

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 March 31, 2021

Commission file number 0-7818

INDEPENDENT BANK CORPORATION

(Exact name of registrant as specified in its charter)

Michigan

(State or jurisdiction of Incorporation or Organization)

38-2032782

(I.R.S. Employer Identification Number)

4200 East Beltline, Grand Rapids, Michigan 49525

(Address of principal executive offices)

(616) 527-5820

(Registrant's telephone number, including area code)

NONE

Former name, address and fiscal year, if changed since last report.

Securities registered pursuant to Section 12(b) of the Act:

Title of each Class	Trading Symbol	Name of each exchange which registered
<u>Common stock, no par value</u>	<u>IBCP</u>	<u>The Nasdaq Stock Market, LLC</u>

Indicate by check mark whether the registrant (1) has filed all documents and reports required to be filed by Sections 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 (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).
Yes NO

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, non-accelerated filer, smaller reporting company or an emerging growth company.
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. Yes No

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date: common stock, no par value, 21,785,299 as of May 5, 2021.

INDEPENDENT BANK CORPORATION AND SUBSIDIARIES
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FORWARD-LOOKING STATEMENTS

Statements in this report that are not statements of historical fact, including statements that include terms such as “will,” “may,” “should,” “believe,” “expect,” “forecast,” “anticipate,” “estimate,” “project,” “intend,” “likely,” “optimistic” and “plan” and statements about future or projected financial and operating results, plans, projections, objectives, expectations, and intentions, are forward-looking statements. Forward-looking statements include, but are not limited to, descriptions of plans and objectives for future operations, products or services; projections of our future revenue, earnings or other measures of economic performance; forecasts of credit losses and other asset quality trends; statements about our business and growth strategies; and expectations about economic and market conditions and trends. These forward-looking statements express our current expectations, forecasts of future events, or long-term goals. They are based on assumptions, estimates, and forecasts that, although believed to be reasonable, may turn out to be incorrect. Actual results could differ materially from those discussed in the forward-looking statements for a variety of reasons, including:

- economic, market, operational, liquidity, credit, and interest rate risks associated with our business including the impact of the ongoing COVID-19 pandemic on each of these items;
- economic conditions generally and in the financial services industry, particularly economic conditions within Michigan and the regional and local real estate markets in which our bank operates including the economic impact of the ongoing COVID-19 pandemic in each of these areas;
- the failure of assumptions underlying the establishment of, and provisions made to, our allowance for credit losses;
- increased competition in the financial services industry, either nationally or regionally;
- our ability to achieve loan and deposit growth;
- volatility and direction of market interest rates;
- the continued services of our management team; and
- implementation of new legislation, which may have significant effects on us and the financial services industry.

This list provides examples of factors that could affect the results described by forward-looking statements contained in this report, but the list is not intended to be all-inclusive. The risk factors disclosed in Part I – Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2020, as updated by any new or modified risk factors disclosed in Part II – Item 1A of any subsequently filed Quarterly Report on Form 10-Q, include the known risks our management believes could materially affect the results described by forward-looking statements in this report. However, those risks may not be the only risks we face. Our results of operations, cash flows, financial position, and prospects could also be materially and adversely affected by additional factors that are not presently known to us that we currently consider to be immaterial, or that develop after the date of this report. We cannot assure you that our future results will meet expectations. While we believe the forward-looking statements in this report are reasonable, you should not place undue reliance on any forward-looking statement. In addition, these statements speak only as of the date made. We do not undertake, and expressly disclaim, any obligation to update or alter any statements, whether as a result of new information, future events, or otherwise, except as required by applicable law.

INDEPENDENT BANK CORPORATION AND SUBSIDIARIES
Condensed Consolidated Statements of Financial Condition

	March 31, 2021	December 31, 2020
	(unaudited)	
	(In thousands, except share amounts)	
Assets		
Cash and due from banks	\$ 49,220	\$ 56,006
Interest bearing deposits	81,287	62,699
	Cash and Cash Equivalents	130,507
	1,247,280	1,072,159
Securities available for sale	18,427	18,427
Federal Home Loan Bank and Federal Reserve Bank stock, at cost	77,799	92,434
Loans held for sale, carried at fair value		
Loans		
Commercial	1,301,223	1,242,415
Mortgage	999,982	1,015,926
Installment	483,019	475,337
	Total Loans	2,784,224
	(46,755)	(35,429)
Allowance for credit losses (1)	Net Loans	2,737,469
	346	766
Other real estate and repossessed assets, net	36,736	36,127
Property and equipment, net	55,318	55,180
Bank-owned life insurance	23,530	16,904
Capitalized mortgage loan servicing rights, carried at fair value	4,063	4,306
Other intangibles	28,300	28,300
Goodwill	66,665	62,456
Accrued income and other assets	Total Assets	\$ 4,426,440
	\$ 4,426,440	\$ 4,204,013
Liabilities and Shareholders' Equity		
Deposits		
Non-interest bearing	\$ 1,301,842	\$ 1,153,473
Savings and interest-bearing checking	1,670,106	1,526,465
Reciprocal	608,689	556,185
Time	275,022	287,402
Brokered time	2,916	113,830
	Total Deposits	3,858,575
	30,006	30,012
Other borrowings	39,300	39,281
Subordinated debt	39,541	39,524
Subordinated debentures	71,689	68,319
Accrued expenses and other liabilities	Total Liabilities	4,039,111
	4,039,111	3,814,491
Commitments and contingent liabilities		
Shareholders' Equity		
Preferred stock, no par value, 200,000 shares authorized; none issued or outstanding	-	-
Common stock, no par value, 500,000,000 shares authorized; issued and outstanding: 21,773,734 shares at March 31, 2021 and 21,853,800 shares at December 31, 2020	335,704	339,353
Retained earnings	47,287	40,145
Accumulated other comprehensive income	4,338	10,024
	Total Shareholders' Equity	387,329
	Total Liabilities and Shareholders' Equity	\$ 4,426,440
	\$ 4,426,440	\$ 4,204,013

(1) Beginning January 1, 2021, calculation is based on CECL methodology. Prior to January 1, 2021, calculation was based on the probable incurred loss methodology.

See notes to interim condensed consolidated financial statements (unaudited)

INDEPENDENT BANK CORPORATION AND SUBSIDIARIES
Condensed Consolidated Statements of Operations

	Three months ended March 31,	
	2021	2020
	(unaudited)	
	(In thousands, except per share amounts)	
Interest Income		
Interest and fees on loans	\$ 28,105	\$ 31,764
Interest on securities available for sale		
Taxable	2,796	3,059
Tax-exempt	1,384	390
Other investments	217	366
Total Interest Income	<u>32,502</u>	<u>35,579</u>
Interest Expense		
Deposits	1,256	4,700
Other borrowings and subordinated debt and debentures	962	688
Total Interest Expense	<u>2,218</u>	<u>5,388</u>
Net Interest Income	30,284	30,191
Provision for credit losses (1)	(474)	6,721
Net Interest Income After Provision for Credit Losses	<u>30,758</u>	<u>23,470</u>
Non-interest Income		
Interchange income	3,049	2,457
Service charges on deposit accounts	1,916	2,591
Net gains on assets		
Mortgage loans	12,828	8,840
Securities available for sale	1,416	253
Mortgage loan servicing, net	5,167	(5,300)
Other	2,030	2,163
Total Non-interest Income	<u>26,406</u>	<u>11,004</u>
Non-interest Expense		
Compensation and employee benefits	18,522	16,509
Occupancy, net	2,343	2,460
Data processing	2,374	2,355
Furniture, fixtures and equipment	1,003	1,036
Interchange expense	948	859
Communications	881	803
Loan and collection	759	805
Advertising	489	683
Legal and professional	499	393
FDIC deposit insurance	330	370
Other	1,873	2,446
Total Non-interest Expense	<u>30,021</u>	<u>28,719</u>
Income Before Income Tax	27,143	5,755
Income tax expense	5,106	945
Net Income	<u>\$ 22,037</u>	<u>\$ 4,810</u>
Net Income Per Common Share		
Basic	<u>\$ 1.01</u>	<u>\$ 0.22</u>
Diluted	<u>\$ 1.00</u>	<u>\$ 0.21</u>

(1) Beginning January 1, 2021, calculation is based on CECL methodology. Prior to January 1, 2021, calculation was based on the probable incurred loss methodology.

See notes to interim condensed consolidated financial statements (unaudited)

INDEPENDENT BANK CORPORATION AND SUBSIDIARIES
Condensed Consolidated Statements of Comprehensive Income

	Three months ended March 31,	
	2021	2020
	(unaudited - In thousands)	
Net income	\$ 22,037	\$ 4,810
Other comprehensive income		
Securities available for sale		
Unrealized losses arising during period	(5,781)	(598)
Change in unrealized gains and losses for which a portion of other than temporary impairment has been recognized in earnings	-	(169)
Reclassification adjustments for gains included in earnings	(1,416)	(253)
Unrealized losses recognized in other comprehensive loss on securities available for sale	(7,197)	(1,020)
Income tax benefit	(1,511)	(214)
Unrealized losses recognized in other comprehensive loss on securities available for sale, net of tax	(5,686)	(806)
Derivative instruments		
Unrealized loss arising during period	-	(406)
Reclassification adjustment for expense recognized in earnings	-	75
Unrealized losses recognized in other comprehensive loss on derivative instruments	-	(331)
Income tax benefit	-	(69)
Unrealized losses recognized in other comprehensive loss on derivative instruments, net of tax	-	(262)
Other comprehensive loss	(5,686)	(1,068)
Comprehensive income	\$ 16,351	\$ 3,742

See notes to interim condensed consolidated financial statements (unaudited)

INDEPENDENT BANK CORPORATION AND SUBSIDIARIES
Condensed Consolidated Statements of Cash Flows

	Three months ended March 31,	
	2021	2020
	(unaudited - In thousands)	
Net Income	\$ 22,037	\$ 4,810
Adjustments to Reconcile Net Income to Net Cash From Operating Activities		
Proceeds from sales of loans held for sale	392,844	241,856
Disbursements for loans held for sale	(365,381)	(227,765)
Provision for credit losses (1)	(474)	6,721
Deferred income tax expense (benefit)	2,067	(1,925)
Net deferred loan fees (costs)	2,982	(358)
Net depreciation, amortization of intangible assets and premiums and accretion of discounts on securities, loans and interest bearing deposits - time	3,158	1,795
Net gains on mortgage loans	(12,828)	(8,840)
Net gains on securities available for sale	(1,416)	(253)
Share based compensation	442	547
Increase in accrued income and other assets	(8,461)	5,095
Increase in accrued expenses and other liabilities	95	599
Total Adjustments	13,028	17,472
Net Cash From Operating Activities	35,065	22,282
Cash Flow Used in Investing Activities		
Proceeds from the sale of securities available for sale	78,179	21,743
Proceeds from maturities, prepayments and calls of securities available for sale	107,834	42,744
Purchases of securities available for sale	(367,654)	(103,901)
Proceeds from the maturity of interest bearing deposits - time	-	350
Net increase in portfolio loans (loans originated, net of principal payments)	(52,939)	(22,432)
Proceeds from the sale of portfolio loans	-	2,395
Proceeds from bank-owned life insurance	-	945
Proceeds from the sale of other real estate and repossessed assets	733	328
Capital expenditures	(1,947)	(760)
Net Cash Used in Investing Activities	(235,794)	(58,588)
Cash Flow From Financing Activities		
Net increase in total deposits	221,220	46,837
Net increase (decrease) in other borrowings	(6)	6,296
Proceeds from Federal Home Loan Bank Advances	-	160,000
Payments of Federal Home Loan Bank Advances	-	(153,000)
Dividends paid	(4,592)	(4,477)
Proceeds from issuance of common stock	19	11
Repurchase of common stock	(3,601)	(13,784)
Share based compensation withholding obligation	(509)	(590)
Net Cash From Financing Activities	212,531	41,293
Net Increase in Cash and Cash Equivalents	11,802	4,987
Cash and Cash Equivalents at Beginning of Period	118,705	65,304
Cash and Cash Equivalents at End of Period	\$ 130,507	\$ 70,291
Cash paid during the period for		
Interest	\$ 1,669	\$ 5,489
Income taxes	-	-
Operating leases	439	476
Transfers to other real estate and repossessed assets	133	66
Purchase of securities available for sale not yet settled	7,212	10,497
Securitization of portfolio loans	-	26,325
Right of use assets obtained in exchange for lease obligations	-	116

(1) Beginning January 1, 2021, calculation is based on CECL methodology. Prior to January 1, 2021, calculation was based on the probable incurred loss methodology.

See notes to interim condensed consolidated financial statements (unaudited)

INDEPENDENT BANK CORPORATION AND SUBSIDIARIES
Condensed Consolidated Statements of Shareholders' Equity

	Common Stock	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Shareholders' Equity
	(Dollars in thousands, except per share amounts)			
Balances at January 1, 2021	\$ 339,353	\$ 40,145	\$ 10,024	\$ 389,522
Adoption of ASU 2016-13	-	(10,303)	-	(10,303)
Balances at January 1, 2021, as adjusted	339,353	29,842	10,024	379,219
Net income, three months ended March 31, 2021	-	22,037	-	22,037
Cash dividends declared, \$0.21 per share	-	(4,592)	-	(4,592)
Repurchase of 180,667 shares of common stock	(3,601)	-	-	(3,601)
Issuance of 19,050 shares of common stock	19	-	-	19
Share based compensation (issuance of 109,075 shares of common stock)	442	-	-	442
Share based compensation withholding obligation (withholding of 27,524 shares of common stock)	(509)	-	-	(509)
Other comprehensive income	-	-	(5,686)	(5,686)
Balances at March 31, 2021	<u>\$ 335,704</u>	<u>\$ 47,287</u>	<u>\$ 4,338</u>	<u>\$ 387,329</u>
Balances at January 1, 2020	\$ 352,344	\$ 1,611	\$ (3,786)	\$ 350,169
Net income, three months ended March 31, 2020	-	4,810	-	4,810
Cash dividends declared, \$0.20 per share	-	(4,477)	-	(4,477)
Repurchase of 678,929 shares of common stock	(13,784)	-	-	(13,784)
Issuance of 11,567 shares of common stock	11	-	-	11
Share based compensation (issuance of 105,894 shares of common stock)	547	-	-	547
Share based compensation withholding obligation (withholding of 28,174 shares of common stock)	(590)	-	-	(590)
Other comprehensive income	-	-	(1,068)	(1,068)
Balances at March 31, 2020	<u>\$ 338,528</u>	<u>\$ 1,944</u>	<u>\$ (4,854)</u>	<u>\$ 335,618</u>

See notes to interim condensed consolidated financial statements (unaudited)

1. Preparation of Financial Statements

The condensed consolidated financial statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and note disclosures normally included in annual financial statements prepared in accordance with U.S. generally accepted accounting principles (“GAAP”) have been condensed or omitted pursuant to those rules and regulations, although we believe that the disclosures made are adequate to make the information not misleading. The unaudited condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes for the year ended December 31, 2020 included in our Annual Report on Form 10-K.

In our opinion, the accompanying unaudited condensed consolidated financial statements contain all the adjustments necessary to present fairly our consolidated financial condition as of March 31, 2021 and December 31, 2020, and the results of operations for the three month periods ended March 31, 2021 and 2020. The results of operations for the three month period ended March 31, 2021, are not necessarily indicative of the results to be expected for the full year. Certain reclassifications have been made in the prior period condensed consolidated financial statements to conform to the current period presentation. Our critical accounting policies include the determination of the allowance for credit losses (“ACL”) and the valuation of capitalized mortgage loan servicing rights. Refer to our 2020 Annual Report on Form 10-K for a disclosure of our accounting policies.

2. New Accounting Standards

In June 2016, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) 2016-13, “Financial Instruments — Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments”. This ASU significantly changes how entities will measure credit losses for most financial assets and certain other instruments that are not measured at fair value through net income.

This ASU:

- Replaces the existing incurred loss impairment guidance and establishes a single allowance framework for financial assets carried at amortized cost, which will reflect our estimate of credit losses over the full remaining expected life of the financial assets and will consider expected future changes in macroeconomic conditions.
- Eliminates existing guidance for purchase credit impaired (“PCI”) loans, and requires recognition of the nonaccretable difference as an increase to the allowance for expected credit losses on financial assets purchased with more than insignificant credit deterioration since origination, which will be offset by an increase in the recorded investment of the related loans.
- Requires inclusion of expected recoveries, limited to the cumulative amount of prior write-offs, when estimating the ACL for in scope financial assets (including collateral dependent assets).
- Amends existing impairment guidance for securities available for sale to incorporate an allowance, which will allow for reversals of credit impairments in the event that the credit of an issuer improves. Credit losses on securities available for sale are limited to the amount of the decline in fair value regardless of what the credit loss model would show for impairment.
- Generally requires a cumulative-effect adjustment to retained earnings as of the beginning of the reporting period of adoption.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

We began evaluating this ASU in 2016 and established a company-wide, cross-discipline governance structure, which provides implementation oversight. We continued to test and refine our current expected credit loss (“CECL”) models that satisfied the requirements of this ASU. Oversight and testing, as well as efforts to meet expanded disclosure requirements, extended through the end of 2020. We currently estimate losses over approximately a one year forecast period using external economic forecast sources, including the Federal Open Market Committee median economic projections, and then revert to longer term historical loss experience to estimate losses over more extended periods. We were originally required to adopt this ASU on January 1, 2020 but section 4014 of the Coronavirus Aid, Relief, and Economic Security (“CARES”) Act allowed for temporary relief from applying this ASU. Under the amended CARES Act we were allowed to delay the adoption of this ASU until the earlier of the termination of the national emergency that was declared on March 13, 2020, or January 1, 2022. Early adoption was also allowed on either January 1, 2020 or January 1, 2021. As such, we chose to delay the adoption of this ASU during 2020 and adopted this ASU on January 1, 2021. Results for the reporting periods after January 1, 2021 are presented under this new ASU while prior period amounts continue to be reported in accordance with previously applicable accounting guidance.

We adopted this ASU using the modified retrospective method for all financial assets measured at amortized cost and unfunded lending commitments. As of January 1, 2021 we increased the ACL by \$11.7 million which was primarily driven by the longer contractual maturities of our mortgage and consumer installment loan portfolio segments. In addition, we increased the allowance for losses related to unfunded loan commitments by \$1.5 million. The ultimate impact of adopting this ASU, and at each subsequent reporting period, is highly dependent on credit quality, economic forecasts and conditions, composition of our loan portfolios and securities available for sale, along with other management judgments. As of January 1, 2021, we recorded a cumulative-effect adjustment of \$10.3 million to decrease retained earnings.

Based on our evaluation of securities available for sale, we did not record an ACL on these securities under this ASU.

We adopted this ASU using the prospective transition approach for financial assets purchased with credit deterioration (“PCD”) that were previously classified as PCI and accounted for under accounting standards codification (“ASC”) 310-30. In accordance with this ASU, we did not reassess whether PCI assets met the definition of PCD assets as of the date of adoption. On January 1, 2021, the amortized cost basis of the PCD assets were adjusted to reflect the addition of \$0.13 million to the ACL for loans. The remaining noncredit discount in the amount of \$0.34 million (based on the adjusted amortized cost basis) will be accreted into interest income at the effective interest rate as of January 1, 2021.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

The impact of the adoption of this ASU follows:

	As Reported Under ASU 2016-13	Pre-ASU 2016-13 Adoption	Impact of ASU 2016-13
Assets			
Loans			
Commercial	\$ 1,242,510	\$ 1,242,415	\$ 95
Mortgage	1,015,944	1,015,926	18
Installment	475,358	475,337	21
Total loans	2,733,812	2,733,678	134
Allowance for credit losses	(47,137)	(35,429)	(11,708)
Net loans	\$ 2,686,675	\$ 2,698,249	\$ (11,574)
Deferred tax assets (1)	\$ 65,196	\$ 62,456	\$ 2,740
Total Assets	\$ 4,195,179	\$ 4,204,013	\$ (8,834)
Liabilities and shareholders's equity			
Allowance for credit losses on unfunded lending commitments (2)	\$ 3,274	\$ 1,805	\$ 1,469
Total liabilities	\$ 3,815,960	\$ 3,814,491	\$ 1,469
Retained earnings	\$ 29,842	\$ 40,145	\$ (10,303)
Total shareholders' equity	\$ 379,219	\$ 389,522	\$ (10,303)
Total liabilities and shareholders' equity	\$ 4,195,179	\$ 4,204,013	\$ (8,834)

(1) Included in Accrued income and other assets in our Condensed Consolidated Statements of Financial Condition.

(2) Included in Accrued expenses and other liabilities in our Condensed Consolidated Statements of Financial Condition.

In March 2020, the FASB issued ASU 2020-04, "Reference Rate Reform (Topic 848), Facilitation of the Effects of Reference Rate Reform on Financial Reporting". This new ASU provides temporary optional expedients and exceptions to GAAP guidance on contract modifications and hedge accounting to ease the financial reporting burdens of the expected market transition from LIBOR and other interbank offered rates to alternative reference rates. Entities can elect not to apply certain modification accounting requirements to contracts affected by reference rate reform, if certain criteria are met. Entities that make such elections would not have to remeasure contracts at the modification date or reassess a previous accounting determination. Entities can elect various optional expedients that would allow them to continue applying hedge accounting for hedging relationships affected by reference rate reform, if certain criteria are met. This amended guidance and our ability to elect its temporary optional expedients and exceptions are effective for us as of March 12, 2020 through December 31, 2022.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

3. Securities

Securities available for sale consist of the following:

	Amortized Cost	Unrealized		Fair Value
		Gains	Losses	
(In thousands)				
March 31, 2021				
U.S. agency	\$ 8,721	\$ 201	\$ 12	\$ 8,910
U.S. agency residential mortgage-backed	399,290	3,315	2,185	400,420
U.S. agency commercial mortgage-backed	11,516	194	6	11,704
Private label mortgage-backed	41,624	1,261	68	42,817
Other asset backed	226,812	1,810	92	228,530
Obligations of states and political subdivisions	438,721	7,274	1,307	444,688
Corporate	105,293	2,866	336	107,823
Trust preferred	1,973	-	99	1,874
Foreign government	500	14	-	514
Total	<u>\$ 1,234,450</u>	<u>\$ 16,935</u>	<u>\$ 4,105</u>	<u>\$ 1,247,280</u>
December 31, 2020				
U.S. agency	\$ 10,456	\$ 305	\$ 13	\$ 10,748
U.S. agency residential mortgage-backed	340,224	4,951	593	344,582
U.S. agency commercial mortgage-backed	6,869	326	-	7,195
Private label mortgage-backed	41,429	1,539	139	42,829
Other asset backed	252,596	1,796	211	254,181
Obligations of states and political subdivisions	315,780	8,691	178	324,293
Corporate	82,307	3,807	97	86,017
Trust preferred	1,971	-	173	1,798
Foreign government	500	16	-	516
Total	<u>\$ 1,052,132</u>	<u>\$ 21,431</u>	<u>\$ 1,404</u>	<u>\$ 1,072,159</u>

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

Our investments' gross unrealized losses and fair values aggregated by investment type and length of time that individual securities have been at a continuous unrealized loss position follows:

	Less Than Twelve Months		Twelve Months or More		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
	(In thousands)					
March 31, 2021						
U.S. agency	\$ 1,394	\$ 3	\$ 2,219	\$ 9	\$ 3,613	\$ 12
U.S. agency residential mortgage-backed	185,615	2,184	36	1	185,651	2,185
U.S. agency commercial mortgage-backed	646	6	-	-	646	6
Private label mortgage-backed	2,053	25	3,662	43	5,715	68
Other asset backed	8,407	17	10,465	75	18,872	92
Obligations of states and political subdivisions	87,301	1,307	-	-	87,301	1,307
Corporate	20,403	323	560	13	20,963	336
Trust preferred	-	-	1,874	99	1,874	99
Total	\$ 305,819	\$ 3,865	\$ 18,816	\$ 240	\$ 324,635	\$ 4,105
December 31, 2020						
U.S. agency	\$ 1,469	\$ 3	\$ 2,329	\$ 10	\$ 3,798	\$ 13
U.S. agency residential mortgage-backed	96,839	592	83	1	96,922	593
Private label mortgage-backed	11,838	95	2,050	44	13,888	139
Other asset backed	7,142	25	21,197	186	28,339	211
Obligations of states and political subdivisions	28,957	177	800	1	29,757	178
Corporate	1,924	97	-	-	1,924	97
Trust preferred	-	-	1,798	173	1,798	173
Total	\$ 148,169	\$ 989	\$ 28,257	\$ 415	\$ 176,426	\$ 1,404

Securities available for sale in unrealized loss positions are evaluated quarterly for impairment related to credit losses. For securities available for sale in an unrealized loss position, we first assess whether we intend to sell, or it is more likely than not that we will be required to sell the security before recovery of its amortized cost basis. If either of the criteria regarding intent or requirement to sell is met, the security's amortized cost basis is written down to fair value through income. For securities available for sale that do not meet this criteria, we evaluate whether the decline in fair value has resulted from credit losses or other factors. In making this assessment, we consider the extent to which fair value is less than amortized cost, adverse conditions specifically related to the security and the issuer and the impact of changes in market interest rates on the market value of the security, among other factors. If this assessment indicates that a credit loss exists, we compare the present value of cash flows expected to be collected from the security with the amortized cost basis of the security. If the present value of cash flows expected to be collected is less than the amortized cost basis for the security, a credit loss exists and an ACL is recorded, limited to the amount that the fair value of the security is less than its amortized cost basis. Any impairment that has not been recorded through an ACL is recognized in other comprehensive income, net of applicable taxes. No ACL for securities available for sale was needed at March 31, 2021. Accrued interest receivable on securities available for sale totaled \$5.1 million at March 31, 2021 and is excluded from the estimate of credit losses.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

U.S. agency, U.S. agency residential mortgage-backed and U.S. agency commercial mortgage-backed securities — at March 31, 2021, we had 25 U.S. agency, 57 U.S. agency residential mortgage-backed and two U.S. agency commercial mortgage-backed securities whose fair value is less than amortized cost. These securities are either explicitly or implicitly guaranteed by the U.S. government, are highly rated by major credit rating agencies, and have a long history of no credit losses. The unrealized losses are largely attributed to widening spreads to Treasury bonds and/or an increase in interest rates since acquisition.

