739	31	260	5
Taxi medallion	6,152	84	3,177	19
Commercial business and other	20,301	482	1,254	6
Total loans with no related allowance recorded	47,351	713	28,466	191
With an allowance recorded:				
Mortgage loans:				
Multi-family residential	1,740	19	2,242	28
Commercial real estate	-	-	2,040	24
One-to-four family mixed-use property	1,201	15	1,445	16
One-to-four family residential	405	4	422	4
Non-mortgage loans:				
Taxi medallion	-	-	14,716	73
Commercial business and other	297	4	385	5
Total loans with an allowance recorded	3,643	42	21,250	150
Total Impaired Loans:				
Total mortgage loans	\$23,505	\$ 154	\$29,924	\$ 233
Total non-mortgage loans	\$27,489	\$ 601	\$19,792	\$ 108



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The following table shows our average recorded investment and interest income recognized for impaired loans for the nine months ended:

	September 30, 2018		September 30, 2017	
	Average	Interest	Average	Interest
	Recorded	Recognized	Recorded	Recognized
	Investment	Investment	Investment	Investment
	(In thousands)			
With no related allowance recorded:				
Mortgage loans:				
Multi-family residential	\$4,201	\$ 67	\$2,650	\$ 57
Commercial real estate	5,300	176	5,881	214
One-to-four family mixed-use property	3,759	108	5,399	123
One-to-four family residential	7,974	32	10,062	85
Construction	243	10	794	22
Non-mortgage loans:				
Small Business Administration	526	33	230	9
Taxi medallion	6,307	252	3,771	74
Commercial business and other	13,560	792	1,584	93
Total loans with no related allowance recorded	41,870	1,470	30,371	677
With an allowance recorded:				
Mortgage loans:				
Multi-family residential	1,896	78	2,391	107
Commercial real estate	1,206	39	2,039	72
One-to-four family mixed-use property	407	12	1,379	50
One-to-four family residential	-	-	422	12
Non-mortgage loans:				
Taxi medallion	-	-	14,663	166
Commercial business and other	307	13	383	17
Total loans with an allowance recorded	3,816	142	21,277	424
Total Impaired Loans:				
Total mortgage loans	\$24,986	\$ 522	\$31,017	\$ 742
Total non-mortgage loans	\$20,700	\$ 1,090	\$20,631	\$ 359





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In accordance with our policy and the current regulatory guidelines, we designate loans as “Special Mention,” which are considered “Criticized Loans,” and “Substandard,” “Doubtful,” or “Loss,” which are considered “Classified Loans”. If a loan does not fall within one of the previous mentioned categories then the loan would be considered “Pass.” Loans that are non-accrual are designated as Substandard, Doubtful or Loss. These loan designations are updated quarterly. We designate a loan as Substandard when a well-defined weakness is identified that may jeopardize the orderly liquidation of the debt. We designate a loan Doubtful when it displays the inherent weakness of a Substandard loan with the added provision that collection of the debt in full, on the basis of existing facts, is highly improbable. We designate a loan as Loss if it is deemed the debtor is incapable of repayment. The Company does not hold any loans designated as Loss, as loans that are designated as Loss are charged to the Allowance for Loan Losses. We designate a loan as Special Mention if the asset does not warrant classification within one of the other classifications, but does contain a potential weakness that deserves closer attention.

The following table sets forth the recorded investment in loans designated as Criticized or Classified at the periods indicated:

(In thousands)	September 30, 2018				
	Special Mention	Substandard	Doubtful	Loss	Total
Multi-family residential	\$3,092	\$ 3,095	\$ -	\$ -	\$6,187
Commercial real estate	2,969	4,206	-	-	7,175
One-to-four family - mixed-use property	1,215	1,967	-	-	3,182
One-to-four family - residential	480	7,005	-	-	7,485
Small Business Administration	487	274	-	-	761
Taxi medallion	-	6,078	-	-	6,078
Commercial business and other	749	25,050	-	-	25,799
Total loans	\$8,992	\$ 47,675	\$ -	\$ -	\$56,667

(In thousands)	December 31, 2017				
	Special Mention	Substandard	Doubtful	Loss	Total
Multi-family residential	\$6,389	\$ 4,793	\$ -	\$ -	\$11,182
Commercial real estate	2,020	8,871	-	-	10,891
One-to-four family - mixed-use property	2,835	3,691	-	-	6,526
One-to-four family - residential	2,076	9,115	-	-	11,191
Small Business Administration	548	108	-	-	656

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Taxi medallion	-	6,834	-	-	6,834
Commercial business and other	14,859	545	-	-	15,404
Total loans	\$28,727	\$ 33,957	\$ -	\$ -	\$62,684

Commitments to extend credit (principally real estate mortgage loans) and lines of credit (principally home equity lines of credit and business lines of credit) amounted to \$45.0 million and \$304.1 million, respectively, at September 30, 2018.

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**6. Loans held for sale**

Loans held for sale are carried at the lower of cost or estimated fair value. At September 30, 2018 and December 31, 2017, the Bank did not have any loans held for sale.

The Company has implemented a strategy of selling certain delinquent and non-performing loans. Once the Company has decided to sell a loan, the sale usually closes in a short period of time, generally within the same quarter. Loans designated held for sale are reclassified from loans held for investment to loans held for sale. Terms of sale include cash due upon the closing of the sale, no contingencies or recourse to the Company and servicing is released to the buyer. Additionally, at times the Company may sell participating interests in performing loans.

The following tables show loans sold during the period indicated:

<i>(Dollars in thousands)</i>	For the three months ended September 30, 2018			
	Loans sold	Proceeds	Net Recoveries (Charge-offs)	Net gain
Delinquent and non-performing loans				
Multi-family residential	1	\$ 595	\$ -	\$-
Commercial real estate	1	2,500	-	-
One-to-four family - mixed-use property	2	725	(4 )	-
One-to-four family - residential	2	390	72	10
Total	6	\$ 4,210	\$ 68	\$ 10

For the three months  
ended September 30,

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	2017		
<i>(Dollars in thousands)</i>	Loans sold	Proceeds	Net gain (loss)
Delinquent and non-performing loans			
Multi-family residential	2	\$707	\$30
Commercial real estate	3	1,118	34
One-to-four family - mixed-use property	3	913	115
Total	8	\$2,738	\$179
Performing loans			
Multi-family residential	10	\$12,704	\$(22 )
Commercial real estate	2	17,832	(7 )
Small Business Administration	1	142	2
Total	13	\$30,678	\$(27 )

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(Unaudited)

<i>(Dollars in thousands)</i>	For the nine months ended September 30, 2018			
	Loans sold	Proceeds	Net Recoveries (Charge-offs)	Net gain (loss)
<b>Delinquent and non-performing loans</b>				
Multi-family residential	4	\$ 1,559	\$ -	\$-
Commercial real estate	4	6,065	-	(235)
One-to-four family - mixed-use property	2	725	(4 )	-
One-to-four family - residential	2	390	72	10
<b>Total</b>	<b>12</b>	<b>\$ 8,739</b>	<b>\$ 68</b>	<b>\$(225)</b>
<b>Performing loans</b>				
Small Business Administration	9	\$ 5,671	\$ -	\$393
<b>Total</b>	<b>9</b>	<b>\$ 5,671</b>	<b>\$ -</b>	<b>\$393</b>

<i>(Dollars in thousands)</i>	For the nine months ended September 30, 2017			
	Loans sold	Proceeds	Net charge-offs	Net gain (loss)
<b>Delinquent and non-performing loans</b>				
Multi-family residential	2	\$707	\$ -	\$30
Commercial real estate	4	1,453	(4 )	35
One-to-four family - mixed-use property	8	2,703	(33 )	143
<b>Total</b>	<b>14</b>	<b>\$4,863</b>	<b>\$ (37 )</b>	<b>\$208</b>
<b>Performing loans</b>				
Multi-family residential	12	\$18,784	\$ -	\$(36 )
Commercial real estate	7	26,283	-	(28 )
Small Business Administration	8	5,061	-	252
<b>Total</b>	<b>27</b>	<b>\$50,128</b>	<b>\$ -</b>	<b>\$188</b>

## **7. Other Real Estate Owned**

During the nine months ended September 30, 2018 we foreclosed on one residential real estate property for \$0.6 million. During the three months ended September 30, 2018 and the three and nine months ended September 30, 2017, we did not foreclose on any consumer mortgages through in-substance repossession. We did not hold any foreclosed residential real estate properties at September 30, 2018 and December 31, 2017. Included within net loans as of September 30, 2018 and December 31, 2017 was a recorded investment of \$8.1 million and \$10.5 million, respectively, of consumer mortgage loans secured by residential real estate properties for which formal foreclosure proceedings were in process according to local requirements of the applicable jurisdiction.

## **8. Stock-Based Compensation**

For the three months ended September 30, 2018 and 2017, the Company's net income, as reported, includes \$1.1 million and \$1.1 million, respectively, of stock-based compensation costs and \$0.2 million and \$0.4 million of income tax benefits, respectively, related to the stock-based compensation plans in each of the periods. For the nine months ended September 30, 2018 and 2017, the Company's net income, as reported, includes \$5.7 million and \$5.2 million, respectively, of stock-based compensation costs and \$1.2 million and \$1.7 million of income tax benefits, respectively, related to the stock-based compensation plans in each of the periods. The Company did not grant any restricted stock units during the three months ended September 30, 2018 and 2017. During the nine months ended September 30, 2018 and 2017, the Company granted 280,590 and 276,900 restricted stock units, respectively. The Company has not granted stock options since 2009. At September 30, 2018, the Company had 600 stock options, all 100% vested, outstanding, at an average exercise price of \$8.44 per share.

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The Company uses the fair value of the common stock on the date of award to measure compensation cost for restricted stock unit awards. Compensation cost is recognized over the vesting period of the award using the straight-line method.

The following table summarizes the Company’s restricted stock unit (“RSU”) awards at or for the nine months ended September 30, 2018:

	Shares	Weighted-Average Grant-Date Fair Value
Non-vested at December 31, 2017	497,322	\$ 22.46
Granted	280,590	28.19
Vested	(248,319)	23.68
Forfeited	(11,955 )	25.31
Non-vested at September 30, 2018	517,638	\$ 24.91
Vested but unissued at September 30, 2018	234,799	\$ 25.14

As of September 30, 2018, there was \$9.4 million of total unrecognized compensation cost related to RSU awards granted. That cost is expected to be recognized over a weighted-average period of 3.0 years. The total fair value of awards vested for the three months ended September 30, 2018 and 2017 was \$0.2 million and \$14,000, respectively. The total fair value of awards vested for each of the nine month periods ended September 30, 2018 and 2017 was \$7.0 million. The vested but unissued RSU awards consist of awards made to employees and directors who are eligible for retirement. According to the terms of these awards, which provide for vesting upon retirement, these employees and directors have no risk of forfeiture. These shares will be issued at the original contractual vesting and settlement dates.

*Phantom Stock Plan:* The Company maintains a non-qualified phantom stock plan as a supplement to its profit sharing plan for officers who have achieved the designated level and completed one year of service. The Company adjusts its liability under this plan to the fair value of the shares at the end of each period.

The following table summarizes the Phantom Stock Plan at or for the nine months ended September 30, 2018:

Phantom Stock Plan	Shares	Fair Value
Outstanding at December 31, 2017	89,180	\$27.50
Granted	9,750	27.47
Forfeited	-	-
Distributions	(65 )	26.16
Outstanding at September 30, 2018	98,865	\$24.40
Vested at September 30, 2018	98,397	\$24.40

The Company recorded stock-based compensation benefit for the Phantom Stock Plan of \$0.1 million and \$0.2 million for the three months ended September 30, 2018 and 2017, respectively. The total fair value of the distributions from the Phantom Stock Plan was less than \$1,000 and \$0.2 million for the three months ended September 30, 2018 and 2017, respectively.

For the nine months ended September 30, 2018 and 2017, the company recorded stock-based compensation benefit for the Phantom Stock Plan of \$0.2 million and \$0.1 million, respectively. The total fair value of the distributions from the Phantom Stock Plan was \$2,000 and \$0.2 million for the nine months ended September 30, 2018 and 2017, respectively.



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**9. Pension and Other Postretirement Benefit Plans**

The following table sets forth information regarding the components of net expense for the pension and other postretirement benefit plans.

(In thousands)	Three months ended		Nine months ended	
	September 30, 2018	2017	September 30, 2018	2017
<b>Employee Pension Plan:</b>				
Interest cost	\$195	\$216	\$585	\$648
Amortization of unrecognized loss	155	174	465	523
Expected return on plan assets	(363)	(348)	(1,089)	(1,044)
Net employee pension (benefit) expense	\$(13 )	\$42	\$(39 )	\$127
<b>Outside Director Pension Plan:</b>				
Service cost	\$11	\$10	\$33	\$30
Interest cost	19	23	60	69
Amortization of unrecognized gain	(23 )	(23 )	(69 )	(69 )
Amortization of past service liability	3	10	9	30
Net outside director pension expense	\$10	\$20	\$33	\$60
<b>Other Postretirement Benefit Plans:</b>				
Service cost	\$88	\$79	\$264	\$237
Interest cost	77	76	231	228
Amortization of past service credit	(13 )	(21 )	(37 )	(64 )
Net other postretirement expense	\$152	\$134	\$458	\$401

The Company previously disclosed in its Consolidated Financial Statements for the year ended December 31, 2017 that it expects to contribute \$0.2 million to each of the Outside Director Pension Plan (the “Outside Director Pension Plan”) and the other postretirement benefit plans (the “Other Postretirement Benefit Plans”), during the year ending December 31, 2018. The Company does not expect to make a contribution to the Employee Pension Plan (the “Employee Pension Plan”). As of September 30, 2018, the Company has contributed \$72,000 to the Outside Director Pension Plan and \$64,000 in contributions were made to the Other Postretirement Benefit Plans. As of September 30, 2018, the Company has not revised its expected contributions for the year ending December 31, 2018.

