PEOPLES FINANCIAL SERVICES CORP.
Form 10-Q
November 06, 2015
Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, DC 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, 2015

or

Transition report pursuant to Section 13 or 15 (d) of the Securities Exchange Act of 1934

for the transition period from

001-36388

(Commission File Number)

PEOPLES FINANCIAL SERVICES CORP.

(Exact name of registrant as specified in its charter)

Pennsylvania	23-2391852

(State of incorporation)	(IRS Employer ID Number)
150 North Washington Avenue, Scranton, PA (Address of principal executive offices)	18503 (Zip code)

(570) 346-7741

(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 and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months or for such shorter period that the registrant was required to submit and post such files. Yes No

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

Large accelerated filer	Accelerated filer
Non-accelerated filer	Smaller reporting company

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

APPLICABLE ONLY TO CORPORATE ISSUERS:

Indicate the number of shares outstanding of the registrant's common stock, as of the latest practicable date: 7,426,282 at October 30, 2015.

Table of Contents

PEOPLES FINANCIAL SERVICES CORP.

FORM 10-Q

For the Quarter Ended September 30, 2015

Contents

Peoples Financial Services Corp.

CONSOLIDATED BALANCE SHEETS (UNAUDITED)

(Dollars in thousands, except share data)

	September 30, 2015	December 31, 2014
Assets:		
Cash and due from banks	$ 36,015	$ 24,656
Interest-bearing deposits in other banks	4,970	6,770
Federal funds sold		
Investment securities:		
Available-for-sale	299,832	339,586
Held-to-maturity: Fair value September 30, 2015, $13,582; December 31, 2014, $15,215	13,107	14,665
Total investment securities	312,939	354,251
Loans held for sale	3,439	3,486
Loans, net	1,270,545	1,209,894
Less: allowance for loan losses	12,043	10,338
Net loans	1,258,502	1,199,556
Premises and equipment, net	27,002	25,433
Accrued interest receivable	5,327	5,580
Goodwill	63,370	63,370
Intangible assets	4,606	5,501
Other assets	56,600	53,066
Total assets	$ 1,772,770	$ 1,741,669
Liabilities:		
Deposits:		
Noninterest-bearing	$ 303,741	$ 313,498
Interest-bearing	1,140,909	1,112,060
Total deposits	1,444,650	1,425,558
Short-term borrowings	30,250	19,557
Long-term debt	31,000	33,140
Accrued interest payable	496	574
Other liabilities	14,286	16,061
Total liabilities	1,520,682	1,494,890
Stockholders' equity:		
Common stock, par value $2.00, authorized 25,000,000 shares, issued and outstanding: September 30, 2015, 7,519,109 shares; December 31, 2014, 7,548,358 shares	15,038	15,097
Capital surplus	139,263	140,214
Retained earnings	99,165	92,297
Accumulated other comprehensive loss	(1,378)	(829)
Total stockholders' equity	252,088	246,779

Total liabilities and stockholders' equity	$ 1,772,770	$ 1,741,669

See notes to consolidated financial statements

Table of Contents

Peoples Financial Services Corp.

CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME (UNAUDITED)

(Dollars in thousands, except per share data)

	Three Months Ended		Nine Months Ended	
September 30,	2015	2014	2015	2014
Interest income:				
Interest and fees on loans:				
Taxable	$ 13,341	$ 13,876	$ 40,072	$ 41,035
Tax-exempt	585	465	1,714	1,607
Interest and dividends on investment securities:				
Taxable	792	1,007	2,508	2,877
Tax-exempt	858	816	2,498	2,462
Dividends	9	2	24	32
Interest on interest-bearing deposits in other banks	13	10	39	29
Interest on federal funds sold		16	9	64
Total interest income	15,598	16,192	46,864	48,106
Interest expense:				
Interest on deposits	1,229	1,354	3,689	4,125
Interest on short-term borrowings	11	9	23	67
Interest on long-term debt	245	279	756	864
Total interest expense	1,485	1,642	4,468	5,056
Net interest income	14,113	14,550	42,396	43,050
Provision for loan losses	900	666	2,400	2,724
Net interest income after provision for loan losses	13,213	13,884	39,996	40,326
Noninterest income:				
Service charges, fees and commissions	1,531	1,634	4,685	4,815
Merchant services income	1,183	1,002	2,936	2,784
Commission and fees on fiduciary activities	541	575	1,487	1,690
Wealth management income	224	217	627	569
Mortgage banking income	197	142	667	434
Life insurance investment income	192	109	569	565
Net gain on sale of investment securities available-for-sale	147	701	979	861
Total noninterest income	4,015	4,380	11,950	11,718
Noninterest expense:				
Salaries and employee benefits expense	5,397	4,754	16,243	14,883
Net occupancy and equipment expense	2,246	2,020	6,863	6,080
Merchant services expense	823	662	2,006	1,722
Amortization of intangible assets	296	334	896	1,010
Acquisition related expense		109		1,725