Private label mortgage backed, other asset backed and corporate securities — at March 31, 2021, we had 11 private label mortgage backed, 20 other asset backed and 19 corporate securities whose fair value is less than amortized cost. The unrealized losses are primarily due to credit spread widening and/or an increase in interest rates since acquisition.

Obligations of states and political subdivisions — at March 31, 2021, we had 107 municipal securities whose fair value is less than amortized cost. The unrealized losses are primarily due to an increase in interest rates since acquisition.

Trust preferred securities — at March 31, 2021, we had two trust preferred securities whose fair value is less than amortized cost. Both of our trust preferred securities are single issue securities issued by a trust subsidiary of a bank holding company. The pricing of trust preferred securities has suffered from credit spread widening. One of the securities is rated by a major rating agency as investment grade while the other one is non-rated. The non-rated issue is a relatively small bank and was never rated. The issuer of this non-rated trust preferred security, which had a total amortized cost of \$1.0 million and total fair value of \$0.92 million as of March 31, 2021, continues to have satisfactory credit metrics and make interest payments.

At March 31, 2021 management does not intend to liquidate any of the securities discussed above and it is more likely than not that we will not be required to sell these securities prior to recovery of these unrealized losses.

We recorded no credit related charges in our Condensed Consolidated Statements of Operations related to securities available for sale during the three month periods ended March 31, 2021 and 2020, respectively.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

The amortized cost and fair value of securities available for sale at March 31, 2021, by contractual maturity, follow:

	Amortized Cost	Fair Value
	(In thousands)	
Maturing within one year	\$ 22,748	\$ 22,888
Maturing after one year but within five years	99,528	102,202
Maturing after five years but within ten years	83,969	85,830
Maturing after ten years	348,963	352,889
	<u>555,208</u>	<u>563,809</u>
U.S. agency residential mortgage-backed	399,290	400,420
U.S. agency commercial mortgage-backed	11,516	11,704
Private label mortgage-backed	41,624	42,817
Other asset backed	226,812	228,530
Total	<u>\$ 1,234,450</u>	<u>\$ 1,247,280</u>

The actual maturity may differ from the contractual maturity because issuers may have the right to call or prepay obligations with or without call or prepayment penalties.

Gains and losses realized on the sale of securities available for sale are determined using the specific identification method and are recognized on a trade-date basis. A summary of proceeds from the sale of securities available for sale and gains and losses for the three month periods ending March 31, follows:

	Proceeds	Realized	
		Gains	Losses
		(In thousands)	
2021	\$ 78,179	\$ 1,464	\$ 48
2020	21,743	253	-

4. Loans

We estimate the ACL based on relevant available information from both internal and external sources, including historical loss trends, current conditions and forecasts, specific analysis of individual loans, and a review of other relevant and appropriate factors. The allowance process is designed to provide for expected future losses based on our reasonable and supportable (“R&S”) forecast as of the reporting date. Our ACL process is administered by our Risk Management group utilizing a third party software solution, with significant input and ultimate approval from our Executive Enterprise Risk Committee. Further, we have established a CECL Forecast Committee, which includes a cross discipline structure with membership from Executive Management, Risk Management, and Accounting, which approves ACL model assumptions each quarter. Our ACL is comprised of three principal elements: (i) specific analysis of individual loans identified during the review of the loan portfolio, (ii) pooled analysis of loans with similar risk characteristics based on historical experience, adjusted for current conditions, R&S forecasts, and expected prepayments, and (iii) additional allowances based on subjective factors, including local and general economic business factors and trends, portfolio concentrations and changes in the size and/or the general terms of the loan portfolios.

The first ACL element (specific allocations) includes loans that do not share similar risk characteristics and are evaluated on an individual basis. We will typically evaluate on an individual basis loans that are on nonaccrual, commercial loans designated as a TDR, or mortgage and installment TDR loans with a rate concession. When we determine that foreclosure is probable or when repayment is expected to be provided substantially through the operation or sale of underlying collateral, expected credit losses are based on the fair value of the collateral at the reporting date, adjusted for selling costs. For loans evaluated on an individual basis that are not determined to be collateral dependent, a discounted cash flow analysis is performed to determine expected credit losses.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

The second ACL element (pooled analysis) includes loans with similar risk characteristics, which are broken down by segment, class, and risk metric. The Bank's primary segments of commercial, mortgage, and installment loans are further classified by other relevant attributes, such as collateral type, lien position, occupancy status, amortization method, and balance size. Commercial classes are additionally segmented by risk rating, and mortgage and installment loan classes by credit score tier, which are updated at least semi-annually.

We utilize a discounted cash flow ("DCF") model to estimate expected future losses for pooled loans. Expected future cash flows are developed from payment schedules over the contractual term, adjusted for forecasted default (probability of default), loss, and prepayment assumptions. We are not required to develop forecasts over the full contractual term of the financial asset or group of financial assets. Rather, for periods beyond which the entity is able to make or obtain R&S forecasts of expected credit losses, we revert to the long term average on a straight line or immediate basis, as determined by the CECL Forecast Committee, and which may vary depending on the economic outlook and uncertainty.

The DCF model for the mortgage and installment pooled loan segments includes using probability of default ("PD") assumptions that are derived through regression analysis with forecasted US unemployment levels by credit score tier. We review the Bloomberg composite forecast of approximately 50 analysts as well as the FOMC projections in setting the unemployment forecast for the R&S period. The current ACL utilizes a one year R&S forecast followed by immediate reversion to the 30 year average unemployment rate. PD assumptions for the remaining segments are based primarily on historical rates by risk metric as defaults were not strongly correlated with any economic indicator. Loss given default ("LGD") assumptions for the mortgage loan segment are based on a two year forecast followed by a two year straight line reversion period to the longer term average, while LGD rates for the remaining segments are the historical average for the entire period. Prepayment assumptions represent the two year average rates per segment as calculated through the Bank's Asset and Liability Management program.

Pooled reserves for the commercial loan segment are calculated using the DCF model with assumptions generally based on historical averages by class and risk rating. Effective risk rating practices allow for strong predictability of defaults and losses over the portfolio's expected shorter duration, relative to mortgage and installment loans. Our rating system is similar to those employed by state and federal banking regulators.

The third ACL element (additional allocations based on subjective factors) is based on factors that cannot be associated with a specific credit or loan category and reflects our attempt to ensure that the overall ACL appropriately reflects a margin for the imprecision necessarily inherent in the estimates of expected credit losses. We adjust our quantitative model for certain qualitative factors to reflect the extent to which management expects current conditions and R&S forecasts to differ from the conditions that existed for the period over which historical information was evaluated. The qualitative framework reflects changes related to relevant data, such as changes in asset quality trends, portfolio growth and composition, national and local economic factors, credit policy and administration and other factors not considered in the base quantitative model. We utilize a survey completed by business unit management throughout the bank, as well as discussion with the CECL Forecast Committee to establish reserves under the qualitative framework. The current period's ACL further recognizes inherent risk related to the ongoing COVID-19 pandemic; specifically to the volume of loans on forbearance, commercial loans in high risk industries, and mortgage and installment borrowers with occupations in those high risk industries. Identified high risk industries include: food service, hospitality, entertainment, retail, investment real estate, assisted living, and non-owner occupied office.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

An analysis of the ACL by portfolio segment for the three month periods ended March 31, follows:

	<u>Commercial</u>	<u>Mortgage</u>	<u>Installment</u> (In thousands)	<u>Subjective Allocation</u>	<u>Total</u>
2021					
Balance at beginning of period	\$ 7,401	\$ 6,998	\$ 1,112	\$ 19,918	\$ 35,429
Additions (deductions)					
Impact of adoption of ASC 326	2,551	12,000	3,052	(6,029)	11,574
Provision for credit losses	(676)	(620)	(87)	909	(474)
Initial allowance on loans purchased with credit deterioration	95	18	21	-	134
Recoveries credited to the allowance	159	212	177	-	548
Loans charged against the allowance	-	(160)	(296)	-	(456)
Balance at end of period	<u>\$ 9,530</u>	<u>\$ 18,448</u>	<u>\$ 3,979</u>	<u>\$ 14,798</u>	<u>\$ 46,755</u>
2020					
Balance at beginning of period	\$ 7,922	\$ 8,216	\$ 1,283	\$ 8,727	\$ 26,148
Additions (deductions)					
Provision for credit losses (1)	2,218	(508)	129	4,882	6,721
Recoveries credited to the allowance	108	117	174	-	399
Loans charged against the allowance	(36)	(409)	(328)	-	(773)
Balance at end of period	<u>\$ 10,212</u>	<u>\$ 7,416</u>	<u>\$ 1,258</u>	<u>\$ 13,609</u>	<u>\$ 32,495</u>

(1) Beginning January 1, 2021, calculation is based on CECL methodology. Prior to January 1, 2021, calculation was based on the probable incurred loss methodology.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

The ACL and recorded investment in loans by portfolio segment at December 31, 2020 follows (1):

	<u>Commercial</u>	<u>Mortgage</u>	<u>Installment</u> (In thousands)	<u>Subjective Allocation</u>	<u>Total</u>
December 31, 2020					
ACL:					
Individually evaluated for impairment	\$ 1,266	\$ 4,124	\$ 191	\$ -	\$ 5,581
Collectively evaluated for impairment	6,135	2,874	921	19,918	29,848
Loans acquired with deteriorated credit quality	-	-	-	-	-
Total ending ACL	<u>\$ 7,401</u>	<u>\$ 6,998</u>	<u>\$ 1,112</u>	<u>\$ 19,918</u>	<u>\$ 35,429</u>
Loans					
Individually evaluated for impairment	\$ 9,431	\$ 39,245	\$ 1,996		\$ 50,672
Collectively evaluated for impairment	1,236,052	980,449	474,379		2,690,880
Loans acquired with deteriorated credit quality	468	410	147		1,025
Total loans recorded investment	1,245,951	1,020,104	476,522		2,742,577
Accrued interest included in recorded investment	3,536	4,178	1,185		8,899
Total loans	<u>\$ 1,242,415</u>	<u>\$ 1,015,926</u>	<u>\$ 475,337</u>		<u>\$ 2,733,678</u>

(1) Beginning January 1, 2021, calculation is based on CECL methodology. Prior to January 1, 2021, calculation was based on the probable incurred loss methodology.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

Loans on non-accrual status and past due more than 90 days (“Non-performing Loans”) follow:

	March 31, 2021					December 31, 2020
	Non- Accrual with no Allowance for Credit Loss	Non-Accrual with an Allowance for Credit Loss	Total Non-Accrual (In thousands)	90+ and Still Accruing	Total Non-Performing Loans	Total Non-Performing Loans (1)
Commercial						
Commercial and industrial (2)	\$ 74	\$ 1,246	\$ 1,320	\$ -	\$ 1,320	\$ 1,387
Commercial real estate	-	-	-	-	-	-
Mortgage						
1-4 family owner occupied - jumbo	619	-	619	-	619	623
1-4 family owner occupied - non-jumbo (3)	-	1,982	1,982	-	1,982	2,281
1-4 family non-owner occupied	280	693	973	-	973	1,112
1-4 family - 2nd lien	186	1,048	1,234	-	1,234	1,344
Resort lending	-	527	527	-	527	607
Installment						
Boat lending	-	72	72	-	72	52
Recreational vehicle lending	-	41	41	-	41	74
Other	-	321	321	-	321	393
Total	\$ 1,159	\$ 5,930	\$ 7,089	\$ -	\$ 7,089	\$ 7,873
Accrued interest excluded from total	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -

(1) Non-performing loans at December 31, 2020 exclude PCI loans.

(2) Non-performing commercial and industrial loans exclude \$0.053 million of government guaranteed loans at both March 31, 2021 and December 31, 2020.

(3) Non-performing 1-4 family owner occupied – non jumbo loans exclude \$0.406 million and \$0.386 million of government guaranteed loans at March 31, 2021 and December 31, 2020, respectively.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

The following table provides collateral information by class of loan for collateral-dependent loans with a specific reserve. A loan is considered to be collateral dependent when the borrower is experiencing financial difficulty and the repayment is expected to be provided substantially through the operation or sale of collateral.

The amortized cost of collateral-dependent loans by class follows:

	<u>Collateral Type</u>		<u>Allowance for Credit Losses</u>
	<u>Real Estate</u>	<u>Other</u>	
	(In thousands)		
March 31, 2021			
Commercial			
Commercial and industrial	\$ 840	\$ 1,209	\$ 681
Commercial real estate	142	-	32
Mortgage			
1-4 family owner occupied - jumbo	619	-	-
1-4 family owner occupied - non-jumbo	886	-	316
1-4 family non-owner occupied	694	-	169
1-4 family - 2nd lien	646	-	163
Resort lending	287	-	48
Installment			
Boat lending	-	11	4
Recreational vehicle lending	-	17	6
Other	77	143	78
Total	<u>\$ 4,191</u>	<u>\$ 1,380</u>	<u>\$ 1,497</u>
Accrued interest excluded from total	<u>\$ 1</u>	<u>\$ 6</u>	

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

An aging analysis of loans by class follows:

	Loans Past Due				Loans not Past Due	Total Loans
	30-59 days	60-89 days	90+ days	Total		
	(In thousands)					
March 31, 2021						
Commercial						
Commercial and industrial	\$ 87	\$ -	\$ 110	\$ 197	\$ 728,971	\$ 729,168
Commercial real estate	-	-	-	-	572,055	572,055
Mortgage						
1-4 family owner occupied - jumbo	819	-	620	1,439	446,426	447,865
1-4 family owner occupied - non-jumbo	1,033	265	354	1,652	249,846	251,498
1-4 family non-owner occupied	1,019	102	401	1,522	156,471	157,993
1-4 family - 2nd lien	351	140	505	996	85,944	86,940
Resort lending	32	188	287	507	55,179	55,686
Installment						
Boat lending	168	103	4	275	211,053	211,328
Recreational vehicle lending	64	14	16	94	173,179	173,273
Other	232	69	185	486	97,932	98,418
Total	\$ 3,805	\$ 881	\$ 2,482	\$ 7,168	\$ 2,777,056	\$ 2,784,224
Accrued interest excluded from total	\$ 49	\$ 15	\$ -	\$ 64	\$ 8,432	\$ 8,496
December 31, 2020						
Commercial						
Commercial and industrial	\$ 5,003	\$ 131	\$ 70	\$ 5,204	\$ 671,115	\$ 676,319
Commercial real estate	2,600	-	-	2,600	567,032	569,632
Mortgage						
1-4 family owner occupied - jumbo	761	-	623	1,384	438,794	440,178
1-4 family owner occupied - non-jumbo	1,888	453	502	2,843	264,730	267,573
1-4 family non-owner occupied	1,184	139	476	1,799	157,977	159,776
1-4 family - 2nd lien	710	228	732	1,670	92,860	94,530
Resort lending	32	195	358	585	57,462	58,047
Installment						
Boat lending	95	101	-	196	207,317	207,513
Recreational vehicle lending	207	37	48	292	169,282	169,574
Other	337	162	199	698	98,737	99,435
Total recorded investment	\$ 12,817	\$ 1,446	\$ 3,008	\$ 17,271	\$ 2,725,306	\$ 2,742,577
Accrued interest included in recorded investment	\$ 147	\$ 22	\$ -	\$ 169	\$ 8,730	\$ 8,899

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

Impaired loans at December 31, 2020 are as follows (1):

	<u>2020</u>
Impaired loans with no allocated ACL	(In thousands)
Troubled debt restructurings ("TDR")	\$ 93
Non - TDR	1,367
Impaired loans with an allocated ACL	
TDR - allowance based on collateral	9,027
TDR - allowance based on present value cash flow	37,953
Non - TDR - allowance based on collateral	1,873
Total impaired loans	<u>\$ 50,313</u>
Amount of ACL allocated (1)	
TDR - allowance based on collateral	\$ 1,058
TDR - allowance based on present value cash flow	3,755
Non - TDR - allowance based on collateral	768
Total amount of ACL allocated	<u>\$ 5,581</u>

(1) Beginning January 1, 2021, calculation is based on CECL methodology. Prior to January 1, 2021, calculation was based on the probable incurred loss methodology.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

Impaired loans by class at December 31, 2020 are as follows (1):

	2020		
	Recorded Investment	Unpaid Principal Balance (In thousands)	Related ACL (1)
With no related ACL recorded:			
Commercial			
Commercial and industrial	\$ 77	\$ 80	\$ -
Commercial real estate	-	-	-
Mortgage			
1-4 family owner occupied - jumbo	623	629	-
1-4 family owner occupied - non-jumbo	-	-	-
1-4 family non-owner occupied	305	473	-
1-4 family - 2nd lien	301	304	-
Resort lending	154	379	-
Installment			
Boat lending	-	-	-
Recreational vehicle lending	-	-	-
Other	-	-	-
	<u>1,460</u>	<u>1,865</u>	<u>-</u>
With an ACL recorded:			
Commercial			
Commercial and industrial	2,227	2,370	756
Commercial real estate	7,127	7,096	510
Mortgage			
1-4 family owner occupied - jumbo	506	880	50
1-4 family owner occupied - non-jumbo	21,655	22,311	2,300
1-4 family non-owner occupied	4,335	4,704	495
1-4 family - 2nd lien	811	829	200
Resort lending	10,555	10,764	1,079
Installment			
Boat lending	7	11	2
Recreational vehicle lending	87	100	19
Other	1,902	2,040	170
	<u>49,212</u>	<u>51,105</u>	<u>5,581</u>
Total			
Commercial			
Commercial and industrial	2,304	2,450	756
Commercial real estate	7,127	7,096	510
Mortgage			
1-4 family owner occupied - jumbo	1,129	1,509	50
1-4 family owner occupied - non-jumbo	21,655	22,311	2,300
1-4 family non-owner occupied	4,640	5,177	495
1-4 family - 2nd lien	1,112	1,133	200
Resort lending	10,709	11,143	1,079
Installment			
Boat lending	7	11	2
Recreational vehicle lending	87	100	19
Other	1,902	2,040	170
Total	<u>\$ 50,672</u>	<u>\$ 52,970</u>	<u>\$ 5,581</u>
Accrued interest included in recorded investment	<u>\$ 359</u>		

(1) Beginning January 1, 2021, calculation is based on CECL methodology. Prior to January 1, 2021, calculation was based on the probable incurred loss methodology.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

Average recorded investment in and interest income earned on impaired loans by class for the three month period ending March 31, 2020, follows (1):

	2020	
	Average Recorded Investment	Interest Income Recognized
(In thousands)		
With no related ACL recorded:		
Commercial		
Commercial and industrial	\$ 171	\$ 1
Commercial real estate	398	-
Mortgage		
1-4 family owner occupied - jumbo	77	1
1-4 family owner occupied - non-jumbo	299	4
1-4 family non-owner occupied	302	2
1-4 family - 2nd lien	396	-
Resort lending	77	-
Installment		
Boat lending	-	-
Recreational vehicle lending	-	-
Other	1	-
	<u>1,721</u>	<u>8</u>
With an a ACL recorded:		
Commercial		
Commercial and industrial	2,032	38
Commercial real estate	11,120	223
Mortgage		
1-4 family owner occupied - jumbo	12,430	360
1-4 family owner occupied - non-jumbo	5,381	4
1-4 family non-owner occupied	4,784	66
1-4 family - 2nd lien	7,436	4
Resort lending	11,827	141
Installment		
Boat lending	38	-
Recreational vehicle lending	65	1
Other	2,767	41
	<u>57,880</u>	<u>878</u>
Total		
Commercial		
Commercial and industrial	2,203	39
Commercial real estate	11,518	223
Mortgage		
1-4 family owner occupied - jumbo	12,507	361
1-4 family owner occupied - non-jumbo	5,680	8
1-4 family non-owner occupied	5,086	68
1-4 family - 2nd lien	7,832	4
Resort lending	11,904	141
Installment		
Boat lending	38	-
Recreational vehicle lending	65	1
Other	2,768	41
Total	<u>\$ 59,601</u>	<u>\$ 886</u>

(1) Beginning January 1, 2021, calculation is based on CECL methodology. Prior to January 1, 2021, calculation was based on the probable incurred loss methodology.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

Cash receipts on impaired loans on non-accrual status are generally applied to the principal balance.

TDRs follow:

	March 31, 2021		
	Commercial	Retail (1)	Total
	(In thousands)		
Performing TDRs	\$ 5,032	\$ 34,679	\$ 39,711
Non-performing TDRs (2)	1,105	1,459 ⁽³⁾	2,564
Total	\$ 6,137	\$ 36,138	\$ 42,275

	December 31, 2020		
	Commercial	Retail (1)	Total
	(In thousands)		
Performing TDRs	\$ 7,956	\$ 36,385	\$ 44,341
Non-performing TDRs (2)	1,148	1,584 ⁽³⁾	2,732
Total	\$ 9,104	\$ 37,969	\$ 47,073

(1) Retail loans include mortgage and installment loan portfolio segments.

(2) Included in non-performing loans table above.

(3) Also includes loans on non-accrual at the time of modification until six payments are received on a timely basis.

We allocated \$4.6 million and \$4.8 million of specific reserves to customers whose loan terms have been modified in troubled debt restructurings (“TDR”) at March 31, 2021 and December 31, 2020, respectively.

During the three months ended March 31, 2021 and 2020, the terms of certain loans were modified as TDRs. The modification of the terms of such loans generally included one or a combination of the following: a reduction of the stated interest rate of the loan; an extension of the maturity date at a stated rate of interest lower than the current market rate for a new loan with similar risk; or a permanent reduction of the recorded investment in the loan.

Modifications involving a reduction of the stated interest rate of the loan have generally been for periods ranging from 9 months to 36 months but have extended to as much as 480 months in certain circumstances. Modifications involving an extension of the maturity date have generally been for periods ranging from 1 month to 60 months but have extended to as much as 230 months in certain circumstances.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

Loans that have been classified as TDRs during the three-month periods ended March 31 follow:

	<u>Number of Contracts</u>	<u>Pre-modification Balance</u>	<u>Post-modification Balance</u>
		(Dollars in thousands)	
2021			
Commercial			
Commercial and industrial	-	\$ -	\$ -
Commercial real estate	-	-	-
Mortgage			
1-4 family owner occupied - jumbo	-	-	-
1-4 family owner occupied - non-jumbo	-	-	-
1-4 family non-owner occupied	-	-	-
1-4 family - 2nd lien	-	-	-
Resort lending	-	-	-
Installment			
Boat lending	-	-	-
Recreational vehicle lending	-	-	-
Other	-	-	-
Total	<u>-</u>	<u>\$ -</u>	<u>\$ -</u>
2020			
Commercial			
Commercial and industrial	1	\$ 99	\$ 99
Commercial real estate	3	1,177	1,177
Mortgage			
1-4 family owner occupied - jumbo	-	-	-
1-4 family owner occupied - non-jumbo	1	49	50
1-4 family non-owner occupied	1	59	62
1-4 family - 2nd lien	-	-	-
Resort lending	-	-	-
Installment			
Boat lending	-	-	-
Recreational vehicle lending	-	-	-
Other	1	33	34
Total	<u>7</u>	<u>\$ 1,417</u>	<u>\$ 1,422</u>

The TDRs described above for 2021 had no impact on the allowance for credit losses and resulted in zero charge offs while the TDRs described above for 2020 increased the allowance for credit losses by \$0.27 million and resulted in zero charge offs.

There were no TDRs that subsequently defaulted within twelve months following the modification during the three months periods ended March 31, 2021 and 2020.

A loan is considered to be in payment default generally once it is 90 days contractually past due under the modified terms.