## **10. Fair Value of Financial Instruments**

The Company carries certain financial assets and financial liabilities at fair value in accordance with GAAP which 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, establishes a framework for measuring fair value and expands disclosures about fair value measurements. GAAP permits entities to choose to measure many financial instruments and certain other items at fair value. At September 30, 2018, the Company carried financial assets and financial liabilities under the fair value option with fair values of \$13.9 million and \$40.2 million, respectively. At December 31, 2017, the Company carried financial assets and financial liabilities under the fair value option with fair values of \$14.3 million and \$37.0 million, respectively. The Company did not elect to carry any additional financial assets or financial liabilities under the fair value option during the three and nine months ended September 30, 2018.

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The following table presents the financial assets and financial liabilities reported at fair value under the fair value option, and the changes in fair value included in the Consolidated Statement of Income – Net gain (loss) from fair value adjustments, at or for the periods ended as indicated:

	Fair Value	Fair Value	Changes in Fair Values For Items Measured at Fair Value Pursuant to Election of the Fair Value Option			
	Measurements at September 30, 2018	Measurements at December 31, 2017	Three Months Ended September 30, 2018	September 30, 2017	September 30, 2018	September 30, 2017
(In thousands)						
Mortgage-backed securities	\$ 1,330	\$ 1,590	\$(6 )	\$(5 )	\$(17 )	\$(15 )
Other securities	12,610	12,685	(72 )	40	(272 )	184
Borrowed funds	40,151	36,986	(607)	(925 )	(3,155)	(2,090 )
Net loss from fair value adjustments <sup>(1)(2)</sup>			\$(685)	\$(890 )	\$(3,444)	\$(1,921 )

The net loss from fair value adjustments presented in the above table does not include net gains (losses) of \$0.5 (1) million and (\$0.4) million for the three months ended September 30, 2018 and 2017, respectively, from the change in the fair value of interest rate swaps.

The net loss from fair value adjustments presented in the above table does not include net gains (losses) of \$2.9 (2) million and (\$0.9) million for the nine months ended September 30, 2018 and 2017, respectively, from the change in the fair value of interest rate swaps.

Included in the fair value of the financial assets and financial liabilities selected for the fair value option is the accrued interest receivable or payable for the related instrument. The Company reports as interest income or interest expense in the Consolidated Statement of Income, the interest receivable or payable on the financial instruments selected for the fair value option at their respective contractual rates.

The borrowed funds had a contractual principal amount of \$61.9 million at both September 30, 2018 and December 31, 2017. The fair value of borrowed funds includes accrued interest payable of \$0.2 million at September 30, 2018 and December 31, 2017.

The Company generally holds its earning assets, other than securities available for sale, to maturity and settles its liabilities at maturity. However, fair value estimates are made at a specific point in time and are based on relevant market information. These estimates do not reflect any premium or discount that could result from offering for sale at one time the Company's entire holdings of a particular instrument. Accordingly, as assumptions change, such as interest rates and prepayments, fair value estimates change and these amounts may not necessarily be realized in an immediate sale.

Disclosure of fair value does not require fair value information for items that do not meet the definition of a financial instrument or certain other financial instruments specifically excluded from its requirements. These items include core deposit intangibles and other customer relationships, premises and equipment, leases, income taxes and equity.

Further, fair value disclosure does not attempt to value future income or business. These items may be material and accordingly, the fair value information presented does not purport to represent, nor should it be construed to represent, the underlying "market" or franchise value of the Company.

Financial assets and financial liabilities reported at fair value are required to be measured based on either: (1) quoted prices in active markets for identical financial instruments (Level 1); (2) significant other observable inputs (Level 2); or (3) significant unobservable inputs (Level 3).

A description of the methods and significant assumptions utilized in estimating the fair value of the Company's assets and liabilities that are carried at fair value on a recurring basis are as follows:

Level 1 – where quoted market prices are available in an active market. At September 30, 2018 and December 31, 2017, Level 1 included one mutual fund.

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Level 2 – when quoted market prices are not available, fair value is estimated using quoted market prices for similar financial instruments and adjusted for differences between the quoted instrument and the instrument being valued. Fair value can also be estimated by using pricing models, or discounted cash flows. Pricing models primarily use market-based or independently sourced market parameters as inputs, including, but not limited to, yield curves, interest rates, equity or debt prices and credit spreads. In addition to observable market information, models also incorporate maturity and cash flow assumptions. At September 30, 2018 and December 31, 2017, Level 2 included mortgage related securities, corporate debt, municipals and interest rate swaps.

Level 3 – when there is limited activity or less transparency around inputs to the valuation, financial instruments are classified as Level 3. At September 30, 2018 and December 31, 2017, Level 3 included trust preferred securities owned and junior subordinated debentures issued by the Company.

The methods described above may produce fair values that may not be indicative of net realizable value or reflective of future fair values. While the Company believes, its valuation methods are appropriate and consistent with those of other market participants, the use of different methodologies, assumptions and models to determine fair value of certain financial instruments could produce different estimates of fair value at the reporting date.

The following table sets forth the assets and liabilities that are carried at fair value on a recurring basis and their respective category in the fair value hierarchy, at September 30, 2018 and December 31, 2017:

	Quoted Prices in Active Markets for Identical Assets (Level 1)		Significant Other Observable Inputs (Level 2)		Significant Other Unobservable Inputs (Level 3)		Total carried at fair value on a recurring basis	
	2018	2017	2018	2017	2018	2017	2018	2017
(In thousands)								
Assets:								
Mortgage-backed Securities	\$-	\$-	\$528,119	\$509,650	\$-	\$-	\$528,119	\$509,650
Other securities	11,405	11,575	220,303	216,019	1,205	1,110	232,913	228,704
Interest rate swaps	-	-	32,600	7,388	-	-	32,600	7,388
Total assets	\$11,405	\$11,575	\$781,022	\$733,057	\$1,205	\$1,110	\$793,632	\$745,742

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Liabilities:

Borrowings	\$-	\$-	\$-	\$-	\$40,151	\$36,986	\$40,151	\$36,986
Interest rate swaps	-	-	449	3,758	-	-	449	3,758
Total liabilities	\$-	\$-	\$449	\$3,758	\$40,151	\$36,986	\$40,600	\$40,744

The following tables sets forth the Company's assets and liabilities that are carried at fair value on a recurring basis, classified within Level 3 of the valuation hierarchy for the periods indicated:

	For the three months ended			
	September 30, 2018		September 30, 2017	
	Trust preferred securities	Junior subordinated debentures	Trust preferred securities	Junior subordinated debentures
Beginning balance	\$ 1,188	\$ 39,566	\$ 7,444	\$ 35,137
Security Call	-	-	(6,300)	-
Net gain from fair value adjustment of financial assets <sup>(1)</sup>	17	-	28	-
Net loss from fair value adjustment of financial liabilities <sup>(1)</sup>	-	607	-	925
Decrease in accrued interest receivable	-	-	(89 )	-
Increase (decrease) in accrued interest payable	-	(9 )	-	9
Change in unrealized gains (losses) included in other comprehensive income	-	(13 )	-	-
Ending balance	\$ 1,205	\$ 40,151	\$ 1,083	\$ 36,071
Changes in unrealized gains (losses) held at period end	\$-	\$ (13 )	\$-	\$ -

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	For the nine months ended			
	September 30, 2018		September 30, 2017	
	Trust preferred securities	Junior subordinated debentures	Trust preferred securities	Junior subordinated debentures
	(In thousands)			
Beginning balance	\$ 1,110	\$ 36,986	\$ 7,361	\$ 33,959
Security call	-	-	(6,300)	-
Net gain from fair value adjustment of financial assets <sup>(1)</sup>	94	-	108	-
Net loss from fair value adjustment of financial liabilities <sup>(1)</sup>	-	3,155	-	2,090
Increase (Decrease) in accrued interest receivable	1	-	(88 )	-
Increase in accrued interest payable	-	42	-	22
Change in unrealized gains (losses) included in other comprehensive income	-	(32 )	2	-
Ending balance	\$ 1,205	\$ 40,151	\$ 1,083	\$ 36,071
Changes in unrealized gains (losses) held at period end	\$-	\$ (32 )	\$ 2	\$ -

<sup>(1)</sup> Totals in the table above are presented in the Consolidated Statement of Income under net gains (losses) from fair value adjustments.

During the three and nine months ended September 30, 2018 and 2017, there were no transfers between Levels 1, 2 and 3.

The following tables present the quantitative information about recurring Level 3 fair value of financial instruments and the fair value measurements at the periods indicated:

	September 30, 2018			Weighted Average
	Fair Value	Valuation Technique	Unobservable Input Range	
(Dollars in thousands)				
Assets:				

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Trust preferred securities	\$1,205	Discounted cash flows	Discount rate	n/a	5.1 %
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Liabilities:

Junior subordinated debentures	\$40,151	Discounted cash flows	Discount rate	n/a	5.1 %
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December 31, 2017

Fair Value	Valuation Technique	Unobservable Input	Range	Weighted Average
------------	---------------------	--------------------	-------	------------------

(Dollars in thousands)

Assets:

Trust preferred securities	\$1,110	Discounted cash flows	Discount rate	n/a	5.7 %
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Liabilities:

Junior subordinated debentures	\$36,986	Discounted cash flows	Discount rate	n/a	5.7 %
--------------------------------	----------	-----------------------	---------------	-----	-------

The significant unobservable inputs used in the fair value measurement of the Company's trust preferred securities and junior subordinated debentures valued under Level 3 at September 30, 2018 and December 31, 2017, are the effective yields used in the cash flow models. Significant increases or decreases in the effective yield in isolation would result in a significantly lower or higher fair value measurement.



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(Unaudited)

The following table sets forth the Company's assets and liabilities that are carried at fair value on a non-recurring basis and their respective category in the fair value hierarchy at September 30, 2018 and December 31, 2017:

	Quoted Prices in Active Markets for Identical Assets (Level 1)		Significant Other Observable Inputs (Level 2)		Significant Other Unobservable Inputs (Level 3)		Total carried at fair value on a recurring basis	
	2018	2017	2018	2017	2018	2017	2018	2017
	(In thousands)							
Assets:								
Impaired loans	\$-	\$-	\$-	\$-	\$12,798	\$16,027	\$12,798	\$16,027
Other repossessed assets	-	-	-	-	35	-	35	-
Total assets	\$-	\$-	\$-	\$-	\$12,833	\$16,027	\$12,833	\$16,027

The following tables present the qualitative information about non-recurring Level 3 fair value of financial instruments and the fair value measurements at the periods indicated:

September 30, 2018						
	Fair Value	Valuation Technique	Unobservable Input	Range		Weighted Average
	(Dollars in thousands)					
Assets:						
Impaired loans	\$1,525	Income approach	Capitalization rate Reduction for planned expedited disposal	6.5% to 15.0%	7.5%	7.0% 15.0%
Impaired loans	\$8,358	Sales approach	Adjustment to sales comparison value to reconcile differences between	-50.0% to	15.0%	-2.1%

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			comparable sales			
			Reduction for planned expedited disposal	-38.6% to	15.0%	11.1%
Impaired loans	\$2,915	Blended income and sales approach	Adjustment to sales comparison value to reconcile differences between comparable sales	-30.0% to	25.0%	-1.2%
			Capitalization rate	5.0% to	9.8%	7.5%
			Reduction for planned expedited disposal	15.0%		15.0%
Other repossessed assets	\$35	Sales approach	Reduction for planned expedited disposal	15.0%		15.0%

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**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

December 31, 2017

	Fair Value (Dollars in thousands)	Valuation Technique	Unobservable Input	Range	Weighted Average
<b>Assets:</b>					
Impaired loans	\$1,818	Income approach	Capitalization rate	6.5% to 7.5%	6.8%
			Reduction planned for expedited disposal	15.0%	15.0%
Impaired loans	\$10,003	Sales approach	Adjustment to sales comparison value to reconcile differences between comparable sales	-50.0% to 16.2%	-0.8%
			Reduction planned for expedited disposal	-30.9% to 15.0%	8.7%
Impaired loans	\$4,206	Blended income and sales approach	Adjustment to sales comparison value to reconcile differences between comparable sales	-30.0% to 25.0%	-1.2%
			Capitalization rate	5.0% to 9.8%	7.2%
			Reduction planned for expedited disposal	15.0%	15.0%

The Company did not have any liabilities that were carried at fair value on a non-recurring basis at September 30, 2018 and December 31, 2017.

The methods and assumptions used to estimate fair value at September 30, 2018 and December 31, 2017 are as follows:

**Securities:**

The fair values of securities are contained in Note 4 of Notes to Consolidated Financial Statements. Fair value is based upon quoted market prices, where available. If a quoted market price is not available, fair value is estimated using

quoted market prices for similar securities and adjusted for differences between the quoted instrument and the instrument being valued. When there is limited activity or less transparency around inputs to the valuation, securities are valued using discounted cash flows.

**Impaired Loans:**

For non-accruing loans, fair value is generally estimated by discounting management's estimate of future cash flows with a discount rate commensurate with the risk associated with such assets or, for collateral dependent loans, 85% of the appraised or internally estimated value of the property, except for taxi medallion loans. The fair value of the underlying collateral of taxi medallion loans is the most recent reported arm's length transaction. When there is no recent sale activity, the fair value is calculated using capitalization rates.

**Other Real Estate Owned and Other Repossessed Assets:**

OREO and other repossessed assets are carried at fair value less selling costs. The fair value for OREO is based on appraised value through a current appraisal, or sometimes through an internal review, additionally adjusted by the estimated costs to sell the property. The fair value for other repossessed assets are based upon the most recently reported arm's length sales transaction. When there is no recent sale activity, the fair value is calculated using capitalization rates.