Other expenses	2,944	3,205	8,303	9,190
Total noninterest expense	11,706	11,084	34,311	34,610
Income before income taxes	5,522	7,180	17,635	17,434
Income tax expense	1,113	1,944	3,751	4,169
Net income	4,409	5,236	13,884	13,265
Other comprehensive income (loss):				
Unrealized gain (loss) on investment securities available-for-sale	826	(825)	134	2,811
Reclassification adjustment for net gain on sales included in net income	(147)	(701)	(979)	(861)
Other comprehensive income (loss)	679	(1,526)	(845)	1,950
Income tax expense (benefit) related to other comprehensive loss	237	(534)	(296)	682
Other comprehensive income (loss), net of income taxes	442	(992)	(549)	1,268
Comprehensive income	$ 4,851	$ 4,244	$ 13,335	$ 14,533
Per share data:				
Net income:				
Basic	$ 0.58	$ 0.70	$ 1.84	$ 1.76
Diluted	$ 0.58	$ 0.70	$ 1.84	$ 1.76
Average common shares outstanding:				
Basic	7,536,824	7,548,358	7,543,751	7,548,983
Diluted	7,536,824	7,548,358	7,543,751	7,566,456
Dividends declared	$ 0.31	$ 0.31	$ 0.93	$ 0.93

See notes to consolidated financial statements

Table of Contents

Peoples Financial Services Corp.

CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS’ EQUITY (UNAUDITED)

(Dollars in thousands, except per share data)

	Common Stock	Capital Surplus	Retained Earnings	Accumulated Other Comprehensive Income/(Loss)	Treasury Stock	Total
Balance, January 1, 2015	$ 15,097	$ 140,214	$ 92,297	$ (829)	$	$ 246,779
Stock based compensation		52				52
Net income			13,884			13,884
Other comprehensive loss, net of income taxes				(549)		(549)
Dividends declared: $0.93 per share			(7,016)			(7,016)
Shares retired: 29,249 shares	(59)	(1,003)				(1,062)
Balance, September 30, 2015	15,038	139,263	99,165	(1,378)		252,088
Balance, January 1, 2014	15,614	146,109	84,008	(698)	(6,241)	238,792
Net income			13,265			13,265
Other comprehensive income, net of income taxes				1,268		1,268
Dividends declared: $0.93 per share			(7,021)			(7,021)
Shares retired: 3,386 shares	(7)	(102)				(109)
Reissuance under option plan: 600 shares		28			11	39
Repurchase and held: 1,800 shares					(70)	(70)
Retirement of stock options		(95)				(95)
Retirement of treasury stock	(510)	(5,790)			6,300	
Balance, September 30, 2014	$ 15,097	$ 140,150	$ 90,252	$ 570	$	$ 246,069

See notes to consolidated financial statements

Table of Contents

Peoples Financial Services Corp.

CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

(Dollars in thousands, except per share data)

For the Nine Months Ended September 30,	2015	2014
Cash flows from operating activities:		
Net income	$ 13,884	$ 13,265
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation of premises and equipment	1,178	1,322
Amortization of deferred loan costs	440	171
Amortization of intangibles	896	1,010
Net accretion of purchase accounting adjustments on tangible assets	(708)	(2,683)
Provision for loan losses	2,400	2,724
Net gain on sale of other real estate owned	(132)	(60)
Net loss on disposal of equipment	87	63
Loans originated for sale	(20,664)	(7,346)
Proceeds from sale of loans originated for sale	21,378	6,752
Net gain on sale of loans originated for sale	(667)	(610)
Net amortization of investment securities	3,171	3,230
Net gain on sale of investment securities	(979)	(861)
Life insurance investment income	(569)	(592)
Deferred income tax expense	119	
Stock based compensation	52	11
Net change in:		
Accrued interest receivable	253	485
Other assets	(3,062)	(3,455)
Accrued interest payable	(78)	(126)
Other liabilities	(1,827)	1,546
Net cash provided by operating activities	15,172	14,846
Cash flows from investing activities:		
Proceeds from sales of investment securities available-for-sale	65,858	15,389
Proceeds from repayments of investment securities:		
Available-for-sale	41,659	32,022
Held-to-maturity	1,526	1,989
Purchases of investment securities:		
Available-for-sale	(70,768)	(98,898)
Held-to-maturity		
Net redemption of restricted equity securities	343	56
Net increase in lending activities	(61,940)	(3,341)
Purchases of premises and equipment	(2,924)	(1,059)
Proceeds from the sale of premises and equipment	14	25
Proceeds from sale of other real estate owned	484	409
Net cash used in investing activities	(25,748)	(53,408)
Cash flows from financing activities:		

