ACNB CORP
Form 10-Q
August 03, 2018

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, DC 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2018

Commission file number 1-35015

ACNB CORPORATION

(Exact name of Registrant as specified in its charter)

Pennsylvania (State or other jurisdiction of incorporation or organization)	**23-2233457** (I.R.S. Employer Identification No.)
16 Lincoln Square, Gettysburg, Pennsylvania (Address of principal executive offices)	**17325** (Zip Code)

Registrant s telephone number, including area code: **(717) 334-3161**

Title of each class	Name of each exchange on which registered
Common Stock, $2.50 par value per share	The NASDAQ Stock Market, LLC

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No o

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 x No o

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

Large accelerated filer o Accelerated filer x

Non-accelerated filer o (Do not check if a smaller reporting company)

Smaller reporting company o

Emerging growth company o

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. o

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

The number of shares of the Registrant s Common Stock outstanding on August 3, 2018, was 7,038,768.

PART I - FINANCIAL INFORMATION

ACNB CORPORATION

ITEM 1 - FINANCIAL STATEMENTS

CONSOLIDATED STATEMENTS OF CONDITION (UNAUDITED)

Dollars in thousands, except per share data		June 30, 2018		June 30, 2017		December 31, 2017
ASSETS						
Cash and due from banks	**$**	**18,403**	$	17,384	$	19,304
Interest bearing deposits with banks		**44,650**		8,896		15,137
Total Cash and Cash Equivalents		**63,053**		26,280		34,441
Equity securities with readily determinable fair values		**1,767**				
Debt securities available for sale		**152,424**		133,719		159,051
Securities held to maturity, fair value $39,145; $50,000; $44,549		**39,894**		50,088		44,829
Loans held for sale		**1,265**		1,278		1,736
Loans, net of allowance for loan losses $13,143; $14,148; $13,976		**1,233,655**		955,527		1,230,194
Premises and equipment		**26,379**		18,170		26,774
Restricted investment in bank stocks		**4,849**		4,899		4,773
Investment in bank-owned life insurance		**45,973**		41,273		44,935
Investments in low-income housing partnerships		**2,213**		2,690		2,446
Goodwill		**19,580**		6,308		19,580
Intangible assets		**2,801**		526		2,569
Foreclosed assets held for resale		**287**		63		436
Other assets		**29,202**		21,115		23,668
Total Assets	**$**	**1,623,342**	$	1,261,936	$	1,595,432
LIABILITIES AND STOCKHOLDERS EQUITY						
LIABILITIES						
Deposits:						
Non-interest bearing	**$**	**288,215**	$	190,572	$	279,413
Interest bearing		**1,045,760**		809,582		1,019,079
Total Deposits		**1,333,975**		1,000,154		1,298,492
Short-term borrowings		**26,418**		30,837		36,908
Long-term borrowings		**89,816**		95,850		94,600
Other liabilities		**12,826**		11,251		11,466
Total Liabilities		**1,463,035**		1,138,092		1,441,466
STOCKHOLDERS EQUITY						
Preferred stock, $2.50 par value; 20,000,000 shares authorized; no shares outstanding						
		17,753		15,349		17,716

Common stock, $2.50 par value; 20,000,000 shares authorized; 7,101,368, 6,139,499 and 7,086,258 shares issued; 7,038,768, 6,076,899 and 7,023,658 shares outstanding						
Treasury stock, at cost (62,600 shares)		**(728)**		(728)		(728)
Additional paid-in capital		**38,193**		11,287		37,777
Retained earnings		**113,772**		103,488		106,293
Accumulated other comprehensive loss		**(8,683)**		(5,552)		(7,092)
Total Stockholders Equity		**160,307**		123,844		153,966
Total Liabilities and Stockholders Equity	**$**	**1,623,342**	$	1,261,936	$	1,595,432

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

ACNB CORPORATION

CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED)