In order to determine whether a borrower is experiencing financial difficulty, we perform an evaluation of the probability that the borrower will be in payment default on any of its debt in the foreseeable future without the modification. This evaluation is performed under our internal underwriting policy.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

Non-TDR Loan Modifications and Paycheck Protection Program (“PPP”) due to COVID-19 - On March 22, 2020, the federal banking agencies issued an “Interagency Statement on Loan Modifications and Reporting for Financial Institutions Working with Customers Affected by the Coronavirus”. This guidance encourages financial institutions to work prudently with borrowers that may be unable to meet their contractual obligations because of the effects of COVID-19. The guidance goes on to explain that in consultation with the Financial Accounting Standards Board staff that the federal banking agencies conclude that short-term modifications (e.g. six months or less) made on a good faith basis to borrowers who were current (less than 30 days past due) as of the implementation date of a relief program are not TDRs. In addition, on March 27, 2020, the CARES Act was signed into law. Section 4013 of the CARES Act also addressed COVID-19 related modifications and specified that COVID-19 related modifications on loans that were current (less than 30 days past due) as of December 31, 2019 are not TDRs. We are assisting both commercial and retail (mortgage and installment) borrowers with reduced or suspended payments. Commercial loan accommodations are typically a three month interest-only period while retail loan (mortgage and installment) forbearances have primarily been payment suspensions for three months. For loans subject to these forbearance agreements each borrower is required to resume making regularly scheduled loan payments at the end of the forbearance period. The deferred principal and interest will be repaid based upon individualized agreements. Options for repayment include separate repayment plans, extending the term of the loan or re-amortizing the loan based upon the affordability of the payment in relationship to a reduced income. While some borrowers may elect to make a lump sum payment, we anticipate the majority will require some type of repayment plan. During the forbearance period, the loan will not be reported as past due in keeping with the guidance discussed previously.

A summary of accommodations entered into under this guidance as of March 31, 2021 follows:

Commercial and Retail Loan COVID-19 Accommodations

Loan Category	Covid-19 Accommodations		Total Loans	% of Total Loans
	Loans (#)	Loans (\$)		
	(Dollars in thousands)			
Commercial	-	\$ -	\$ 1,301,223	0.0%
Mortgage	111	15,263	999,982	1.5%
Installment	32	537	483,019	0.1%
Total	143	\$ 15,800	\$ 2,784,224	0.6%
Mortgage loans serviced for others(1)	205	\$ 26,975	\$ 3,072,491	0.9%

1) We have delegated authority from all investors to grant these deferrals on their behalf.

Information on subsequent accommodation extensions follows:

Commercial and Retail Loan COVID-19 Subsequent Accommodations (1)

Loan Category	Loans (#)	Loans (\$)
	(Dollars in thousands)	
Commercial	-	\$ -
Mortgage	86	11,658
Installment	23	428
Total	109	\$ 12,086

(1) Subsequent accommodations are extensions of the original accommodations that were given as summarized in the paragraph above.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

The CARES Act also included an initial \$349 billion loan program administered through the U.S. Small Business Administration (“SBA”) referred to as the PPP. Under the PPP, small businesses and other entities and individuals can apply for loans from existing SBA lenders and other approved regulated lenders that enroll in the program, subject to numerous limitations and eligibility criteria. We are participating as a lender in the PPP. The PPP opened on April 3, 2020 intending to provide American small businesses with eight weeks of cash-flow assistance through 100 percent federally guaranteed loans through the SBA. In late April 2020 the Paycheck Protection Program and Health Care Enhancement Act, added another \$310 billion in funding while the Paycheck Protection Program Flexibility Act made certain changes to the program, by allowing for more time to spend the funds, and making it easier to get a loan fully forgiven. The PPP initially closed on August 8, 2020 (“Round 1”). On December 27, 2020, the Economic Aid to Hard-Hit Small Businesses, Nonprofits, and Venues Act (“Economic Aid Act”) was signed into law which allocates an additional \$284 billion in funding for the PPP (“Round 2”). The Economic Aid Act reopens the PPP through March 31, 2021 with generally the same terms and conditions as originally enacted under the CARES Act while clarifying eligibility and ineligibility for certain entities and expanding the permitted uses of PPP funds. In addition, the Economic Aid Act simplifies the loan forgiveness process for PPP loans of \$150,000 or less. The Economic Aid Act also establishes second draw loans for entities that have already used the initial PPP funds, subject to numerous limitations and eligibility criteria. PPP Round 2 loans are eligible for forgiveness similar to Round 1 PPP loans, subject to limitations set forth in the Economic Aid Act.

The following table summarizes PPP loans outstanding:

Paycheck Protection Program

	As of March 31, 2021		As of December 31, 2020	
	Amount (#)	Amount	Amount (#)	Amount
	(Dollars in thousands)		(Dollars in thousands)	
Closed and outstanding - Round 1 loans	698	\$ 105,934	1,483	\$ 169,782
Closed and outstanding - Round 2 loans	1,250	128,240	-	-
Total closed and outstanding	1,948	\$ 234,174	1,483	\$ 169,782
Unaccreted net fees remaining at period end		\$ 6,816		\$ 3,216

PPP loans are included in the commercial and industrial class of the commercial loan portfolio segment. As these loans are 100% guaranteed through the SBA the allowance for credit losses recorded on these loans is zero. Interest and fees on loans in our consolidated statement of operations includes \$2.1 million during the three month period ended March 31, 2021, related to the accretion of net loan fees on PPP loans. No such accretion is included in the comparable prior year period.

Credit Quality Indicators – As part of our on-going monitoring of the credit quality of our loan portfolios, we track certain credit quality indicators including (a) risk grade of commercial loans, (b) the level of classified commercial loans, (c) credit scores of mortgage and installment loan borrowers, and (d) delinquency history and non-performing loans.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

For commercial loans, we use a loan rating system that is similar to those employed by state and federal banking regulators. Loans are graded on a scale of 1 to 12. A description of the general characteristics of the ratings follows:

Rating 1 through 6: These loans are generally referred to as our “non-watch” commercial credits that include very high or exceptional credit fundamentals through acceptable credit fundamentals.

Rating 7 and 8: These loans are generally referred to as our “watch” commercial credits. These ratings include loans to borrowers that exhibit potential credit weakness or downward trends. If not checked or cured these trends could weaken our asset or credit position. While potentially weak, no loss of principal or interest is envisioned with these ratings.

Rating 9: These loans are generally referred to as our “substandard accruing” commercial credits. This rating includes loans to borrowers that exhibit a well-defined weakness where payment default is probable and loss is possible if deficiencies are not corrected. Generally, loans with this rating are considered collectible as to both principal and interest primarily due to collateral coverage.

Rating 10 and 11: These loans are generally referred to as our “substandard - non-accrual” and “doubtful” commercial credits. Our doubtful rating includes a sub classification for a loss rate other than 50% (which is the standard doubtful loss rate). These ratings include loans to borrowers with weaknesses that make collection of the loan in full, on the basis of current facts, conditions and values at best questionable and at worst improbable. All of these loans are placed in non-accrual.

Rating 12: These loans are generally referred to as our “loss” commercial credits. This rating includes loans to borrowers that are deemed incapable of repayment and are charged-off.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

The following table summarizes loan ratings by loan class for our commercial portfolio loan segment as of March 31, 2021:

	Commercial						Revolving Loans Amortized Cost Basis	Total
	Term Loans Amortized Cost Basis by Origination Year					Prior		
	2021	2020	2019	2018	2017			
(In thousands)								
March 31, 2021								
Commercial and industrial								
Non-watch (1-6)	\$ 142,043	\$ 206,986	\$ 67,404	\$ 48,651	\$ 59,051	\$ 47,122	\$ 130,580	\$ 701,837
Watch (7-8)	666	5,458	1,846	3,736	704	4,020	6,731	23,161
Substandard Accrual (9)	-	15	1,280	298	87	1,081	-	2,761
Non-Accrual (10-11)	-	158	40	719	386	106	-	1,409
Total	\$ 142,709	\$ 212,617	\$ 70,570	\$ 53,404	\$ 60,228	\$ 52,329	\$ 137,311	\$ 729,168
Accrued interest excluded from total	\$ 193	\$ 1,300	\$ 173	\$ 130	\$ 132	\$ 159	\$ 255	\$ 2,342
Commercial real estate								
Non-watch (1-6)	\$ 40,963	\$ 108,863	\$ 161,142	\$ 88,190	\$ 57,047	\$ 68,429	\$ 43,270	\$ 567,904
Watch (7-8)	82	-	278	1,509	243	747	110	2,969
Substandard Accrual (9)	-	-	36	1,130	16	-	-	1,182
Non-Accrual (10-11)	-	-	-	-	-	-	-	-
Total	\$ 41,045	\$ 108,863	\$ 161,456	\$ 90,829	\$ 57,306	\$ 69,176	\$ 43,380	\$ 572,055
Accrued interest excluded from total	\$ 60	\$ 209	\$ 271	\$ 184	\$ 133	\$ 153	\$ 86	\$ 1,096
Total Commercial								
Non-watch (1-6)	\$ 183,006	\$ 315,849	\$ 228,546	\$ 136,841	\$ 116,098	\$ 115,551	\$ 173,850	\$ 1,269,741
Watch (7-8)	748	5,458	2,124	5,245	947	4,767	6,841	26,130
Substandard Accrual (9)	-	15	1,316	1,428	103	1,081	-	3,943
Non-Accrual (10-11)	-	158	40	719	386	106	-	1,409
Total	\$ 183,754	\$ 321,480	\$ 232,026	\$ 144,233	\$ 117,534	\$ 121,505	\$ 180,691	\$ 1,301,223
Accrued interest excluded from total	\$ 253	\$ 1,509	\$ 444	\$ 314	\$ 265	\$ 312	\$ 341	\$ 3,438

The following table summarizes loan ratings by loan class for our commercial portfolio loan segment as of December 31, 2020:

	Commercial				Total
	Non-watch 1-6	Watch 7-8	Substandard Accrual 9	Non- Accrual 10-11	
	(In thousands)				
December 31, 2020					
Commercial and industrial	\$ 637,826	\$ 32,765	\$ 4,341	\$ 1,387	\$ 676,319
Commercial real estate	561,382	5,978	2,272	-	569,632
Total	\$ 1,199,208	\$ 38,743	\$ 6,613	\$ 1,387	\$ 1,245,951
Accrued interest included in total	\$ 3,408	\$ 105	\$ 23	\$ -	\$ 3,536

For each of our mortgage and installment portfolio segment classes, we generally monitor credit quality based on the credit scores of the borrowers. These credit scores are generally updated semi-annually.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

The following tables summarize credit scores by loan class for our mortgage and installment loan portfolio segments at March 31, 2021:

	Mortgage (1)						Revolving Loans Amortized Cost Basis	Total
	Term Loans Amortized Cost Basis by Origination Year							
	2021	2020	2019	2018	2017	Prior		
	(In thousands)							
March 31, 2021								
1-4 family owner occupied - jumbo								
800 and above	\$ 12,641	\$ 30,345	\$ 10,513	\$ 3,190	\$ 3,292	\$ 1,610	\$ -	\$ 61,591
750-799	50,247	106,976	36,152	12,328	19,061	4,146	-	228,910
700-749	14,776	35,677	21,894	10,623	11,256	4,383	-	98,609
650-699	1,663	17,060	13,041	5,881	6,451	2,721	-	46,817
600-649	-	1,470	2,779	-	2,007	1,698	-	7,954
550-599	-	1,872	-	-	558	-	-	2,430
500-549	-	-	477	458	619	-	-	1,554
Under 500	-	-	-	-	-	-	-	-
Unknown	-	-	-	-	-	-	-	-
Total	<u>\$ 79,327</u>	<u>\$ 193,400</u>	<u>\$ 84,856</u>	<u>\$ 32,480</u>	<u>\$ 43,244</u>	<u>\$ 14,558</u>	<u>\$ -</u>	<u>\$ 447,865</u>
Accrued interest excluded from total	<u>\$ 150</u>	<u>\$ 450</u>	<u>\$ 231</u>	<u>\$ 122</u>	<u>\$ 132</u>	<u>\$ 40</u>	<u>\$ -</u>	<u>\$ 1,125</u>
1-4 family owner occupied - non-jumbo								
800 and above	\$ 1,791	\$ 7,858	\$ 5,336	\$ 3,713	\$ 5,912	\$ 5,676	\$ 1,997	\$ 32,283
750-799	14,187	25,424	11,786	10,516	13,208	12,371	3,960	91,452
700-749	5,114	5,187	7,567	4,364	5,334	27,813	1,776	57,155
650-699	5,752	3,655	3,681	3,654	3,841	12,348	1,342	34,273
600-649	520	2,584	1,541	2,174	3,341	8,851	226	19,237
550-599	284	280	251	1,587	418	6,430	190	9,440
500-549	252	-	774	329	508	3,842	18	5,723
Under 500	-	478	528	100	152	662	15	1,935
Unknown	-	-	-	-	-	-	-	-
Total	<u>\$ 27,900</u>	<u>\$ 45,466</u>	<u>\$ 31,464</u>	<u>\$ 26,437</u>	<u>\$ 32,714</u>	<u>\$ 77,993</u>	<u>\$ 9,524</u>	<u>\$ 251,498</u>
Accrued interest excluded from total	<u>\$ 867</u>	<u>\$ 136</u>	<u>\$ 125</u>	<u>\$ 109</u>	<u>\$ 124</u>	<u>\$ 295</u>	<u>\$ 30</u>	<u>\$ 1,686</u>
1-4 family non-owner occupied								
800 and above	\$ 807	\$ 3,658	\$ 3,517	\$ 2,553	\$ 4,025	\$ 6,225	\$ 2,989	\$ 23,774
750-799	12,275	24,455	12,627	6,502	5,948	11,586	9,866	83,259
700-749	3,236	10,143	2,318	3,463	2,735	6,541	4,293	32,729
650-699	815	959	1,763	662	478	5,377	1,757	11,811
600-649	-	-	40	22	143	1,450	766	2,421
550-599	-	60	121	506	28	1,282	348	2,345
500-549	-	-	-	-	719	489	133	1,341
Under 500	-	40	-	-	-	218	55	313
Unknown	-	-	-	-	-	-	-	-
Total	<u>\$ 17,133</u>	<u>\$ 39,315</u>	<u>\$ 20,386</u>	<u>\$ 13,708</u>	<u>\$ 14,076</u>	<u>\$ 33,168</u>	<u>\$ 20,207</u>	<u>\$ 157,993</u>
Accrued interest excluded from total	<u>\$ 27</u>	<u>\$ 108</u>	<u>\$ 71</u>	<u>\$ 53</u>	<u>\$ 48</u>	<u>\$ 133</u>	<u>\$ 72</u>	<u>\$ 512</u>
1-4 family - 2nd lien								
800 and above	\$ 135	\$ 410	\$ 262	\$ 466	\$ 521	\$ 224	\$ 9,192	\$ 11,210
750-799	582	4,494	1,388	1,859	2,741	985	27,423	39,472
700-749	943	1,559	1,305	853	1,800	186	14,713	21,359
650-699	15	282	625	353	1,082	56	6,909	9,322
600-649	-	166	-	101	181	45	2,337	2,830
550-599	-	-	67	76	34	-	1,286	1,463
500-549	-	-	237	-	30	14	670	951
Under 500	-	-	192	-	-	-	141	333
Unknown	-	-	-	-	-	-	-	-
Total	<u>\$ 1,675</u>	<u>\$ 6,911</u>	<u>\$ 4,076</u>	<u>\$ 3,708</u>	<u>\$ 6,389</u>	<u>\$ 1,510</u>	<u>\$ 62,671</u>	<u>\$ 86,940</u>
Accrued interest excluded from total	<u>\$ 2</u>	<u>\$ 13</u>	<u>\$ 9</u>	<u>\$ 10</u>	<u>\$ 19</u>	<u>\$ 3</u>	<u>\$ 242</u>	<u>\$ 298</u>

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

Mortgage - continued (1)								
	Term Loans Amortized Cost Basis by Origination Year						Revolving Loans Amortized Cost Basis	Total
	2021	2020	2019	2018	2017	Prior		
(In thousands)								
March 31, 2021								
Resort lending								
800 and above	\$ -	\$ 919	\$ 291	\$ 277	\$ -	\$ 9,877	\$ -	\$ 11,364
750-799	320	908	112	786	361	21,455	-	23,942
700-749	-	345	66	380	242	10,554	-	11,587
650-699	-	-	-	-	-	6,481	-	6,481
600-649	-	-	-	-	-	1,479	-	1,479
550-599	-	-	-	-	-	542	-	542
500-549	-	-	-	-	-	291	-	291
Under 500	-	-	-	-	-	-	-	-
Unknown	-	-	-	-	-	-	-	-
Total	<u>\$ 320</u>	<u>\$ 2,172</u>	<u>\$ 469</u>	<u>\$ 1,443</u>	<u>\$ 603</u>	<u>\$ 50,679</u>	<u>\$ -</u>	<u>\$ 55,686</u>
Accrued interest excluded from total	<u>\$ -</u>	<u>\$ 6</u>	<u>\$ 1</u>	<u>\$ 6</u>	<u>\$ 2</u>	<u>\$ 224</u>	<u>\$ -</u>	<u>\$ 239</u>
Total Mortgage								
800 and above	\$ 15,374	\$ 43,190	\$ 19,919	\$ 10,199	\$ 13,750	\$ 23,612	\$ 14,178	140,222
750-799	77,611	162,257	62,065	31,991	41,319	50,543	41,249	467,035
700-749	24,069	52,911	33,150	19,683	21,367	49,477	20,782	221,439
650-699	8,245	21,956	19,110	10,550	11,852	26,983	10,008	108,704
600-649	520	4,220	4,360	2,297	5,672	13,523	3,329	33,921
550-599	284	2,212	439	2,169	1,038	8,254	1,824	16,220
500-549	252	-	1,488	787	1,876	4,636	821	9,860
Under 500	-	518	720	100	152	880	211	2,581
Unknown	-	-	-	-	-	-	-	-
Total	<u>\$ 126,355</u>	<u>\$ 287,264</u>	<u>\$ 141,251</u>	<u>\$ 77,776</u>	<u>\$ 97,026</u>	<u>\$ 177,908</u>	<u>\$ 92,402</u>	<u>\$ 999,982</u>
Accrued interest excluded from total	<u>\$ 1,046</u>	<u>\$ 713</u>	<u>\$ 437</u>	<u>\$ 300</u>	<u>\$ 325</u>	<u>\$ 695</u>	<u>\$ 344</u>	<u>\$ 3,860</u>

(1) Credit scores have been updated within the last twelve months.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

	Installment (1)						
	Term Loans Amortized Cost Basis by Origination Year						
	2021	2020	2019	2018	2017	Prior	Total
	(In thousands)						
March 31, 2021							
Boat lending							
800 and above	\$ 4,460	\$ 6,201	\$ 8,255	\$ 6,903	\$ 3,705	\$ 6,267	\$ 35,791
750-799	11,981	31,120	26,975	21,766	13,199	16,095	121,136
700-749	3,604	11,575	9,823	6,117	4,302	5,442	40,863
650-699	502	2,592	2,464	1,918	1,209	2,145	10,830
600-649	-	134	411	240	209	500	1,494
550-599	-	27	77	182	78	418	782
500-549	-	-	57	4	213	128	402
Under 500	-	-	-	22	8	-	30
Unknown	-	-	-	-	-	-	-
Total	<u>\$ 20,547</u>	<u>\$ 51,649</u>	<u>\$ 48,062</u>	<u>\$ 37,152</u>	<u>\$ 22,923</u>	<u>\$ 30,995</u>	<u>\$ 211,328</u>
Accrued interest excluded from total	<u>\$ 44</u>	<u>\$ 115</u>	<u>\$ 111</u>	<u>\$ 89</u>	<u>\$ 54</u>	<u>\$ 68</u>	<u>\$ 481</u>
Recreational vehicle lending							
800 and above	\$ 2,756	\$ 5,426	\$ 6,531	\$ 6,640	\$ 3,118	\$ 5,012	\$ 29,483
750-799	9,600	30,007	22,986	15,962	7,913	9,776	96,244
700-749	4,317	12,690	7,246	5,361	2,317	3,128	35,059
650-699	376	3,541	2,531	1,192	617	1,486	9,743
600-649	-	307	484	467	155	250	1,663
550-599	-	89	161	132	147	191	720
500-549	-	33	-	165	26	93	317
Under 500	-	-	22	-	11	11	44
Unknown	-	-	-	-	-	-	-
Total	<u>\$ 17,049</u>	<u>\$ 52,093</u>	<u>\$ 39,961</u>	<u>\$ 29,919</u>	<u>\$ 14,304</u>	<u>\$ 19,947</u>	<u>\$ 173,273</u>
Accrued interest excluded from total	<u>\$ 38</u>	<u>\$ 117</u>	<u>\$ 95</u>	<u>\$ 66</u>	<u>\$ 34</u>	<u>\$ 43</u>	<u>\$ 393</u>
Other							
800 and above	\$ 791	\$ 2,112	\$ 2,022	\$ 1,658	\$ 772	\$ 1,205	\$ 8,560
750-799	3,407	12,478	8,538	4,952	3,499	3,889	36,763
700-749	4,026	7,567	5,492	3,279	2,013	3,061	25,438
650-699	12,143	3,031	2,256	1,254	1,296	2,148	22,128
600-649	166	564	636	630	446	833	3,275
550-599	2	98	153	181	222	376	1,032
500-549	-	45	94	233	95	155	622
Under 500	-	6	49	7	23	33	118
Unknown	482	-	-	-	-	-	482
Total	<u>\$ 21,017</u>	<u>\$ 25,901</u>	<u>\$ 19,240</u>	<u>\$ 12,194</u>	<u>\$ 8,366</u>	<u>\$ 11,700</u>	<u>\$ 98,418</u>
Accrued interest excluded from total	<u>\$ 109</u>	<u>\$ 54</u>	<u>\$ 54</u>	<u>\$ 36</u>	<u>\$ 20</u>	<u>\$ 51</u>	<u>\$ 324</u>
Total installment							
800 and above	\$ 8,007	\$ 13,739	\$ 16,808	\$ 15,201	\$ 7,595	\$ 12,484	\$ 73,834
750-799	24,988	73,605	58,499	42,680	24,611	29,760	254,143
700-749	11,947	31,832	22,561	14,757	8,632	11,631	101,360
650-699	13,021	9,164	7,251	4,364	3,122	5,779	42,701
600-649	166	1,005	1,531	1,337	810	1,583	6,432
550-599	2	214	391	495	447	985	2,534
500-549	-	78	151	402	334	376	1,341
Under 500	-	6	71	29	42	44	192
Unknown	482	-	-	-	-	-	482
Total	<u>\$ 58,613</u>	<u>\$ 129,643</u>	<u>\$ 107,263</u>	<u>\$ 79,265</u>	<u>\$ 45,593</u>	<u>\$ 62,642</u>	<u>\$ 483,019</u>
Accrued interest excluded from total	<u>\$ 191</u>	<u>\$ 286</u>	<u>\$ 260</u>	<u>\$ 191</u>	<u>\$ 108</u>	<u>\$ 162</u>	<u>\$ 1,198</u>

(1) Credit scores have been updated within the last twelve months.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

The following tables summarize credit scores by loan class for our mortgage and installment loan portfolio segments at December 31, 2020:

	Mortgage					
	1-4 Family Owner Occupied - Jumbo	1-4 Family Owner Occupied - Non-jumbo	1-4 Family Non-owner Occupied	1-4 Family 2nd Lien	Resort Lending	Total
	(In thousands)					
December 31, 2020						
800 and above	\$ 61,077	\$ 40,187	\$ 25,468	\$ 12,490	\$ 9,546	\$ 148,768
750-799	223,177	70,642	82,124	42,138	27,530	445,611
700-749	101,086	75,489	30,326	22,962	11,726	241,589
650-699	40,296	44,344	13,182	11,269	6,393	115,484
600-649	11,146	18,519	4,303	2,703	1,670	38,341
550-599	-	11,021	2,388	1,608	917	15,934
500-549	3,396	5,129	1,580	1,012	192	11,309
Under 500	-	2,242	405	348	73	3,068
Total	<u>\$ 440,178</u>	<u>\$ 267,573</u>	<u>\$ 159,776</u>	<u>\$ 94,530</u>	<u>\$ 58,047</u>	<u>\$ 1,020,104</u>
Accrued interest included in total	<u>\$ 1,301</u>	<u>\$ 1,641</u>	<u>\$ 587</u>	<u>\$ 373</u>	<u>\$ 276</u>	<u>\$ 4,178</u>

	Installment			
	Boat Lending	Recreational Vehicle Lending	Other	Total
	(In thousands)			
December 31, 2020				
800 and above		\$ 32,231	\$ 29,223	\$ 9,154
750-799		123,689	95,890	37,512
700-749		38,223	33,476	25,262
650-699		10,189	8,794	21,138
600-649		2,083	1,305	3,730
550-599		661	551	1,299
500-549		342	283	767
Under 500		95	52	63
Unknown		-	-	510
Total		<u>\$ 207,513</u>	<u>\$ 169,574</u>	<u>\$ 99,435</u>
Accrued interest included in total		<u>\$ 572</u>	<u>\$ 457</u>	<u>\$ 156</u>

Foreclosed residential real estate properties included in other real estate and repossessed assets on our Condensed Consolidated Statements of Financial Condition totaled \$0.3 million and \$0.7 million at March 31, 2021 and December 31, 2020, respectively. Retail mortgage loans secured by residential real estate properties for which formal foreclosure proceedings are in process according to local requirements totaled \$0.3 million at both March 31, 2021 and December 31, 2020.