Net increase in deposits	19,619	46,939
Repayment of long-term debt	(2,099)	(2,682)
Net increase (decrease) in short-term borrowings	10,693	(15,538)
Redemption of common stock	(1,062)	(70)
Settlement of stock options		(95)
Purchase of treasury stock		(70)
Cash dividends paid	(7,016)	(7,021)
Net cash provided by financing activities	20,135	21,463
Net increase (decrease) in cash and cash equivalents	9,559	(17,099)
Cash and cash equivalents at beginning of year	31,426	51,310
Cash and cash equivalents at end of year	$ 40,985	$ 34,211

Table of Contents

Peoples Financial Services Corp.

CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

(Dollars in thousands, except per share data)

For the Nine Months Ended September 30,	2015	2014
Supplemental disclosures:		
Cash paid during the period for:		
Interest	$ 5,114	$ 5,182
Income taxes	2,900	3,100
Noncash items:		
Transfers of loans to other real estate	$ 370	$ 541
Retirement of treasury shares		6,300
Acquisition:		
Fair value of assets acquired:		
Loans, net	$ 216	$ 1,900
Premises and equipment	(76)	(76)
Core deposit and other intangible assets	(896)	(1,010)
	$ (756)	$ 814
Fair value of liabilities assumed:		
Deposits	$ 527	$ 818
Long-term debt	41	41
	$ 568	$ 859

See notes to consolidated financial statements

Table of Contents

Peoples Financial Services Corp.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands, except per share data)

1. Summary of significant accounting policies:

Nature of operations:

Peoples Financial Services Corp., a bank holding company incorporated under the laws of Pennsylvania, provides a full range of financial services through its wholly-owned subsidiary, Peoples Security Bank and Trust Company (“Peoples Bank”), including its subsidiaries, Peoples Advisors, LLC and Penseco Realty, Inc. (collectively, the “Company” or “Peoples”). The Company services its retail and commercial customers through twenty-six full-service community banking offices located within the Lackawanna, Lehigh, Luzerne, Monroe, Susquehanna, Wayne and Wyoming Counties of Pennsylvania and Broome County of New York.

Basis of presentation:

The accompanying unaudited consolidated financial statements of the Company have been prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP’) for interim financial information and with the instructions to Form 10-Q and Article 10-01 of Regulation S-X. In the opinion of management, all normal recurring adjustments necessary for a fair presentation of the financial position and results of operations for the periods presented have been included. All significant intercompany balances and transactions have been eliminated in consolidation. Prior-period amounts are reclassified when necessary to conform to the current year’s presentation. These reclassifications did not have any effect on the operating results or financial position of the Company. The operating results and financial position of the Company for the three and nine months ended and as of September 30, 2015, are not necessarily indicative of the results of operations and financial position that may be expected in the future.

The preparation of consolidated 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 consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Significant estimates that are particularly susceptible to material change in the near term relate to the determination of the allowance for loan losses, fair value of financial instruments, the valuation of real estate acquired in connection with foreclosures or in satisfaction of loans, the valuation of deferred tax assets, determination of other-than-temporary impairment losses on securities, impairment of goodwill and fair value of assets acquired and liabilities assumed in business combinations. Actual results could differ from those estimates. For additional information and disclosures required under GAAP, reference is made to the Company's Annual Report on Form 10-K for the period ended December 31, 2014.

The Company has evaluated events and transactions occurring subsequent to the balance sheet date of September 30, 2015, for items that should potentially be recognized or disclosed in these consolidated financial statements. The evaluation was conducted through the date these consolidated financial statements were issued.

Recent accounting standards:

In April 2015, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2015-03, "Interest—Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs."

ASU 2015-03 requires that debt issuance costs be reported in the balance sheet as a direct deduction from the face amount of the related liability, consistent with the presentation of debt discounts. Prior to the amendments, debt issuance costs were presented as a deferred charge (i.e., an asset) on the balance sheet. The ASU provides examples illustrating the balance sheet presentation of notes net of their related discounts and debt issuance costs. Further, the amendments require the amortization of debt issuance costs to be reported as interest expense. Similarly, debt issuance costs and any discount or premium are considered in the aggregate when determining the effective interest rate on the debt.

The amendments are effective for public business entities for fiscal years beginning after December 15, 2015, and interim periods within those fiscal years. The amendments must be applied retrospectively. The adoption of ASU 2015-03 on January 1, 2016, is not expected to have a material effect on the operating results or financial position of the Company.