Dollars in thousands, except per share data	Three Months Ended June 30, 2018	Three Months Ended June 30, 2017	Six Months Ended June 30, 2018	Six Months Ended June 30, 2017
INTEREST AND DIVIDEND INCOME				
Loans, including fees	**$ 14,623**	$ 9,964	**$ 28,780**	$ 19,494
Securities:				
Taxable	**929**	784	**1,832**	1,584
Tax-exempt	**59**	117	**124**	267
Dividends	**74**	64	**152**	113
Other	**179**	33	**231**	37
Total Interest Income	**15,864**	10,962	**31,119**	21,495
INTEREST EXPENSE				
Deposits	**1,206**	687	**2,340**	1,322
Short-term borrowings	**11**	15	**27**	60
Long-term borrowings	**556**	429	**1,099**	816
Total Interest Expense	**1,773**	1,131	**3,466**	2,198
Net Interest Income	**14,091**	9,831	**27,653**	19,297
PROVISION FOR LOAN LOSSES	**320**		**570**	
Net Interest Income after Provision for Loan Losses	**13,771**	9,831	**27,083**	19,297
OTHER INCOME				
Service charges on deposit accounts	**810**	617	**1,626**	1,187
Income from fiduciary, investment management and brokerage activities	**559**	478	**1,130**	920
Earnings on investment in bank-owned life insurance	**281**	276	**538**	531
Gain on life insurance proceeds			**52**	
Net gains on sales of securities	**13**		**13**	
Net gains (losses) on equity securities	**6**		**(27)**	
Service charges on ATM and debit card transactions	**614**	381	**1,144**	739
Commissions from insurance sales	**1,707**	1,564	**2,908**	2,718
Other	**327**	212	**645**	515
Total Other Income	**4,317**	3,528	**8,029**	6,610
OTHER EXPENSES				
Salaries and employee benefits	**6,683**	5,934	**13,310**	11,682
Net occupancy	**720**	496	**1,499**	1,033
Equipment	**1,321**	844	**2,483**	1,627
Other tax	**235**	168	**441**	379
Professional services	**344**	344	**713**	583
Supplies and postage	**177**	168	**392**	337
Marketing and corporate relations	**165**	138	**268**	202
FDIC and regulatory	**164**	140	**348**	279
Merger related expenses		208		370
Intangible assets amortization	**182**	82	**366**	162
Foreclosed real estate expenses (income)	**84**	(14)	**132**	16

Other operating		**1,176**		1,126		**2,285**		1,964
Total Other Expenses		**11,251**		9,634		**22,237**		18,634
Income before Income Taxes		**6,837**		3,725		**12,875**		7,273
PROVISION FOR INCOME TAXES		**1,330**		1,003		**2,455**		1,914
Net Income	**$**	**5,507**	$	2,722	**$**	**10,420**	$	5,359
PER SHARE DATA								
Basic earnings	**$**	**0.78**	$	0.45	**$**	**1.48**	$	0.88
Cash dividends declared	**$**	**0.23**	$	0.20	**$**	**0.43**	$	0.40

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

ACNB CORPORATION

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (UNAUDITED)

Dollars in thousands	Three Months Ended June 30, 2018	Three Months Ended June 30, 2017	Six Months Ended June 30, 2018	Six Months Ended June 30, 2017
NET INCOME	**$ 5,507**	$ 2,722	**$ 10,420**	$ 5,359
OTHER COMPREHENSIVE (LOSS) INCOME				
SECURITIES				
Unrealized (losses) gains arising during the period, net of income taxes of $(228), $52, $(603) and $131, respectively	**(430)**	95	**(1,719)**	252
Reclassification adjustment for net gains included in net income, net of income taxes of $3, $0, $3 and $0, respectively (A) (C)	**10**		**10**	
PENSION				
Amortization of pension net loss, transition liability, and prior service cost, net of income taxes of $29, $59, $58 and $118, respectively (B) (C)	**100**	110	**200**	220
TOTAL OTHER COMPREHENSIVE (LOSS) INCOME	**(320)**	205	**(1,509)**	472
TOTAL COMPREHENSIVE INCOME	**$ 5,187**	$ 2,927	**$ 8,911**	$ 5,831

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

(A) Gross amounts are included in net gains on sales or calls of securities on the Consolidated Statements of Income in total other income.