**Junior Subordinated Debentures:**

The fair value of the junior subordinated debentures was developed using a credit spread based on the subordinated debt issued by the Company adjusting for differences in the junior subordinated debt's credit rating, liquidity and time to maturity. The unrealized net gain/loss attributable to changes in our own credit risk was determined by adjusting the fair value as determined in the proceeding sentence by the average rate of default on debt instruments with a similar debt rating as our junior subordinated debentures, with the difference from the original calculation and this calculation resulting in the instrument-specific unrealized gain/loss.

**Interest Rate Swaps:**

The fair value of interest rate swaps is based upon broker quotes.



**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

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The following tables set forth the carrying amounts and estimated fair values of selected financial instruments based on the assumptions described above used by the Company in estimating fair value at the periods indicated:

	September 30, 2018				
	Carrying Amount	Fair Value	Level 1	Level 2	Level 3
	(In thousands)				
<b>Assets:</b>					
Cash and due from banks	\$45,094	\$45,094	\$45,094	\$-	\$-
Securities held-to-maturity					
Mortgage-backed securities	7,958	7,221	-	7,221	-
Other securities	23,207	20,996	-	-	20,996
Securities available for sale					
Mortgage-backed securities	528,119	528,119	-	528,119	-
Other securities	232,913	232,913	11,405	220,303	1,205
Loans	5,380,062	5,301,783	-	-	5,301,783
FHLB-NY stock	54,942	54,942	-	54,942	-
Accrued interest receivable	24,673	24,673	5	1,962	22,706
Interest rate swaps	32,600	32,600	-	32,600	-
<b>Liabilities:</b>					
Deposits	\$4,716,315	\$4,706,114	\$3,153,353	\$1,552,761	\$-
Borrowings	1,197,101	1,184,589	-	1,144,438	40,151
Accrued interest payable	6,732	6,732	-	6,732	-
Interest rate swaps	449	449	-	449	-

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

	December 31, 2017				
	Carrying	Fair	Level 1	Level 2	Level 3
	Amount	Value			
	(In thousands)				
<b>Assets:</b>					
Cash and due from banks	\$51,546	\$51,546	\$51,546	\$-	\$-
Securities held-to-maturity					
Mortgage-backed securities	7,973	7,810	-	7,810	-
Other securities	22,913	21,889	-	-	21,889
Securities available for sale					
Mortgage-backed securities	509,650	509,650	-	509,650	-
Other securities	228,704	228,704	11,575	216,019	1,110
Loans	5,176,999	5,169,108	-	-	5,169,108
FHLB-NY stock	60,089	60,089	-	60,089	-
Accrued interest receivable	21,405	21,405	16	1,916	19,473
Interest rate swaps	7,388	7,388	-	7,388	-
<b>Liabilities:</b>					
Deposits	\$4,383,278	\$4,380,174	\$3,031,345	\$1,348,829	\$-
Borrowings	1,309,653	1,310,487	-	1,273,501	36,986
Accrued interest payable	2,659	2,659	-	2,659	-
Interest rate swaps	3,758	3,758	-	3,758	-

**11. Derivative Financial Instruments**

At September 30, 2018 and December 31, 2017, the Company's derivative financial instruments consist of interest rate swaps. The Company's interest rate swaps are used for three purposes: 1) to mitigate the Company's exposure to rising interest rates on a portion (\$18.0 million) of its floating rate junior subordinated debentures that have a contractual value of \$61.9 million, at September 30, 2018 and December 31, 2017; 2) to mitigate the Company's exposure to rising interest rates on certain fixed rate loans totaling \$288.1 million and \$280.2 million at September 30, 2018 and December 31, 2017, respectively; and 3) to mitigate exposure to rising interest rates on certain short-term advances totaling \$441.5 million at September 30, 2018 and December 31, 2017.

At September 30, 2018 and December 31, 2017, we held derivatives designated as cash flow hedges, fair value hedges and certain derivatives not designated as hedges.

The Company's derivative instruments are carried at fair value in the Company's financial statements as part of Other Assets for derivatives with positive fair values and Other Liabilities for derivatives with negative fair values. The accounting for changes in the fair value of a derivative instrument is dependent upon whether or not it qualifies and has been designated as a hedge for accounting purposes, and further, by the type of hedging relationship.

At September 30, 2018 and December 31, 2017, derivatives with a combined notional amount of \$36.3 million were not designated as hedges. At September 30, 2018 and December 31, 2017, derivatives with a combined notional amount of \$269.7 million and \$261.9 million were designated as fair value hedges. At September 30, 2018 and December 31, 2017, derivatives with a combined notional amount of \$441.5 million were designated as cash flow hedges.

For cash flow hedges, the effective portion of changes in the fair value of the derivative is reported in AOCL, net of tax, with the ineffective portion of changes in the fair value of the derivative is recognized directly in earnings. Amounts in accumulated other comprehensive income are reclassified into earnings in the same period during which the hedged forecasted transaction affects earnings. During the three and nine months ended September 30, 2018, \$0.1 million and \$0.2 million, respectively, was reclassified from accumulated other comprehensive loss to interest expense.



**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

Changes in the fair value of interest rate swaps not designated as hedges are reflected in “Net gain/loss from fair value adjustments” in the Consolidated Statements of Income.

The following table sets forth information regarding the Company’s derivative financial instruments at the periods indicated:

<i>(In thousands)</i>	September 30, 2018		December 31, 2017	
	Notional Amount	Net Carrying Value <sup>(1)</sup>	Notional Amount	Net Carrying Value <sup>(1)</sup>
Interest rate swaps (fair value hedge)	\$269,734	\$18,150	\$199,341	\$6,971
Interest rate swaps (fair value hedge)	-	-	62,564	(921 )
Interest rate swaps (cash flow hedge)	441,500	14,450	250,000	417
Interest rate swaps (cash flow hedge)	-	-	191,500	(7 )
Interest rate swaps (non-hedge)	36,321	(449 )	36,321	(2,830 )
Total derivatives	\$747,555	\$32,151	\$739,726	\$3,630

<sup>(1)</sup> Derivatives in a net positive position are recorded as “Other assets” and derivatives in a net negative position are recorded as “Other liabilities” in the Consolidated Statements of Financial Condition.

The following table sets forth the effect of derivative instruments on the Consolidated Statements of Income for the periods indicated:

<i>(In thousands)</i>	For the three months ended		For the nine months ended	
	September 30, 2018	September 30, 2017	September 30, 2018	September 30, 2017

Financial Derivatives:

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Interest rate swaps (non-hedge)	\$668	\$(56 )	\$2,382	\$(316)
Interest rate swaps (fair value hedge)	(153)	(351)	525	(597)
Net gain <sup>(1)</sup>	\$515	\$(407)	\$2,907	\$(913)

(1) Net gains and losses are recorded as part of “Net gain/loss from fair value adjustments” in the Consolidated Statements of Income.

During the three and nine months ended September 30, 2018 and 2017, the Company did not record any hedge ineffectiveness.

The Company’s interest rate swaps are subject to master netting arrangements between the Company and its two designated counterparties. The Company has not made a policy election to offset its derivative positions.

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

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The following tables present the effect of the master netting arrangements on the presentation of the derivative assets and liabilities in the Consolidated Statements of Condition as of the dates indicated:

		September 30, 2018				
				Gross Amounts Not Offset in the Consolidated Statement of Condition		
(In thousands)	Gross Amount of Recognized Assets	Gross Amount Offset in the Statement of Condition	Net Amount of Assets Presented in the Statement of Condition	Financial Instruments	Cash Collateral Received	Net Amount
Interest rate swaps	\$ 32,600	\$ -	\$ 32,600	\$ -	\$ 32,990	\$ (390 )

				Gross Amounts Not Offset in the Consolidated Statement of Condition		
(In thousands)	Gross Amount of Recognized Liabilities	Gross Amount Offset in the Statement of Condition	Net Amount of Liabilities Presented in the Statement of Condition	Financial Instruments	Cash Collateral Pledged	Net Amount
Interest rate swaps	\$ 449	\$ -	\$ 449	\$ -	\$ -	\$ 449

December 31, 2017

(In thousands)	Gross Amount of Recognized Assets	Gross Amount Offset in the Statement of Condition	Net Amount of Assets Presented in the Statement of Condition	Gross Amounts Not Offset in the Consolidated Statement of Condition		Net Amount
				Financial Instruments	Cash Collateral Received	
Interest rate swaps	\$7,388	\$ -	\$ 7,388	\$ -	\$ 3,660	\$ 3,728

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

(In thousands)	Gross Amount of Recognized Liabilities	Gross Amount Offset in the Statement of Condition	Net Amount of Liabilities Presented in the Statement of Condition	Gross Amounts Not Offset in the Consolidated Statement of Condition		Net Amount
				Financial Instruments	Cash Collateral Pledged	
Interest rate swaps	\$ 3,758	\$ -	\$ 3,758	\$ -	\$ -	\$ 3,758

**12. Income Taxes**

Flushing Financial Corporation files consolidated Federal and combined New York State and New York City income tax returns with its subsidiaries, with the exception of the Company's trusts, which file separate Federal income tax returns as trusts, and Flushing Preferred Funding Corporation, which files a separate Federal income tax return as a real estate investment trust. Additionally, the Bank files New Jersey State tax returns. As of September 30, 2018, the Company is undergoing examination for its Federal income tax return for 2015, its New York State income tax returns for 2014, 2015 and 2016 and its New York City income tax return for 2014.

Income tax provisions are summarized as follows:

(In thousands)	For the three months ended September 30,		For the nine months ended September 30,	
	2018	2017	2018	2017
Federal:				
Current	\$2,899	\$6,703	\$9,064	\$16,308
Deferred	(592 )	(2,023 )	(839 )	(1,303 )

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Total federal tax provision	2,307	4,680	8,225	15,005
State and Local:				
Current	33	1,398	1,722	2,817
Deferred	(430 )	(787 )	(598 )	(502 )
Total state and local tax provision (benefit)	(397 )	611	1,124	2,315
Total income tax provision	\$1,910	\$5,291	\$9,349	\$17,320

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**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

**13. Accumulated Other Comprehensive Income (Loss):**

The following tables sets forth the changes in accumulated other comprehensive income (loss) by component for the periods indicated:

	For the three months ended September 30, 2018				
	Unrealized Gains (Losses) on Available for Sale Securities (In thousands)	Unrealized Gains (Losses) on Cash flow Hedges	Defined Benefit Pension Items	Fair Value Option Elected on Liabilities	Total
Beginning balance, net of tax	\$(16,501)	\$ 8,027	\$(4,325)	\$ 792	\$(12,007)
Other comprehensive income before reclassifications, net of tax	(3,505 )	1,950	-	9	(1,546 )
Amounts reclassified from accumulated other comprehensive income, net of tax	-	(80 )	84	-	4
Net current period other comprehensive income (loss), net of tax	(3,505 )	1,870	84	9	(1,542 )
Ending balance, net of tax	\$(20,006)	\$ 9,897	\$(4,241)	\$ 801	\$(13,549)

For the three months ended September  
30, 2017

Unrealized Gains (Losses)	Unrealized Gains (Losses)	Defined Benefit Pension	Total
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	on	on	Items	
	Available	Cash flow		
	for Sale	Hedges		
	Securities			
	(In thousands)			
Beginning balance, net of tax	\$(2,110)	\$ (124 )	\$ (4,342)	\$(6,576)
Other comprehensive income before reclassifications, net of tax	(333 )	56	-	(277 )
Amounts reclassified from accumulated other comprehensive income, net of tax	108	-	81	189
Net current period other comprehensive income, net of tax	(225 )	56	81	(88 )
Ending balance, net of tax	\$(2,335)	\$ (68 )	\$ (4,261)	\$(6,664)

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**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

	For the nine months ended September 30, 2018				
	Unrealized Gains (Losses) on Available for Sale Securities (In thousands)	Unrealized Gains (Losses) on Cash flow Hedges	Defined Benefit Pension Items	Fair Value Option Elected on Liabilities	Total
Beginning balance, net of tax	\$(5,522 )	\$ 231	\$(3,695 )	\$ -	\$(8,986 )
Reclassification of the Income Tax Effects of the Tax Cuts and Jobs Act from AOCL to Retained Earnings	(1,325 )	50	(798 )	-	(2,073 )
Impact of adoption of Accounting Standard Update 2016-01	-	-	-	779	779
Other comprehensive income before reclassifications, net of tax	(13,159)	9,455	-	22	(3,682 )
Amounts reclassified from accumulated other comprehensive income (loss), net of tax	-	161	252	-	413
Net current period other comprehensive income, net of tax	(13,159)	9,616	252	22	(3,269 )
Ending balance, net of tax	\$(20,006)	\$ 9,897	\$(4,241)	\$ 801	\$(13,549)

	For the nine months ended September 30, 2017				
	Unrealized Gains (Losses) on Available for Sale Securities (In thousands)	Unrealized Gains (Losses) on Cash flow Hedges	Defined Benefit Pension Items	Fair Value Option Elected on Liabilities	Total
Beginning balance, net of tax	\$(3,859)	\$ -	\$(4,503)	\$ -	\$(8,362)

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Other comprehensive income before reclassifications, net of tax	1,416	(68 )	-	1,348
Amounts reclassified from accumulated other comprehensive income, net of tax	108	-	242	350
Net current period other comprehensive income, net of tax	1,524	(68 )	242	1,698
Ending balance, net of tax	\$(2,335)	\$ (68 )	\$(4,261)	\$(6,664)

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

The following tables set forth significant amounts reclassified from accumulated other comprehensive income (loss) by component for the periods indicated:

For the three months ended September 30, 2018

Details about Accumulated Other Comprehensive Loss Components	Amounts Reclassified from Accumulated Other Comprehensive Loss (In thousands)	Affected Line Item in the Statement Where Net Income is Presented
Cash flow hedges:		
Interest rate swaps	\$ 116 (36) \$ 80	Other interest expense Tax expense Net of tax
Amortization of defined benefit pension items:		
Actuarial losses	\$ (132) (1)	Other operating expense
Prior service credits	10 (1) (122) 38 \$ (84)	Other operating expense Total before tax Tax benefit Net of tax