Table of Contents

Peoples Financial Services Corp.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands, except per share data)

In July 2015, the FASB issued ASU 2015-12, "Plan Accounting: Defined Benefit Pension Plans (Topic 960), Defined Contribution Pension Plans (Topic 962), Health and Welfare Benefit Plans (Topic 965): (Part I) Fully Benefit-Responsive Investment Contracts, (Part II) Plan Investment Disclosures, (Part III) Measurement Date Practical Expedient."

The amendments in ASU 2015-12 (i) require fully benefit-responsive investment contracts to be measured, presented and disclosed only at contract value, not fair value; (ii) simplify the investment disclosure requirements; and (iii) provide a measurement date practical expedient for employee benefit plans.

Part I. Fully Benefit-Responsive Investment Contracts – the amendments designate contract value as the only required measurement for fully benefit-responsive investments contracts within the scope of Topics 962 and 965, eliminating the requirement to measure, present and disclose such contracts also at fair value and reconcile fair value to contract value.

Part II. Plan Investment Disclosures – the amendments eliminate certain disclosure requirements for both participant-directed investments and nonparticipant-directed investments, and also reduce disclosures required specifically for investments using the net asset value per share practical expedient. The amendments also require that both participant-directed and nonparticipant-directed investments be grouped only by general type, eliminating the need to disaggregate the investments in multiple ways (i.e., also on the basis of nature, characteristics, and risks as required by Topic 820, Fair Value Measurement).

Part III. Measurement Date Practical Expedient – the amendments provide a measurement date practical expedient for employee benefit plans similar to the practical expedient allowing employers to measure defined benefit plan assets on a month-end date that is nearest to the employer's fiscal year-end, when the fiscal period does not coincide with a month-end.

The amendments are effective for fiscal years beginning after December 15, 2015. Early adoption is permitted for all three parts individually or in the aggregate. Parts I and II of the ASU should be applied retrospectively, while Part III should be applied prospectively. Only the nature and reason for the change in accounting principle is required to be disclosed in the annual period of adoption. The adoption of ASU 2015-12 on January 1, 2016, is not expected to have a material effect on the operating results or financial position of the Company.

In August 2015, the FASB issued ASU 2015-14, “Revenue from Contracts (Topic 606): Deferral of the Effective Date.”

ASU 2015-14 defers the effective date of the new revenue recognition standard by one year. As such, it now takes effect for public entities in fiscal years beginning after December 15, 2017. Early adoption is permitted for any entity that chooses to adopt the new standard as of the original effective date. The adoption of ASU 2015-14 on January 1, 2018, is not expected to have a material effect on the operating results or financial position of the Company.

In August 2015, the FASB issued ASU 2015-15, “Interest – Imputation of Interest (Subtopic 835-30): Presentation and Subsequent Measurement of Debt Issuance Costs Associated with Line-of-Credit Arrangements.”

ASU 2015-15 codifies a Securities and Exchange Commission (“SEC”) staff announcement that entities are permitted to defer and present debt issuance costs related to line-of-credit arrangements as assets. ASU 2015-15 clarifies that the SEC staff would not object to an entity deferring and presenting debt issuance costs as an asset and subsequently amortizing the deferred debt issuance costs ratably over the term of the line-of-credit arrangement, regardless of whether there are any outstanding borrowings on the line-of-credit arrangement. ASU 2015-15 is effective immediately. The adoption of ASU 2015-15 did not have a material effect on the operating results or financial position of the Company.

In September, 2015, the FASB issued ASU 2015-16, “Business Combination (Topic 805): Simplifying the Accounting for Measurement-Period Adjustments.”

ASU 2015-16 requires adjustments to provisional amounts that are identified during the measurement period to be recognized in the reporting period in which the adjustment amounts are determined. This includes any effect on earnings

Peoples Financial Services Corp.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands, except per share data)

of changes in depreciation, amortization, or other income effects as a result of the change to the provisional amounts, calculated as if the accounting had been completed at the acquisition date.

In addition, the amendments in the proposed Update would require an entity to disclose, either on the face of the income statement or in the notes, the nature and amount of measurement-period adjustments recognized in the current period, including separately the amounts in current-period income statement line items that would have been recorded in previous reporting periods if the adjustment to the provisional amounts had been recognized as of the acquisition date.

The amendments are effective for public business entities for fiscal years, and for interim periods within those fiscal years, beginning after December 15, 2015. Early adoption is permitted. The amendments in this Update should be applied prospectively to measurement-period adjustments that occur after the effective date of this ASU. The adoption of ASU 2015-16 on January 1, 2016, is not expected to have a material effect on the operating results or financial position of the Company.