(B) Gross amounts are included in the computation of net periodic benefit cost and are included in salaries and employee benefits on the Consolidated Statements of Income in total other expenses.

(C) Income tax amounts are included in the provision for income taxes on the Consolidated Statements of Income.

ACNB CORPORATION

CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS EQUITY (UNAUDITED)

Six Months Ended June 30, 2018 and 2017

Dollars in thousands	Common Stock	Treasury Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Total Stockholders Equity
BALANCE JANUARY 1, 2017	$ 15,317	$ (728)	$ 10,941	$ 100,555	$ (6,024)	$ 120,061
Net income				5,359		5,359
Other comprehensive income, net of taxes					472	472
Common stock shares issued (6,568 shares)	17		121			138
Restricted stock grants (6,193 shares)	15		105			120
Restricted stock compensation expense			120			120
Cash dividends declared				(2,426)		(2,426)
BALANCE JUNE 30, 2017	$ 15,349	$ (728)	$ 11,287	$ 103,488	$ (5,552)	$ 123,844
BALANCE JANUARY 1, 2018	**$ 17,716**	**$ (728)**	**$ 37,777**	**$ 106,293**	**$ (7,092)**	**$ 153,966**
Net income				**10,420**		**10,420**
Other comprehensive loss, net of taxes					**(1,509)**	**(1,509)**
Reclassification of certain income tax effects from AOCI (1)				**82**	**(82)**	
Common stock shares issued (8,366 shares)	**20**		**234**			**254**
Restricted stock grants (6,744 shares)	**17**		**(4)**			**13**
Restricted stock compensation expense			**186**			**186**
Cash dividends declared				**(3,023)**		**(3,023)**
BALANCE JUNE 30, 2018	**$ 17,753**	**$ (728)**	**$ 38,193**	**$ 113,772**	**$ (8,683)**	**$ 160,307**

(1) In January 2018, the Corporation adopted ASU 2018-02, as a result, the Corporation made a policy election to release income tax effects, as a result of the Tax Act, from AOCI to retained earnings.

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

ACNB CORPORATION

CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

Dollars in thousands	Six Months Ended June 30, 2018	2017
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	**$ 10,420**	$ 5,359
Adjustments to reconcile net income to net cash provided by operating activities:		
Gain on sales of loans originated for sale	**(272)**	(206)
Loss (gain) on sales of foreclosed assets held for resale, including writedowns	**45**	(36)
Earnings on investment in bank-owned life insurance	**(538)**	(531)
Gain on sales or calls of securities	**(13)**	
Loss on equity securities	**27**	
Restricted stock compensation expense	**186**	120
Depreciation and amortization	**1,418**	942
Provision for loan losses	**570**	
Net amortization of investment securities premiums	**238**	264
Increase in accrued interest receivable	**(698)**	(103)
Increase in accrued interest payable	**284**	103
Mortgage loans originated for sale	**(15,975)**	(12,102)
Proceeds from sales of loans originated for sale	**16,718**	12,800
Decrease (increase) in other assets	**440**	(943)
Decrease (increase) in deferred tax expense	**396**	(159)
Increase in other liabilities	**1,334**	1,688
Net Cash Provided by Operating Activities	**14,580**	7,196
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from maturities of investment securities held to maturity	**4,932**	5,438
Proceeds from maturities of investment securities available for sale	**7,418**	13,456
Proceeds from sales of investment securities available for sale	**1,446**	
Purchase of investment securities available for sale	**(11,459)**	(4,024)
Purchase of restricted investment in bank stocks	**(76)**	(550)
Net increase in loans	**(4,266)**	(61,811)
Purchase of bank-owned life insurance	**(500)**	
Insurance book- acquisition	**(600)**	
Capital expenditures	**(655)**	(803)
Proceeds from sales of premises and equipment		6
Proceeds from sales of foreclosed real estate	**339**	229
Net Cash Used in Investing Activities	**(3,421)**	(48,059)
CASH FLOWS FROM FINANCING ACTIVITIES		
Net increase in demand deposits	**8,802**	9,979
Net increase in time certificates of deposits and interest bearing deposits	**26,681**	22,554
Net decrease in short-term borrowings	**(10,490)**	(3,753)
Proceeds from long-term borrowings	**8,716**	24,600
Repayments on long-term borrowings	**(13,500)**	(3,000)
Dividends paid	**(3,023)**	(2,426)
Common stock issued	**267**	258
Net Cash Provided by Financing Activities	**17,453**	48,212
Net Increase in Cash and Cash Equivalents	**28,612**	7,349
CASH AND CASH EQUIVALENTS BEGINNING	**34,441**	18,931
CASH AND CASH EQUIVALENTS ENDING	**$ 63,053**	$ 26,280
Supplemental disclosures of cash flow information		
Interest paid	**$ 3,182**	$ 2,095
Income taxes paid	**$ 1,700**	$ 1,750
Loans transferred to foreclosed assets held for resale and other foreclosed transactions	**$ 235**	$