During the first quarter of 2020, we securitized \$26.3 million of portfolio residential fixed rate mortgage loans servicing retained with Freddie Mac and recognized a gain on sale of \$0.72 million. We also sold \$2.4 million of portfolio residential fixed rate mortgage loans servicing retained into the secondary market and recognized a gain on sale of \$0.07 million. These transactions were done primarily for asset/liability management purposes.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

5. Shareholders' Equity and Earnings Per Common Share

On December 18, 2020, our Board of Directors authorized a share repurchase plan (the "Repurchase Plan") to buy back up to 1,100,000 shares of our outstanding common stock through December 31, 2021. Shares would be repurchased through open market transactions, though we could execute repurchases through other means, such as privately negotiated transactions. The timing and amount of any share repurchases will depend on a variety of factors, including, among others, securities law restrictions, the trading price of our common stock, regulatory requirements, potential alternative uses for capital, and our financial performance. During the three month periods ended March 31, 2021 and 2020 repurchases were made totaling 180,667 shares and 678,929 shares of common stock, respectively, for an aggregate purchase price of \$3.6 million and \$13.8 million, respectively.

A reconciliation of basic and diluted net income per common share follows:

	Three Months Ended March 31,	
	2021	2020
	(In thousands, except per share data)	
Net income	\$ 22,037	\$ 4,810
Weighted average shares outstanding (1)	21,826	22,271
Stock units for deferred compensation plan for non-employee directors	120	122
Effect of stock options	83	99
Performance share units	30	37
Weighted average shares outstanding for calculation of diluted earnings per share	22,059	22,529
Net income per common share		
Basic (1)	\$ 1.01	\$ 0.22
Diluted	\$ 1.00	\$ 0.21

(1) Basic net income per common share includes weighted average common shares outstanding during the period and participating share awards.

Weighted average stock options outstanding that were not considered in computing diluted net income per common share because they were anti-dilutive were zero for both three month periods ended March 31, 2021 and 2020.

6. Derivative Financial Instruments

We are required to record derivatives on our Condensed Consolidated Statements of Financial Condition as assets and liabilities measured at their fair value. The accounting for increases and decreases in the value of derivatives depends upon the use of derivatives and whether the derivatives qualify for hedge accounting.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

Our derivative financial instruments according to the type of hedge in which they are designated follows:

	March 31, 2021		
	Notional Amount	Average Maturity (years)	Fair Value
(Dollars in thousands)			
Fair value hedge designation			
Pay-fixed interest rate swap agreements - commercial	\$ 7,005	8.1	\$ (423)
Pay-fixed interest rate swap agreements - securities available for sale	148,895	6.6	4,887
Total	\$ 155,900	6.7	\$ 4,464
No hedge designation			
Rate-lock mortgage loan commitments	\$ 187,834	0.1	\$ 3,198
Mandatory commitments to sell mortgage loans	165,609	0.1	896
Pay-fixed interest rate swap agreements - commercial	149,328	4.3	(6,425)
Pay-variable interest rate swap agreements - commercial	149,328	4.3	6,425
Pay-fixed interest rate swap agreements	25,000	0.3	(177)
Interest rate cap agreements	135,000	1.5	20
Purchased options	2,193	0.4	60
Written options	2,193	0.4	(60)
Total	\$ 816,485	1.9	\$ 3,937
December 31, 2020			
	Notional Amount	Average Maturity (years)	Fair Value
(Dollars in thousands)			
Fair value hedge designation			
Pay-fixed interest rate swap agreements - commercial	\$ 7,088	8.4	\$ (776)
Pay-fixed interest rate swap agreements - securities available for sale	41,950	7.1	15
Total	\$ 49,038	7.3	\$ (761)
No hedge designation			
Rate-lock mortgage loan commitments	\$ 168,816	0.1	\$ 7,020
Mandatory commitments to sell mortgage loans	186,092	0.1	(941)
Pay-fixed interest rate swap agreements - commercial	147,456	4.5	(9,700)
Pay-variable interest rate swap agreements - commercial	147,456	4.5	9,700
Pay-fixed interest rate swap agreements	25,000	0.6	(295)
Interest rate cap agreements	135,000	1.8	5
Purchased options	2,908	0.5	42
Written options	2,848	0.5	(42)
Total	\$ 815,576	2.0	\$ 5,789

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

We have used variable-rate and short-term fixed-rate (less than 12 months) debt obligations to fund a portion of our Condensed Consolidated Statements of Financial Condition, which exposed us to variability in interest rates. To meet our asset/liability management objectives, we may periodically enter into derivative financial instruments to mitigate exposure to fluctuations in cash flows resulting from changes in interest rates (“Cash Flow Hedges”). Cash Flow Hedges had included certain pay-fixed interest rate swap and interest rate cap agreements. Pay-fixed interest rate swap agreements convert the variable-rate cash flows on debt obligations to fixed-rates. Under interest-rate cap agreements, we will receive cash if interest rates rise above a predetermined level. As a result, we effectively have variable-rate debt with an established maximum rate. We paid an upfront premium on interest rate caps which was recognized in earnings in the same period in which the hedged item affected earnings. During the first and third quarters of 2020 we transferred all of our Cash Flow Hedge interest rate cap and pay-fixed interest rate swap agreements, respectively to a no hedge designation. The \$2.0 million and \$0.5 million unrealized loss on our Cash Flow Hedge interest rate cap and pay-fixed interest rate swap agreements, respectively, which were included as a component of accumulated other comprehensive income at the time of the transfers, were being reclassified into earnings over the remaining life of the interest rate cap agreements and pay-fixed interest rate swap agreements. In the fourth quarter of 2020 it became probable that the forecasted transactions being hedged by these interest rate cap and pay-fixed interest rate swap agreements would not occur by the end of the originally specified time period. As a result, all remaining unrealized losses included as a component of accumulated other comprehensive income were reclassified into earnings at that time. The interest rate cap and pay-fixed interest rate swap agreements are now classified as a no hedge designation at March 31, 2021 and any changes in fair value since the transfers to the no hedge designation are recorded in earnings.

We have entered into a pay-fixed interest rate swap to protect a portion of the fair value of a certain fixed rate commercial loan (“Fair Value Hedge – Commercial Loan”). As a result, changes in the fair value of the pay-fixed interest rate swap is expected to offset changes in the fair value of the fixed rate commercial loan due to fluctuations in interest rates. We record the fair value of Fair Value Hedge – Commercial Loan in accrued income and other assets and accrued expenses and other liabilities on our Condensed Consolidated Statements of Financial Condition. The hedged item (fixed rate commercial loan) is also recorded at fair value which offsets the adjustment to the Fair Value Hedge – Commercial Loan. On an ongoing basis, we adjust our Condensed Consolidated Statements of Financial Condition to reflect the then current fair value of both the Fair Value Hedge – Commercial Loan and the hedged item. The related gains or losses are reported in interest income – interest and fees on loans in our Condensed Consolidated Statements of Operations.

We have entered into pay-fixed interest rate swaps to protect a portion of the fair value of certain securities available for sale (“Fair Value Hedge – AFS Securities”). As a result, the change in the fair value of the pay-fixed interest rate swaps is expected to offset a portion of the change in the fair value of the fixed rate securities available for sale due to fluctuations in interest rates. We record the fair value of Fair Value Hedge – AFS Securities in accrued income and other assets and accrued expenses and other liabilities on our Condensed Consolidated Statements of Financial Condition. The hedged items (fixed rate securities available for sale) are also recorded at fair value which offsets the adjustment to the Fair Value Hedge – AFS Securities. On an ongoing basis, we adjust our Condensed Consolidated Statements of Financial Condition to reflect the then current fair value of both the Fair Value Hedge – AFS Securities and the hedged item. The related gains or losses are reported in interest income – interest on securities available for sale – tax-exempt in our Condensed Consolidated Statements of Operations.

Certain financial derivative instruments have not been designated as hedges. The fair value of these derivative financial instruments has been recorded on our Condensed Consolidated Statements of Financial Condition and is adjusted on an ongoing basis to reflect their then current fair value. The changes in fair value of derivative financial instruments not designated as hedges are recognized in our Condensed Consolidated Statements of Operations.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

In the ordinary course of business, we enter into rate-lock mortgage loan commitments with customers (“Rate-Lock Commitments”). These commitments expose us to interest rate risk. We also enter into mandatory commitments to sell mortgage loans (“Mandatory Commitments”) to reduce the impact of price fluctuations of mortgage loans held for sale and Rate-Lock Commitments. Mandatory Commitments help protect our loan sale profit margin from fluctuations in interest rates. The changes in the fair value of Rate-Lock Commitments and Mandatory Commitments are recognized currently as part of net gains on mortgage loans in our Condensed Consolidated Statements of Operations. We obtain market prices on Mandatory Commitments and Rate-Lock Commitments. Net gains on mortgage loans, as well as net income may be more volatile as a result of these derivative instruments, which are not designated as hedges.

In prior periods we offered to our deposit customers an equity linked time deposit product (“Altitude CD”). The Altitude CD was a time deposit that provides the customer a guaranteed return of principal at maturity plus a potential equity return (a written option), while we receive a like stream of funds based on the equity return (a purchased option). The written and purchased options will generally move in opposite directions resulting in little or no net impact on our Condensed Consolidated Statements of Operations. All of the written and purchased options in the table above relate to this Altitude CD product.

We have a program that allows commercial loan customers to lock in a fixed rate for a longer period of time than we would normally offer for interest rate risk reasons. We will enter into a variable rate commercial loan and an interest rate swap agreement with a customer and then enter into an offsetting interest rate swap agreement with an unrelated party. The interest rate swap agreement fair values will generally move in opposite directions resulting in little or no net impact on our Condensed Consolidated Statements of Operations. All of the interest rate swap agreements noted as commercial in the table above with no hedge designation relate to this program.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

The following tables illustrate the impact that the derivative financial instruments discussed above have on individual line items in the Condensed Consolidated Statements of Financial Condition for the periods presented:

Fair Values of Derivative Instruments

	Asset Derivatives				Liability Derivatives			
	March 31, 2021		December 31, 2020		March 31, 2021		December 31, 2020	
	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value
	(In thousands)							
Derivatives designated as hedging instruments								
Pay-fixed interest rate swap agreements	Other assets	\$ 4,887	Other assets	\$ 15	Other liabilities	\$ 423	Other liabilities	\$ 776
Derivatives not designated as hedging instruments								
Rate-lock mortgage loan commitments	Other assets	3,198	Other assets	\$ 7,020	Other liabilities	-	Other liabilities	\$ -
Mandatory commitments to sell mortgage loans	Other assets	896	Other assets	-	Other liabilities	-	Other liabilities	941
Pay-fixed interest rate swap agreements - commercial	Other assets	140	Other assets	-	Other liabilities	6,565	Other liabilities	9,700
Pay-variable interest rate swap agreements - commercial	Other assets	6,565	Other assets	9,700	Other liabilities	140	Other liabilities	-
Pay-fixed interest rate swap agreements	Other assets	-	Other assets	-	Other liabilities	177	Other liabilities	295
Interest rate cap agreements	Other assets	20	Other assets	5	Other liabilities	-	Other liabilities	-
Purchased options	Other assets	60	Other assets	42	Other liabilities	-	Other liabilities	-
Written options	Other assets	-	Other assets	-	Other liabilities	60	Other liabilities	42
		<u>10,879</u>		<u>16,767</u>		<u>6,942</u>		<u>10,978</u>
Total derivatives		<u>\$ 15,766</u>		<u>\$ 16,782</u>		<u>\$ 7,365</u>		<u>\$ 11,754</u>

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

The effect of derivative financial instruments on the Condensed Consolidated Statements of Operations follows:

Three Month Periods Ended March 31,						
	Loss Recognized in Other Comprehensive Loss (Effective Portion)		Location of Loss Reclassified from Accumulated Other Comprehensive Income into Income (Effective Portion)	Loss Reclassified from Accumulated Other Comprehensive Income into Income (Effective Portion)		Location of Gain (Loss) Recognized in Income
	2021	2020	(Effective Portion)	2021	2020	Gain (Loss) Recognized in Income
(In thousands)						
Fair Value Hedges						
Pay-fixed interest rate swap agreement - Commercial loan						Interest and fees on loans \$ 352 \$ (546)
Pay-fixed interest rate swap agreement - Securities available for sale						Interest on securities available for sale - tax-exempt 4,873 -
Total						\$ 5,225 \$ (546)
Cash Flow Hedges						
Interest rate cap agreements	\$ -	\$ (14)	Interest expense	\$ -	\$ (53)	
Pay-fixed interest rate swap agreements	-	(392)	Interest expense	-	(22)	
Total	\$ -	\$ (406)		\$ -	\$ (75)	
No hedge designation						
Rate-lock mortgage loan commitments						Net gains on mortgage loans \$ (3,822) \$ 4,320
Mandatory commitments to sell mortgage loans						Net gains on mortgage loans 1,837 (1,954)
Pay-fixed interest rate swap agreements - commercial						Interest income 3,275 (8,173)
Pay-variable interest rate swap agreements - commercial						Interest income (3,275) 8,173
Pay-fixed interest rate swap agreements						Interest expense 118 -
Interest rate cap agreements						Interest expense 15 (35)
Purchased options						Interest expense 18 (104)
Written options						Interest expense (18) 103
Total						\$ (1,852) \$ 2,330

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

7. Goodwill and Other Intangibles

The following table summarizes intangible assets, net of amortization:

	March 31, 2021		December 31, 2020	
	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
	(In thousands)			
Amortized intangible assets - core deposits	\$ 11,916	\$ 7,853	\$ 11,916	\$ 7,610
Unamortized intangible assets - goodwill	\$ 28,300		\$ 28,300	

A summary of estimated core deposit intangible amortization at March 31, 2021 follows:

	(In thousands)
Nine months ending December 31, 2021	\$ 727
2022	785
2023	547
2024	516
2025	487
2026 and thereafter	1,001
Total	\$ 4,063

8. Share Based Compensation

We maintain share based payment plans that include a non-employee director stock purchase plan and a long-term incentive plan that permits the issuance of share based compensation, including stock options and non-vested share awards. The long-term incentive plan, which is shareholder approved, permits the grant of additional share based awards for up to 0.4 million shares of common stock as of March 31, 2021. The non-employee director stock purchase plan permits the issuance of additional share based payments for up to 0.1 million shares of common stock as of March 31, 2021. Share based awards and payments are measured at fair value at the date of grant and are expensed over the requisite service period. Common shares issued upon exercise of stock options come from currently authorized but unissued shares.

A summary of restricted stock and performance stock units (“PSU”) granted pursuant to our long-term incentive plan follows:

	Three Months Ended March 31,	
	2021	2020
Restricted stock	75,584	52,996
PSU	23,981	20,897

The shares of restricted stock and PSUs shown in the above table cliff vest after a period of three years. The performance feature of the PSUs is based on a comparison of our total shareholder return over the three year period starting on the grant date to the total shareholder return over that period for an index of our banking peers.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

Our directors may elect to receive all or a portion of their cash retainer fees in the form of common stock (either on a current basis or on a deferred basis) pursuant to the non-employee director stock purchase plan referenced above. Shares equal in value to that portion of each director's fees that he or she has elected to receive in stock on a current basis are issued each quarter and vest immediately. Shares issued on a deferred basis are credited at the rate of 90% of the current fair value of our common stock and vest immediately. During the three month periods ended March 31, 2021 and 2020 we issued 0.005 million and 0.004 million shares, respectively and expensed their value during those same periods.

Total compensation expense recognized for grants pursuant to our long-term incentive plan was \$0.3 million and \$0.5 million during the three month periods ended March 31, 2021 and 2020, respectively. The corresponding tax benefit relating to this expense was \$0.1 million for each period. Total expense recognized for non-employee director share based payments was \$0.09 million during both three month periods ended March 31, 2021 and 2020. The corresponding tax benefit relating to this expense was \$0.02 million during each period.

At March 31, 2021, the total expected compensation cost related to non-vested restricted stock and PSUs not yet recognized was \$3.2 million. The weighted-average period over which this amount will be recognized is 2.3 years.

A summary of outstanding stock option grants and related transactions follows:

	Number of Shares	Average Exercise Price	Weighted- Average Remaining Contractual Term (Years)	Aggregated Intrinsic Value (In thousands)
Outstanding at January 1, 2021	121,189	\$ 4.81		
Granted	-			
Exercised	(19,050)	3.16		
Forfeited	-			
Expired	-			
Outstanding at March 31, 2021	<u>102,139</u>	<u>\$ 5.12</u>	<u>2.0</u>	<u>\$ 1,892</u>
Vested and expected to vest at March 31, 2021	<u>102,139</u>	<u>\$ 5.12</u>	<u>2.0</u>	<u>\$ 1,892</u>
Exercisable at March 31, 2021	<u>102,139</u>	<u>\$ 5.12</u>	<u>2.0</u>	<u>\$ 1,892</u>

A summary of outstanding non-vested restricted stock and PSUs and related transactions follows:

	Number of Shares	Weighted- Average Grant Date Fair Value
Outstanding at January 1, 2021	207,117	\$ 22.70
Granted	99,565	20.81
Vested	(54,982)	23.53
Forfeited	(10,229)	22.69
Outstanding at March 31, 2021	<u>241,471</u>	<u>\$ 21.73</u>

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

Certain information regarding options exercised during the periods follows:

	Three Months Ended March 31,	
	2021	2020
	(In thousands)	
Intrinsic value	\$ 313	\$ 210
Cash proceeds received	\$ 60	\$ 41
Tax benefit realized	\$ 66	\$ 44

9. Income Tax

Income tax expense was \$5.1 million and \$0.9 million during the three month periods ended March 31, 2021 and 2020, respectively. Our actual federal income tax expense is different than the amount computed by applying our statutory income tax rate to our income before income tax primarily due to tax-exempt interest income and tax-exempt income from the increase in the cash surrender value on life insurance. In addition, the first quarters of 2021 and 2020 include reductions of \$0.1 million and \$0.2 million of income tax expense related to impact of the excess value of stock awards that vested and stock options that were exercised as compared to the initial fair values that were expensed.

We assess whether a valuation allowance should be established against our deferred tax assets based on the consideration of all available evidence using a “more likely than not” standard. The ultimate realization of this asset is primarily based on generating future income. We concluded at March 31, 2021, March 31, 2020 and December 31, 2020 that the realization of substantially all of our deferred tax assets continues to be more likely than not.

At both March 31, 2021 and December 31, 2020, we had approximately \$0.2 million, of gross unrecognized tax benefits. We do not expect the total amount of unrecognized tax benefits to significantly increase or decrease during the balance of 2021.

10. Regulatory Matters

Capital guidelines adopted by federal and state regulatory agencies and restrictions imposed by law limit the amount of cash dividends our Bank can pay to us. Under these guidelines, the amount of dividends that may be paid in any calendar year is limited to the Bank’s current year net profits, combined with the retained net profits of the preceding two years. Further, the Bank cannot pay a dividend at any time that it has negative undivided profits. As of March 31, 2021, the Bank had positive undivided profits of \$81.6 million. It is not our intent to have dividends paid in amounts that would reduce the capital of our Bank to levels below those which we consider prudent or that would not be in accordance with guidelines of regulatory authorities.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

We are also subject to various regulatory capital requirements. The prompt corrective action regulations establish quantitative measures to ensure capital adequacy and require minimum amounts and ratios of total, Tier 1, and common equity Tier 1 capital to risk-weighted assets and Tier 1 capital to average assets. Failure to meet minimum capital requirements can result in certain mandatory, and possibly discretionary, actions by regulators that could have a material effect on our interim condensed consolidated financial statements. In addition, capital adequacy rules include a common equity Tier 1 capital conservation buffer of 2.5% of risk-weighted assets that applies to all supervised financial institutions. To avoid limits on capital distributions and certain discretionary bonus payments we must meet the minimum ratio for adequately capitalized institutions plus the buffer. Under capital adequacy guidelines, we must meet specific capital requirements that involve quantitative measures as well as qualitative judgments by the regulators. The most recent regulatory filings as of March 31, 2021 and December 31, 2020, categorized our Bank as well capitalized. Management is not aware of any conditions or events that would have changed the most recent Federal Deposit Insurance Corporation (“FDIC”) categorization.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

Our actual capital amounts and ratios follow (1):

	Actual		Minimum for Adequately Capitalized Institutions		Minimum for Well-Capitalized Institutions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
(Dollars in thousands)						
March 31, 2021						
Total capital to risk-weighted assets						
Consolidated	\$ 467,880	15.82%	\$ 236,589	8.00%	NA	NA
Independent Bank	414,246	13.99	236,819	8.00	\$ 296,024	10.00%
Tier 1 capital to risk-weighted assets						
Consolidated	\$ 390,875	13.22%	\$ 177,442	6.00%	NA	NA
Independent Bank	377,199	12.74	177,614	6.00	\$ 236,819	8.00%
Common equity tier 1 capital to risk-weighted assets						
Consolidated	\$ 352,558	11.92%	\$ 133,081	4.50%	NA	NA
Independent Bank	377,199	12.74	133,211	4.50	\$ 192,415	6.50%
Tier 1 capital to average assets						
Consolidated	\$ 390,875	9.28%	\$ 168,473	4.00%	NA	NA
Independent Bank	377,199	8.95	168,622	4.00	\$ 210,778	5.00%
December 31, 2020						
Total capital to risk-weighted assets						
Consolidated	\$ 455,072	15.95%	\$ 228,214	8.00%	NA	NA
Independent Bank	401,005	14.06	228,111	8.00	\$ 285,139	10.00%
Tier 1 capital to risk-weighted assets						
Consolidated	\$ 379,395	13.30%	\$ 171,161	6.00%	NA	NA
Independent Bank	365,343	12.81	171,083	6.00	\$ 228,111	8.00%
Common equity tier 1 capital to risk-weighted assets						
Consolidated	\$ 341,095	11.96%	\$ 128,370	4.50%	NA	NA
Independent Bank	365,343	12.81	128,312	4.50	\$ 185,340	6.50%
Tier 1 capital to average assets						
Consolidated	\$ 379,395	9.15%	\$ 165,825	4.00%	NA	NA
Independent Bank	365,343	8.81	165,828	4.00	\$ 207,285	5.00%

(1) These ratios do not reflect a capital conservation buffer of 2.50% at March 31, 2021 and December 31, 2020.

NA - Not applicable

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

The components of our regulatory capital are as follows:

	Consolidated		Independent Bank	
	March 31, 2021	December 31, 2020	March 31, 2021	December 31, 2020
	(In thousands)			
Total shareholders' equity	\$ 387,329	\$ 389,522	\$ 411,970	\$ 413,770
Add (deduct)				
Accumulated other comprehensive income for regulatory purposes	(10,135)	(15,821)	(10,135)	(15,821)
Goodwill and other intangibles	(32,363)	(32,606)	(32,363)	(32,606)
CECL (1)	7,727	-	7,727	-
Common equity tier 1 capital	352,558	341,095	377,199	365,343
Qualifying trust preferred securities	38,317	38,300	-	-
Tier 1 capital	390,875	379,395	377,199	365,343
Subordinated debt	40,000	40,000	-	-
Allowance for credit losses and allowance for unfunded lending commitments limited to 1.25% of total risk-weighted assets (2)	37,005	35,677	37,047	35,662
Total risk-based capital	<u>\$ 467,880</u>	<u>\$ 455,072</u>	<u>\$ 414,246</u>	<u>\$ 401,005</u>

(1) We elected the three year CECL transition method for regulatory purposes.

(2) Beginning January 1, 2021, calculation of allowances are based on CECL methodology. Prior to January 1, 2021, calculation was based on the probable incurred loss methodology.

11. Fair Value Disclosures

FASB ASC topic 820 defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. FASB ASC topic 820 also establishes a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value.

The standard describes three levels of inputs that may be used to measure fair value:

Level 1: Valuation is based upon quoted prices for identical instruments traded in active markets. Level 1 instruments include securities traded on active exchange markets, such as the New York Stock Exchange, as well as U.S. Treasury securities that are traded by dealers or brokers in active over-the-counter markets.

Level 2: Valuation is based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market. Level 2 instruments include securities traded in less active dealer or broker markets.

Level 3: Valuation is generated from model-based techniques that use at least one significant assumption not observable in the market. These unobservable assumptions reflect estimates of assumptions that market participants would use in pricing the asset or liability. Valuation techniques include use of option pricing models, discounted cash flow models and similar techniques.

We used the following methods and significant assumptions to estimate fair value:

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

Securities: Where quoted market prices are available in an active market, securities available for sale are classified as Level 1 of the valuation hierarchy. We currently do not have any Level 1 securities. If quoted market prices are not available for the specific security, then fair values are estimated by (1) using quoted market prices of securities with similar characteristics, (2) matrix pricing, which is a mathematical technique used widely in the industry to value debt securities without relying exclusively on quoted prices for specific securities but rather by relying on the securities' relationship to other benchmark quoted prices, or (3) a discounted cash flow analysis whose significant fair value inputs can generally be verified and do not typically involve judgment by management. These securities are classified as Level 2 of the valuation hierarchy and primarily include agency securities, private label mortgage-backed securities, other asset backed securities, obligations of states and political subdivisions, trust preferred securities, corporate securities and foreign government securities.

Loans held for sale: The fair value of mortgage loans held for sale, carried at fair value is based on agency cash window loan pricing for comparable assets (recurring Level 2).

Collateral dependent loans with specific loss allocations based on collateral value: From time to time, certain collateral dependent loans will have an ACL established. When the fair value of the collateral is based on an appraised value or when an appraised value is not available we record the collateral dependent loan as nonrecurring Level 3. These appraisals may utilize a single valuation approach or a combination of approaches including comparable sales and the income approach. Adjustments are routinely made in the appraisal process by the independent appraisers to adjust for differences between the comparable sales and income data available. Such adjustments can be significant and thus will typically result in a Level 3 classification of the inputs for determining fair value.

Other real estate: At the time of acquisition, other real estate is recorded at fair value, less estimated costs to sell, which becomes the property's new basis. Subsequent write-downs to reflect declines in value since the time of acquisition may occur from time to time and are recorded in net (gains) losses on other real estate and repossessed assets, which is part of non-interest expense - other in the Condensed Consolidated Statements of Operations. The fair value of the property used at and subsequent to the time of acquisition is typically determined by a third party appraisal of the property. These appraisals may utilize a single valuation approach or a combination of approaches including comparable sales and the income approach. Adjustments are routinely made in the appraisal process by the independent appraisers to adjust for differences between the comparable sales and income data available. Such adjustments can be significant and typically result in a Level 3 classification of the inputs for determining fair value.

Appraisals for both collateral-dependent loans and other real estate are performed by certified general appraisers (for commercial properties) or certified residential appraisers (for residential properties) whose qualifications and licenses have been reviewed and verified by us. Once received, an independent third party, or a member of our Collateral Evaluation Department (for commercial properties), or a member of our Special Assets Group (for residential properties) reviews the assumptions and approaches utilized in the appraisal as well as the overall resulting fair value in comparison with independent data sources such as recent market data or industry-wide statistics. We compare the actual selling price of collateral that has been sold to the most recent appraised value of our properties to determine what additional adjustment, if any, should be made to the appraisal value to arrive at fair value. For commercial and residential properties we typically discount an appraisal to account for various factors that the appraisal excludes in its assumptions. These additional discounts generally do not result in material adjustments to the appraised value.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

Capitalized mortgage loan servicing rights: The fair value of capitalized mortgage loan servicing rights is based on a valuation model used by an independent third party that calculates the present value of estimated net servicing income. The valuation model incorporates assumptions that market participants would use in estimating future net servicing income. Certain model assumptions are generally unobservable and are based upon the best information available including data relating to our own servicing portfolio, reviews of mortgage servicing assumption and valuation surveys and input from various mortgage servicers and, therefore, are recorded as Level 3. Management evaluates the third party valuation for reasonableness each quarter as part of our financial reporting control processes.

Derivatives: The fair value of rate-lock mortgage loan commitments is based on agency cash window loan pricing for comparable assets and the fair value of mandatory commitments to sell mortgage loans is based on mortgage backed security pricing for comparable assets (recurring Level 2). The fair value of interest rate swap and interest rate cap agreements are derived from proprietary models which utilize current market data. The significant fair value inputs can generally be observed in the market place and do not typically involve judgment by management (recurring Level 2). The fair value of purchased and written options is based on prices of financial instruments with similar characteristics and do not typically involve judgment by management (recurring Level 2).

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

Assets and liabilities measured at fair value, including financial assets for which we have elected the fair value option, were as follows:

	Fair Value Measure- ments	Fair Value Measurements Using		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Un- observable Inputs (Level 3)
(In thousands)				
March 31, 2021:				
Measured at Fair Value on a Recurring Basis				
Assets				
Securities available for sale				
U.S. agency	\$ 8,910	\$ -	\$ 8,910	\$ -
U.S. agency residential mortgage-backed	400,420	-	400,420	-
U.S. agency commercial mortgage-backed	11,704	-	11,704	-
Private label mortgage-backed	42,817	-	42,817	-
Other asset backed	228,530	-	228,530	-
Obligations of states and political subdivisions	444,688	-	444,688	-
Corporate	107,823	-	107,823	-
Trust preferred	1,874	-	1,874	-
Foreign government	514	-	514	-
Loans held for sale, carried at fair value	77,799	-	77,799	-
Capitalized mortgage loan servicing rights	23,530	-	-	23,530
Derivatives (1)	15,766	-	15,766	-
Liabilities				
Derivatives (2)	7,365	-	7,365	-
Measured at Fair Value on a Non-recurring Basis:				
Assets				
Collateral dependent loans (3)				
Commercial				
Commercial and industrial	1,293	-	-	1,293
Commercial real estate	110	-	-	110
Mortgage				
1-4 family owner occupied - non-jumbo	570	-	-	570
1-4 family non-owner occupied	246	-	-	246
1-4 family - 2nd lien	298	-	-	298
Resort lending	239	-	-	239
Installment				
Boat lending	7	-	-	7
Recreational vehicle lending	11	-	-	11
Other	142	-	-	142

(1) Included in accrued income and other assets

(2) Included in accrued expenses and other liabilities

(3) Only includes individually evaluated loans with specific loss allocations based on collateral value.

(4) Only includes other real estate with subsequent write downs to fair value.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

	Fair Value Measurements Using			
	Fair Value Measure- ments	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Un- observable Inputs (Level 3)
(In thousands)				
December 31, 2020:				
Measured at Fair Value on a Recurring Basis				
Assets				
Securities available for sale				
U.S. agency	\$ 10,748	\$ -	\$ 10,748	\$ -
U.S. agency residential mortgage-backed	344,582	-	344,582	-
U.S. agency commercial mortgage-backed	7,195	-	7,195	-
Private label mortgage-backed	42,829	-	42,829	-
Other asset backed	254,181	-	254,181	-
Obligations of states and political subdivisions	324,293	-	324,293	-
Corporate	86,017	-	86,017	-
Trust preferred	1,798	-	1,798	-
Foreign government	516	-	516	-
Loans held for sale, carried at fair value	92,434	-	92,434	-
Capitalized mortgage loan servicing rights	16,904	-	-	16,904
Derivatives (1)	16,782	-	16,782	-
Liabilities				
Derivatives (2)	11,754	-	11,754	-
Measured at Fair Value on a Non-recurring Basis:				
Assets				
Impaired loans (3)				
Commercial				
Commercial and industrial	1,468	-	-	1,468
Commercial real estate	6,586	-	-	6,586
Mortgage				
1-4 family owner occupied - jumbo	-	-	-	-
1-4 family owner occupied - non-jumbo	321	-	-	321
1-4 family non-owner occupied	155	-	-	155
1-4 family - 2nd lien	324	-	-	324
Resort lending	61	-	-	61
Installment				
Boat lending	4	-	-	4
Recreational vehicle lending	31	-	-	31
Other	124	-	-	124
Other real estate (4)				
1-4 family owner occupied - non-jumbo	102	-	-	102

(1) Included in accrued income and other assets

(2) Included in accrued expenses and other liabilities

(3) Only includes impaired loans with specific loss allocations based on collateral value.

(4) Only includes other real estate with subsequent write downs to fair value.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

Changes in fair values for financial assets which we have elected the fair value option for the periods presented were as follows:

	Changes in Fair Values for the Three-Month Periods Ended March 31 for Items Measured at Fair Value Pursuant to Election of the Fair Value Option		
	Net Gains on Assets Mortgage Loans	Mortgage Loan Servicing, net	Total Change in Fair Values Included in Current Period Earnings
	(In thousands)		
2021			
Loans held for sale	\$ (2,598)	\$ -	\$ (2,598)
Capitalized mortgage loan servicing rights	-	3,257	3,257
2020			
Loans held for sale	523	-	523
Capitalized mortgage loan servicing rights	-	(6,974)	(6,974)

For those items measured at fair value pursuant to our election of the fair value option, interest income is recorded within the Condensed Consolidated Statements of Operations based on the contractual amount of interest income earned on these financial assets and dividend income is recorded based on cash dividends received.

The following represent impairment charges recognized during the three month periods ended March 31, 2021 and 2020 relating to assets measured at fair value on a non-recurring basis:

- Loans that are individually evaluated using the fair value of collateral for collateral dependent loans had a carrying amount of \$2.9 million, which is net of a valuation allowance of \$1.5 million at March 31, 2021, and had a carrying amount of \$9.1 million, which is net of a valuation allowance of \$1.8 million at December 31, 2020. The provision for credit losses included in our results of operations relating to collateral dependent loans was an expense of \$0.2 million and \$2.4 million during the three month periods ended March 31, 2021 and 2020, respectively.
- Other real estate, which is measured using the fair value of the property, had a carrying amount of zero which is net of a valuation allowance of \$0.06 million at March 31, 2021, and a carrying amount of \$0.10 million which is net of a valuation allowance of \$0.09 million, at December 31, 2020. An additional charge relating to other real estate measured at fair value of zero and \$0.09 million was included in our results of operations during the three month periods ended March 31, 2021 and 2020, respectively.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

A reconciliation for all assets measured at fair value on a recurring basis using significant unobservable inputs (Level 3) follows:

	Capitalized Mortgage Loan Servicing Rights	
	Three Months Ended March 31,	
	2021	2020
	(In thousands)	
Beginning balance	\$ 16,904	\$ 19,171
Total gains (losses) realized and unrealized:		
Included in results of operations	3,257	(6,974)
Included in other comprehensive income	-	-
Purchases, issuances, settlements, maturities and calls	3,369	2,632
Transfers in and/or out of Level 3	-	-
Ending balance	\$ 23,530	\$ 14,829
Amount of total gains (losses) for the period included in earnings attributable to the change in unrealized gains (losses) relating to assets and liabilities still held at March 31	\$ 3,257	\$ (6,974)

The fair value of our capitalized mortgage loan servicing rights has been determined based on a valuation model used by an independent third party as discussed above. The significant unobservable inputs used in the fair value measurement of the capitalized mortgage loan servicing rights are discount rate, cost to service, ancillary income, float rate and prepayment rate. Significant changes in all five of these assumptions in isolation would result in significant changes to the value of our capitalized mortgage loan servicing rights. Quantitative information about our Level 3 fair value measurements measured on a recurring basis follows:

	Asset Fair Value	Valuation Technique	Unobservable Inputs	Range	Weighted Average
	(In thousands)				
March 31, 2021					
Capitalized mortgage loan servicing rights	\$ 23,530	Present value of net servicing revenue	Discount rate	10.00% to 13.00%	10.09%
			Cost to service	\$ 69 to \$215	\$ 78
			Ancillary income	20 to 37	22
			Float rate	1.05%	1.05%
			Prepayment rate	7.48% to 50.27%	13.91%
December 31, 2020					
Capitalized mortgage loan servicing rights	\$ 16,904	Present value of net servicing revenue	Discount rate	10.00% to 13.00%	10.09%
			Cost to service	\$ 69 to \$289	\$ 79
			Ancillary income	20 to 37	22
			Float rate	0.43%	0.43%
			Prepayment rate	7.92% to 64.70%	20.85%

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

Quantitative information about Level 3 fair value measurements measured on a non-recurring basis follows:

	Asset Fair Value <u>(In thousands)</u>	Valuation Technique	Unobservable Inputs	Range	Weighted Average
March 31, 2021					
Collateral dependent loans					
Commercial					
	\$ 1,403	Sales comparison approach	Adjustment for differences between comparable sales	(31.0)% to 12.0%	(1.5)%
Mortgage and Installment(1)	1,513	Sales comparison approach	Adjustment for differences between comparable sales	(73.3) to 104.6	(1.3)
December 31, 2020					
Collateral dependent loans					
Commercial					
	\$ 8,054	Sales comparison approach	Adjustment for differences between comparable sales	(40.0)% to 75.0%	3.8%
Mortgage and Installment(1)	1,020	Sales comparison approach	Adjustment for differences between comparable sales	(73.3) to 104.6	(1.5)
Other real estate					
Mortgage					
	102	Sales comparison approach	Adjustment for differences between comparable sales	(13.1) to 2.4	(3.6)

(1) In addition to the valuation techniques and unobservable inputs discussed above, at March 31, 2021 and December 31, 2020 certain collateral dependent installment loans totaling approximately \$0.11 million and \$0.16 million, respectively are secured by collateral other than real estate. For the majority of these loans, we apply internal discount rates to industry valuation guides.

The following table reflects the difference between the aggregate fair value and the aggregate remaining contractual principal balance outstanding for loans held for sale for which the fair value option has been elected for the periods presented.

	Aggregate Fair Value	Difference <u>(In thousands)</u>	Contractual Principal
Loans held for sale			
March 31, 2021	\$ 77,799	\$ 1,258	\$ 76,541
December 31, 2020	92,434	3,856	88,578

12. Fair Values of Financial Instruments

Most of our assets and liabilities are considered financial instruments. Many of these financial instruments lack an available trading market and it is our general practice and intent to hold the majority of our financial instruments to maturity. Significant estimates and assumptions were used to determine the fair value of financial instruments. These estimates are subjective in nature, involving uncertainties and matters of judgment, and therefore, fair values may not be a precise estimate. Changes in assumptions could significantly affect the estimates.

Estimated fair values have been determined using available data and methodologies that are considered suitable for each category of financial instrument. For instruments with adjustable interest rates which reprice frequently and without significant credit risk, it is presumed that estimated fair values approximate the recorded book balances.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

The estimated recorded book balances and fair values follow:

	Recorded Book Balance	Fair Value	Fair Value Using		
			Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Un- observable Inputs (Level 3)
(In thousands)					
March 31, 2021					
Assets					
Cash and due from banks	\$ 49,220	\$ 49,220	\$ 49,220	\$ -	\$ -
Interest bearing deposits	81,287	81,287	81,287	-	-
Securities available for sale	1,247,280	1,247,280	-	1,247,280	-
Federal Home Loan Bank and Federal Reserve Bank Stock	18,427	NA	NA	NA	NA
Net loans and loans held for sale	2,815,268	2,828,523	-	77,799	2,750,724
Accrued interest receivable	13,628	13,628	3	5,130	8,495
Derivative financial instruments	15,766	15,766	-	15,766	-
Liabilities					
Deposits with no stated maturity (1)	\$ 3,544,206	\$ 3,544,206	\$ 3,544,206	\$ -	\$ -
Deposits with stated maturity (1)	314,369	316,123	-	316,123	-
Other borrowings	30,006	30,404	-	30,404	-
Subordinated debt	39,300	43,823	-	43,823	-
Subordinated debentures	39,541	32,107	-	32,107	-
Accrued interest payable	1,150	1,150	64	1,086	-
Derivative financial instruments	7,365	7,365	-	7,365	-
December 31, 2020					
Assets					
Cash and due from banks	\$ 56,006	\$ 56,006	\$ 56,006	\$ -	\$ -
Interest bearing deposits	62,699	62,699	62,699	-	-
Securities available for sale	1,072,159	1,072,159	-	1,072,159	-
Federal Home Loan Bank and Federal Reserve Bank Stock	18,427	NA	NA	NA	NA
Net loans and loans held for sale	2,790,683	2,794,058	-	92,434	2,701,624
Accrued interest receivable	12,315	12,315	3	3,414	8,898
Derivative financial instruments	16,782	16,782	-	16,782	-
Liabilities					
Deposits with no stated maturity (1)	\$ 3,198,338	\$ 3,198,338	\$ 3,198,338	\$ -	\$ -
Deposits with stated maturity (1)	439,017	441,457	-	441,457	-
Other borrowings	30,012	30,844	-	30,844	-
Subordinated debt	39,281	41,417	-	41,417	-
Subordinated debentures	39,524	30,265	-	30,265	-
Accrued interest payable	601	601	59	542	-
Derivative financial instruments	11,754	11,754	-	11,754	-

(1) Deposits with no stated maturity include reciprocal deposits with a recorded book balance of \$572.258 million and \$518.400 million at March 31, 2021 and December 31, 2020, respectively. Deposits with a stated maturity include reciprocal deposits with a recorded book balance of \$36.431 million and \$37.785 million at March 31, 2021 and December 31, 2020, respectively.

The fair values for commitments to extend credit and standby letters of credit are estimated to approximate their aggregate book balance, which is nominal and therefore are not disclosed.

Fair value estimates are made at a specific point in time, based on relevant market information and information about the financial instrument. These estimates do not reflect any premium or discount that could result from offering for sale the entire holdings of a particular financial instrument.

Fair value estimates are based on existing on- and off-balance sheet financial instruments without attempting to estimate the value of anticipated future business, the value of future earnings attributable to off-balance sheet activities and the value of assets and liabilities that are not considered financial instruments.

Fair value estimates for deposit accounts do not include the value of the core deposit intangible asset resulting from the low-cost funding provided by the deposit liabilities compared to the cost of borrowing funds in the market.

13. Contingencies

COVID-19 Pandemic

On March 11, 2020, the World Health Organization declared COVID-19, the disease caused by the novel coronavirus, a pandemic as a result of the global spread of the coronavirus illness. In response to the outbreak, federal and state authorities in the U.S. introduced various measures to try to limit or slow the spread of the virus. As a result the pandemic and related government measures, Michigan has experienced an increase in unemployment. On December 11, 2020, the U.S. Food and Drug Administration (FDA) issued its first emergency use authorization for a COVID-19 vaccine. Since that time, the FDA has issued other emergency use authorizations for additional vaccines, and the United States has seen a rapid increase in the number of individuals receiving vaccinations. The U.S. Centers for Disease Control and Prevention (CDC) states that widespread vaccinations may lead to greater immunity, which ultimately is expected to result in slowing the spread of the virus.

The COVID-19 pandemic and the related government restrictions and guidance have had and continue to have a significant effect on us, our customers and the markets we serve. Our business, results of operations and financial condition may be adversely affected by a number of factors that could impact us and our customers, including but not limited to:

- restrictions on activity and high levels of unemployment may cause increases in loan delinquencies, foreclosures and defaults;
- increases in allowance for credit losses may be necessary;
- declines in collateral values may occur;
- third party disruptions, including outages at network providers, on-line banking vendors and other suppliers;
- increased cyber and payment fraud risk, as cybercriminals attempt to profit from the disruption, given increased online and remote activity;
- operational failures due to changes in our normal business practices necessitated by the pandemic and related governmental actions; and/or
- key personnel or significant numbers of our employees being unable to work effectively, including because of illness or restrictions in connection with COVID-19.

These factors may continue for a significant period of time.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
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The extent to which the COVID-19 pandemic will impact our business, results of operations and financial condition will depend on future developments, which are highly uncertain and difficult to predict. Those developments and factors include, the duration and spread of the pandemic, its severity, the actions to contain the pandemic or address its impact, and how quickly and to what extent normal economic and operating conditions can resume. We do not yet know the full extent of the impact. However, the effects could have a material adverse impact on our business, asset valuations, financial condition and results of operations. Material adverse impacts may include all or a combination of valuation impairments on our intangible assets, securities available for sale, loans, capitalized mortgage loan servicing rights or deferred tax assets.

Certain industries (such as hotels and restaurants) have been more adversely impacted by the COVID-19 pandemic and related periodic shut downs of our economy. We believe that the following industry concentrations within our commercial loan portfolio represent greater potential risk in the current economic environment. The balances below are as of March 31, 2021.

Commercial and industrial portfolio segment:

- Retail - \$93 million
- Food service - \$55 million
- Hotel - \$44 million

Commercial real estate portfolio segment:

- Retail - \$98 million
- Office - \$65 million
- Multifamily - \$60 million

We are closely monitoring these industry concentrations and at present do not foresee any significant losses relative to this portion of our loan portfolio given the current economic conditions in Michigan and the fact that many businesses have reopened. However, a high degree of uncertainty still exists with respect to the impact of the COVID-19 pandemic and the related economic disruptions on the future performance of our loan portfolio, including these concentrations.

Litigation

We are involved in various litigation matters in the ordinary course of business. At the present time, we do not believe any of these matters will have a significant impact on our consolidated financial position or results of operations. The aggregate amount we have accrued for losses we consider probable as a result of these litigation matters is immaterial. However, because of the inherent uncertainty of outcomes from any litigation matter, we believe it is reasonably possible we may incur losses in addition to the amounts we have accrued. At this time, we estimate the maximum amount of additional losses that are reasonably possible is insignificant. However, because of a number of factors, including the fact that certain of these litigation matters are still in their early stages, this maximum amount may change in the future.

The litigation matters described in the preceding paragraph primarily include claims that have been brought against us for damages, but do not include litigation matters where we seek to collect amounts owed to us by third parties (such as litigation initiated to collect delinquent loans). These excluded, collection-related matters may involve claims or counterclaims by the opposing party or parties, but we have excluded such matters from the disclosure contained in the preceding paragraph in all cases where we believe the possibility of us paying damages to any opposing party is remote.

Loss Reimbursement Obligations

The provision for loss reimbursement on sold loans represents our estimate of incurred losses related to mortgage loans that we have sold to investors (primarily Fannie Mae, Freddie Mac, Ginnie Mae and the Federal Home Loan Bank of Indianapolis). Since we sell mortgage loans without recourse, loss reimbursements only occur in those instances where we have breached a representation or warranty or other contractual requirement related to the loan sale. The provision for loss reimbursement on sold loans was an expense of \$0.04 million for both three month periods ended March 31, 2021 and 2020. The reserve for loss reimbursements on sold mortgage loans totaled \$1.05 million and \$1.02 million at March 31, 2021 and December 31, 2020, respectively. This reserve is included in accrued expenses and other liabilities in our Condensed Consolidated Statements of Financial Condition. This reserve is based on an analysis of mortgage loans that we have sold which are further categorized by delinquency status, loan to value, and year of origination. The calculation includes factors such as probability of default, probability of loss reimbursement (breach of representation or warranty) and estimated loss severity. We believe that the amounts that we have accrued for incurred losses on sold mortgage loans are appropriate given our analyses. However, future losses could exceed our current estimate.

Visa Stock

We own 12,566 shares of VISA Class B common stock. At the present time, these shares can only be sold to other Class B shareholders. As a result, there has generally been limited transfer activity in private transactions between buyers and sellers. Given the limited activity that we have become aware of and the continuing uncertainty regarding the likelihood, ultimate timing and eventual exchange rate for Class B shares into Class A shares, we continue to carry these shares at zero, representing cost basis less impairment. However, given the current conversion ratio of 1.6228 Class A shares for every 1 Class B share and the closing price of VISA Class A shares on April 20, 2021 of \$223.26 per share, our 12,566 Class B shares would have a current “value” of approximately \$4.6 million. We continue to monitor Class B trading activity and the status of the resolution of certain litigation matters at VISA that would trigger the conversion of Class B common shares into Class A common shares, which would not have any trading restrictions.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

14. Accumulated Other Comprehensive Income (Loss) (“AOCIL”)

A summary of changes in AOCIL follows:

	Unrealized Gains on Securities Available for Sale	Dispropor- tionate Tax Effects from Securities Available for Sale	Unrealized Losses on Cash Flow Hedges	Total
	(In thousands)			
For the three months ended March 31, 2021				
Balances at beginning of period	\$ 15,822	\$ (5,798)	\$ -	\$ 10,024
Other comprehensive loss before reclassifications	(6,805)	-	-	(6,805)
Amounts reclassified from AOCIL	1,119	-	-	1,119
Net current period other comprehensive loss	(5,686)	-	-	(5,686)
Balances at end of period	<u>\$ 10,136</u>	<u>\$ (5,798)</u>	<u>\$ -</u>	<u>\$ 4,338</u>
2020				
Balances at beginning of period	\$ 3,739	\$ (5,798)	\$ (1,727)	\$ (3,786)
Other comprehensive loss before reclassifications	(606)	-	(321)	(927)
Amounts reclassified from AOCIL	(200)	-	59	(141)
Net current period other comprehensive loss	(806)	-	(262)	(1,068)
Balances at end of period	<u>\$ 2,933</u>	<u>\$ (5,798)</u>	<u>\$ (1,989)</u>	<u>\$ (4,854)</u>

The disproportionate tax effects from securities available for sale arose due to tax effects of other comprehensive income (“OCI”) in the presence of a valuation allowance against our deferred tax assets and a pretax loss from operations. Generally, the amount of income tax expense or benefit allocated to operations is determined without regard to the tax effects of other categories of income or loss, such as OCI. However, an exception to the general rule is provided when, in the presence of a valuation allowance against deferred tax assets, there is a pretax loss from operations and pretax income from other categories in the current period. In such instances, income from other categories must offset the current loss from operations, the tax benefit of such offset being reflected in operations. Release of material disproportionate tax effects from other comprehensive income to earnings is done by the portfolio method whereby the effects will remain in AOCIL as long as we carry a more than inconsequential portfolio of securities available for sale.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

A summary of reclassifications out of each component of AOCIL for the three months ended March 31 follows:

AOCIL Component	Amount Reclassified From AOCIL (In thousands)	Affected Line Item in Condensed Consolidated Statements of Operations
2021		
Unrealized gains on securities available for sale		
	\$ 1,416	Net gains on securities available for sale
	297	Income tax expense
	<u>\$ 1,119</u>	Reclassifications, net of tax
2020		
Unrealized gains on securities available for sale		
	\$ 253	Net gains on securities available for sale
	-	Net impairment loss recognized in earnings
	253	Total reclassifications before tax
	53	Income tax expense
	<u>\$ 200</u>	Reclassifications, net of tax
Unrealized losses on cash flow hedges		
	\$ 75	Interest expense
	16	Income tax expense
	<u>\$ 59</u>	Reclassification, net of tax
	<u>\$ 141</u>	Total reclassifications for the period, net of tax

15. Revenue from Contracts with Customers

We account for revenue in accordance with ASC Topic 606, Revenue from Contracts with Customers. We derive the majority of our revenue from financial instruments and their related contractual rights and obligations which for the most part are excluded from the scope of this topic. These sources of revenue that are excluded from the scope of this topic include interest income, net gains on mortgage loans, net gains on securities available for sale, mortgage loan servicing, net and bank owned life insurance and were approximately 88.4% and 85.1% of total revenues for the three month periods ending March 31, 2021 and 2020, respectively.

Material sources of revenue that are included in the scope of this topic include service charges on deposit accounts, other deposit related income, interchange income and investment and insurance commissions and are discussed in the following paragraphs. Generally these sources of revenue are earned at the time the service is delivered or over the course of a monthly period and do not result in any contract asset or liability balance at any given period end. As a result, there were no contract assets or liabilities recorded as of March 31, 2021 and December 31, 2020.

Service charges on deposit accounts and other deposit related income: Revenues are earned on depository accounts for commercial and retail customers and include fees for transaction-based, account maintenance and overdraft services. Transaction-based fees, which includes services such as ATM use fees, stop payment charges and ACH fees are recognized at the time the transaction is executed as that is the time we fulfill our customer's request. Account maintenance fees, which includes monthly maintenance services are earned over the course of a month representing the period over which the performance obligation is satisfied. Our obligation for overdraft services is satisfied at the time of the overdraft.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

Interchange income: Interchange income primarily includes debit card interchange and network revenues. Debit card interchange and network revenues are earned on debit card transactions conducted through payment networks such as MasterCard, NYCE and Accel. Interchange income is recognized concurrently with the delivery of services on a daily basis. Interchange and network revenues are presented gross of interchange expenses, which are presented separately as a component of non-interest expense.

Investment and insurance commissions: Investment and insurance commissions include fees and commissions from asset management, custody, recordkeeping, investment advisory and other services provided to our customers. Revenue is recognized on an accrual basis at the time the services are performed and is generally based on either the market value of the assets managed or the services provided. We have an agent relationship with a third party provider of these services and net certain direct costs charged by the third party provider associated with providing these services to our customers.

Net (gains) losses on other real estate and repossessed assets: We record a gain or loss from the sale of other real estate when control of the property transfers to the buyer, which generally occurs at the time of an executed deed. If we were to finance the sale of other real estate to the buyer, we would assess whether the buyer is committed to perform their obligations under the contract and whether collectability of the transaction is probable. Once these criteria are met, the other real estate asset would be derecognized and the gain or loss on sale would be recorded upon the transfer of control of the property to the buyer. There were no other real estate properties sold during the three month periods ending March 31, 2021 and 2020 that were financed by us.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

Disaggregation of our revenue sources by attribute follows:

Three months ending March 31, 2021

	<u>Service Charges on Deposit Accounts</u>	<u>Other Deposit Related Income</u>	<u>Interchange Income</u>	<u>Investment and Insurance Commissions</u>	<u>Total</u>
	(In thousands)				
Retail					
Overdraft fees	\$ 1,212	\$ -	\$ -	\$ -	\$ 1,212
Account service charges	512	-	-	-	512
ATM fees	-	268	-	-	268
Other	-	198	-	-	198
Business					
Overdraft fees	192	-	-	-	192
ATM fees	-	6	-	-	6
Other	-	89	-	-	89
Interchange income	-	-	3,049	-	3,049
Asset management revenue	-	-	-	383	383
Transaction based revenue	-	-	-	201	201
Total	<u>\$ 1,916</u>	<u>\$ 561</u>	<u>\$ 3,049</u>	<u>\$ 584</u>	<u>\$ 6,110</u>

Reconciliation to Condensed Consolidated Statement of Operations:

Non-interest income - other:	
Other deposit related income	\$ 561
Investment and insurance commissions	584
Bank owned life insurance	139
Other	746
Total	<u>\$ 2,030</u>

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

Three months ending March 31, 2020

	Service Charges on Deposit Accounts	Other Deposit Related Income	Interchange Income	Investment and Insurance Commissions	Total
	(In thousands)				
Retail					
Overdraft fees	\$ 1,740	\$ -	\$ -	\$ -	\$ 1,740
Account service charges	506	-	-	-	506
ATM fees	-	300	-	-	300
Other	-	236	-	-	236
Business					
Overdraft fees	345	-	-	-	345
ATM fees	-	7	-	-	7
Other	-	90	-	-	90
Interchange income	-	-	2,457	-	2,457
Asset management revenue	-	-	-	313	313
Transaction based revenue	-	-	-	200	200
Total	\$ 2,591	\$ 633	\$ 2,457	\$ 513	\$ 6,194

Reconciliation to Condensed Consolidated Statement of Operations:

Non-interest income - other:					
Other deposit related income					\$ 633
Investment and insurance commissions					513
Bank owned life insurance					270
Other					747
Total					\$ 2,163

16. Leases

We have entered into leases in the normal course of business primarily for office facilities, some of which include renewal options and escalation clauses. Certain leases also include both lease components (fixed payments including rent, taxes and insurance costs) and non-lease components (common area or other maintenance costs) which are accounted for as a single lease component as we have elected the practical expedient to group lease and non-lease components together for all leases. We have also elected not to recognize leases with original lease terms of 12 months or less (short-term leases) on our Condensed Consolidated Statements of Financial Condition. Most of our leases include one or more options to renew. The exercise of lease renewal options is typically at our sole discretion and are included in our right of use ("ROU") assets and lease liabilities if they are reasonably certain of exercise.

Leases are classified as operating or finance leases at the lease commencement date (we did not have any finance leases as of March 31, 2021). Lease expense for operating leases and short-term leases is recognized on a straight-line basis over the lease term. The ROU assets represent our right to use an underlying asset for the lease term and lease liabilities represent our obligation to make lease payments arising from the lease. ROU assets and lease liabilities are recognized at the lease commencement date based on the estimated present value of the lease payment over the lease term.

As most of our leases do not provide an implicit rate, we use our incremental borrowing rate based on the information available at the lease commencement date in determining the present value of the lease payments.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

The cost components of our operating leases follows:

	Three Months Ended March 31,	
	2021	2020
	(In thousands)	
Operating lease cost	\$ 423	\$ 486
Variable lease cost	16	15
Short-term lease cost	14	7
Total	<u>\$ 453</u>	<u>\$ 508</u>

Variable lease costs consist primarily of taxes, insurance, and common area or other maintenance costs for our leased facilities.

Supplemental balance sheet information related to our operating leases follows:

	March 31, 2021	December 31, 2020
		(Dollars in thousands)
Lease right of use asset (1)	<u>\$ 7,268</u>	<u>\$ 7,646</u>
Lease liabilities (2)	<u>\$ 7,478</u>	<u>\$ 7,868</u>
Weighted average remaining lease term (years)	<u>7.00</u>	<u>7.12</u>
Weighted average discount rate	<u>2.4%</u>	<u>2.4%</u>

(1) Included in Accrued income and other assets in our Condensed Consolidated Statements of Financial Condition.

(2) Included in Accrued expenses and other liabilities in our Condensed Consolidated Statements of Financial Condition.

Maturity analysis of our lease liabilities at March 31, 2021 based on required contractual payments follows:

	(In thousands)
Nine months ending December 31, 2021	\$ 1,230
2022	1,489
2023	1,222
2024	815
2025	809
2026 and thereafter	2,529
Total lease payments	<u>8,094</u>
Less imputed interest	(616)
Total	<u>\$ 7,478</u>

ITEM 2.

**MANAGEMENT'S DISCUSSION AND ANALYSIS
OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

Introduction. The following section presents additional information to assess the financial condition and results of operations of Independent Bank Corporation ("IBCP"), its wholly-owned bank, Independent Bank (the "Bank"), and their subsidiaries. This section should be read in conjunction with the Condensed Consolidated Financial Statements. We also encourage you to read our 2020 Annual Report on Form 10-K filed with the U.S. Securities and Exchange Commission ("SEC"). That report includes a list of risk factors that you should consider in connection with any decision to buy or sell our securities.

Overview. We provide banking services to customers located primarily in Michigan's Lower Peninsula. We also have two loan production offices in Ohio (Columbus and Fairlawn). As a result, our success depends to a great extent upon the economic conditions in Michigan's Lower Peninsula.

Recent Developments. On March 11, 2020, the World Health Organization declared COVID-19, the disease caused by the novel coronavirus, a pandemic as a result of the global spread of the coronavirus illness. In response to the outbreak, federal and state authorities in the U.S. introduced various measures to try to limit or slow the spread of the virus, including travel restrictions, nonessential business closures, stay-at-home orders, and strict social distancing. As a result of the pandemic and related government measures, Michigan has experienced an increase in unemployment. On December 11, 2020, the U.S. Food and Drug Administration (FDA) issued its first emergency use authorization for a COVID-19 vaccine. Since that time, the FDA has issued other emergency use authorizations for additional vaccines, and the United States has seen a rapid increase in the number of individuals receiving vaccinations. The U.S. Centers for Disease Control and Prevention (CDC) states that widespread vaccinations may lead to greater immunity, which ultimately is expected to result in slowing the spread of the virus.

The COVID-19 pandemic, and the related government restrictions and guidance have had and continue to have a significant effect on us, our customers and the markets we serve. Our business, results of operations and financial condition may be adversely affected by a number of factors that could impact us and our customers, including but not limited to:

- restrictions on activity and high levels of unemployment may cause increases in loan delinquencies, foreclosures and defaults;
- increases in allowance for credit losses ("ACL") may be necessary;
- declines in collateral values may occur;
- third party disruptions, including outages at network providers, on-line banking vendors and other suppliers;
- increased cyber and payment fraud risk, as cybercriminals attempt to profit from the disruption, given increased online and remote activity;
- operational failures due to changes in our normal business practices necessitated by the pandemic and related governmental actions; and/or
- key personnel or significant numbers of our employees being unable to work effectively, including because of illness or restrictions in connection with COVID-19.

These factors may continue for a significant period of time. The spread of COVID-19 has caused us to modify many of our business practices. Currently, approximately 38% of our total employees are working remotely. We have also expanded sick and vacation time for certain employees. We may take further actions as may be required or as we determine to be prudent. There is no certainty that such measures will be sufficient to mitigate the risks posed by COVID-19. Similarly, while we hope vaccinations will lessen the impact of the virus on our business, there is still a significant degree of uncertainty with respect to the potential impact of widespread vaccinations.

The extent to which the COVID-19 pandemic will impact our business, results of operations and financial condition will depend on future developments, which are highly uncertain and difficult to predict. Those developments and factors include the duration and spread of the pandemic, its severity, the actions to contain the pandemic or address its impact, and how quickly and to what extent normal economic and operating conditions can resume. We do not yet know the full extent of the impact. However, the effects could have a material adverse impact on our business, financial condition and results of operations. Material adverse impacts may include valuation impairments on our intangible assets, securities available for sale, loans, capitalized mortgage loan servicing rights and deferred tax assets.

It is against this backdrop that we discuss our results of operations and financial condition in 2021 as compared to earlier periods.

RESULTS OF OPERATIONS

Summary. We recorded net income of \$22.0 million and \$4.8 million during the three months ended March 31, 2021 and 2020, respectively. The increase in 2021 first quarter results as compared to 2020 primarily reflects increases in net interest income, non-interest income and a decrease in provision for credit losses that were partially offset by increases in non-interest expense and income tax expense.

Key performance ratios

	Three months ended March 31,	
	<u>2021</u>	<u>2020</u>
Net income (annualized) to		
Average assets	2.10%	0.54%
Average shareholders' equity	23.51%	5.54%
Net income per common share		
Basic	\$ 1.01	\$ 0.22
Diluted	1.00	0.21

Net interest income. Net interest income is the most important source of our earnings and thus is critical in evaluating our results of operations. Changes in our net interest income are primarily influenced by our level of interest-earning assets and the income or yield that we earn on those assets and the manner and cost of funding our interest-earning assets. Certain macro-economic factors can also influence our net interest income such as the level and direction of interest rates, the difference between short-term and long-term interest rates (the steepness of the yield curve) and the general strength of the economies in which we are doing business. Finally, risk management plays an important role in our level of net interest income. The ineffective management of credit risk or interest-rate risk, in particular, can adversely impact our net interest income.

Our net interest income totaled \$30.3 million during the first quarter of 2021, an increase of \$0.1 million, or 0.3% from the year-ago period. This increase primarily reflects a \$697.0 million increase in average interest-earning assets that was partially offset by a 58 basis point decrease in our tax equivalent net interest income as a percent of average interest-earning assets (the “net interest margin”).

The significant increases in average interest-earning assets for the three month period ended March 31, 2021 versus the comparable year period is primarily due to the deployment of funds from a substantial increase in deposits.

Interest and fees on loans include \$2.1 million for the first quarter of 2021, of accretion of net loan fees on PPP loans. No such accretion is included in the comparable prior year periods. Interest and fees on loans also include \$0.4 million and \$0.3 million for the first quarter of 2021 and 2020, respectively, of accretion of the discount recorded on loans acquired in the April 2018 acquisition of Traverse City State Bank (“TCSB”).

Our net interest income is also impacted by our level of non-accrual loans. In the first quarter of 2021, non-accrual loans averaged \$7.6 million compared to \$11.1 million in the first quarter of 2020. In addition, in the first quarter of 2021, we had net recoveries of \$0.17 million of unpaid interest on loans placed on or taken off non-accrual or on loans previously charged-off compared to net recoveries of \$0.16 million during the same period in 2020.

Average Balances and Tax Equivalent Rates

	Three Months Ended March 31,					
	2021			2020		
	Average Balance	Interest	Rate ⁽²⁾	Average Balance	Interest	Rate ⁽²⁾
(Dollars in thousands)						
Assets						
Taxable loans	\$ 2,827,335	\$ 28,039	4.00%	\$ 2,758,909	\$ 31,688	4.61%
Tax-exempt loans ⁽¹⁾	6,677	84	5.10	7,861	97	4.96
Taxable securities	782,471	2,796	1.43	468,095	3,059	2.61
Tax-exempt securities ⁽¹⁾	311,147	1,770	2.28	59,300	490	3.31
Interest bearing cash	101,895	29	0.12	38,424	128	1.34
Other investments	18,427	188	4.14	18,359	238	5.21
Interest Earning Assets	<u>4,047,952</u>	<u>32,906</u>	3.27	<u>3,350,948</u>	<u>35,700</u>	4.28
Cash and due from banks	56,371			49,610		
Other assets, net	149,971			165,271		
Total Assets	<u>\$ 4,254,294</u>			<u>\$ 3,565,829</u>		
Liabilities						
Savings and interest bearing checking	\$ 2,140,405	675	0.13	\$ 1,615,589	1,930	0.48
Time deposits	339,872	581	0.69	594,871	2,770	1.87
Other borrowings	108,825	962	3.59	99,535	688	2.78
Interest Bearing Liabilities	<u>2,589,102</u>	<u>2,218</u>	0.35	<u>2,309,995</u>	<u>5,388</u>	0.94
Non-interest bearing deposits	1,218,534			855,838		
Other liabilities	66,547			51,033		
Shareholders' equity	380,111			348,963		
Total liabilities and shareholders' equity	<u>\$ 4,254,294</u>			<u>\$ 3,565,829</u>		
Net Interest Income		<u>\$ 30,688</u>			<u>\$ 30,312</u>	
Net Interest Income as a Percent of Average Interest Earning Assets			<u>3.05%</u>			<u>3.63%</u>

(1) Interest on tax-exempt loans and securities is presented on a fully tax equivalent basis assuming a marginal tax rate of 21%.

(2) Annualized

Reconciliation of Non-GAAP Financial Measures

	Three Months Ended March 31,	
	2021	2020
	(Dollars in thousands)	
Net Interest Margin, Fully Taxable Equivalent ("FTE")		
Net interest income	\$ 30,284	\$ 30,191
Add: taxable equivalent adjustment	404	121
Net interest income - taxable equivalent	<u>\$ 30,688</u>	<u>\$ 30,312</u>
Net interest margin (GAAP) ⁽¹⁾	<u>3.01%</u>	<u>3.61%</u>
Net interest margin (FTE) ⁽¹⁾	<u>3.05%</u>	<u>3.63%</u>

Provision for credit losses. We adopted Financial Accounting Standards Board Accounting Standards Update 2016-13, Financial Instruments — Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments ("CECL") on January 1, 2021. The primary drivers of the decrease in provision for credit losses were a decrease in balances of loans at risk, a decrease in commercial watch credits and an improvement in the employment forecast that decreased the retail pooled reserve. See note #2 to the Condensed Consolidated Financial Statements included within this report for our discussion on CECL implementation.

The provision for credit losses was a credit of \$0.5 million during the first quarter of 2021 compared to an expense of \$6.7 million for three months ended March 31, 2020. The provision reflects our assessment of the ACL taking into consideration factors such as loan growth, loan mix, levels of non-performing and classified loans and loan net charge-offs. While we use relevant information to recognize losses on loans, additional provisions for related losses may be necessary based on changes in economic conditions, customer circumstances and other credit risk factors. In particular, the credit impact of the COVID-19 pandemic, and more specifically the periodic closing of various segments of the economy in order to contain it, may have a negative impact on our level of non-performing loans and assets in the future, but as of yet, the magnitude of that impact is undeterminable. See "Portfolio Loans and asset quality" for a discussion of the various components of the ACL and their impact on the provision for credit losses in the first quarter of 2021.

Non-interest income. Non-interest income is a significant element in assessing our results of operations. Non-interest income totaled \$26.4 million during the first quarter of 2021 compared to \$11.0 million in 2020. Net gains on mortgage loan sales, as well as the change in mortgage loan servicing, net, were the key contributors to this increase.

The components of non-interest income are as follows:

Non-Interest Income

	Three months ended March 31,	
	2021	2020
	(In thousands)	
Interchange income	\$ 3,049	\$ 2,457
Service charges on deposit accounts	1,916	2,591
Net gains on assets		
Mortgage loans	12,828	8,840
Securities available for sale	1,416	253
Mortgage loan servicing, net	5,167	(5,300)
Investment and insurance commissions	583	513
Bank owned life insurance	139	270
Other	1,308	1,380
Total non-interest income	<u>\$ 26,406</u>	<u>\$ 11,004</u>

Interchange income increased \$0.6 million on a comparative quarterly basis in 2021 as compared to 2020 due to an increase in transaction volume.

Service charges on deposit accounts decreased on a comparative quarterly basis in 2021 as compared to 2020. These decreases were principally due to a decrease in non-sufficient funds occurrences (and related fees) caused in part by the COVID-19 pandemic and reduced checking account activity.

Net gains on mortgage loans increased substantially in the first quarter of 2021 compared to the first quarter of 2020. Mortgage loan activity is summarized as follows:

Mortgage Loan Activity

	Three months ended March 31,	
	2021	2020
	(Dollars in thousands)	
Mortgage loans originated	\$ 509,003	\$ 311,078
Mortgage loans sold	377,418	262,260
Net gains on mortgage loans	12,828	8,840
Net gains as a percent of mortgage loans sold ("Loan Sales Margin")	3.40%	3.37%
Fair value adjustments included in the Loan Sales Margin	(0.98)	0.78

The increase in mortgage loans originated is due primarily to lower interest rates spurring higher mortgage loan refinance volumes. Mortgage loans sold increased due to a rise in mortgage loan refinance activity. This resulted in net gains on mortgage loans increasing in the first quarter of 2021 as compared to the first quarter of 2020.

The volume of loans sold is dependent upon our ability to originate mortgage loans as well as the demand for fixed-rate obligations and other loans that we choose to not put into portfolio because of our established interest-rate risk parameters. (See “Portfolio Loans and asset quality.”) Net gains on mortgage loans are also dependent upon economic and competitive factors as well as our ability to effectively manage exposure to changes in interest rates and thus can often be a volatile part of our overall revenues.

Our Loan Sales Margin is impacted by several factors including competition and the manner in which the loan is sold. Net gains on mortgage loans are also impacted by recording fair value accounting adjustments. Excluding these fair value accounting adjustments, the Loan Sales Margin would have been 4.38% and 2.59% in the first quarters of 2021 and 2020, respectively. The increase in the Loan Sales Margin (excluding fair value adjustments) in 2021 was generally due to a substantial widening of primary-to-secondary market pricing spreads as mortgage loan volumes dramatically increased. Once mortgage loan volumes abate, we would expect our Loan Sales Margin to decline to more normal levels. The changes in the fair value accounting adjustments are primarily due to changes in the amount of commitments to originate mortgage loans for sale and changes in the loan sales margin.

Net gains on securities available for sale during the first quarter of 2021 totaled \$1.4 million compared to \$0.3 million during the first quarter of 2020. The significant increase during the first quarter of 2021 is primarily due to the divestiture of certain mortgage back securities. We recorded no net impairment losses in either 2021 or 2020 on securities available for sale. See “Securities” below and note #3 to the Condensed Consolidated Financial Statements.

Mortgage loan servicing, net, generated a gain of \$5.2 million and a loss \$5.3 million in the first quarters of 2021 and 2020, respectively. The significant variances in mortgage loan servicing, net are primarily due to changes in the fair value of capitalized mortgage loan servicing rights associated with changes in mortgage loan interest rates and expected future prepayment levels.

This activity is summarized in the following table:

Mortgage Servicing Revenue

	Three months ended March 31,	
	2021	2020
Mortgage loan servicing	(In thousands)	
Revenue, net	\$ 1,910	\$ 1,673
Fair value change due to price	4,640	(5,931)
Fair value change due to pay-downs	(1,383)	(1,042)
Total	<u>\$ 5,167</u>	<u>\$ (5,300)</u>

The significant variance in the fair value change due to price relates primarily to the increase in mortgage loan interest rates in the first quarter of 2021. That increase decreased projected prepayment rates for mortgage loans serviced for others, leading to an increase in fair value.

Activity related to capitalized mortgage loan servicing rights is as follows:

Capitalized Mortgage Loan Servicing Rights

	Three months ended March 31,	
	2021	2020
	(In thousands)	
Balance at beginning of period	\$ 16,904	\$ 19,171
Originated servicing rights capitalized	3,369	2,632
Change in fair value	3,257	(6,974)
Balance at end of period	<u>\$ 23,530</u>	<u>\$ 14,829</u>

At March 31, 2021 we were servicing approximately \$3.1 billion in mortgage loans for others on which servicing rights have been capitalized. This servicing portfolio had a weighted average coupon rate of 3.64% and a weighted average service fee of approximately 25.7 basis points. Capitalized mortgage loan servicing rights at March 31, 2021 totaled \$23.5 million, representing approximately 77 basis points on the related amount of mortgage loans serviced for others.

Investment and insurance commissions represent revenues generated on the sale or management of investments and insurance for our customers. Total investment and insurance commissions totaled \$0.6 million and \$0.5 million in the first quarter of 2021 and 2020, respectively.

Income from bank owned life insurance (“BOLI”) was \$0.1 million in the first quarter of 2021 compared to \$0.3 million in the first quarter of 2020. Our BOLI separate account is primarily invested in agency mortgage-backed securities. The decrease in the first quarter 2021 is due to a 0.86% decrease in the crediting rate from the prior year. The crediting rate (on which the earnings are based) reflects the performance of the separate account. The total cash surrender value of our BOLI was \$55.3 million and \$55.2 million at March 31, 2021 and December 31, 2020, respectively.

Other non-interest income decreased on a comparative quarterly basis in 2021 as compared to 2020. Several categories of fees have been reduced in 2021 due to the impact of the COVID-19 pandemic on transaction volumes, including ATM fees. In addition, we have elected to suspend certain electronic banking fees because of the COVID-19 pandemic and the increased need for our customers to access these channels. Commercial loan swap fee income is also lower in 2021 as customers have not felt the need to execute such transactions given the low interest rate environment.

Non-interest expense. Non-interest expense is an important component of our results of operations. We strive to efficiently manage our cost structure.

Non-interest expense increased by \$1.3 million to \$30.0 million in the first quarter of 2021 compared to the first quarter of 2020.

The components of non-interest expense are as follows:

Non-Interest Expense

	Three months ended March 31,	
	2021	2020
	(In thousands)	
Compensation	\$ 10,121	\$ 10,703
Performance-based compensation	4,292	2,121
Payroll taxes and employee benefits	4,109	3,685
Compensation and employee benefits	18,522	16,509
Data processing	2,374	2,355
Occupancy, net	2,343	2,460
Furniture, fixtures and equipment	1,003	1,036
Interchange expense	948	859
Communications	881	803
Loan and collection	759	805
Legal and professional	499	393
Advertising	489	683
FDIC deposit insurance	330	370
Amortization of intangible assets	242	255
Conversion related expenses	218	56
Supplies	174	184
Correspondent bank service fees	100	99
Provision for loss reimbursement on sold loans	34	37
Costs (recoveries) related to unfunded lending commitments	(32)	119
Net (gains) losses on other real estate and repossessed assets	(180)	109
Other	1,317	1,587
Total non-interest expense	<u>\$ 30,021</u>	<u>\$ 28,719</u>

Compensation and employee benefits expenses, in total, increased \$2.0 million on a quarterly comparative basis.

Compensation expense decreased by \$0.6 million in the first quarter of 2021 compared to the first quarter of 2020. The comparative decreases in 2021 is primarily due to an increased level of compensation that was deferred as direct loan origination costs (due to higher loan origination volumes) that was partially offset by salary increases that were predominantly effective on January 1, 2021.

Performance-based compensation for the first quarter of 2021 increased by \$2.2 million versus the same period in 2020, due primarily to a higher accrual for anticipated incentive compensation based on our estimated full-year performance as compared to goals.

Payroll taxes and employee benefits increased by \$0.4 million in the first quarter of 2021, compared to the same period in 2020. The quarterly comparative increase is due primarily to higher payroll taxes and our employer 401(k) match reflecting higher overall compensation levels in 2021, excluding deferred direct loan origination costs.

Interchange expense primarily represents our third-party cost to process debit card transactions. This cost increased in the first quarter of 2021 compared to the first quarter of 2020 due principally to changes in transaction volume and transaction channel mix.

Legal and professional fees increased by approximately \$0.1 million in 2021 on a comparative quarterly basis, as compared to 2020. This increase is due primarily to an increase in professional fees, title search fees and bank examination fees (due to an increase in our asset size).

Advertising expense decreased by approximately \$0.2 million in 2021 on a comparative quarterly basis as compared to 2020. The 2021 comparative decrease is due primarily to a shift in advertising channels.

Conversion related expenses totaled \$0.2 million and \$0.1 million for the first quarter 2021 and 2020, respectively. We are in the process of converting our core data processing system to a new system hosted by a new vendor. The 2021 expenses represent costs incurred for assistance from our existing vendor and fees from consultants who are assisting us in this conversion. We currently expect that the conversion will be substantially complete by the end of the second quarter of 2021.

The provision for loss reimbursement on sold loans was an expense of \$0.03 million and \$0.04 million in the first quarter of 2021 and the first quarter of 2020, respectively. This provision represents our estimate of incurred losses related to mortgage loans that we have sold to investors (primarily Fannie Mae, Freddie Mac, Ginnie Mae and the Federal Home Loan Bank of Indianapolis). The decrease in provision during the first quarter of 2021 as compared to the same period in 2020 is due primarily to lower loan defaults. Since we sell mortgage loans without recourse, loss reimbursements only occur in those instances where we have breached a representation or warranty or other contractual requirement related to the loan sale. The reserve for loss reimbursements on sold mortgage loans totaled \$1.05 million and \$1.02 million at March 31, 2021 and December 31, 2020, respectively. This reserve is included in accrued expenses and other liabilities in our Condensed Consolidated Statements of Financial Condition.

The changes in costs (recoveries) related to unfunded lending commitments are primarily impacted by changes in the amounts of such commitments to originate portfolio loans as well as (for commercial loan commitments) the grade (pursuant to our loan rating system) of such commitments.

Net (gains) losses on other real estate and repossessed assets primarily represent the gain or loss on the sale or additional write downs on these assets subsequent to the transfer of the asset from our loan portfolio. This transfer occurs at the time we acquire the collateral that secured the loan. At the time of acquisition, the other real estate or repossessed asset is valued at fair value, less estimated costs to sell, which becomes the new basis for the asset. Any write-downs at the time of acquisition are charged to the allowance for credit losses.

Other non-interest expenses decreased by \$0.3 million in the first quarter of 2021, compared to the same period in 2020. These decreases in 2020 are primarily due to a decline in travel and entertainment costs due to COVID-19 pandemic related travel restrictions as well as a reduction in deposit account and debit card related fraud costs.

Income tax expense. We recorded an income tax expense of \$5.1 million and \$1.0 million in the first quarters of 2021 and 2020, respectively.

Our actual income tax expense is different than the amount computed by applying our statutory income tax rate to our income before income tax primarily due to tax-exempt interest income, tax-exempt income from the increase in the cash surrender value on life insurance, and differences in the value of stock awards that vest and stock options that are exercised as compared to the initial fair values that were expensed.

We assess whether a valuation allowance should be established against our deferred tax assets based on the consideration of all available evidence using a “more likely than not” standard. The ultimate realization of this asset is primarily based on generating future income. We concluded at both March 31, 2021 and 2020 and at December 31, 2020 that the realization of substantially all of our deferred tax assets continues to be more likely than not.

FINANCIAL CONDITION

Summary. Our total assets increased by \$222.4 million during the first quarter of 2021. Loans, excluding loans held for sale, were \$2.78 billion at March 31, 2021, compared to \$2.73 billion at December 31, 2020. Growth in commercial loans of \$58.8 million and installment loans of \$7.7 million were partially offset by a decline in mortgage loans of \$15.9 million, due primarily to an increase in loan payoffs relative to new portfolio loan production. (See “Portfolio Loans and asset quality.”)

Deposits totaled \$3.86 billion at March 31, 2021, an increase of \$221.2 million from December 31, 2020. The increase in deposits is primarily due to growth in non-interest bearing deposits, savings and interest bearing checking deposits and reciprocal deposits that were partially offset by a decline in time and brokered time deposits.

The increase in commercial loans in the first quarter of 2021 is due primarily to loans extended under the Paycheck Protection Program (“PPP”) administered by the U.S. Small Business Administration (“SBA”). The increase in deposits is due in part to the significant liquidity that has been injected into the economy through government programs, such as the PPP, as well as by monetary actions by the Federal Reserve Bank, all in response to the COVID-19 pandemic.

It is unclear as to when these various government stimulus programs may end and when ended, what the impact will be on our levels of Portfolio Loans and deposits. However, our liquidity and funding contingency plans take into account the possibility of significant reductions in commercial loans and deposits during 2021.

Securities. We maintain diversified securities portfolios, which include obligations of U.S. government-sponsored agencies, securities issued by states and political subdivisions, residential and commercial mortgage-backed securities, asset-backed securities, corporate securities, trust preferred securities and foreign government securities (that are denominated in U.S. dollars). We regularly evaluate asset/liability management needs and attempt to maintain a portfolio structure that provides sufficient liquidity and cash flow. Except as discussed below, we believe that the unrealized losses on securities available for sale are temporary in nature and are expected to be recovered within a reasonable time period. We believe that we have the ability to hold securities with unrealized losses to maturity or until such time as the unrealized losses reverse. (See “Asset/liability management.”)

Securities

	Amortized Cost	Unrealized		Fair Value
		Gains	Losses	
Securities available for sale		(in thousands)		
March 31, 2021	\$ 1,234,450	\$ 16,935	\$ 4,105	\$ 1,247,280
December 31, 2020	1,052,132	21,431	1,404	1,072,159

Securities available for sale in unrealized loss positions are evaluated quarterly for impairment related to credit losses. For securities available for sale in an unrealized loss position, we first assess whether we intend to sell, or it is more likely than not that we will be required to sell the security before recovery of its amortized cost basis. If either of the criteria regarding intent or requirement to sell is met, the security's amortized cost basis is written down to fair value through income. For securities available for sale that do not meet this criteria, we evaluate whether the decline in fair value has resulted from credit losses or other factors. In making this assessment, we consider the extent to which fair value is less than amortized cost, adverse conditions specifically related to the security and the issuer and the impact of changes in market interest rates on the market value of the security, among other factors. If this assessment indicates that a credit loss exists, we compare the present value of cash flows expected to be collected from the security with the amortized cost basis of the security. If the present value of cash flows expected to be collected is less than the amortized cost basis for the security, a credit loss exists and an ACL is recorded, limited to the amount that the fair value of the security is less than its amortized cost basis. Any impairment that has not been recorded through an ACL is recognized in other comprehensive income, net of applicable taxes. No ACL for securities available for sale was needed at March 31, 2021.

Sales of securities were as follows (See "Non-interest income."):

Sales of Securities

	Three months ended March 31,	
	2021	2020
	(in thousands)	
Proceeds	\$ 78,179	\$ 21,743
Gross gains	1,464	253
Gross losses	48	-
Net impairment charges	-	-
Net gains	\$ 1,416	\$ 253

Portfolio Loans and asset quality. In addition to the communities served by our Bank branch and loan production office network, our principal lending markets also include nearby communities and metropolitan areas. Subject to established underwriting criteria, we also may participate in commercial lending transactions with certain non-affiliated banks and make whole loan purchases from other financial institutions.

The senior management and board of directors of our Bank retain authority and responsibility for credit decisions and we have adopted uniform underwriting standards. Our loan committee structure and the loan review process attempt to provide requisite controls and promote compliance with such established underwriting standards. However, there can be no assurance that our lending procedures and the use of uniform underwriting standards will prevent us from incurring significant credit losses in our lending activities.

We generally retain loans that may be profitably funded within established risk parameters. (See “Asset/liability management.”) As a result, we may hold adjustable-rate conventional and fixed rate jumbo mortgage loans as Portfolio Loans, while 15- and 30-year fixed-rate non-jumbo mortgage loans are generally sold to mitigate exposure to changes in interest rates. (See “Non-interest income.”) Due primarily to the expansion of our mortgage-banking activities and a change in mix in our mortgage loan originations, we are now originating and putting into Portfolio Loans more fixed rate mortgage loans as compared to past periods. These fixed rate mortgage loans generally have terms from 15 to 30 years, do not have prepayment penalties and expose us to more interest rate risk. To date, our interest rate risk profile has not changed significantly. However, we are carefully monitoring this change in the composition of our Portfolio Loans and the impact of potential future changes in interest rates on our changes in market value of portfolio equity and changes in net interest income. (See “Asset/liability management.”). As a result, we may add some longer-term borrowings, may utilize derivatives (interest rate swaps and interest rate caps) to manage interest rate risk and may continue to sell some fixed rate jumbo and other portfolio mortgage loans in the future.

The PPP, is a short-term, forgivable loan program primarily intended to help businesses impacted by COVID-19 to continue paying their employees. Also see Part II, Item 1A. Risk Factors below regarding the PPP.

A short summary of the PPP is as follows:

- Terms of two years (five years for loans originated after June 5, 2020) with payments automatically deferred to the date the SBA remits the borrower’s loan forgiveness amount to the lender (or, if the borrower does not apply for loan forgiveness, 10 months after the end of the borrower’s loan forgiveness covered period);
- One percent interest rate;
- No collateral or personal guarantees required;
- No fees paid by the borrower, rather lenders are paid a fee through the SBA according to a set schedule based on loan size;
- Loans are forgivable if at least 60% of the loan proceeds are used for payroll with the remainder being used for rent, mortgage interest and/or utilities; and
- Streamlined forgiveness application process for PPP loans of \$50,000 or less.

A summary of our participation in the PPP follows:

Paycheck Protection Program Volume

	March 31, 2021	
	Amount (#)	Amount
	(Dollars in thousands)	
Closed and outstanding	1,948	\$ 234,174
Forgiveness applications submitted to the SBA	1,477	183,346
Fees accreted into interest income during the quarter	n/a	2,072
Unaccreted fees remaining at quarter-end	n/a	6,816
Average loan yield for the quarter	n/a	4.98%

Congress and the major bank regulatory agencies have encouraged banks to work with their borrowers to provide short-term loan payment relief during the COVID-19 national emergency. On March 22, 2020, an interagency statement was released by the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, the Office of the Comptroller of the Currency, the Consumer Financial Protection Bureau, the State Banking Regulators and the National Credit Union Administration that contained their interpretation as to which modifications would qualify for these exceptions. In general, to qualify for this exception:

- The modified loan must be current when the modification is made;
- The modification must be short term in nature (up to six months), and;
- Modifications may include payment deferrals, fee waivers, extensions of repayment terms or other delays in payment that are insignificant.

In addition, Section 4013 of the CARES Act provides temporary relief from the accounting and reporting requirements for TDRs regarding certain loan modifications for our customers. Section 4013 specified that COVID-19 related modifications on loans that were current as of December 31, 2019 are not TDRs. The provisions of Section 4013 were extended to the earlier of 60 days after the termination of the national emergency that was previously declared on March 13, 2020 or January 21, 2022 by the Economic Aid to Hard-Hit Small Businesses, Nonprofits, and Venues Act which was signed into law on December 27, 2020.

In response to our customers' needs during this time of economic uncertainty, we have initiated forbearance programs for our retail (mortgage and installment loans) and our commercial customers. We also have similar programs for mortgage loans that we service for others. Commercial loan accommodations are typically a three month interest-only period while retail loan (mortgage and installment) forbearances have primarily been payment suspensions for three months. To date, there have not been a significant number of requests for additional modifications. See note #4 to the Condensed Consolidated Financial Statements included within this report.

A summary of accommodations as of March 31, 2021 follows:

Commercial and Retail Loan COVID-19 Accommodations

Loan Category	Covid-19 Accommodations		Total Loans	% of Total Loans
	Loans (#)	Loans (\$)		
	(Dollars in thousands)			
Commercial	-	\$ -	\$ 1,301,223	0.0%
Mortgage	111	15,263	999,982	1.5%
Installment	32	537	483,019	0.1%
Total	<u>143</u>	<u>\$ 15,800</u>	<u>\$ 2,784,224</u>	<u>0.6%</u>
Mortgage loans serviced for others(1)	<u>205</u>	<u>\$ 26,975</u>	<u>\$ 3,072,491</u>	<u>0.9%</u>

(1) We have delegated authority from all investors to grant these deferrals on their behalf.

A summary of our Portfolio Loans follows:

	March 31, 2021	December 31, 2020
	(In thousands)	
Real estate(1)		
Residential first mortgages	\$ 789,699	\$ 792,762
Residential home equity and other junior mortgages	126,691	138,128
Construction and land development	233,189	232,693
Other(2)	673,772	669,150
Consumer	476,371	468,090
Commercial	480,568	429,011
Agricultural	3,934	3,844
Total loans	<u>\$ 2,784,224</u>	<u>\$ 2,733,678</u>

(1) Includes both residential and non-residential commercial loans secured by real estate.

(2) Includes loans secured by multi-family residential and non-farm, non-residential property.

Non-performing assets ⁽¹⁾

	March 31, 2021	December 31, 2020
(Dollars in thousands)		
Non-accrual loans	\$ 7,548	\$ 8,312
Loans 90 days or more past due and still accruing interest	-	-
Subtotal	7,548	8,312
Less: Government guaranteed loans	459	439
Total non-performing loans	7,089	7,873
Other real estate and repossessed assets	346	766
Total non-performing assets	\$ 7,435	\$ 8,639
As a percent of Portfolio Loans		
Non-performing loans	0.25%	0.29%
Allowance for credit losses	1.68	1.30
Non-performing assets to total assets	0.17	0.21
Allowance for credit losses as a percent of non-performing loans	659.54	450.01

(1) Excludes loans classified as "troubled debt restructured" that are not past due.

Troubled debt restructurings ("TDR")

	March 31, 2021		
	Commercial	Retail ⁽¹⁾	Total
	(In thousands)		
Performing TDR's	\$ 5,032	\$ 34,679	\$ 39,711
Non-performing TDR's ⁽²⁾	1,105	1,459 ⁽³⁾	2,564
Total	\$ 6,137	\$ 36,138	\$ 42,275
	December 31, 2020		
	Commercial	Retail ⁽¹⁾	Total
	(In thousands)		
Performing TDR's	\$ 7,956	\$ 36,385	\$ 44,341
Non-performing TDR's ⁽²⁾	1,148	1,584 ⁽³⁾	2,732
Total	\$ 9,104	\$ 37,969	\$ 47,073

(1) Retail loans include mortgage and installment loan portfolio segments.

(2) Included in non-performing assets table above.

(3) Also includes loans on non-accrual at the time of modification until six payments are received on a timely basis.

Non-performing loans decreased by \$0.8 million since year-end 2020 due to a decrease in non-performing mortgage loans. Our collection and resolution efforts have generally resulted in a stable trend in non-performing loans. However, the credit impact of the COVID-19 pandemic, and more specifically the periodic, government-mandated closing of various segments of the economy in order to contain it, may have a negative impact on the level of non-performing loans and assets in the future, but as yet, the magnitude of that impact is undeterminable.

Non-performing loans exclude performing loans that are classified as TDRs. Performing TDRs totaled \$39.7 million, or 1.4% of total Portfolio Loans, and \$44.3 million, or 1.6% of total Portfolio Loans, at March 31, 2021 and December 31, 2020, respectively. The decrease in the amount of performing TDRs in the first quarter of 2021 reflects a decrease in both commercial and retail performing TDRs.

Other real estate and repossessed assets totaled \$0.3 million and \$0.8 million at March 31, 2021 and December 31, 2020, respectively.

We will place a loan that is 90 days or more past due on non-accrual, unless we believe the loan is both well secured and in the process of collection. Accordingly, we have determined that the collection of the accrued and unpaid interest on any loans that are 90 days or more past due and still accruing interest is probable.

The following tables reflect activity in our allowance for credit losses (“ACL”) on loans and ACL for unfunded lending commitments as well as the allocation of our ACL on loans.

Allowance for credit losses on loans and unfunded lending commitments

	Three months ended March 31,			
	2021		2020	
	Loans	Unfunded Commitments	Loans	Unfunded Commitments
	(Dollars in thousands)			
Balance at beginning of period	\$ 35,429	\$ 1,805	\$ 26,148	\$ 1,542
Additions (deductions)				
Impact of adoption of ASC 326	11,574	1,469	-	-
Provision for credit losses ⁽¹⁾	(474)	-	6,721	-
Initial allowance on loans purchased with credit deterioration	134	-	-	-
Recoveries credited to allowance	548	-	399	-
Loans charged against the allowance	(456)	-	(773)	-
Additions (recoveries) included in non-interest expense	-	(32)	-	119
Balance at end of period	<u>\$ 46,755</u>	<u>\$ 3,242</u>	<u>\$ 32,495</u>	<u>\$ 1,661</u>
Net loans charged (recovered) against the allowance to average Portfolio Loans	(0.01)%		0.06%	

(1) Beginning January 1, 2021, calculation is based on CECL methodology. Prior to January 1, 2021, calculation was based on the probable incurred loss methodology.

Allocation of the Allowance for Credit Losses (1)

	March 31, 2021	January 1, 2021
	(Dollars in thousands)	
Specific allocations	\$ 2,171	\$ 2,452
Pooled analysis allocations	29,786	30,796
Additional allocations based on subjective factors	14,798	13,889
Total	<u>\$ 46,755</u>	<u>\$ 47,137</u>

(1) January 1, 2021 includes impact of the adoption of CECL.

Beginning January 1, 2021, we calculated the ACL using the current expected credit losses methodology. As of January 1, 2021, we increased the ACL for loans by \$11.7 million and increased the ACL for unfunded loan commitments by \$1.5 million.

Some loans will not be repaid in full. Therefore, an ACL is maintained at a level which represents our best estimate of expected credit losses. Our ACL is comprised of three principal elements: (i) specific analysis of individual loans identified during the review of the loan portfolio, (ii) pooled analysis of loans with similar risk characteristics based on historical experience, adjusted for current conditions, R&S forecasts, and expected prepayments, and (iii) additional allowances based on subjective factors, including local and general economic business factors and trends, portfolio concentrations and changes in the size and/or the general terms of the loan portfolios. See note #4 to the Condensed Consolidated Financial Statements included within this report for further discussion on the ACL.

While we use relevant information to recognize losses on loans, additional provisions for related losses may be necessary based on changes in economic conditions, customer circumstances and other credit risk factors.

The ACL decreased \$0.4 million to \$46.8 million at March 31, 2021 from \$47.1 million at January 1, 2021 (CECL adoption date) and was equal to 1.68% of total Portfolio Loans at March 31, 2021.

Two of the three components of the ACL outlined above decreased during the first quarter of 2021. The ACL related to specific loans decreased \$0.3 million during the first quarter of 2021 due primarily to a \$3.3 million decrease in the amount of such loans. The ACL related to pooled analysis of loans decreased \$1.0 million due primarily to a \$9.1 million decrease in the balance of such loans. The ACL related to subjective factors increased \$0.9 million during the first quarter of 2021, due in part to the potential impact of the reported increase in COVID-19 cases in the State of Michigan.

Deposits and borrowings. Historically, the loyalty of our customer base has allowed us to price deposits competitively, contributing to a net interest margin that compares favorably to our peers. However, we still face a significant amount of competition for deposits within many of the markets served by our branch network, which limits our ability to materially increase deposits without adversely impacting the weighted-average cost of core deposits.

To attract new core deposits, we have implemented various account acquisition strategies as well as branch staff sales training. Account acquisition initiatives have historically generated increases in customer relationships. Over the past several years, we have also expanded our treasury management products and services for commercial businesses and municipalities or other governmental units and have also increased our sales calling efforts in order to attract additional deposit relationships from these sectors. We view long-term core deposit growth as an important objective. Core deposits generally provide a more stable and lower cost source of funds than alternative sources such as short-term borrowings. (See “Liquidity and capital resources.”)

Deposits totaled \$3.86 billion and \$3.64 billion at March 31, 2021 and December 31, 2020, respectively. The increase in deposits is primarily due to growth in non-interest bearing deposits, savings and interest bearing checking deposits and reciprocal deposits that were partially offset by a decline in time and brokered time deposits. Reciprocal deposits totaled \$608.7 million and \$556.2 million at March 31, 2021 and December 31, 2020, respectively. These deposits represent demand, money market and time deposits from our customers that have been placed through IntraFi Network. This service allows our customers to access multi-million dollar FDIC deposit insurance on deposit balances greater than the standard FDIC insurance maximum. The continued increase in reciprocal deposits is due in part to an automated sweep product that we introduced in mid-2018 as well as the marketing and sales efforts of our treasury management team.

We cannot be sure that we will be able to maintain our current level of core deposits. In particular, those deposits that are uninsured may be susceptible to outflow. At March 31, 2021, we had approximately \$850.9 million of uninsured deposits. A reduction in core deposits would likely increase our need to rely on wholesale funding sources.

We have also implemented strategies that incorporate using federal funds purchased, other borrowings and Brokered CDs to fund a portion of our interest-earning assets. The use of such alternate sources of funds supplements our core deposits and is also an integral part of our asset/liability management efforts.

Other borrowings, comprised primarily of advances from the FHLB, totaled \$30.0 million at both March 31, 2021 and December 31, 2020, respectively.

As described above, we utilize wholesale funding, including federal funds purchased, FHLB and FRB borrowings and Brokered CDs to augment our core deposits and fund a portion of our assets. At March 31, 2021, our use of such wholesale funding sources (including reciprocal deposits) amounted to approximately \$641.6 million, or 16.5% of total funding (deposits and all borrowings, excluding subordinated debt and debentures). Because wholesale funding sources are affected by general market conditions, the availability of such funding may be dependent on the confidence these sources have in our financial condition and operations. The continued availability to us of these funding sources is not certain, and Brokered CDs may be difficult for us to retain or replace at attractive rates as they mature. Our liquidity may be constrained if we are unable to renew our wholesale funding sources or if adequate financing is not available in the future at acceptable rates of interest or at all. Our financial performance could also be affected if we are unable to maintain our access to funding sources or if we are required to rely more heavily on more expensive funding sources. In such case, our net interest income and results of operations could be adversely affected.

We historically employed derivative financial instruments to manage our exposure to changes in interest rates. During the first quarter of 2021 and 2020, we entered into \$7.6 million and \$21.2 million (aggregate notional amounts), respectively, of interest rate swaps with commercial loan customers, which were offset with interest rate swaps that the Bank entered into with a broker-dealer. We recorded \$0.09 million and \$0.17 million of fee income related to these transactions during the first quarter of 2021 and 2020, respectively. See note #6 to the Condensed Consolidated Financial Statements included within this report for more information on our derivative financial instruments.

Liquidity and capital resources. Liquidity risk is the risk of being unable to timely meet obligations as they come due at a reasonable funding cost or without incurring unacceptable losses. Our liquidity management involves the measurement and monitoring of a variety of sources and uses of funds. Our Condensed Consolidated Statements of Cash Flows categorize these sources and uses into operating, investing and financing activities. We primarily focus our liquidity management on maintaining adequate levels of liquid assets (primarily funds on deposit with the FRB and certain securities available for sale) as well as developing access to a variety of borrowing sources to supplement our deposit gathering activities and provide funds for purchasing securities available for sale or originating Portfolio Loans as well as to be able to respond to unforeseen liquidity needs.

Our primary sources of funds include our deposit base, secured advances from the FHLB and FRB, federal funds purchased borrowing facilities with other banks, and access to the capital markets (for Brokered CDs).

At March 31, 2021, we had \$232.5 million of time deposits that mature in the next 12 months. Historically, a majority of these maturing time deposits are renewed by our customers. Additionally, \$3.54 billion of our deposits at March 31, 2021, were in account types from which the customer could withdraw the funds on demand. Changes in the balances of deposits that can be withdrawn upon demand are usually predictable and the total balances of these accounts have generally grown or have been stable over time as a result of our marketing and promotional activities. However, there can be no assurance that historical patterns of renewing time deposits or overall growth or stability in deposits will continue in the future.

We have developed contingency funding plans that stress test our liquidity needs that may arise from certain events such as an adverse change in our financial metrics (for example, credit quality or regulatory capital ratios). Our liquidity management also includes periodic monitoring that measures quick assets (defined generally as highly liquid or short-term assets) to total assets, short-term liability dependence and basic surplus (defined as quick assets less volatile liabilities to total assets). Policy limits have been established for our various liquidity measurements and are monitored on a quarterly basis. In addition, we also prepare cash flow forecasts that include a variety of different scenarios.

We believe that we currently have adequate liquidity at our Bank because of our cash and cash equivalents, our portfolio of securities available for sale, our access to secured advances from the FHLB and FRB and our ability to issue Brokered CDs.

We also believe that the available cash on hand at the parent company (including time deposits) of approximately \$49.7 million as of March 31, 2021 provides sufficient liquidity resources at the parent company to meet operating expenses, to make interest payments on the subordinated debt and debentures, and, along with dividends from the Bank, to pay projected cash dividends on our common stock.

Effective management of capital resources is critical to our mission to create value for our shareholders. In addition to common stock, our capital structure also currently includes subordinated debt and cumulative trust preferred securities.

Capitalization

	March 31, 2021	December 31, 2020
	(In thousands)	
Subordinated debt	\$ 39,300	\$ 39,281
Subordinated debentures	39,541	39,524
Amount not qualifying as regulatory capital	(524)	(505)
Amount qualifying as regulatory capital	78,317	78,300
Shareholders' equity		
Common stock	335,704	339,353
Retained earnings	47,287	40,145
Accumulated other comprehensive income	4,338	10,024
Total shareholders' equity	387,329	389,522
Total capitalization	\$ 465,646	\$ 467,822

In May 2020, we issued \$40.0 million of fixed to floating subordinated notes with a ten year maturity and a five year call option. The initial coupon rate is 5.95% fixed for five years and then floats at the Secured Overnight Financing Rate ("SOFR") plus 5.825%. These notes are presented in the Condensed Consolidated Statement of Financial Condition under the caption "Subordinated debt" and the March 31, 2021 balance of \$39.3 million is net of remaining unamortized deferred issuance costs of approximately \$0.7 million that are being amortized through the maturity date into interest expense on other borrowings and subordinated debt and debentures in our Condensed Consolidated Statement of Operations.

We currently have four special purpose entities with \$39.5 million of outstanding cumulative trust preferred securities as of March 31, 2021. These special purpose entities issued common securities and provided cash to our parent company that in turn issued subordinated debentures to these special purpose entities equal to the trust preferred securities and common securities. The subordinated debentures represent the sole asset of the special purpose entities. The common securities and subordinated debentures are included in our Condensed Consolidated Statements of Financial Condition.

The FRB has issued rules regarding trust preferred securities as a component of the Tier 1 capital of bank holding companies. The aggregate amount of trust preferred securities (and certain other capital elements) are limited to 25 percent of Tier 1 capital elements, net of goodwill (net of any associated deferred tax liability). The amount of trust preferred securities and certain other elements in excess of the limit can be included in Tier 2 capital, subject to restrictions. At the parent company, all of these securities qualified as Tier 1 capital at March 31, 2021 and December 31, 2020.

Common shareholders' equity decreased to \$387.3 million at March 31, 2021, from \$389.5 million at December 31, 2020, due primarily to a \$10.3 million reduction in capital related to the adoption of CECL, a \$5.7 million decrease in our accumulated other comprehensive income, by share repurchases and cash dividend payments that were partially offset by net income. Our tangible common equity ("TCE") totaled \$355.0 million and \$356.9 million, respectively, at those same dates. Our ratio of TCE to tangible assets was 8.08% and 8.56% at March 31, 2021, and December 31, 2020, respectively. TCE and the ratio of TCE to tangible assets are non-GAAP measures. TCE represents total common equity less goodwill and other intangible assets.

In December 2020, our Board of Directors authorized a 2021 share repurchase plan. Under the terms of the 2021 share repurchase plan, we were authorized to buy back up to 1,100,000, or approximately 5% of our outstanding common stock. During the first three months of 2021, the Company repurchased 180,667 shares at a weighted average purchase price of \$19.93 per share.

We pay a quarterly cash dividend on our common stock. These dividends totaled \$0.21 per share and \$0.20 per share in the first quarters of 2021 and 2020, respectively. We generally favor a dividend payout ratio between 30% and 50% of net income.

As of March 31, 2021 and December 31, 2020, our Bank (and holding company) continued to meet the requirements to be considered “well-capitalized” under federal regulatory standards (also see note #10 to the Condensed Consolidated Financial Statements included within this report).

Asset/liability management. Interest-rate risk is created by differences in the cash flow characteristics of our assets and liabilities. Options embedded in certain financial instruments, including caps on adjustable-rate loans as well as borrowers’ rights to prepay fixed-rate loans, also create interest-rate risk.

Our asset/liability management efforts identify and evaluate opportunities to structure our assets and liabilities in a manner that is consistent with our mission to maintain profitable financial leverage within established risk parameters. We evaluate various opportunities and alternate asset/liability management strategies carefully and consider the likely impact on our risk profile as well as the anticipated contribution to earnings. The marginal cost of funds is a principal consideration in the implementation of our asset/liability management strategies, but such evaluations further consider interest-rate and liquidity risk as well as other pertinent factors. We have established parameters for interest-rate risk. We regularly monitor our interest-rate risk and report at least quarterly to our board of directors.

We employ simulation analyses to monitor our interest-rate risk profile and evaluate potential changes in our net interest income and market value of portfolio equity that result from changes in interest rates. The purpose of these simulations is to identify sources of interest-rate risk. The simulations do not anticipate any actions that we might initiate in response to changes in interest rates and, accordingly, the simulations do not provide a reliable forecast of anticipated results. The simulations are predicated on immediate, permanent and parallel shifts in interest rates and generally assume that current loan and deposit pricing relationships remain constant. The simulations further incorporate assumptions relating to changes in customer behavior, including changes in prepayment rates on certain assets and liabilities.

CHANGES IN MARKET VALUE OF PORTFOLIO EQUITY AND NET INTEREST INCOME

Change in Interest Rates	Market Value of Portfolio Equity(1)	Percent Change	Net Interest Income(2)	Percent Change
		(Dollars in thousands)		
March 31, 2021				
200 basis point rise	\$ 526,600	1.37%	\$ 134,700	4.66%
100 basis point rise	539,500	3.85	132,600	3.03
Base-rate scenario	519,500	-	128,700	-
100 basis point decline	460,200	(11.41)	122,800	(4.58)
December 31, 2020				
200 basis point rise	\$ 494,600	15.02%	\$ 125,200	4.16%
100 basis point rise	483,200	12.37	123,700	2.91
Base-rate scenario	430,000	-	120,200	-
100 basis point decline	395,500	(8.02)	114,900	(4.41)

- (1) Simulation analyses calculate the change in the net present value of our assets and liabilities, including debt and related financial derivative instruments, under parallel shifts in interest rates by discounting the estimated future cash flows using a market-based discount rate. Cash flow estimates incorporate anticipated changes in prepayment speeds and other embedded options.
- (2) Simulation analyses calculate the change in net interest income under immediate parallel shifts in interest rates over the next twelve months, based upon a static statement of financial condition, which includes debt and related financial derivative instruments, and do not consider loan fees.

Accounting standards update. See note #2 to the Condensed Consolidated Financial Statements included elsewhere in this report for details on recently issued accounting pronouncements and their impact on our financial statements.

Fair valuation of financial instruments. Financial Accounting Standards Board (“FASB”) Accounting Standards Codification (“ASC”) Topic 820 - “Fair Value Measurements and Disclosures” (“FASB ASC Topic 820”) defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date.

We utilize fair value measurements to record fair value adjustments to certain financial instruments and to determine fair value disclosures. FASB ASC Topic 820 differentiates between those assets and liabilities required to be carried at fair value at every reporting period (“recurring”) and those assets and liabilities that are only required to be adjusted to fair value under certain circumstances (“nonrecurring”). Securities available for sale, loans held for sale, carried at fair value, derivatives and capitalized mortgage loan servicing rights are financial instruments recorded at fair value on a recurring basis. Additionally, from time to time, we may be required to record at fair value other financial assets on a nonrecurring basis, such as loans held for investment and certain other assets. These nonrecurring fair value adjustments typically involve application of lower of cost or fair value accounting or write-downs of individual assets. See note #11 to the Condensed Consolidated Financial Statements included within this report for a complete discussion on our use of fair valuation of financial instruments and the related measurement techniques.

LITIGATION MATTERS

The aggregate amount we have accrued for losses we consider probable as a result of litigation matters is immaterial. However, because of the inherent uncertainty of outcomes from any litigation matter, we believe it is reasonably possible we may incur losses in addition to the amounts we have accrued. At this time, we estimate the maximum amount of additional losses that are reasonably possible is insignificant. However, because of a number of factors, including the fact that certain of these litigation matters are still in their early stages, this maximum amount may change in the future.

The litigation matters described in the preceding paragraph primarily include claims that have been brought against us for damages, but do not include litigation matters where we seek to collect amounts owed to us by third parties (such as litigation initiated to collect delinquent loans). These excluded, collection-related matters may involve claims or counterclaims by the opposing party or parties, but we have excluded such matters from the disclosure contained in the preceding paragraph in all cases where we believe the possibility of us paying damages to any opposing party is remote.

CRITICAL ACCOUNTING POLICIES

Our accounting and reporting policies are in accordance with accounting principles generally accepted in the United States of America and conform to general practices within the banking industry. Accounting and reporting policies for the ACL and capitalized mortgage loan servicing rights are deemed critical since they involve the use of estimates and require significant management judgments. Application of assumptions different than those that we have used could result in material changes in our consolidated financial position or results of operations. We adopted CECL on January 1, 2021 which changed the way we calculate our ACL. See notes #2 and #4 to the Condensed Consolidated Financial Statements included within this report for further discussion on CECL. There was no material change to our critical accounting policy on capitalized mortgage loan servicing rights as disclosed in our Annual Report on Form 10-K for the year ended December 31, 2020.

Item 3.

QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

See applicable disclosures set forth in “Management’s Discussion and Analysis of Financial Condition and Results of Operations” in Item 2 under the caption “Asset/liability management.”

Item 4.

CONTROLS AND PROCEDURES

(a) Evaluation of Disclosure Controls and Procedures.

With the participation of management, our chief executive officer and chief financial officer, after evaluating the effectiveness of our disclosure controls and procedures (as defined in Exchange Act Rules 13a – 15(e) and 15d – 15(e)) for the period ended March 31, 2021, have concluded that, as of such date, our disclosure controls and procedures were effective.

(b) Changes in Internal Controls.

During the quarter ended March 31, 2021, there were no changes in our internal control over financial reporting that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Item 1A. Risk Factors

In addition to the risk factors disclosed in the Company's Annual Report on Form 10-K for the year ended December 31, 2020, the following risk factors apply to the Company:

The ongoing COVID-19 pandemic and measures intended to prevent its spread could have a material adverse effect on our business, results of operations and financial condition, and such effects will depend on future developments, which are highly uncertain and are difficult to predict.

Global health concerns relating to the COVID-19 pandemic and related government actions have resulted in significant disruptions and increased economic uncertainty. Government restrictions and recommendations designed to contain the virus and limit its effects have substantially limited the activities of individuals and the operations of businesses in the markets we serve.

The Governor of Michigan issued her first "stay home, stay safe" executive order effective March 24, 2020. In general, that order and subsequent modifications required individuals in Michigan to stay at home or their place of residence, except for certain specified activities that were deemed necessary to sustain or protect life. That original executive order was amended several times and was later rescinded and replaced entirely by a series of "Safer at Home" executive orders, which generally extended certain social distancing restrictions, but lifted the requirement that individuals remain in their homes. The series of "Safer at Home" orders, along with all other executive orders relating to the pandemic issued by Michigan's Governor after April 30, 2020, were then deemed unconstitutional by the Michigan Supreme Court on October 2, 2020. Since then, the Michigan Department of Health and Human Services (MDHHS) has issued orders similar to the Governor's executive orders under authority granted to the MDHHS by the Michigan Public Health Code – a different statute than the law on which the Governor based her executive orders. Under the MDHHS' orders, social distancing restrictions remain in place; however, certain retail operations, restaurants and bars, and other businesses are permitted to conduct in-person operations, subject to capacity limitations and other workplace safety requirements. The degree to which businesses may resume operations varies based on the region of the state in which they are located. It is currently expected that various forms of state and local government restrictions similar to those described above will continue through the fourth quarter and perhaps beyond. As a result of these events, Michigan has experienced an increase in unemployment. On December 11, 2020, the U.S. Food and Drug Administration (FDA) issued its first emergency use authorization for a COVID-19 vaccine. Since that time, the FDA has issued other emergency use authorizations for additional vaccines, and the United States has seen a rapid increase in the number of individuals receiving vaccinations. The U.S. Centers for Disease Control and Prevention (CDC) states that widespread vaccinations may lead to greater immunity, which ultimately is expected to result in slowing the spread of the virus.

The COVID-19 pandemic and the related other government restrictions and guidance have had and continue to have a significant effect on us, our customers and the markets we serve. Our business, results of operations and financial condition may be adversely affected by a number of factors that could impact us and our customers, including but not limited to:

- restrictions on activity and high levels of unemployment may cause increases in loan delinquencies, foreclosures and defaults;
- increases in allowance for credit losses may be necessary;

- declines in collateral values may occur;
- third party disruptions, including outages at network providers, on-line banking vendors and other suppliers;
- increased cyber and payment fraud risk, as cybercriminals attempt to profit from the disruption, given increased online and remote activity;
- operational failures due to changes in our normal business practices necessitated by the pandemic and related governmental actions; and/or
- key personnel or significant numbers of our employees being unable to work effectively, including because of illness or restrictions in connection with COVID-19.

These factors may continue for a significant period of time.

The spread of COVID-19 has caused us to modify many of our business practices. Currently, approximately 38% of our total employees are working remotely. We have also expanded sick and vacation time for certain employees. We may take further actions as may be required or as we determine to be prudent. There is no certainty that such measures will be sufficient to mitigate the risks posed by COVID-19. Similarly, while we hope vaccinations will lessen the impact of the virus on our business, there is still a significant degree of uncertainty with respect to the potential impact of widespread vaccinations.

The extent to which the COVID-19 pandemic will impact our business, results of operations and financial condition will depend on future developments, which are highly uncertain and difficult to predict. Those developments and factors include the duration and spread of the pandemic, its severity, the actions to contain the pandemic or address its impact, and how quickly and to what extent normal economic and operating conditions can resume. We do not yet know the full extent of the impact. However, the effects could have a material adverse impact on our business, financial condition and results of operations. Material adverse impacts may include valuation impairments on our intangible assets, securities available for sale, loans, capitalized mortgage loan servicing rights and deferred tax assets.

As a participating lender in the U.S. Small Business Administration (“SBA”) Paycheck Protection Program (“PPP”), the Company and the Bank are subject to additional risks regarding the Bank’s processing of loans for the PPP and risks that the SBA may not fund some or all PPP loan guaranties.

On March 27, 2020, the Coronavirus Aid, Relief, and Economic Security Act (“CARES Act”), was signed into law which included a \$349 billion loan program administered through the SBA referred to as the PPP. Under the PPP, small businesses and other entities and individuals can apply for loans from existing SBA lenders and other approved regulated lenders that enroll in the program, subject to numerous limitations and eligibility criteria. PPP loans are eligible for forgiveness, subject to numerous limitations. The Bank is participating as a lender in the PPP. The PPP opened on April 3, 2020; however, because of the short timeframe between the passing of the CARES Act and the opening of the PPP, there is some ambiguity in the laws, rules and guidance regarding the operation of the PPP, which exposes us to potential risks relating to noncompliance with the PPP. Since then, the SBA and U.S. Department of Treasury have provided additional guidance and clarity on the PPP through the issuance of over 20 interim final rules implementing the PPP. On or about April 16, 2020, the SBA notified lenders that the \$349 billion earmarked for the PPP was exhausted. The PPP was then expanded by the Paycheck Protection Program and Health Care Enhancement Act in late April 2020, adding an additional \$310 billion in funding while the Paycheck Protection Program Flexibility Act made certain changes to the PPP by allowing for more time to spend the funds and making it easier to get a loan fully forgiven. The PPP initially closed on August 8, 2020 (“Round 1”). On December 27, 2020, the Economic Aid to Hard-Hit Small Businesses, Nonprofits, and Venues Act (“Economic Aid Act”) was signed into law which allocates an additional \$284 billion in funding for the PPP (“Round 2”). The Economic Aid Act reopens the PPP through March 31, 2021 with generally the same terms and conditions as originally enacted under the CARES Act while clarifying eligibility and ineligibility for certain entities and expanding the permitted uses of PPP funds. In addition, the Economic Aid Act simplifies the loan forgiveness process for PPP loans of \$150,000 or less. The Economic Aid Act also establishes second draw loans for entities that have already used the initial PPP funds, subject to numerous limitations and eligibility criteria. PPP Round 2 loans are eligible for forgiveness similar to Round 1 PPP loans, subject to limitations set forth in the Economic Aid Act.

As of March 31, 2021, we had 1,948 PPP loans outstanding with a total balance of \$234.2 million.

Since the initiation of the PPP, several larger banks have been subject to litigation regarding the protocols and procedures that they used in processing applications for the PPP. We may be exposed to the risk of similar litigation, from both customers and non-customers that approached us regarding PPP loans, regarding our policies and procedures used in processing applications for the PPP. If any such litigation is filed against the Company or the Bank and is not resolved in a manner favorable to us, it could result in financial liability or adversely affect our reputation. In addition, litigation can be costly, regardless of outcome. Any financial liability, litigation costs or reputational damage caused by PPP related litigation could have an adverse impact on our business, financial condition and results of operations.

We also have credit risk on PPP loans if a determination is made by the SBA that there is a deficiency in the manner in which the loan was originated, funded, or serviced by the Bank, such as an issue with the eligibility of a borrower to receive a PPP loan, which may or may not be related to the ambiguity in the laws, rules and guidance regarding the operation of the PPP. In the event of a loss resulting from a default on a PPP loan and a determination by the SBA that there was a deficiency in the manner in which the PPP loan was originated, funded, or serviced by us, the SBA may deny its liability under the guaranty, reduce the amount of the guaranty, or, if it has already paid under the guaranty, seek recovery of any loss related to the deficiency from us.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

The Company maintains a Deferred Compensation and Stock Purchase Plan for Non-Employee Directors (the "Plan") pursuant to which non-employee directors can elect to receive shares of the Company's common stock in lieu of fees otherwise payable to the director for his or her service as a director. A director can elect to receive shares on a current basis or to defer receipt of the shares, in which case the shares are issued to a trust to be held for the account of the director and then generally distributed to the director after his or her retirement from the Board. Pursuant to this Plan, during the first quarter of 2021, the Company issued 374 shares of common stock to non-employee directors on a current basis and 4,692 shares of common stock to the trust for distribution to directors on a deferred basis. These shares were issued on January 1, 2021 representing aggregate fees of \$0.09 million. The shares on a current basis were issued at a price of \$18.47 per share and the shares on a deferred basis were issued at a price of \$16.62 per share, representing 90% of the fair value of the shares on the credit date. The price per share was the consolidated closing bid price per share of the Company's common stock as of the date of issuance, as determined in accordance with NASDAQ Marketplace Rules. The Company issued the shares pursuant to an exemption from registration under Section 4(2) of the Securities Act of 1933 due to the fact that the issuance of the shares was made on a private basis pursuant to the Plan.

The following table shows certain information relating to repurchases of common stock for the three-months ended March 31, 2021:

Period	Total Number of Shares Purchased (1)	Average Price Paid Per Share	Total Number of Shares Purchased as Part of a Publicly Announced Plan	Remaining Number of Shares Authorized for Purchase Under the Plan
January 2021	25,865	\$ 19.88	-	1,100,000
February 2021	235,643	20.03	180,667	919,333
March 2021	1,579	21.52	-	919,333
Total	263,087	\$ 20.02	180,667	919,333

- (1) January, February and March include 25,865 shares, 80 and 1,579 shares, respectively, withheld from the shares that would otherwise have been issued to certain officers in order to satisfy tax withholding obligations resulting from the vesting of restricted stock as well as satisfy tax withholding obligations and stock option exercise price resulting from the exercise of stock options. February also includes 54,896 shares of our common stock purchased in the open market by the Independent Bank Corporation Employee Stock Ownership Trust as part of our employee stock ownership plan.

Item 6. Exhibits

(a) The following exhibits (listed by number corresponding to the Exhibit Table as Item 601 in Regulation S-K) are filed with this report:

- [31.1](#) Certificate of the Chief Executive Officer of Independent Bank Corporation pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. 1350).
- [31.2](#) Certificate of the Chief Financial Officer of Independent Bank Corporation pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. 1350).
- [32.1](#) Certificate of the Chief Executive Officer of Independent Bank Corporation pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. 1350).
- [32.2](#) Certificate of the Chief Financial Officer of Independent Bank Corporation pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. 1350).
- 101. INS Inline XBRL Instance Document (the instance document does not appear in the Interactive Data File because its XBRL tags are embedded within the Inline XBRL document)
- 101. SCH Inline XBRL Taxonomy Extension Schema Document
- 101. CAL Inline XBRL Taxonomy Extension Calculation Linkbase Document
- 101. DEF Inline XBRL Taxonomy Extension Definition Linkbase Document
- 101. LAB Inline XBRL Taxonomy Extension Label Linkbase Document
- 101. PRE Inline XBRL Taxonomy Extension Presentation Linkbase Document
- 104 Cover page interactive data file (formatted as inline XBRL and contained in Exhibit 101)

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.

Date May 6, 2021

By /s/ Gavin A. Mohr
Gavin A. Mohr, Principal Financial Officer

Date May 6, 2021

By /s/ James J. Twarozynski
James J. Twarozynski, Principal Accounting Officer

CERTIFICATION

I, William B. Kessel, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Independent Bank Corporation;
2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;
3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and we have:
 - a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;
 - b) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) disclosed in this quarterly report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting;
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls over financial reporting.

INDEPENDENT BANK CORPORATION

/s/ William B. Kessel

William B. Kessel

President and Chief Executive Officer

Date: May 6, 2021

CERTIFICATION

I, Gavin A. Mohr, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Independent Bank Corporation;
2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;
3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and we have:
 - a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;
 - b) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) disclosed in this quarterly report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting;
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls over financial reporting.

INDEPENDENT BANK CORPORATION

Date: May 6, 2021

/s/ Gavin A. Mohr
Gavin A. Mohr
Chief Financial Officer

CERTIFICATE OF THE
CHIEF EXECUTIVE OFFICER OF
INDEPENDENT BANK CORPORATION

Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. 1350):

I, William B. Kessel, President and Chief Executive Officer of Independent Bank Corporation, certify, to the best of my knowledge and belief, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. 1350) that:

(1) The quarterly report on Form 10-Q for the quarterly period ended March 31, 2021, which this statement accompanies, fully complies with requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and;

(2) The information contained in this quarterly report on Form 10-Q for the quarterly period ended March 31, 2021, fairly presents, in all material respects, the financial condition and results of operations of Independent Bank Corporation.

INDEPENDENT BANK CORPORATION

Date: May 6, 2021

/s/ William B. Kessel
William B. Kessel
President and Chief Executive Officer

The signed original of this written statement required by Section 906, or other document authenticating, acknowledging, or otherwise adopting the signature that appears in typed form within the electronic version of this written statement required by Section 906, has been provided to Independent Bank Corporation and will be retained by Independent Bank Corporation and furnished to the Securities and Exchange Commission or its staff upon request.

CERTIFICATE OF THE
CHIEF FINANCIAL OFFICER OF
INDEPENDENT BANK CORPORATION

Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. 1350):

I, Gavin A. Mohr, Chief Financial Officer of Independent Bank Corporation, certify, to the best of my knowledge and belief, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. 1350) that:

(1) The quarterly report on Form 10-Q for the quarterly period ended March 31, 2021, which this statement accompanies, fully complies with requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and;

(2) The information contained in this quarterly report on Form 10-Q for the quarterly period ended March 31, 2021, fairly presents, in all material respects, the financial condition and results of operations of Independent Bank Corporation.

INDEPENDENT BANK CORPORATION

Date: May 6, 2021

/s/ Gavin A. Mohr
Gavin A. Mohr
Chief Financial Officer

The signed original of this written statement required by Section 906, or other document authenticating, acknowledging, or otherwise adopting the signature that appears in typed form within the electronic version of this written statement required by Section 906, has been provided to Independent Bank Corporation and will be retained by Independent Bank Corporation and furnished to the Securities and Exchange Commission or its staff upon request.