2. Other comprehensive income (loss):

The components of other comprehensive loss and their related tax effects are reported in the Consolidated Statements of Income and Comprehensive Income. The accumulated other comprehensive income (loss) included in the Consolidated Balance Sheets relates to net unrealized gains and losses on investment securities available-for-sale and benefit plan adjustments.

The components of accumulated other comprehensive loss included in stockholders' equity at September 30, 2015 and December 31, 2014 is as follows:

	September 30, 2015	December 31, 2014

Net unrealized gain on investment securities available-for-sale	$ 5,447	$ 6,292
Income tax expense (benefit)	1,906	2,202
Net of income taxes	3,541	4,090
Benefit plan adjustments	(7,567)	(7,567)
Income tax expense (benefit)	(2,648)	(2,648)
Net of income taxes	(4,919)	(4,919)
Accumulated other comprehensive loss	$ (1,378)	$ (829)

Table of Contents

Peoples Financial Services Corp.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands, except per share data)

Other comprehensive income (loss) and related tax effects for the three and nine months ended September 30, 2015 and 2014 is as follows:

Three Months Ended September 30,	2015	2014
Unrealized gain (loss) on investment securities available-for-sale	$ 826	$ (825)
Net gain on the sale of investment securities available-for-sale(1)	(147)	(701)
Other comprehensive income (loss) gain before taxes	679	(1,526)
Income tax expense (benefit)	237	(534)
Other comprehensive income (loss)	$ 442	$ (992)

Nine Months Ended September 30,	2015	2014
Unrealized gain (loss) on investment securities available-for-sale	$ 134	$ 2,811
Net gain on the sale of investment securities available-for-sale(1)	(979)	(861)
Other comprehensive income (loss) gain before taxes	(845)	1,950
Income tax expense (benefit)	(296)	682
Other comprehensive income (loss)	$ (549)	$ 1,268

(1)Represents amounts reclassified out of accumulated comprehensive income and included in gains on sale of investment securities on the consolidated statements of income and comprehensive income.

3. Earnings per share:

Basic earnings per share represent income available to common stockholders divided by the weighted-average number of common shares outstanding during the period. Diluted earnings per share reflect additional common shares that would have been outstanding if dilutive potential common shares had been issued, as well as any adjustment to income that would result from the assumed issuance. Potential common shares that may be issued by the Company relate solely to outstanding stock options, and are determined using the treasury stock method.

There were no shares considered anti-dilutive for the three and nine month periods ended September 30, 2015 and 2014.

	2015		2014	
For the Three Months Ended September 30,	Basic	Diluted	Basic	Diluted
Net Income (Numerator)	$ 4,409	$ 4,409	$ 5,236	$ 5,236
Average common shares outstanding (Denominator)	7,536,824	7,536,824	7,548,358	7,548,358
Earnings per share	$ 0.58	$ 0.58	$ 0.70	$ 0.70

	2015		2014	
For the Nine Months Ended September 30,	Basic	Diluted	Basic	Diluted
Net Income (Numerator)	$ 13,884	$ 13,884	$ 13,265	$ 13,265
Average common shares outstanding (Denominator)	7,543,751	7,543,751	7,548,983	7,566,456
Earnings per share	$ 1.84	$ 1.84	$ 1.76	$ 1.76

Table of Contents

Peoples Financial Services Corp.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands, except per share data)

4. Investment securities:

The amortized cost and fair value of investment securities aggregated by investment category at September 30, 2015 and December 31, 2014 are summarized as follows:

September 30, 2015	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available-for-sale:				
U.S. Treasury securities	$ 15,915	$ 152	—	$ 16,067
U.S. Government-sponsored enterprises	79,077	547	$ 1	79,623
State and municipals:				
Taxable	15,886	864	19	16,731
Tax-exempt	113,198	3,913	302	116,809
Mortgage-backed securities:				
U.S. Government agencies	34,027	198	31	34,194
U.S. Government-sponsored enterprises	36,282	235	109	36,408
Total	$ 294,385	$ 5,909	$ 462	$ 299,832
Held-to-maturity:				
Tax-exempt state and municipals	$ 7,369	$ 125	$ 50	$ 7,444
Mortgage-backed securities:				
U.S. Government agencies	88	1	—	89
U.S. Government-sponsored enterprises	5,650	399	—	6,049
Total	$ 13,107	$ 525	$ 50	$ 13,582

December 31, 2014	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available-for-sale:				
U.S. Treasury securities	$ 48,393	$ 157		$ 48,550
U.S. Government-sponsored enterprises	95,990	337	$ 82	96,245
State and municipals:				