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

ACNB CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Basis of Presentation and Nature of Operations

ACNB Corporation (the Corporation or ACNB), headquartered in Gettysburg, Pennsylvania, provides banking, insurance, and financial services to businesses and consumers through its wholly-owned subsidiaries, ACNB Bank (Bank) and Russell Insurance Group, Inc. (RIG). The Bank engages in full-service commercial and consumer banking and wealth management services, including trust and retail brokerage, through twenty-two community banking office locations in Adams, Cumberland, Franklin and York Counties, Pennsylvania. There is also a loan production office situated in York County, Pennsylvania, as well as plans to establish, subject to regulatory requirements, another loan production office in Hunt Valley, Maryland.

On July 1, 2017, ACNB completed its acquisition of New Windsor Bancorp, Inc. (New Windsor) of Taneytown, Maryland. At the effective time of the acquisition, New Windsor merged with and into a wholly-owned subsidiary of ACNB, immediately followed by the merger of New Windsor State Bank (NWSB) with and into ACNB Bank. ACNB Bank now operates in the Maryland market as NWSB Bank, A Division of ACNB Bank and serves this marketplace with banking and wealth management services via a network of seven community banking offices located in Carroll County, Maryland.

RIG is a full-service insurance agency based in Westminster, Maryland, with a second location in Germantown, Maryland. The agency offers a broad range of property and casualty, life, and health insurance to both commercial and individual clients.

The Corporation s primary source of revenue is interest income on loans and investment securities and fee income on its products and services. Expenses consist of interest expense on deposits and borrowed funds, provisions for loan losses, and other operating expenses.

The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (US GAAP) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. In the opinion of management, the accompanying unaudited consolidated financial statements contain all adjustments necessary to present fairly ACNB Corporation s financial position and the results of operations, comprehensive income, changes in stockholders equity, and cash flows. All such adjustments are of a normal recurring nature.

The accounting policies followed by the Corporation are set forth in Note A to the Corporation s consolidated financial statements in the 2017 ACNB Corporation Annual Report on Form 10-K, filed with the SEC on March 9, 2018. It is suggested that the consolidated financial statements contained herein be read in conjunction with the consolidated financial statements and notes included in the Corporation s Annual Report on Form 10-K. The results of operations for the three and six month periods ended June 30, 2018, are not necessarily indicative of the results to be expected for the full year.

On January 1, 2018, the Corporation adopted ASU 2014-09, *Revenue from Contracts with Customers,* and all subsequent amendments to the ASU (collectively ASC 606), which (i) creates a single framework for recognizing revenue from contracts with customers that fall within its scope and (ii) revises when it is appropriate to recognize a gain (loss) from the transfer of nonfinancial assets, such as OREO. The majority of the Corporation s revenue comes from interest income, including loans and securities, that are outside the scope of ASC 606. The Corporation s services that fall within the scope of ASC 606 are presented within other income on the consolidated statement of income and are recognized as revenue as the Corporation satisfies its obligation to the customer. Services within the scope of ASC 606 include service charges on deposit accounts, service charges on ATM and debit card transactions, income from fiduciary, investment management and brokerage activities and commissions from insurance sales. ASC 606 did not result in a change to the accounting for any in-scope revenue streams; as such, no cumulative effect adjustment was recorded.

On January 1, 2018, the Corporation adopted ASU 2016-01, *Financial Instruments Overall (Topic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities,* which amended the guidance on the classification and measurement of financial instruments. Upon adoption of ASU 2016-01, the Corporation recognized the equity securities fair value change in net income. Previously, the fair value changes were recognized, net of tax, in other comprehensive income (loss). The adoption of this ASU did not have a material effect on the Corporation s consolidated financial condition or results of operations.

The Corporation early adopted ASU 2018-02, *Income Statement Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income.* The amendments in this ASU required a reclassification from accumulated other comprehensive income to retained earnings for tax effects resulting from the newly enacted federal corporate income tax rate. The amount of the reclassification would be the difference between the historical corporate income tax rate and the newly enacted 21% corporate income tax rate. The amendments in this ASU would be effective for the Corporation for fiscal years beginning after December 15, 2018, and interim periods within those fiscal years. The adoption of this ASU did not have a material effect on the Corporation s consolidated financial condition or results of operations.

The Corporation has evaluated events and transactions occurring subsequent to the balance sheet date of June 30, 2018, for items that should potentially be recognized or disclosed in the consolidated financial statements. The evaluation was conducted through the date these consolidated financial statements were issued.

2. Acquisition of New Windsor Bancorp, Inc.

On July 1, 2017, ACNB completed its acquisition of New Windsor Bancorp Inc. (New Windsor) of Taneytown, Maryland. New Windsor was a locally owned and managed institution with seven locations in north central Maryland that complemented, enhanced and expanded ACNB s physical presence in north central Maryland. ACNB transacted the acquisition to enhance its competitive strategic position, potential prospective business opportunities, operations, management, prospective financial condition, future earnings and business prospects. Specifically, ACNB believes that the acquisition will enhance its business opportunities in Northern Maryland due to the combined company having a greater market share, market presence and the ability to offer more diverse (i.e. Trust Services) and more profitable products, as well as a broader based and geographically diversified branch system to enhance deposit collection and potentially improve funding costs. The fair value of total assets acquired as a result of the acquisition totaled $319.8 million, loans totaled $263.5 million and deposits totaled $293.3 million. Goodwill recorded in the acquisition was $13.3 million. In accordance with the terms of the Reorganization Agreement, dated November 21, 2016, as amended, New Windsor shareholders received, in aggregate, $4.5 million in cash and 938,360 shares or approximately 13% of the post transaction outstanding shares of the Corporation s common stock. The transaction was valued at $33.3 million based on the Corporation s June 30, 2017 closing price of $30.50 as quoted on NASDAQ. The results of the combined entity s operations are included in the Corporation s Consolidated Financial Statements from the date of acquisition.

The acquisition of New Windsor is being accounted for as a business combination using the acquisition method of accounting and, accordingly, assets acquired, liabilities assumed, and consideration paid were recorded at estimated fair values on the acquisition date.