For the three months ended September 30, 2017

Details about Accumulated Other Comprehensive Loss Components	Amounts Reclassified from Accumulated Other Comprehensive Loss (In thousands)	Affected Line Item in the Statement Where Net Income is Presented
Unrealized losses on available for sale securities:	\$ (186)	

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			Net loss on sale of securities
	78		Tax benefit
	\$ (108)		Net of tax
Amortization of defined benefit pension items:			
Actuarial losses	\$ (152)	(1)	Other operating expense
Prior service credits	12	(1)	Other operating expense
	(140)		Total before tax
	59		Tax benefit
	\$ (81)		Net of tax

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

For the nine months ended September 30, 2018

Details about Accumulated Other Comprehensive Loss Components	Amounts Reclassified from Accumulated Other Comprehensive Loss (In thousands)	Affected Line Item in the Statement Where Net Income is Presented
Cash flow hedges:		
Interest rate swaps	\$ (235)	Interest expense
	74	Tax benefit
	\$ (161)	Net of tax
Amortization of defined benefit pension items:		
Actuarial losses	\$ (396) (1)	Other operating expense
Prior service credits	28 (1)	Other operating expense
	(368)	Total before tax
	116	Tax benefit
	\$ (252)	Net of tax

For the nine months ended September 30, 2017

Details about Accumulated Other Comprehensive Loss Components	Amounts Reclassified from Accumulated Other Comprehensive Loss (In thousands)	Affected Line Item in the Statement Where Net Income is Presented
Unrealized losses on available for sale securities:	\$ (186)	Net loss on sale of securities
	78	Tax benefit
	\$ (108)	Net of tax
Amortization of defined benefit pension items:		
Actuarial losses	\$ (454) (1)	Other operating expense

Prior service credits	34	(1)	Other operating expense
	(420)		Total before tax
	178		Tax benefit
	\$ (242)		Net of tax

These accumulated other comprehensive loss components are included in the computation of net periodic pension (1) cost (See Note 9 of the Notes to Consolidated Financial Statements “Pension and Other Postretirement Benefit Plans”.)

#### 14. Regulatory Capital

Under current capital regulations, the Bank is required to comply with four separate capital adequacy standards. As of September 30, 2018, the Bank continues to be categorized as “well-capitalized” under the prompt corrective action regulations and continues to exceed all regulatory capital requirements. In 2016, a Capital Conservation Buffer (“CCB”) requirement became effective for banks. The CCB is designed to establish a capital range above minimum capital requirements and impose constraints on dividends, share buybacks and discretionary bonus payments when capital levels fall below prescribed levels. The minimum CCB in 2018 is 1.875% and increases 0.625% annually through 2019 to 2.5%. The CCB for the Bank at September 30, 2018 was 5.88%.

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

Set forth below is a summary of the Bank's compliance with banking regulatory capital standards.

	September 30, 2018		December 31, 2017	
	Amount	Percent of Assets	Amount	Percent of Assets
	(Dollars in thousands)			
<b>Tier I (leverage) capital:</b>				
Capital level	\$655,965	10.12 %	\$631,285	10.11 %
Requirement to be well capitalized	324,032	5.00	312,343	5.00
Excess	331,933	5.12	318,942	5.11
<b>Common Equity Tier I risk-based capital:</b>				
Capital level	\$655,965	13.46 %	\$631,285	13.87 %
Requirement to be well capitalized	316,766	6.50	295,937	6.50
Excess	339,199	6.96	335,348	7.37
<b>Tier 1 risk-based capital:</b>				
Capital level	\$655,965	13.46 %	\$631,285	13.87 %
Requirement to be well capitalized	389,865	8.00	364,230	8.00
Excess	266,100	5.46	267,055	5.87
<b>Total risk-based capital:</b>				
Capital level	\$676,274	13.88 %	\$651,636	14.31 %
Requirement to be well capitalized	487,332	10.00	455,288	10.00
Excess	188,942	3.88	196,348	4.31

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

The Holding Company is subject to the same regulatory capital requirements as the Bank. As of September 30, 2018, the Holding Company continues to be categorized as “well-capitalized” under the prompt corrective action regulations and continues to exceed all regulatory capital requirements. The CCB for the Holding Company at September 30, 2018 was 5.82%.

Set forth below is a summary of the Holding Company’s compliance with banking regulatory capital standards.

	September 30, 2018		December 31, 2017	
	Amount	Percent of Assets	Amount	Percent of Assets
	(Dollars in thousands)			
Tier I (leverage) capital:				
Capital level	\$578,034	8.92 %	\$563,426	9.02 %
Requirement to be well capitalized	324,008	5.00	312,278	5.00
Excess	254,026	3.92	251,148	4.02
Common Equity Tier I risk-based capital:				
Capital level	\$539,306	11.07 %	\$527,727	11.59 %
Requirement to be well capitalized	316,714	6.50	295,865	6.50
Excess	222,592	4.57	231,862	5.09
Tier 1 risk-based capital:				
Capital level	\$578,034	11.86 %	\$563,426	12.38 %
Requirement to be well capitalized	389,801	8.00	364,141	8.00
Excess	188,233	3.86	199,285	4.38
Total risk-based capital:				
Capital level	\$673,343	13.82 %	\$658,777	14.47 %
Requirement to be well capitalized	487,252	10.00	455,177	10.00
Excess	186,091	3.82	203,600	4.47



## **PART I – FINANCIAL INFORMATION**

### **FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES**

#### **Notes to Consolidated Financial Statements**

(Unaudited)

#### **15. New Authoritative Accounting Pronouncements**

##### *Accounting Standards Adopted in 2018:*

In February 2018, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) No. 2018-02, “Income Statement – Reporting Comprehensive Income (Topic 220).” As a result of the Tax Cuts and Jobs Act (the “TCJA”), concerns arose regarding the guidance which requires deferred tax assets and liabilities to be adjusted for the effect of a change in tax laws or rates with the effect included in income from continuing operations in the reporting period that includes the enactment date. The amendments in this ASU require a reclassification for stranded tax effects from accumulated other comprehensive income to retained earnings, furthermore eliminating the stranded tax effects resulting from the TCJA. The amount of the reclassification is the difference between the previous corporate income tax rate of 35% and the newly enacted corporate income tax rate of 21%. The amendments of this ASU are effective for fiscal years beginning after December 15, 2018, and interim periods within those fiscal years, with early adoption permitted in any interim period or fiscal year before the effective date. We have elected to early adopt this guidance as of January 1, 2018. Our Consolidated Statements of Financial Condition reflect adoption of this ASU and reclassification of \$2.1 million in stranded tax effects from accumulated other comprehensive income to retained earnings. See Note 12 “Income Taxes” for additional information.

In August 2016, the FASB issued ASU No. 2016-15 “Classification of Certain Cash Receipts and Cash Payments”, to clarify how certain cash receipts and cash payments are presented and classified in the statements of cash flows. The amendments are intended to reduce diversity in practice by clarifying whether the following items should be categorized as operating, investing or financing in the statement of cash flows: (i) debt prepayments and extinguishment costs, (ii) settlement of zero-coupon debt, (iii) settlement of contingent consideration, (iv) insurance proceeds, (v) settlement of corporate-owned life insurance (COLI) and bank-owned life insurance (BOLI) policies, (vi) distributions from equity method investees, (vii) beneficial interests in securitization transactions, and (viii) receipts and payments with aspects of more than one class of cash flows. The ASU will be effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2017. Early adoption is permitted. If an entity early adopts the amendments in an interim period, any adjustments should be reflected as of the beginning of the fiscal year that includes that interim period. An entity that elects early adoption must adopt all of the amendments in the same period. This ASU was adopted on January 1, 2018 and did not have a significant impact on the presentation of our cash flows.

In January 2016, FASB issued ASU No. 2016-01 “Financial Instruments” which requires an entity to: (i) measure equity investments at fair value through net income, with certain exceptions; (ii) present in other comprehensive income the changes in instrument-specific credit risk for financial liabilities measured using the fair value option; (iii) present financial assets and financial liabilities by measurement category and form of financial asset; (iv) calculate the fair

value of financial instruments for disclosure purposes based on an exit price and; (v) assess a valuation allowance on deferred tax assets related to unrealized losses of available for sale debt securities in combination with other deferred tax assets. The ASU provides an election to subsequently measure certain nonmarketable equity investments at cost less any impairment and adjusted for certain observable price changes. The ASU also requires a qualitative impairment assessment of such equity investments and amends certain fair value disclosure requirements. This ASU became effective for us on January 1, 2018. The adoption of the guidance resulted in a cumulative-effect adjustment totaling \$0.8 million and did not have a significant impact on our results of operations, financial condition and cash flows.

In May 2014, the FASB issued ASU 2014-09, "Revenue from Contracts with Customers (Topic 606)". This ASU establishes a comprehensive revenue recognition standard for virtually all industries under GAAP, including those that previously followed industry-specific guidance such as real estate, construction and software industries. The revenue standard's core principle is built on the contract between a vendor and a customer for the provision of goods and services. It attempts to depict the exchange of rights and obligations between the parties in the pattern of revenue recognition based on the consideration to which the vendor is entitled. The guidance in this ASU for public companies is effective for the annual periods beginning after December 15, 2016, including interim periods therein. In August 2015, the FASB approved a one-year delay of the effective date of this standard to reporting periods beginning after December 15, 2017. This ASU allows for either full retrospective adoption or modified retrospective adoption. This ASU became effective for us on January 1, 2018. We adopted this standard through the modified retrospective transition method. The modified retrospective method requires application of ASU 2014-09 to uncompleted contracts at the date of adoption; however, periods prior to the date of adoption have not been retrospectively revised as the impact of the new standard on uncompleted contracts as the date of adoption was not material as such a cumulative effective adjustment to opening retained earnings was not deemed necessary.

## **PART I – FINANCIAL INFORMATION**

### **FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES**

#### **Notes to Consolidated Financial Statements**

(Unaudited)

Topic 606 does not apply to the majority of our revenue streams which are primarily comprised of interest and dividend income and associated fees within those revenue streams. The revenue streams derived by the Company that are within the scope of Topic 606 are primarily certain banking service fees, including wire transfer fees, ATM fees, account maintenance fees, overdraft fees and other deposit fees. We generally satisfy our performance obligations on contracts with customers as services are rendered, and the transaction prices are typically fixed and charged either on a periodic basis or based on activity. Being that performance obligations are satisfied as services are rendered and the transaction prices are fixed, there is little judgment involved in applying Topic 606 that significantly affects the determination of the amount and timing of revenue from contracts with customers. Additionally, the Company will receive revenue from the sale of investment products through a third party as part of a revenue sharing agreement. This revenue is included in “Other Income” in the Consolidated Statements of Income. These fees are remitted to the Company monthly as our performance obligation is satisfied. We have evaluated the nature of our contracts with customers and determined that further disaggregation of revenue from contracts with customers into more granular categories beyond what is present in the Consolidated Statements of Income was not necessary.

#### *Accounting Standards Pending Adoption:*

In August 2018, the FASB issued ASU No. 2018-14, “Compensation – Retirement Benefits – Defined Benefit Plans – General (Subtopic 715-20)” providing targeted improvements to the disclosures required for Defined Benefit Plans. The amendments in in this Update are effective for fiscal years ended after December 15, 2020. Early adoption is permitted. The amendments are to be applied on a retrospective basis to all periods presented. We are currently evaluating the impact of adopting this new guidance on our disclosures.

In August 2018, the FASB issued ASU No. 2018-13, “Fair Value Measurement (Topic 820)”. The amendments in this Update modify the disclosure requirements on fair value measurements in Topic 820. The amendments in in this Update are effective for fiscal years, and interim periods within those fiscal years beginning after December 15, 2019. Early adoption is permitted. The amendments are to be applied on a retrospective basis to all periods presented. We are currently evaluating the impact of adopting this new guidance on our disclosures.

In August 2017, the FASB issued ASU No. 2017-12, “Derivatives and Hedging (Topic 815)” providing targeted improvements to the accounting for hedging activities, which is effective January 1, 2019, with early adoption permitted in any interim period or fiscal year before the effective date. The guidance introduces a number of amendments, several of which are optional, that are designed to simplify the application of hedge accounting, improve financial statement transparency and more closely align hedge accounting with an entity’s risk management strategies. This ASU eliminates the requirement to separately measure and report hedge ineffectiveness and changes the presentation so that all items that affect earnings are in the same income statement line as the hedged item. We are

currently evaluating the impact of adopting this new guidance on our consolidated results of operations, financial condition and cash flows.

In March 2017, the FASB issued ASU No. 2017-08, “Premium Amortization on Purchased Callable Debt Securities” which shortens the amortization period for premiums on purchased callable debt securities to the earliest call date, rather than amortizing over the full contractual term. The ASU does not change the accounting for securities held at a discount. The amendments in this ASU require companies to reset the effective yield using the payment terms of the debt security if the call option is not exercised on the earliest call date. If the security has additional future call dates, any excess of the amortized cost basis over the amount repayable by the issuer at the next call date should be amortized to the next call date. The amendments in this update are effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. Early adoption is permitted, including adoption in an interim period. If an entity early adopts the amendments in an interim period, any adjustments should be reflected as of the beginning of the fiscal year that includes that interim period. The guidance is not expected to have an impact on the Company's financial positions, results of operations or disclosures.