Taxable	16,490	943	26	17,407
Tax-exempt	87,954	4,971	24	92,901
Mortgage-backed securities:				
U.S. Government agencies	37,511	132	167	37,476
U.S. Government-sponsored enterprises	46,956	277	226	47,007
Total	$ 333,294	$ 6,817	$ 525	$ 339,586
Held-to-maturity:				
Tax-exempt state and municipals	$ 7,370	$ 105	$ 38	$ 7,437
Mortgage-backed securities:				
U.S. Government agencies	100	2		102
U.S. Government-sponsored enterprises	7,195	481		7,676
Total	14,665	$ 588	$ 38	$ 15,215

Table of Contents

Peoples Financial Services Corp.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands, except per share data)

The maturity distribution of the fair value, which is the net carrying amount, of the debt securities classified as available-for-sale at September 30, 2015, is summarized as follows:

September 30, 2015	Fair Value
Within one year	$ 33,161
After one but within five years	98,388
After five but within ten years	46,705
After ten years	50,976
	229,230
Mortgage-backed securities	70,602
Total	$ 299,832

The maturity distribution of the amortized cost and fair value, of debt securities classified as held-to-maturity at September 30, 2015, is summarized as follows:

September 30, 2015	Amortized Cost	Fair Value
Within one year		
After one but within five years	$ 503	$ 515
After five but within ten years	—	—
After ten years	6,866	6,929
	7,369	7,444
Mortgage-backed securities	5,738	6,138
Total	$ 13,107	$ 13,582

Securities with a carrying value of $206,467 and $216,192 at September 30, 2015 and December 31, 2014, respectively, were pledged to secure public deposits and repurchase agreements as required or permitted by law.

Securities and short-term investment activities are conducted with a diverse group of government entities, corporations and state and local municipalities. The counterparty’s creditworthiness and type of collateral is evaluated on a case-by-case basis. At September 30, 2015 and December 31, 2014, there were no significant concentrations of credit risk from any one issuer, with the exception of U.S. Government agencies and sponsored enterprises that exceeded 10.0 percent of stockholders' equity.

The fair value and gross unrealized losses of investment securities with unrealized losses for which an other-than-temporary impairment ("OTTI") has not been recognized at September 30, 2015 and December 31, 2014, aggregated by investment category and length of time that the individual securities have been in a continuous unrealized loss position, are summarized as follows:

	Less Than 12 Months		12 Months or More		Total	
September 30, 2015	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
U.S. Government-sponsored enterprises	$ 3,006	$ 1	$	$	$ 3,006	$ 1
State and municipals:						
Taxable			546	19	546	19
Tax-exempt	41,034	325	789	27	41,823	352
Mortgage-backed securities:						
U.S. Government agencies	877	7	5,119	24	5,996	31
U.S. Government-sponsored enterprises	9,819	20	6,682	89	16,501	109
Total	$ 54,736	$ 353	$ 13,136	$ 159	$ 67,872	$ 512

13

Table of Contents

Peoples Financial Services Corp.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands, except per share data)

	Less Than 12 Months		12 Months or More		Total	
December 31, 2014	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
U.S. Government-sponsored enterprises	$ 21,228	$ 33	$ 7,954	$ 49	$ 29,182	$ 82
State and municipals:						
Taxable			544	26	544	26
Tax-exempt	4,702	23	2,423	39	7,125	62
Mortgage-backed securities:						
U.S. Government agencies	20,148	167			20,148	167
U.S. Government-sponsored enterprises	22,870	226			22,870	226
Total	$ 68,948	$ 449	$ 10,921	$ 114	$ 79,869	$ 563

The Company had 97 investment securities, consisting of 76 tax-exempt state and municipal obligations, one taxable state and municipal obligation, one U.S. Government-sponsored enterprise security, and 19 mortgage-backed securities that were in unrealized loss positions at September 30, 2015. Of these securities, one taxable state and municipal obligation, eight mortgage-backed securities and three tax-exempt state and municipal securities were in a continuous unrealized loss position for twelve months or more. Management does not consider the unrealized losses on the debt securities, as a result of changes in interest rates, to be OTTI based on historical evidence that indicates the cost of these securities is recoverable within a reasonable period of time in relation to normal cyclical changes in the market rates of interest. Moreover, because there has been no material change in the credit quality of the issuers or other events or circumstances that may cause a significant adverse impact on the fair value of these securities, and management does not intend to sell these securities and it is unlikely that the Company will be required to sell these securities before recovery of their amortized cost basis, which may be maturity, the Company does not consider the unrealized losses to be OTTI at September 30, 2015. There was no OTTI recognized for the three or nine months ended September 30, 2015 and 2014.