The following table summarizes the consideration paid for New Windsor and the fair value of assets acquired and liabilities assumed as of the acquisition date:

Purchase Price Consideration in Common Stock

New Windsor shares outstanding		1,003,703
Shares paid cash consideration		150,555
Cash consideration (per New Windsor share)	$	30.00
Cash portion of purchase price	$	4,519,995
New Windsor shares outstanding		1,003,703

Shares paid stock consideration		853,148
Exchange ratio		1.10
Total ACNB shares issued		938,360
ACNB s share price for purposes of calculation	$	30.50
Equity portion of purchase price	$	28,619,980
Cost of shares owned by buyer	$	150,000
Total consideration paid	$	33,289,975

	In thousands		
Allocation of Purchase Price			
Total Purchase Price		$	33,290
Fair Value of Assets Acquired			
Cash and cash equivalents	10,964		
Investment securities	21,624		
Loans held for sale	1,463		
Loans	263,450		
Restricted stock	486		
Premises and equipment	8,624		
Core deposit intangible asset	2,418		
Other assets	10,792		
Total assets	319,821		
Fair Value of Liabilities Assumed			
Non-interest bearing deposits	80,006		
Interest bearing deposits	213,327		
Subordinated debt	4,688		
Other liabilities	1,782		
Total liabilities	299,803		
Net Assets Acquired			20,018
Goodwill Recorded in Acquisition		$	13,272

Pursuant to the accounting requirements, the Corporation assigned a fair value to the assets acquired and liabilities assumed of New Windsor. ASC 820 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

Goodwill and core deposit intangibles are allocated to the banking business segment.

Fair values of the major categories of assets acquired and liabilities assumed were determined as follows:

Investment securities available-for-sale

The estimated fair values of the investment securities available for sale, primarily comprised of U.S. Government agency mortgage-backed securities, U.S. government agencies and municipal bonds, were determined using Level 2 inputs in the fair value hierarchy. The fair values were determined using independent pricing services. The Corporation s independent pricing service utilized matrix pricing, which is a mathematical technique used widely in the industry to value debt securities without relying exclusively on quoted market prices for the specific security but rather relying on the security s relationship to other benchmark quoted prices. Management reviewed the data and assumptions used in pricing the securities.

Loans

Acquired loans (impaired and non-impaired) are initially recorded at their acquisition-date fair values using Level 3 inputs. Fair values are based on a discounted cash flow methodology that involves assumptions and judgments as to credit risk, expected life time losses, environmental factors, collateral values, discount rates, expected payments and expected prepayments. Specifically, the Corporation has prepared three separate loan fair value adjustments that it believed a market participant might employ in estimating the entire fair value adjustment necessary under ASC 820-10 for the acquired loan portfolio. The three-separate fair valuation methodology employed are: 1) an interest rate loan fair value adjustment, 2) a general credit fair value adjustment, and 3) a specific credit fair value adjustment for purchased credit impaired loans subject to ASC 310-30 procedures. The acquired loans were recorded at fair value at the acquisition date without carryover of New Windsor s previously established allowance for loan losses. The fair value of the financial assets acquired included loans receivable with a gross amortized cost basis of $272,646,000. The table below illustrates the fair value adjustments made to the amortized cost basis in order to present a fair value of the loans acquired. The credit adjustment on purchased credit impaired loans is derived in accordance with ASC 310-30 and represents the portion of the loan balances that has been deemed uncollectible based on the Corporation s expectations of future cash flows for each respective loan.

In thousands		
Gross amortized cost basis at July 1, 2017	$	272,646
Interest rate fair value adjustment on pools of homogeneous loans		(731)
Credit fair value adjustment on pools of homogeneous loans		(4,501)
Credit fair value adjustment on purchased credit impaired loans		(3,964)
Fair value of acquired loans at July 1, 2017	$	263,450

For loans acquired without evidence of credit quality deterioration, ACNB prepared the interest rate loan fair value and credit fair value adjustments. Loans were grouped into homogeneous pools by characteristics such as loan type, term, collateral and rate. Market rates for similar loans were obtained from various internal and external data sources and reviewed by management for reasonableness. The average of these rates was used as the fair value interest rate a market participant would utilize. A present value approach was utilized to calculate the interest rate fair value discount of $731,000.