In January 2017, the FASB issued ASU No. 2017-04, “Intangibles - Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment.” The ASU simplifies the subsequent measurement of goodwill and eliminates Step 2 from the goodwill impairment test. Under this ASU, the Company should perform its goodwill impairment test by comparing the fair value of a reporting unit with its carrying amount. An impairment charge should be recognized for the amount by which the carrying amount exceeds the reporting unit's fair value. The impairment charge is limited to the amount of goodwill allocated to that reporting unit. The amendments in this update are effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. Early adoption is permitted for goodwill impairment tests performed on testing dates after January 1, 2017. The guidance is not expected to have a significant impact on the Company's financial positions, results of operations or disclosures.

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#### **Notes to Consolidated Financial Statements**

(Unaudited)

In June 2016, the FASB issued ASU No. 2016-13, “Financial Instruments – Credit Losses” which sets forth a “current expected credit loss” (“CECL”) model which requires the Company to measure all expected credit losses for financial instruments held at the reporting date based on historical experience, current conditions and reasonable supportable forecasts. This replaces the existing incurred loss model and will apply to the measurement of credit losses on financial assets measured at amortized cost and to some off-balance sheet credit exposures. This ASU will be effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. The Company has been collecting and evaluating data and system requirements to implement this standard. Management has developed inter-departmental steering and working committees to evaluate and implement CECL. We have chosen a vendor solution to model CECL results and are in the beginning stages of implementing this solution. The adoption of this update could have a material impact on the Company’s consolidated results of operations and financial condition. The extent of the impact is still unknown and will depend on many factors, such as the composition of the Company’s loan portfolio and expected loss history at adoption.

In February 2016, the FASB issued ASU No. 2016-02, “Leases”. From the lessee's perspective, the new standard establishes a right-of-use (“ROU”) model that requires a lessee to record a ROU asset and a lease liability on the balance sheet for all leases with terms longer than 12 months. Leases will be classified as either finance or operating, with classification affecting the pattern of expense recognition in the income statement for a lessee. From the lessor's perspective, the new standard requires a lessor to classify leases as either sales-type, finance or operating. A lease will be treated as a sale if it transfers all of the risks and rewards, as well as control of the underlying asset, to the lessee. If risks and rewards are conveyed without the transfer of control, the lease is treated as a financing. If the lessor doesn't convey risks and rewards or control, an operating lease results. The new standard is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. A modified retrospective transition approach is required for lessees for capital and operating leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements, with certain practical expedients available. A modified retrospective transition approach is required to be applied for leases in existence as of the date of initial application. Reporting entities may elect to apply the transition approach either as of the beginning of the earliest period presented in the financial statements, or as of the beginning of the period of adoption. The Company has not adopted the new accounting policy as of the filing date. The Company has yet to make an election on the method of adoption or which practical expedients, if any, will be elected. Our operating leases relate primarily to office space and bank branches. Under current accounting standards, substantially all of the Company’s leases are considered operating leases and, as such, are not recognized on the Company’s Consolidated Balance Sheet. Based on our current lease portfolio, upon adoption of the new accounting standard, we anticipate recognizing a lease liability and related right-of-use asset on our balance sheet. Management is continuing to evaluate the Company’s outstanding inventory of leases and determining the effect of recognizing operating leases on the Consolidated Statements of Financial Condition which is expected to be material. However, the final impact of the standard will depend on the company’s leases composition as of the adoption date.



**PART I – FINANCIAL INFORMATION**

**FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES**

**Management’s Discussion and Analysis of**

**Financial Condition and Results of Operations**

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

*This Quarterly Report should be read in conjunction with the more detailed and comprehensive disclosures included in our Annual Report on Form 10-K for the year ended December 31, 2017. In addition, please read this section in conjunction with our Consolidated Financial Statements and Notes to Consolidated Financial Statements contained herein.*

*As used in this Quarterly Report, the words “we,” “us,” “our” and the “Company” are used to refer to Flushing Financial Corporation and its direct and indirect wholly owned subsidiaries, Flushing Bank (the “Bank”), Flushing Preferred Funding Corporation, Flushing Service Corporation, and FSB Properties Inc.*

Statements contained in this Quarterly Report relating to plans, strategies, objectives, economic performance and trends, projections of results of specific activities or investments and other statements that are not descriptions of historical facts may be forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. Forward-looking information is inherently subject to risks and uncertainties and actual results could differ materially from those currently anticipated due to a number of factors, which include, but are not limited to, factors discussed elsewhere in this Quarterly Report and in other documents filed by us with the Securities and Exchange Commission from time to time, including, without limitation, our Annual Report on Form 10-K for the year ended December 31, 2017. Forward-looking statements may be identified by terms such as “may,” “will,” “should,” “could,” “expects,” “plans,” “intends,” “anticipates,” “believes,” “estimates,” “predicts,” “forecasts,” “potential” or “continue” or similar terms or the negative of these terms. Although we believe that the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee future results, levels of activity, performance or achievements. We have no obligation to update these forward-looking statements.

**Executive Summary**

We are a Delaware corporation organized in May 1994. The Bank was organized in 1929 as a New York State-chartered mutual savings bank. Today the Bank operates as a full-service New York State commercial bank. The Bank’s primary regulator is the New York State Department of Financial Services, and its primary federal regulator is the Federal Deposit Insurance Corporation (“FDIC”). Deposits are insured to the maximum allowable amount by the FDIC. Additionally, the Bank is a member of the Federal Home Loan Bank system. The primary business of Flushing Financial Corporation has been the operation of the Bank. The Bank owns three subsidiaries: Flushing Preferred

Funding Corporation, Flushing Service Corporation, and FSB Properties Inc. The Bank also operates an internet branch, which operates under the brands of iGObanking.com® and BankPurely® (the “Internet Branch”). The activities of Flushing Financial Corporation are primarily funded by dividends, if any, received from the Bank, issuances of subordinated debt, junior subordinated debt, and issuances of equity securities. Flushing Financial Corporation’s common stock is traded on the NASDAQ Global Select Market under the symbol “FFIC.”

Our principal business is attracting retail deposits from the general public and investing those deposits together with funds generated from ongoing operations and borrowings, primarily in (1) originations and purchases of multi-family residential loans, commercial business loans, commercial real estate mortgage loans and, to a lesser extent, one-to-four family loans (focusing on mixed-use properties, which are properties that contain both residential dwelling units and commercial units); (2) Small Business Administration (“SBA”) loans and other small business loans; (3) construction loans; (4) mortgage loan surrogates such as mortgage-backed securities; and (5) U.S. government securities, corporate fixed-income securities and other marketable securities. We also originate certain other consumer loans including overdraft lines of credit. Our results of operations depend primarily on net interest income, which is the difference between the income earned on our interest-earning assets and the cost of our interest-bearing liabilities. Net interest income is the result of our interest rate margin, which is the difference between the average yield earned on interest-earning assets and the average cost of interest-bearing liabilities, adjusted for the difference in the average balance of interest-earning assets as compared to the average balance of interest-bearing liabilities. We also generate non-interest income primarily from loan fees, service charges on deposit accounts, mortgage servicing fees, and other fees, income earned on Bank Owned Life Insurance (“BOLI”), dividends on Federal Home Loan Bank of New York stock and net gains and losses on sales of securities and loans. Our operating expenses consist principally of employee compensation and benefits, occupancy and equipment costs, other general and administrative expenses and income tax expense. Our results of operations also can be significantly affected by changes in the fair value of financial assets and financial liabilities for which changes in value are recorded through earnings, our periodic provision for loan losses and specific provision for losses on real estate owned.



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Our strategy is to continue our focus on being an institution serving consumers, businesses, and governmental units in our local markets. In furtherance of this objective, we intend to:

- increase core deposits and continue to improve funding mix to manage cost of funds;
- manage net interest income by leveraging loan pricing opportunities and portfolio mix;
- enhance earnings power by improving scalability and efficiency;
- manage credit risk;
- remain well capitalized;
- increase our commitment to the multi-cultural marketplace, with a particular focus on the Asian community in Queens;
- manage enterprise-wide risk.

There can be no assurance that we will be able to effectively implement this strategy. Our strategy is subject to change by the Board of Directors.

Our investment policy, which is approved by the Board of Directors, is designed primarily to manage the interest rate sensitivity of our overall assets and liabilities, to generate a favorable return without incurring undue interest rate risk and credit risk, to complement our lending activities and to provide and maintain liquidity. In establishing our investment strategies, we consider our business and growth strategies, the economic environment, our interest rate risk exposure, our interest rate sensitivity “gap” position, the types of securities to be held and other factors. We classify our investment securities as available for sale or held-to-maturity.

We carry a portion of our financial assets and financial liabilities at fair value and record changes in their fair value through earnings in non-interest income on our Consolidated Statements of Income and Comprehensive Income. A

description of the financial assets and financial liabilities that are carried at fair value through earnings can be found in Note 10 of the Notes to the Consolidated Financial Statements.

Our strategic focus of increasing net interest income through emphasizing rate over volume and reducing our liability sensitive position has resulted in net loans growth of 0.9% (non-annualized) for the third quarter. Similar to the prior quarter, we allowed \$62 million of participations with another financial institution to repay, as the rates offered during the refinancing process did not meet our rate criteria. Year-to-date, we have allowed approximately \$139 million of participations to repay rather than refinance at a rate below our criteria. During the quarter, approximately 70% of our new loans and 40% of our new investment securities were adjustable rate products. Additionally, approximately \$450 million of forward swaps entered in late 2017 have provided a benefit of one basis point to the quarter's net interest margin. These swaps coupled with the extension of the maturity of liabilities has mitigated our liability sensitive position.

The yield on interest-earning assets increased 17 basis points to 4.27% during the three months ended September 30, 2018, from 4.10% for the three months ended June 30, 2018, while the cost of interest-bearing liabilities increased 26 basis points to 1.76% from 1.50% during the same period. This resulted in the net interest margin declining five basis points to 2.71% for the three months ended September 30, 2018 from 2.76% for the linked quarter. The increase in the cost of interest-bearing liabilities was driven primarily by the Bank raising the rates we pay on our deposit products to stay competitive within our market and an increase in borrowing costs from recent increases in the Fed Funds rate.

As we continued to improve loan yields we have retained our focus on credit quality. Non-performing assets decreased by 30% and total delinquencies have decreased 17% since December 31, 2017. The allowance for loan losses to gross loans was 0.38% while the allowance for loan losses to non-performing loans increased to 161% from 137% in the linked quarter. The loan-to-value on our non-performing real estate loans at September 30, 2018 remains conservative at 35.1%. During the three months ended September 30, 2018 we recorded net recoveries of \$89,000.

The Bank and Company are subject to the same regulatory capital requirements. See Note 14 of the Notes to the Consolidated Financial Statements "Regulatory Capital."

## PART I – FINANCIAL INFORMATION

### FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES

#### Management's Discussion and Analysis of

#### Financial Condition and Results of Operations

### COMPARISON OF OPERATING RESULTS FOR THE THREE MONTHS ENDED

#### SEPTEMBER 30, 2018 AND 2017

**General.** Net income for the three months ended September 30, 2018 was \$17.3 million, an increase of \$7.2 million, or 70.3%, compared to \$10.2 million for the three months ended September 30, 2017. Diluted earnings per common share were \$0.61 for the three months ended September 30, 2018, an increase of \$0.26, or 74.3%, from \$0.35 for the three months ended September 30, 2017.

Return on average equity increased to 12.9% for the three months ended September 30, 2018 from 7.6% for the three months ended September 30, 2017. Return on average assets increased to 1.1% for the three months ended September 30, 2018 from 0.7% for the three months ended September 30, 2017.

**Interest Income.** Total interest and dividend income increased \$6.2 million, or 10.4%, to \$65.5 million for the three months ended September 30, 2018 from \$59.3 million for the three months ended September 30, 2017. The increase in interest income was primarily attributable to an increase of 27 basis points in the yield of interest-earning assets to 4.27% for the three months ended September 30, 2018 from 4.00% in the comparable prior year period, combined with an increase of \$194.3 million in the average balance of interest-earning assets to \$6,130.4 million for the three months ended September 30, 2018 from \$5,936.1 million for the comparable prior year period. The increase in the yield on interest-earning assets was primarily due to an increase of 28 basis points in the yield of total loans, net to 4.52% for the three months ended September 30, 2018 from 4.24% for the comparable prior year period. Additionally, interest income increased due to an increase of \$246.5 million in the average balance of total loans, net, which have a higher yield than the yield of total interest-earning assets. Excluding prepayment penalty income and recovered interest from loans, the yield on total loans, net, would have increased 20 basis points to 4.29% for the three months ended September 30, 2018 from 4.09% for the three months ended September 30, 2017.

**Interest Expense.** Interest expense increased \$7.7 million, or 47.2%, to \$24.0 million for the three months ended September 30, 2018 from \$16.3 million for the three months ended September 30, 2017. The increase in interest expense was primarily due to an increase of 53 basis points in the average cost of interest-bearing liabilities to 1.76% for the three months ended September 30, 2018 from 1.23% for the three months ended September 30, 2017, combined with an increase of \$180.0 million in the average balance of interest-bearing liabilities to \$5,455.9 million for the three months ended September 30, 2018, from \$5,275.9 million for the comparable prior year period. The 53 basis point increase in the cost of interest-bearing liabilities was primarily due to the Bank raising the rates we pay on our deposit products to stay competitive within our market and an increase in borrowing costs from increases in the Fed Funds rate.

**Net Interest Income.** For the three months ended September 30, 2018, net interest income was \$41.5 million, a decrease of \$1.5 million, or 3.5%, from \$43.0 million for the three months ended September 30, 2017. The decrease in net interest income was primarily due to the 53 basis point increase in the cost of interest-bearing liabilities to 1.76% for the three months ended September 30, 2018 from 1.23% for the comparable prior year period, partially offset by an increase of 27 basis points in the yield of interest-earning assets to 4.27% for the three months ended September 30, 2018 as compared to 4.00% for the three months ended September 30, 2017. The effects of the above on both the net interest spread and net interest margin were decreases of 26 basis points to 2.51% and 19 basis points to 2.71%, respectively, for the quarter ended September 30, 2018, compared to the quarter ended September 30, 2017. Included in net interest income was prepayment penalty income from loans for the three months ended September 30, 2018 and 2017 totaling \$1.9 million and \$1.6 million, respectively, and recovered interest from non-accrual loans totaling \$1.1 million and \$0.3 million, respectively. Without the prepayment penalty income and recovered interest, the net interest margin for the three months ended September 30, 2018 would have been 2.51%, a decrease of 26 basis points, as compared to 2.77% for the three months ended September 30, 2017.

**Provision for Loan Losses.** There was no provision for loan losses recorded for the three months ended September 30, 2018 compared to \$3.3 million for three months ended in September 30, 2017. No provision was recorded due to the Company's analysis of the adequacy of the allowance for loan losses indicating that the reserve was at an appropriate level. During the three months ended September 30, 2018, the Bank recorded net recoveries totaling \$89,000, while non-accrual loans decreased \$1.5 million to \$12.5 million at September 30, 2018 from \$14.1 million at June 30, 2018. The current average loan-to-value ratio for our non-performing loans collateralized by real estate was 35.1% at September 30, 2018. The Bank continues to maintain conservative underwriting standards. We anticipate that we will continue to see low loss content in our loan portfolio. See Note 5 of the Notes to the Consolidated Financial Statements "Loans" and "ALLOWANCE FOR LOAN LOSSES."

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**Non-Interest Income.** Non-interest income for the three months ended September 30, 2018 was \$5.0 million, an increase of \$3.3 million, or 198.3%, from \$1.7 million for the three months ended September 30, 2017. The increase in non-interest income was primarily due to an increase of \$2.0 million in gains from life insurance proceeds to \$2.2 million for the three months ended September 30, 2018 compared to \$0.2 million for the three months ended September 30, 2017 and a decline of \$1.1 million in net losses from fair value adjustments to \$0.2 million for the three months ended September 30, 2018 from \$1.3 million for the comparable prior year period.

**Non-Interest Expense.** Non-interest expense was \$27.2 million for the three months ended September 30, 2018, an increase of \$1.3 million, or 4.9%, from \$26.0 million for the three months ended September 30, 2017. The increase in non-interest expense was primarily due to increases in salaries and benefits, legal, consulting and depreciation expense due to the growth of the Bank.

**Income before Income Taxes.** Income before the provision for income taxes increased \$3.8 million, or 24.4%, to \$19.2 million for the three months ended September 30, 2018 from \$15.5 million for the three months ended September 30, 2017, for the reasons discussed above.

**Provision for Income Taxes.** The provision for income taxes was \$1.9 million for the three months ended September 30, 2018, a decrease of \$3.4 million, or 63.9%, from \$5.3 million for the three months ended September 30, 2017. The effective tax rate decreased to 9.9% for the three months ended September 30, 2018 from 34.2% in the comparable prior year period. The decrease in the effective tax rate was primarily due to the release of a previously accrued tax liability totaling \$1.8 million and the impact of the top federal tax rate declining to 21% in 2018 from 35% in 2017, as a result of the Tax Cuts and Jobs Act (the “TCJA”).

## COMPARISON OF OPERATING RESULTS FOR THE NINE MONTHS ENDED

### SEPTEMBER 30, 2018 AND 2017

**General.** Net income for the nine months ended September 30, 2018 was \$42.7 million, an increase of \$7.5 million, or 21.3%, compared to \$35.2 million for the nine months ended September 30, 2017. Diluted earnings per common share were \$1.48 for the nine months ended September 30, 2018, an increase of \$0.27, or 22.3%, from \$1.21 for the nine months ended September 30, 2017.

Return on average equity was 10.7% and 8.9% for the nine months ended September 30, 2018 and 2017. Return on average assets was 0.9% and 0.8% for the nine months ended September 30, 2018 and 2017.

**Interest Income.** Total interest and dividend income increased \$14.7 million, or 8.4%, to \$189.6 million for the nine months ended September 30, 2018 from \$174.9 million for the nine months ended September 30, 2017. The increase in interest income was primarily attributable to an increase of \$227.0 million in the average balance of interest-earning assets to \$6,136.9 million for the nine months ended September 30, 2018 from \$5,909.9 million for the comparable prior year period, combined with an increase of 17 basis points in the yield of interest-earning assets to 4.12% for the nine months ended September 30, 2018 from 3.95% for the comparable prior year period. The increase in the yield on interest-earning assets was primarily due to a 16 basis point increase in the yield of total loans, net to 4.35% for the nine months ended September 30, 2018 from 4.19% for the nine months ended September 30, 2017. The yield on interest-earning assets was also positively impacted by an increase of \$320.6 million in the average balance of total loans, net, which have a higher yield than the yield of total interest-earning assets, combined with a decrease of \$105.5 million in the average balance of total securities, which have a lower yield than the yield of total interest-earning assets. In addition, the yield of interest-earning assets improved due to increases of four basis points in the yield of total securities to 2.84% for the nine months ended September 30, 2018 from 2.80% for the comparable prior year period and 68 basis points in the yield of interest-earning deposits and federal funds sold to 1.49% for the nine months ended September 30, 2018 from 0.81% for the comparable prior year period. The 16 basis point increase in the yield on the total loans, net was primarily due to new loans being originated at a higher rate than the average yield of the existing loan portfolio and adjustable rate loans repricing higher. Excluding prepayment penalty income and recovered interest from loans, the yield on total loans, net, would have increased 13 basis points to 4.20% for the nine months ended September 30, 2018 from 4.07% for the nine months ended September 30, 2017.

**Interest Expense.** Interest expense increased \$18.0 million, or 40.0%, to \$62.8 million for the nine months ended September 30, 2018 from \$44.8 million for the nine months ended September 30, 2017. The increase in interest expense was primarily due to an increase of 40 basis points in the average cost of interest-bearing liabilities to 1.53% for the nine months ended September 30, 2018 from 1.13% for the nine months ended September 30, 2017, combined with an increase of \$198.5 million in the average balance of interest-bearing liabilities to \$5,471.4 million for the nine months ended September 30, 2018 from \$5,272.8 million for the comparable prior year period. The 40 basis point increase in the cost of interest-bearing liabilities was primarily due to the Bank raising the rates we pay on our deposit products to stay competitive within our market and an increase in borrowing costs from recent increases in the Fed Funds rate.

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**Net Interest Income.** For the nine months ended September 30, 2018, net interest income was \$126.8 million, a decrease of \$3.3 million, or 2.5%, from \$130.0 million for the nine months ended September 30, 2017. The decrease in net interest income was primarily due to the 40 basis point increase in the cost of interest-bearing liabilities to 1.53% for the nine months ended September 30, 2018 from 1.13% for the comparable prior year period, partially offset by an increase of 17 basis points in the yield of interest-earning assets to 4.12% for the nine months ended September 30, 2018 as compared to 3.95% for the nine months ended September 30, 2017. The effects of the above on both the net interest spread and net interest margin were decreases of 23 basis points to 2.59% and 18 basis points to 2.75%, respectively, for the nine months ended September 30, 2018, compared to the nine months ended September 30, 2017. Included in net interest income was prepayment penalty income from loans and securities for the nine months ended September 30, 2018 and 2017 totaling \$4.3 million and \$3.6 million, respectively, recovered interest from non-accrual loans totaling \$1.5 million and \$1.1 million, respectively, and accelerated accretion of discount upon the call of CLO securities totaling \$0.1 million and \$0.4 million, respectively. Without the prepayment penalty income, recovered interest and accelerated discount upon call, the net interest margin for the nine months ended September 30, 2018 would have been 2.62%, a decrease of 20 basis points, as compared to 2.82% for the nine months ended September 30, 2017.

**Provision for Loan Losses.** During the nine month ended September 30, 2018, a provision for loan losses was recorded for \$0.2 million, compared to \$3.3 million recorded during the comparable prior year period. The \$0.2 million provision was recorded during the nine months ended September 30, 2018 due to the quarterly analysis of the adequacy of the allowance for loan losses indicating that the provision was necessary to maintain the reserve at an appropriate level. During the nine months ended September 30, 2018, the Bank recorded net charge-offs totaling \$0.2 million, while non-accrual loans decreased \$3.2 million to \$12.5 million at September 30, 2018 from \$15.7 million at December 31, 2017. The current average loan-to-value ratio for our non-performing loans collateralized by real estate was 35.1% at September 30, 2018. The Bank continues to maintain conservative underwriting standards. We anticipate that we will continue to see low loss content in our loan portfolio. See Note 5 of the Notes to the Consolidated Financial Statements “Loans” and “ALLOWANCE FOR LOAN LOSSES.”

**Non-Interest Income.** Non-interest income for the nine months ended September 30, 2018 was \$11.3 million, an increase of \$4.0 million, or 55.2%, from \$7.3 million for the nine months ended September 30, 2017. The increase in non-interest income was primarily due to a decline of \$2.3 million in net losses from fair value adjustments to \$0.5 million for the nine months ended September 30, 2018 from \$2.8 million for the comparable prior year period, coupled with an increase of \$1.6 million in gains from life insurance proceeds to \$3.0 million for the nine months ended September 30, 2018 from \$1.4 million for the comparable prior year period.

**Non-Interest Expense.** Non-interest expense was \$85.9 million for the nine months ended September 30, 2018, an increase of \$4.3 million, or 5.3%, from \$81.6 million for the nine months ended September 30, 2017. The increase in non-interest expense was primarily due to increases in salaries and benefits, legal, consulting, depreciation, data

processing and FDIC insurance premiums all due to the growth of the Bank.

***Income before Income Taxes.*** Income before the provision for income taxes decreased \$0.5 million, or 0.9%, to \$52.0 million for the nine months ended September 30, 2018 from \$52.5 million for the nine months ended September 30, 2017 for the reasons discussed above.

***Provision for Income Taxes.*** The provision for income taxes for the nine months ended September 30, 2018 was \$9.3 million, a decrease of \$8.0 million, or 46.0%, from \$17.3 million for the comparable prior year period. The decrease was primarily due to a decrease in the effective tax rate to 18.0% for the nine months ended September 30, 2018 from 33.0% in the comparable prior year period and the \$0.5 million decrease in income before income taxes. The decrease in the effective tax rate reflects the impact of the TCJA on the tax provision and the release of a previously accrued tax liability totaling \$1.8 million for the nine months ended September 30, 2018.

## **FINANCIAL CONDITION**

***Assets.*** Total assets at September 30, 2018 were \$6,539.5 million, an increase of \$240.3 million, or 3.8%, from \$6,299.3 million at December 31, 2017. Total loans, net increased \$203.1 million, or 3.9%, during the nine months ended September 30, 2018 to \$5,359.8 million from \$5,156.6 million at December 31, 2017. Loan originations and purchases were \$906.1 million for the nine months ended September 30, 2018, an increase of \$195.4 million, or 27.5%, from \$710.7 million for the nine months ended September 30, 2017. During the nine months ended September 30, 2018, we continued to focus on the origination of multi-family residential, commercial real estate and commercial business loans with a full banking relationship. The loan pipeline totaled \$355.2 million at September 30, 2018 compared to \$359.8 million at December 31, 2017.



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The following table shows loan originations and purchases for the periods indicated:

(In thousands)	For the three months ended September 30,		For the nine months ended September 30,	
	2018	2017	2018	2017
Multi-family residential <sup>(1)</sup>	\$102,484	\$64,551	254,637	\$254,728
Commercial real estate <sup>(2)</sup>	38,569	25,385	175,013	184,676
One-to-four family – mixed-use property <sup>(3)</sup>	16,870	13,136	45,232	45,334
One-to-four family – residential <sup>(4)</sup>	11,362	5,843	35,304	16,623
Co-operative apartments	-	232	1,500	232
Construction	6,008	148	30,627	7,121
Small Business Administration	344	4,276	2,539	6,787
Commercial business and other <sup>(5)</sup>	133,188	69,354	361,207	195,150
Total	\$308,825	\$182,925	\$906,059	\$710,651

(1) Includes purchases of \$50.2 million for the three months ended September 30, 2018. Includes purchases of \$64.3 million and \$31.0 million for the nine months ended September 30, 2018 and 2017, respectively.

Includes purchases of \$6.6 million and \$25.9 million for the three months ended September 30, 2018 and 2017, (2) respectively, Includes purchases of \$12.4 million and \$25.9 million nine months ended September 30, 2018 and 2017, respectively.

(3) Includes purchases of \$0.7 million for the nine-month ended September 30, 2018.

(4) Includes purchases of \$0.4 million and \$1.3 million for three and nine months ended September 30, 2018.

Includes purchases of \$67.8 million and \$9.0 million for the three months ended September 30, 2018 and 2017, (5) respectively. Includes purchases of \$156.5 million and \$18.9 million for the nine months ended September 30, 2018 and 2017, respectively.

The Bank maintains its conservative underwriting standards that include, among other things, a loan-to-value ratio of 75% or less and a debt coverage ratio of at least 125%. Multi-family residential (excluding underlying co-operative mortgages), commercial real estate and one-to-four family mixed-use property mortgage loans originated and purchased during the three months ended September 30, 2018 had an average loan-to-value ratio of 42.2% and an average debt coverage ratio of 173%.

The Bank’s non-performing assets totaled \$12.7 million at September 30, 2018, a decrease of \$5.5 million, or 30.1%, from \$18.1 million at December 31, 2017. Total non-performing assets as a percentage of total assets were 0.19% at September 30, 2018 compared to 0.29% at December 31, 2017. The ratio of allowance for loan losses to total non-performing loans was 160.62% at September 30, 2018 and 112.23% at December 31, 2017.

During the nine months ended September 30, 2018, mortgage-backed securities including held-to-maturity increased \$18.5 million, or 3.6%, to \$536.1 million from \$517.6 million at December 31, 2017. The increase in mortgage-backed securities during the nine months ended September 30, 2018 was primarily due to purchases of \$92.6 million at an average yield of 3.54%, partially offset by principal repayments of \$57.8 million and a decline in the fair value of \$15.2 million.

During the nine months ended September 30, 2018, other securities, including held-to-maturity, increased \$4.5 million, or 1.8%, to \$256.1 million from \$251.6 million at December 31, 2017. The increase in other securities during the nine months ended September 30, 2018 was primarily due to the purchase of one collateralized loan obligation (“CLO”) security and one corporate security totaling \$20.0 million, partially offset by the call of one CLO at par for \$10.0 million and the decline in fair value of \$4.3 million. At September 30, 2018, other securities primarily consist of securities issued by mutual or bond funds that invest in government and government agency securities, municipal bonds, corporate bonds and CLO’s.

**Liabilities.** Total liabilities were \$5,997.8 million at September 30, 2018, an increase of \$231.1 million, or 4.0%, from \$5,766.7 million at December 31, 2017. During the nine months ended September 30, 2018, due to depositors increased \$317.0 million, or 7.3%, to \$4,657.6 million, due to increases of \$105.9 million in non-maturity deposits and \$211.0 million in certificates of deposit. The increase in non-maturity deposits was due to increases of \$243.7 million and \$13.3 million in money market and demand accounts, respectively, partially offset by a decrease of \$77.8 million and \$73.3 million in NOW and savings accounts. Borrowed funds decreased \$112.6 million during the nine months ended September 30, 2018. The decrease in borrowed funds was primarily due to a decrease in FHLB short-term borrowings as funding needs were provided by increased deposits.

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### **FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES**

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**Equity.** Total stockholders’ equity increased \$9.1 million, or 1.7%, to \$541.8 million at September 30, 2018 from \$532.6 million at December 31, 2017. Stockholders’ equity increased primarily due to net income of \$42.7 million and the net impact of vesting and exercising of shares of employee and director stock plans totaling \$6.5 million. These increases were partially offset by the purchase of 744,953 treasury shares, at an average cost of \$26.18 per share, totaling \$19.5 million, the declaration and payment of dividends on the Company’s common stock of \$0.60 per common share totaling \$17.2 million and an increase of \$4.6 million in accumulated other comprehensive loss. Book value per common share was \$19.33 at September 30, 2018 compared to \$18.63 at December 31, 2017.

**Cash flow.** During the nine months ended September 30, 2018, funds provided by the Company's operating activities amounted to \$59.4 million. These funds, combined with \$178.0 million provided from financing activities and \$51.5 million available from the beginning of the period, were utilized to fund net investing activities of \$243.8 million. The Company's primary business objective is the origination and purchase of multi-family residential loans, commercial business loans and commercial real estate mortgage loans and to a lesser extent one-to-four family (including mixed-use properties) and SBA loans. During the nine months ended September 30, 2018, the net total of loan originations and purchases less loan repayments and sales was \$217.2 million. During the nine months ended September 30, 2018, the Company also funded \$102.8 million in purchases of securities available for sale and \$0.7 million of securities held-to-maturity. During the nine months ended September 30, 2018, funds were provided by net increases in total deposits of \$332.7 million and short-term borrowed funds of \$115.3 million, as well as proceeds from new long-term borrowing of \$25.0 million. In addition to funding loan growth, these funds were used to repay \$256.1 million in long-term borrowings. The Company also used funds of \$21.6 million and \$17.2 million for purchases of treasury stock and dividend payments, respectively, during the nine months ended September 30, 2018.

#### **INTEREST RATE RISK**

The Consolidated Statements of Financial Position have been prepared in accordance with generally accepted accounting principles in the United States of America, which require the measurement of financial position and operating results in terms of historical dollars without considering the changes in fair value of certain investments due to changes in interest rates. Generally, the fair value of financial investments such as loans and securities fluctuates inversely with changes in interest rates. As a result, increases in interest rates could result in decreases in the fair value of the Company’s interest-earning assets which could adversely affect the Company’s results of operations if such assets were sold, or, in the case of securities classified as available for sale, decreases in the Company’s stockholders’ equity, if such securities were retained.

The Company manages the mix of interest-earning assets and interest-bearing liabilities on a continuous basis to maximize return and adjust its exposure to interest rate risk. On a quarterly basis, management prepares the “Earnings

and Economic Exposure to Changes in Interest Rate” report for review by the Asset Liability Committee of the Board of Directors, as summarized below. This report quantifies the potential changes in net interest income and net portfolio value should interest rates go up or down (shocked) 200 basis points, assuming the yield curves of the rate shocks will be parallel to each other. The Company’s regulators currently place focus on the net portfolio value, focusing on a rate shock up or down of 200 basis points. Net portfolio value is defined as the market value of assets net of the market value of liabilities. The market value of assets and liabilities is determined using a discounted cash flow calculation. The net portfolio value ratio is the ratio of the net portfolio value to the market value of assets. All changes in income and value are measured as percentage changes from the projected net interest income and net portfolio value at the base interest rate scenario. The base interest rate scenario assumes interest rates at September 30, 2018. Various estimates regarding prepayment assumptions are made at each level of rate shock. However, prepayment penalty income is excluded from this analysis. Actual results could differ significantly from these estimates. At September 30, 2018, the Company was within the guidelines set forth by the Board of Directors for each interest rate level.

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The following table presents the Company’s interest rate shock as of September 30, 2018:

Change in Interest Rate	Projected Percentage Change					
	In Net Interest Income		Net Portfolio Value		Net Portfolio Value Ratio	
		%		%		%
-200 Basis points	10.63	%	10.87	%	12.75	%
-100 Basis points	5.78		5.51		12.45	
Base interest rate	0.00		0.00		12.11	
+100 Basis points	-6.54		-6.46		11.62	
+200 Basis points	-12.64		-12.13		11.18	

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Net interest income represents the difference between income on interest-earning assets and expense on interest-bearing liabilities. Net interest income depends upon the relative amount of interest-earning assets and interest-bearing liabilities and the interest rate earned or paid on them. The following tables sets forth certain information relating to the Company’s Consolidated Statements of Financial Condition and Consolidated Statements of Income for the three and nine months ended September 30, 2018 and 2017, and reflects the average yield on assets and average cost of liabilities for the periods indicated. Such yields and costs are derived by dividing income or expense by the average balance of assets or liabilities, respectively, for the periods shown. Average balances are derived from average daily balances. The yields include amortization of fees which are considered adjustments to yields.

	For the three months ended September 30,					
	2018			2017		
	Average Balance	Interest	Yield/ Cost	Average Balance	Interest	Yield/ Cost
	(Dollars in thousands)					
<b>Assets</b>						
<b>Interest-earning assets:</b>						
Mortgage loans, net	\$4,467,349	\$49,612	4.44 %	\$4,350,338	\$46,121	4.24 %
Other loans, net	812,823	10,046	4.94	683,328	7,197	4.21
Total loans, net <sup>(1)</sup>	5,280,172	59,658	4.52	5,033,666	53,318	4.24
<b>Taxable securities:</b>						
Mortgage-backed securities	542,192	3,800	2.80	520,889	3,335	2.56
Other securities	123,174	928	3.01	189,957	1,600	3.37
Total taxable securities	665,366	4,728	2.84	710,846	4,935	2.78
<b>Tax-exempt securities: <sup>(2)</sup></b>						
Other securities	123,472	852	2.76	142,899	945	2.65
Total tax-exempt securities	123,472	852	2.76	142,899	945	2.65
Interest-earning deposits and federal funds sold	61,412	248	1.62	48,718	121	0.99
Total interest-earning assets	6,130,422	65,486	4.27	5,936,129	59,319	4.00
Other assets	316,118			303,192		
Total assets	\$6,446,540			\$6,239,321		
<b>Liabilities and Equity</b>						
<b>Interest-bearing liabilities:</b>						
<b>Deposits:</b>						
Savings accounts	\$219,749	304	0.55	\$330,316	583	0.71
NOW accounts	1,336,873	4,416	1.32	1,340,228	2,468	0.74
Money market accounts	1,169,130	5,126	1.75	927,067	2,337	1.01

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Certificate of deposit accounts	1,487,366	7,453	2.00	1,375,052	5,218	1.52
Total due to depositors	4,213,118	17,299	1.64	3,972,663	10,606	1.07
Mortgagors' escrow accounts	57,573	126	0.88	54,236	49	0.36
Total deposits	4,270,691	17,425	1.63	4,026,899	10,655	1.06
Borrowed funds	1,185,176	6,540	2.21	1,249,038	5,623	1.80
Total interest-bearing liabilities	5,455,867	23,965	1.76	5,275,937	16,278	1.23
Non interest-bearing deposits	380,825			354,149		
Other liabilities	73,432			72,767		
Total liabilities	5,910,124			5,702,853		
Equity	536,416			536,468		
Total liabilities and equity	\$6,446,540			\$6,239,321		
Net interest income / net interest rate spread		\$41,521	2.51 %		\$43,041	2.77 %
Net interest-earning assets / net interest margin	\$674,555		2.71 %	\$660,192		2.90 %
Ratio of interest-earning assets to interest-bearing liabilities			1.12 X			1.13 X

Loan interest income includes loan fee income (which includes net amortization of deferred fees and costs, late (1) charges, and prepayment penalties) of approximately \$1.2 million and \$0.9 million for the three months ended September 30, 2018 and 2017.

(2) Interest income on tax-exempt securities does not include the tax benefit of the tax-exempt securities.

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	For the nine months ended September 30,					
	2018			2017		
	Average	Interest	Yield/	Average	Interest	Yield/
	Balance		Cost	Balance		Cost
	(Dollars in thousands)					
<b>Assets</b>						
<b>Interest-earning assets:</b>						
Mortgage loans, net	\$4,473,422	\$143,397	4.27 %	\$4,287,674	\$135,429	4.21 %
Other loans, net	802,617	28,600	4.75	667,749	20,405	4.07
Total loans, net <sup>(1)</sup>	5,276,039	171,997	4.35	4,955,423	155,834	4.19
<b>Taxable securities:</b>						
Mortgage-backed securities	533,394	11,061	2.76	527,890	10,122	2.56
Other securities	125,589	3,072	3.26	215,453	5,650	3.50
Total taxable securities	658,983	14,133	2.86	743,343	15,772	2.83
<b>Tax-exempt securities: <sup>(2)</sup></b>						
Other securities	123,882	2,562	2.76	145,058	2,897	2.66
Total tax-exempt securities	123,882	2,562	2.76	145,058	2,897	2.66
Interest-earning deposits and federal funds sold	77,983	873	1.49	66,042	403	0.81
Total interest-earning assets	6,136,887	189,565	4.12	5,909,866	174,906	3.95
Other assets	308,210			299,139		
Total assets	\$6,445,097			\$6,209,005		
<b>Liabilities and Equity</b>						
<b>Interest-bearing liabilities:</b>						
<b>Deposits:</b>						
Savings accounts	\$240,234	978	0.54	\$288,376	1,289	0.60
NOW accounts	1,439,997	10,928	1.01	1,474,572	7,006	0.63
Money market accounts	1,102,374	12,184	1.47	882,213	5,487	0.83
Certificate of deposit accounts	1,450,885	20,034	1.84	1,396,583	15,257	1.46
Total due to depositors	4,233,490	44,124	1.39	4,041,744	29,039	0.96
Mortgagors' escrow accounts	64,620	199	0.41	60,895	106	0.23
Total deposits	4,298,110	44,323	1.37	4,102,639	29,145	0.95
Borrowed funds	1,173,272	18,472	2.10	1,170,203	15,696	1.79
Total interest-bearing liabilities	5,471,382	62,795	1.53	5,272,842	44,841	1.13
Non interest-bearing deposits	372,257			340,221		
Other liabilities	68,857			67,967		
Total liabilities	5,912,496			5,681,030		
Equity	532,601			527,975		
Total liabilities and equity	\$6,445,097			\$6,209,005		
Net interest income / net interest rate spread		\$126,770	2.59 %		\$130,065	2.82 %
	\$665,505		2.75 %	\$637,024		2.93 %



Net interest-earning assets / net interest margin

Ratio of interest-earning assets to interest-bearing liabilities

1.12 X

1.12 X

Loan interest income includes loan fee income (which includes net amortization of deferred fees and costs, late (1) charges, and prepayment penalties) of approximately \$1.6 million and \$1.9 million for the nine months ended September 30, 2018 and 2017, respectively.

(2) Interest income on tax-exempt securities does not include the tax benefit of the tax-exempt securities.

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**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Management’s Discussion and Analysis of****Financial Condition and Results of Operations****LOANS**

The following table sets forth the Company’s loan originations (including the net effect of refinancing) and the changes in the Company’s portfolio of loans, including purchases, sales and principal reductions for the periods indicated.

(In thousands)	For the nine months ended September 30,	
	2018	2017
Mortgage Loans		
At beginning of period	\$4,401,950	\$4,187,818
Mortgage loans originated:		
Multi-family residential	190,315	223,766
Commercial real estate	162,598	158,749
One-to-four family – mixed-use property	44,547	45,334
One-to-four family – residential	34,046	16,623
Co-operative apartments	1,500	232
Construction	30,627	7,121
Total mortgage loans originated	463,633	451,825
Mortgage loans purchased:		
Multi-family residential	64,322	30,962
Commercial real estate	12,415	25,927
One-to-four family – mixed-use property	685	-
One-to-four family – residential	1,258	-
Total mortgage loans purchased	78,680	56,889
Less:		
Principal and other reductions	436,674	300,897
Loans transferred to held for sale	-	30,565
Loans transferred to OREO	638	-
Sales	8,739	18,975
At end of period	\$4,498,212	\$4,346,095

## Non-Mortgage Loans

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At beginning of period	\$758,286	\$631,316
Other loans originated:		
Small Business Administration	2,539	6,787
Commercial business	203,262	174,541
Other	1,433	1,666
Total other loans originated	207,234	182,994
Other loans purchased:		
Commercial business	156,513	18,943
Total other loans purchased	156,513	18,943
Less:		
Principal and other reductions	250,143	121,055
Sales	5,266	4,842
At end of period	\$866,624	\$707,356

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**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Management’s Discussion and Analysis of****Financial Condition and Results of Operations****TROUBLED DEBT RESTRUCUTURED (“TDR”) AND NON-PERFORMING ASSETS**

The following table shows loans classified as TDR that are performing according to their restructured terms at the periods indicated:

<i>(In thousands)</i>	September 30, 2018	June 30, 2018	December 31, 2017
Accrual Status:			
Multi-family residential	\$ 1,927	\$ 2,488	\$ 2,518
Commercial real estate	-	-	1,986
One-to-four family - mixed-use property	1,713	1,726	1,753
One-to-four family - residential	557	562	572
Commercial business and other	1,885	351	462
Total	6,082	5,127	7,291
Non-Accrual Status:			
Taxi medallion	5,366	5,482	5,916
Total	5,366	5,482	5,916
Total performing troubled debt restructured	\$ 11,448	\$ 10,609	\$ 13,207

During the three months ended September 30, 2018, one commercial business loan for \$1.6 million became a TDR.

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The following table shows non-performing assets at the periods indicated:

(In thousands)	September 30, 2018	June 30, 2018	December 31, 2017
Loans 90 days or more past due and still accruing:			
Commercial real estate	\$ 111	\$-	\$2,424
Construction	-	730	-
Total	111	730	2,424
Non-accrual loans:			
Multi-family residential	862	2,165	3,598
Commercial real estate	1,398	1,448	1,473
One-to-four family - mixed-use property	795	2,157	1,867
One-to-four family - residential	6,610	6,969	7,808
Co-operative apartments	-	575	-
Small business administration	1,395	-	46
Taxi medallion	712	743	918
Commercial business and other	761	2	-
Total	12,533	14,059	15,710
Total non-performing loans	12,644	14,789	18,134
Other non-performing assets:			
Other assets acquired through foreclosure	35	35	-
Total	35	35	-
Total non-performing assets	\$ 12,679	\$ 14,824	\$ 18,134
Non-performing assets to total assets	0.19 %	0.23 %	0.29 %
Allowance for loan losses to non-performing loans	160.62 %	136.72 %	112.23 %

Included in loans over 90 days past due and still accruing was one loan for \$0.1 million, one loan for \$0.7 million and three loans totaling \$2.4 million at September 30, 2018, June 30, 2018 and December 31, 2017, respectively, which are past their respective maturity dates and are still remitting payments. The Bank actively works with borrowers to extend the loans maturity or have the loan repaid when loans go past their contractual maturity date.

Included in non-performing loans was one multi-family loan totaling \$0.4 million at September 30, 2018, June 30, 2018 and December 31, 2017 which was restructured as TDR and not performing in accordance with its restructured terms.

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#### **CRITICIZED AND CLASSIFIED ASSETS**

Our policy is to review our assets, focusing primarily on the loan portfolio, OREO and the investment portfolios, to ensure that credit quality is maintained at the highest levels. See Note 5 of the Notes to the Consolidated Financial Statements “Loans” for a description of how loans are determined to be criticized or classified and a table displaying criticized and classified loans at September 30, 2018 and December 31, 2017. The Company had classified other assets acquired through foreclosure totaling \$35,000 at September 30, 2018 and none at December 31, 2017. The Company did not hold any criticized or classified investment securities at September 30, 2018 and December 31, 2017. Our total Criticized and Classified assets were \$56.7 million at September 30, 2018, a decrease of \$6.0 million from \$62.7 million at December 31, 2017.

On a quarterly basis, all collateral dependent loans that are classified as Substandard or Doubtful are internally reviewed for impairment, based on updated cash flows for income producing properties, or updated independent appraisals. The loan balances of collateral dependent loans reviewed for impairment are then compared to the loans updated fair value. We consider fair value of collateral dependent loans to be 85% of the appraised or internally estimated value of the property, except for taxi medallion loans. The fair value of the underlying collateral of taxi medallion loans is the value of the underlying medallion based upon the most recently reported arm’s length transaction. When there is no recent sale activity, the fair value is calculated using the income approach. All taxi medallion loans are classified and impaired. For collateral dependent mortgage loans and taxi medallion loans, the portion of the loan balance which exceeds fair value is generally charged-off. At September 30, 2018, the current average loan-to-value ratio on our collateral dependent loans reviewed for impairment was 50.3%.

#### **ALLOWANCE FOR LOAN LOSSES**

The Allowance for loan losses (“ALLL”) represents the expense charged to earnings based upon management’s quarterly analysis of credit risk. The amount of the ALLL is based upon multiple factors that reflect management’s assessment of the credit quality of the loan portfolio. The factors are both quantitative and qualitative in nature including, but not limited to, historical losses, economic conditions, trends in delinquencies, value and adequacy of underlying collateral, volume and portfolio mix, and internal loan processes.

Management has developed a comprehensive analytical process to monitor the adequacy of the ALLL. The process and guidelines were developed using, among other factors, the guidance from federal banking regulatory agencies and GAAP. The results of this process, along with the conclusions of our independent loan review officer, support management's assessment as to the adequacy of the ALLL at each balance sheet date. See Note 5 of the Notes to the Consolidated Financial Statements "Loans" for a detailed explanation of management's methodology and policy.

As a component of the credit risk assessment, the Bank has established an Asset Classification Committee which carefully evaluates loans which are past due 90 days and/or are classified. The Asset Classification Committee thoroughly assesses the condition and circumstances surrounding each loan meeting the criteria. The Bank also has a Delinquency Committee that evaluates loans meeting specific criteria. The Bank's loan policy requires loans to be placed into non-accrual status once the loan becomes 90 days delinquent unless there is, in our opinion, compelling evidence the borrower will bring the loan current in the immediate future.

As described in Note 5 of the Notes to the Consolidated Financial Statements "Loans", during the three months ended September 30, 2018, the Company revised its ALLL methodology to no longer segregated its loans into two portfolios based on year of origination and converged our qualitative factors. This change in methodology increased slightly the portion of the ALLL related to the loss history, while the qualitative factors decreased slightly, partially offset by growth in the loan portfolio. Charge-offs recorded in the past twelve quarters were minimal, with the exception of taxi medallion charge-offs recorded in the fourth quarter of 2017, as credit conditions have remained stable. An unallocated component is maintained as part of our ALLL to cover uncertainties that could affect management's estimate of probable losses. The unallocated component of the ALLL reflects the margin of imprecision inherent in the underlying assumptions used in the methodologies for estimating specific and general losses in the portfolio. The impact from the above resulted in the ALLL totaling \$20.3 million, a decrease of \$42,000 million, or 0.2%, from December 31, 2017. Based upon management consistently applying the ALLL methodology and review of the loan portfolio, management concluded a charge to earnings to increase the ALLL was not warranted. The ALLL at September 30, 2018 and December 31, 2017, represented 0.38% and 0.39% of gross loans outstanding, respectively. The ALLL represented 160.6% of non-performing loans at September 30, 2018 compared to 112.2% at December 31, 2017.

Management recommends to the Board of Directors the amount of the ALLL quarterly. The Board of Directors approves the ALLL.



**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Management’s Discussion and Analysis of****Financial Condition and Results of Operations**

The following table sets forth the activity in the Company's allowance for loan losses for the periods indicated:

(Dollars in thousands)	At or for the nine months ended September 30,			
	2018	2017		
Balance at beginning of period	\$20,351	\$22,229		
Provision for loan losses	153	3,266		
Loans charged-off:				
Multi-family residential	(99 )	(452 )		
Commercial real estate	-	(4 )		
One-to-four family – mixed-use property	(3 )	(36 )		
One-to-four family – residential	(1 )	(170 )		
Small Business Administration	(196 )	(89 )		
Taxi medallion	(393 )	(54 )		
Commercial business and other	(29 )	(48 )		
Total loans charged-off	(721 )	(853 )		
Recoveries:				
Multi-family residential	2	297		
Commercial real estate	-	93		
One-to-four family – mixed-use property	118	68		
One-to-four family – residential	371	58		
Small Business Administration	25	66		
Commercial business and other	10	45		
Total recoveries	526	627		
Net charge-offs	(195 )	(226 )		
Balance at end of period	\$20,309	\$25,269		
Ratio of net charge-offs during the period to average loans outstanding during the period	-	%	0.01	%
Ratio of allowance for loan losses to gross loans at end of period	0.38	%	0.50	%
Ratio of allowance for loan losses to non-performing assets at end of period	160.17	%	181.92	%
Ratio of allowance for loan losses to non-performing loans at end of period	160.62	%	181.92	%



**PART I – FINANCIAL INFORMATION**

**FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES**

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

For a discussion of the qualitative and quantitative disclosures about market risk, see the information under the caption "Management's Discussion and Analysis of Financial Condition and Results of Operations - Interest Rate Risk."

**ITEM 4. CONTROLS AND PROCEDURES**

The Company carried out, under the supervision and with the participation of the Company's management, including its Chief Executive Officer and Chief Financial Officer, an evaluation of the effectiveness of the design and operation of the Company's disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934) as of the end of the period covered by this Quarterly Report. Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that, as of September 30, 2018, the design and operation of these disclosure controls and procedures were effective. During the period covered by this Quarterly Report, there have been no changes in the Company's internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

**PART II – OTHER INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****ITEM 1. LEGAL PROCEEDINGS**

The Company is a defendant in various lawsuits. Management of the Company, after consultation with outside legal counsel, believes that the resolution of these various matters will not result in any material adverse effect on the Company's consolidated financial condition, results of operations and cash flows.

**ITEM 1A. RISK FACTORS**

There have been no material changes from the risk factors disclosed in the Company's Annual Report on Form 10-K for the year ended December 31, 2017.

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

The following table sets forth information regarding the shares of common stock repurchased by the Company during the three months ended September 30, 2018:

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares That May Yet Be Purchased Under the Plans or Programs
July 1 to July 31, 2018	27,893	\$25.47	27,893	780,943
August 1 to August 31, 2018	225,516	25.56	225,516	555,427
September 1 to September 30, 2018	46,100	25.74	46,100	509,327
Total	299,509	25.58	299,509	

During the quarter ended September 30, 2018, the Company repurchased 299,509 shares of the Company's common stock at an average cost of \$25.58 per share. On September 30, 2018, 509,327 shares may still be repurchased under the currently authorized stock repurchase program. Stock will be purchased under the current stock repurchase programs from time to time, in the open market or through private transactions, subject to market conditions. There is no expiration or maximum dollar amount under these authorizations.

**ITEM 3. DEFAULTS UPON SENIOR SECURITIES**

None.

**ITEM 4. MINE SAFETY DISCLOSURES**

Not applicable.

**ITEM 5. OTHER INFORMATION**

None.



**PART II – OTHER INFORMATION**

**FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES**

**ITEM 6. EXHIBITS**

Exhibit Number Description

- 3.1 P Certificate of Incorporation of Flushing Financial Corporation (1)
- 3.2 Certificate of Amendment to Certificate of Incorporation of Flushing Financial Corporation (3)
- 3.3 Certificate of Amendment to Certificate of Incorporation of Flushing Financial Corporation (5)
- 3.4 Certificate of Designations of Series A Junior Participating Preferred Stock of Flushing Financial Corporation (4)
- 3.5 Certificate of Increase of Shares Designated as Series A Junior Participating Preferred Stock of Flushing Financial Corporation (2)
- 3.6 Amended and Restated By-Laws of Flushing Financial Corporation (6)
- 4.1 Flushing Financial Corporation has outstanding certain long-term debt. None of such debt exceeds ten percent of Flushing Financial Corporation's total assets; therefore, copies of constituent instruments defining the rights of the holders of such debt are not included as exhibits. Copies of instruments with respect to such long-term debt will be furnished to the Securities and Exchange Commission upon request.
- 31.1 Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 by the Chief Executive Officer (filed herewith)
- 31.2 Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 by the Chief Financial Officer (filed herewith)
- 32.1 Certification Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes Oxley Act of 2002 by the Chief Executive Officer (furnished herewith)
- 32.2 Certification Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes Oxley Act of 2002 by the Chief Financial Officer (furnished herewith)
- 101.INS XBRL Instance Document (filed herewith)
- 101.SCH XBRL Taxonomy Extension Schema Document (filed herewith)
- 101.CAL XBRL Taxonomy Extension Calculation Linkbase Document (filed herewith)
- 101.DEF XBRL Taxonomy Extension Definition Linkbase Document (filed herewith)
- 101.LAB XBRL Taxonomy Extension Label Linkbase Document (filed herewith)
- 101.PRE XBRL Taxonomy Extension Presentation Linkbase Document (filed herewith)
- (1) Incorporated by reference to Exhibits filed with the Registration Statement on Form S-1 filed September 1, 1995, Registration No. 33-96488. (P: Indicates a filing submitted in paper)
- (2) Incorporated by reference to Exhibit filed with Form 8-K filed September 27, 2006.
- (3) Incorporated by reference to Exhibits filed with Form S-8 filed May 31, 2002.
- (4) Incorporated by reference to Exhibits filed with Form 10-Q for the quarter ended September 30, 2002.
- (5) Incorporated by reference to Exhibit filed with Form 10-K for the year ended December 31, 2011.
- (6) Incorporated by reference to Exhibit filed with Form 10-Q for the quarter ended June 30, 2014.

**FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES**

**SIGNATURES**

Pursuant to the requirements 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.

Flushing Financial Corporation,

Dated: November 8, 2018 By: /s/John R. Buran  
John R. Buran  
President and Chief Executive Officer

Dated: November 8, 2018 By: /s/Susan K. Cullen  
Susan K. Cullen  
Senior Executive Vice President, Treasurer and  
Chief Financial Officer





**FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES**

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