The Company had 52 investment securities, consisting of 16 tax-exempt state and municipal obligations, one taxable state and municipal obligation, nine U.S. Government-sponsored enterprise securities and 26 mortgage-backed securities that were in unrealized loss positions at December 31, 2014. Of these securities, two U.S. Government-sponsored enterprise securities, four tax-exempt state and municipal securities, and one taxable state and municipal obligation were in a continuous unrealized loss position for twelve months or more.

5. Loans, net and allowance for loan losses:

The major classifications of loans outstanding, net of deferred loan origination fees and costs at September 30, 2015 and December 31, 2014 are summarized as follows. Net deferred loan costs were $686 and $651 at September 30, 2015 and December 31, 2014.

	September 30, 2015	December 31, 2014
Commercial	$ 342,937	$ 319,590
Real estate:		
Commercial	529,499	493,481
Residential	306,740	322,454
Consumer	91,369	74,369
Total	$ 1,270,545	$ 1,209,894

14

Table of Contents

Peoples Financial Services Corp.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands, except per share data)

The changes in the allowance for loan losses account by major classification of loan for the three and nine months ended September 30, 2015 and 2014 are summarized as follows:

		Real estate			
September 30, 2015	Commercial	Commercial	Residential	Consumer	Total
Allowance for loan losses:					
Beginning Balance July 1, 2015	$ 2,435	$ 3,190	$ 4,027	$ 1,776	$ 11,428
Charge-offs		(120)	(128)	(67)	(315)
Recoveries	2	2	2	24	30
Provisions		342	369	189	900
Ending balance	$ 2,437	$ 3,414	$ 4,270	$ 1,922	$ 12,043

		Real estate			
September 30, 2014	Commercial	Commercial	Residential	Consumer	Total
Allowance for loan losses:					
Beginning Balance July 1, 2014	$ 2,201	$ 2,675	$ 3,458	$ 1,288	$ 9,622
Charge-offs		(57)	(56)	(64)	(177)
Recoveries	5	22		33	60
Provisions	152	185	239	90	666
Ending balance	$ 2,358	$ 2,825	$ 3,641	$ 1,347	$ 10,171

		Real estate			
September 30, 2015	Commercial	Commercial	Residential	Consumer	Total
Allowance for loan losses:					
Beginning Balance January 1, 2015	$ 2,321	$ 3,037	$ 3,690	$ 1,290	$ 10,338
Charge-offs	(40)	(199)	(362)	(253)	(854)
Recoveries	66	8	10	75	159
Provisions	90	568	932	810	2,400
Ending balance	$ 2,437	$ 3,414	$ 4,270	$ 1,922	$ 12,043

		Real estate			
September 30, 2014	Commercial	Commercial	Residential	Consumer	Total
Allowance for loan losses:					
Beginning Balance January 1, 2014	$ 2,008	$ 2,394	$ 3,135	$ 1,114	$ 8,651

Charge-offs	(376)	(489)	(566)	(219)	(1,650)
Recoveries	6	291	38	111	446
Provisions	720	629	1,034	341	2,724
Ending balance	$ 2,358	$ 2,825	$ 3,641	$ 1,347	$ 10,171

15

Table of Contents

Peoples Financial Services Corp.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands, except per share data)

The allocation of the allowance for loan losses and the related loans by major classifications of loans at September 30, 2015 and December 31, 2014 is summarized as follows:

September 30, 2015	Commercial	Real estate Commercial	Residential	Consumer	Unallocated	Total
Allowance for loan losses:						
Ending balance	$ 2,437	$ 3,414	$ 4,270	$ 1,922	$	$ 12,043
Ending balance: individually evaluated for impairment	2,032	269	1,000	179		3,480
Ending balance: collectively evaluated for impairment	405	3,038	3,270	1,743		8,456
Ending balance: loans acquired with deteriorated credit quality	$	$ 107	$	$		$ 107
Loans receivable:						
Ending balance	$ 342,937	$ 529,499	$ 306,740	$ 91,369	$	$ 1,270,545
Ending balance: individually evaluated for impairment	3,120	5,309	4,829	191		13,449
Ending balance: collectively evaluated for impairment	338,780	522,812	301,857	91,178		1,254,627
Ending balance: loans acquired with deteriorated credit quality	1,037	1,378	54			$ 2,469