Additionally for loans acquired without credit deterioration, a credit fair value adjustment was calculated using a two-part credit fair value analysis: 1) expected lifetime credit migration losses; and 2) estimated fair value adjustment for certain qualitative factors. The expected lifetime losses were calculated using historical losses observed at the Bank, NWSB and peer banks. ACNB also estimated an environmental factor to apply to each loan type. The environmental factor represents a potential discount which may arise due to general credit and economic factors. A credit fair value discount of $4.5 million was determined. Both the interest rate and credit fair value adjustments relate to loans acquired without evidence of credit quality deterioration will be substantially recognized as interest income on a level yield amortization method over the expected life of the loans.

The following table presents the acquired purchased credit impaired loans receivable at the Acquisition Date:

In thousands		
Contractual principal and interest at acquisition	$	13,439
Nonaccretable difference		(5,651)
Expected cash flows at acquisition		7,788
Accretable yield		(1,458)
Fair value of purchased impaired loans	$	6,330

Premises and Equipment

The Corporation acquired seven branches from New Windsor. The fair value of New Windsor s premises, including land, buildings, and improvements, was determined based upon independent third-party appraisals and other data in the market in which the premises are located. The Corporation prepared an internal analysis to compare the lease contract obligations to comparable market rental rates. The Corporation believed that the leased contract rates were in a reasonable range of market rental rates and concluded that no fair market value adjustment related to leasehold interest was necessary.

Core Deposit Intangible

The fair value of the core deposit intangible was determined based on a discounted cash flow analysis using a discount rate commensurate with market participants. To calculate cash flows, deposit account servicing costs (net of deposit fee income) and interest expense on deposits were compared to the cost of alternative funding sources available through national brokered CD offering rates. The projected cash flows were developed using projected deposit attrition rates. The core deposit intangible will be amortized over ten years using the sum-of-years digits method.

Time Deposits

The fair value adjustment for time deposits represents a discount from the value of the contractual repayments of fixed-maturity deposits using prevailing market interest rates for similar-term time deposits. The time deposit discount of approximately $847,500 is being amortized into income on a level yield amortization method over the contractual life of the deposits.

Long-term Borrowings

The Corporation assumed a trust preferred subordinated debt in connection with the acquisition. The fair value of the trust preferred subordinated debt was determined based upon an estimated fair value from an independent brokerage firm. The trust preferred capital note was valued at a discount of $312,500, which is being amortized into income on a level yield amortization method based upon the assumed market rate, and the term of the trust preferred subordinated debt instrument.

3. Earnings Per Share and Restricted Stock Plan

The Corporation has a simple capital structure. Basic earnings per share of common stock is computed based on 7,030,441 and 6,066,675 weighted average shares of common stock outstanding for the six months ended June 30, 2018 and 2017, respectively, and 7,035,237 and 6,068,673 for the three months ended June 30, 2018 and 2017, respectively. All outstanding unvested restricted stock awards that contain rights to nonforfeitable dividends are considered participating securities for this calculation.

The Corporation has a restricted stock plan available to selected employees and directors of the Corporation and the Bank to advance the best interests of the Corporation and its stockholders. The plan provides those persons who have responsibility for its growth with additional incentives by allowing them to acquire ownership in the Corporation and, thereby, encouraging them to contribute to the success of the Corporation and the Bank. Plan expense is recognized over the vesting period of the stock issued under the plan. As of June 30, 2018, 26,045 shares were issued to employees under this plan, of which 19,485 were fully vested, no shares vested during the quarter, and the remaining 6,560 will vest over the next two years. $42,000 and $61,000 of compensation expenses related to the grants were recognized during the three months ended June 30, 2018 and 2017, respectively. $118,000 and $120,000 of compensation expenses related to the grants were recognized during the six months ended June 30, 2018 and 2017, respectively.

4. Retirement Benefits

The components of net periodic benefit expense related to the non-contributory, defined benefit pension plan for the three and six month periods ended June 30 were as follows:

	Three Months Ended June 30,	Six Months Ended June 30