December 31, 2014	Commercial	Real estate Commercial	Residential	Consumer	Unallocated	Total
Allowance for loan losses:						
Ending balance	$ 2,321	$ 3,037	$ 3,690	$ 1,290	$	$ 10,338
Ending balance: individually evaluated for	1,072	805	767	38		2,682

impairment						
Ending balance: collectively evaluated for impairment	1,081	2,125	2,921	1,252		7,379
Ending balance: loans acquired with deteriorated credit quality	$ 168	$ 107	$ 2	$		$ 277
Loans receivable:						
Ending balance	$ 319,590	$ 493,481	$ 322,454	$ 74,369	$	$ 1,209,894
Ending balance: individually evaluated for impairment	2,595	5,084	4,001	127		11,807
Ending balance: collectively evaluated for impairment	315,642	487,024	318,395	$ 74,242		1,195,303
Ending balance: loans acquired with deteriorated credit quality	$ 1,353	$ 1,373	$ 58		$	$ 2,784

The Company segments loans into risk categories based on relevant information about the ability of borrowers to service their debt such as current financial information, historical payment experience, credit documentation, public information, and current economic trends, among other factors. Loans are individually analyzed for credit risk by classifying them within the Company’s internal risk rating system. The Company’s risk rating classifications are defined as follows:

· Pass- A loan to borrowers with acceptable credit quality and risk that is not adversely classified as Substandard, Doubtful, Loss nor designated as Special Mention.

· Special Mention- A loan that has potential weaknesses that deserves management’s close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan

Table of Contents

Peoples Financial Services Corp.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands, except per share data)

or in the institution's credit position at some future date. Special Mention loans are not adversely classified since they do not expose the Company to sufficient risk to warrant adverse classification.

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

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

· Loss- A loan classified as Loss is considered uncollectible and of such little value that its continuance as bankable loan is not warranted. This classification does not mean that the loan has absolutely no recovery or salvage value, but rather it is not practical or desirable to defer writing off this basically worthless asset even though partial recovery may be affected in the future.

The following tables present the major classification of loans summarized by the aggregate pass rating and the classified ratings of special mention, substandard and doubtful within the Company's internal risk rating system at September 30, 2015 and December 31, 2014:

September 30, 2015	Pass	Special Mention	Substandard	Doubtful	Total
Commercial	$ 329,803	$ 3,690	$ 9,444	$	$ 342,937
Real estate:					
Commercial	502,017	10,395	17,087		529,499
Residential	295,998	1,438	9,304		306,740
Consumer	91,178		191		91,369
Total	$ 1,218,996	$ 15,523	$ 36,026	$	$ 1,270,545

December 31, 2014	Pass	Special Mention	Substandard	Doubtful	Total

Commercial	$ 306,066	$ 6,135	$ 7,389	$	$ 319,590
Real estate:					
Commercial	472,270	9,858	11,353		493,481
Residential	312,086	2,123	8,245		322,454
Consumer	74,250	13	106		74,369
Total	$ 1,164,672	$ 18,129	$ 27,093	$	$ 1,209,894

Information concerning nonaccrual loans by major loan classification at September 30, 2015 and December 31, 2014 is summarized as follows:

	September 30, 2015	December 31, 2014
Commercial	$ 1,444	$ 1,322
Real estate:		
Commercial	3,415	3,732
Residential	4,326	3,523
Consumer	190	122
Total	$ 9,375	$ 8,699

Table of Contents

Peoples Financial Services Corp.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands, except per share data)

The major classifications of loans by past due status are summarized as follows:

September 30, 2015	30-59 Days Past Due	60-89 Days Past Due	Greater than 90 Days	Total Past Due	Current	Total Loans	Loans > 90 Days and Accruing
Commercial	$ 503	$	$ 1,444	$ 1,947	$ 340,990	$ 342,937	
Real estate:							
Commercial	1,371	908	3,415	5,694	523,805	529,499	
Residential	883	631	5,684	7,198	299,542	306,740	$ 1,358
Consumer	608	258	463	1,329	90,040	91,369	273
Total	$ 3,365	$ 1,797	$ 11,006	$ 16,168	$ 1,254,377	$ 1,270,545	$ 1,631

December 31, 2014	30-59 Days Past Due	60-89 Days Past Due	Greater than 90 Days	Total Past Due	Current	Total Loans	Loans > 90 Days and Accruing
Commercial	$ 898	$ 117	$ 1,322	$ 2,337	$ 317,253	$ 319,590	
Real estate:							
Commercial	2,100	888	3,868	6,856	486,625	493,481	$ 136
Residential	3,154	1,239	4,585	8,978	313,476	322,454	1,062
Consumer	848	247	547	1,642	72,727	74,369	425
Total	$ 7,000	$ 2,491	$ 10,322	$ 19,813	$ 1,190,081	$ 1,209,894	$ 1,623

The following tables summarize information concerning impaired loans as of and for the three and nine months ended September 30, 2015 and September 30, 2014, and as of and for the year ended, December 31, 2014 by major loan classification: