FLUSHING FINANCIAL CORP
Form 10-Q
May 10, 2018

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF

THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended **March 31, 2018**

Commission file number **001-33013**

FLUSHING FINANCIAL CORPORATION

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of incorporation or organization)

11-3209278

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

220 RXR Plaza, Uniondale, New York 11556

(Address of principal executive offices)

(718) 961-5400

(Registrant's telephone number, including area code)

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

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

Large accelerated filer X

Accelerated filer __

Non-accelerated filer __

Smaller reporting company __

Emerging growth company __

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the exchange act.__

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). ___Yes X No

The number of shares of the registrant’s Common Stock outstanding as of April 30, 2018 was 28,522,021.

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(Unaudited)

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	March 31, 2018	December 31, 2017
	(Dollars in thousands, except per share data)	
Assets		
Cash and due from banks	$ 91,959	$ 51,546
Securities held-to-maturity:		
Mortgage-backed securities (none pledged; fair value of $7,564 and $7,810 at March 31, 2018 and December 31, 2017, respectively)	7,968	7,973
Other securities (none pledged; fair value of $21,347 and $21,889 at March 31, 2018 and December 31, 2017, respectively)	23,267	22,913
Securities available for sale, at fair value:		
Mortgage-backed securities (including assets pledged of $245,531 and $148,505 at March 31, 2018 and December 31, 2017, respectively; $1,505 and $1,590 at fair value pursuant to the fair value option at March 31, 2018 and December 31, 2017, respectively)	512,781	509,650
Other securities (including assets pledged of $41,647 and $44,052 at March 31, 2018 and December 31, 2017, respectively; $12,612 and $12,685 at fair value pursuant to the fair value option at March 31, 2018 and December 31, 2017, respectively)	216,480	228,704
Loans:		
Multi-family residential	2,286,803	2,273,595
Commercial real estate	1,426,847	1,368,112
One-to-four family mixed-use property	566,930	564,206
One-to-four family residential	190,115	180,663
Co-operative apartments	6,826	6,895
Construction	23,887	8,479
Small Business Administration	20,004	18,479
Taxi medallion	6,617	6,834
Commercial business and other	768,440	732,973
Net unamortized premiums and unearned loan fees	16,395	16,763
Allowance for loan losses	(20,542)	(20,351)
Net loans	5,292,322	5,156,648

Interest and dividends receivable	22,578	21,405
Bank premises and equipment, net	31,314	30,836
Federal Home Loan Bank of New York stock, at cost	54,045	60,089
Bank owned life insurance	130,653	131,856
Goodwill	16,127	16,127
Other assets	83,277	61,527
Total assets	$ 6,482,771	$ 6,299,274
Liabilities		
Due to depositors:		
Non-interest bearing	$ 377,861	$ 385,269
Interest-bearing	4,257,942	3,955,403
Mortgagors' escrow deposits	65,979	42,606
Borrowed funds:		
Federal Home Loan Bank advances	1,064,641	1,198,968
Subordinated debentures	73,768	73,699
Junior subordinated debentures, at fair value	38,692	36,986
Total borrowed funds	1,177,101	1,309,653
Other liabilities	68,581	73,735
Total liabilities	5,947,464	5,766,666
Stockholders' Equity		
Preferred stock ($0.01 par value; 5,000,000 shares authorized; none issued)	-	-
Common stock ($0.01 par value; 100,000,000 shares authorized; 31,530,595 shares issued at March 31, 2018 and December 31, 2017; 28,546,443 shares and 28,588,266 shares outstanding at March 31, 2018 and December 31, 2017, respectively)	315	315
Additional paid-in capital	219,115	217,906
Treasury stock, at average cost (2,984,152 shares and 2,942,329 at March 31, 2018 and December 31, 2017, respectively)	(60,737)	(57,675)
Retained earnings	387,793	381,048
Accumulated other comprehensive loss, net of taxes	(11,179)	(8,986)
Total stockholders' equity	535,307	532,608
Total liabilities and stockholders' equity	$ 6,482,771	$ 6,299,274

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

PART I – FINANCIAL INFORMATION

FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES

Consolidated Statements of Income

(Unaudited)

	For the three months ended March 31,	
(Dollars in thousands, except per share data)	2018	2017
Interest and dividend income		
Interest and fees on loans	$55,017	$50,885
Interest and dividends on securities:		
Interest	5,468	6,095
Dividends	14	121
Other interest income	287	153
Total interest and dividend income	60,786	57,254
Interest expense		
Deposits	12,110	8,980
Other interest expense	6,067	4,885
Total interest expense	18,177	13,865
Net interest income	42,609	43,389
Provision for loan losses	153	-
Net interest income after provision for loan losses	42,456	43,389
Non-interest income		
Banking services fee income	948	874
Net (loss) gain on sale of loans	(263)	210
Net loss from fair value adjustments	(100)	(378)
Federal Home Loan Bank of New York stock dividends	876	823
Gain from life insurance proceeds	776	1,161
Bank owned life insurance	762	795
Other income	201	204
Total non-interest income	3,200	3,689
Non-interest expense		
Salaries and employee benefits	18,455	17,104
Occupancy and equipment	2,577	2,496
Professional services	2,185	1,996
FDIC deposit insurance	500	326

Data processing	1,401	1,203
Depreciation and amortization	1,389	1,165
Other real estate owned/foreclosure expense	96	351
Net gain from sales of real estate owned	-	(50)
Other operating expenses	4,691	4,973
Total non-interest expense	31,294	29,564
Income before income taxes	14,362	17,514
Provision for income taxes		
Federal	2,607	4,749
State and local	343	505
Total taxes	2,950	5,254
Net income	$11,412	$12,260
Basic earnings per common share	$0.39	$0.42
Diluted earnings per common share	$0.39	$0.42
Dividends per common share	$0.20	$0.18

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

PART I – FINANCIAL INFORMATION

FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES

Consolidated Statements of Comprehensive Income

(Unaudited)

(In thousands)	For the three months ended March 31, 2018	2017
Net income	$ 11,412	$ 12,260
Other comprehensive income (loss), net of tax:		
Amortization of actuarial losses, net of taxes of ($41) and ($64) for the three months ended March 31, 2018 and 2017, respectively.	91	87
Amortization of prior service credits, net of taxes of $3 and $4 for the three months ended March 31, 2018 and 2017, respectively.	(7)	(7)
Net unrealized (losses) gains on securities, net of taxes of $3,055 and ($811) for the three months ended March 31, 2018 and 2017, respectively.	(6,640)	1,148
Net unrealized gain on cash flow hedges, net of taxes of ($2,604) for the three months ended March 31, 2018.	5,661	-
Total other comprehensive income (loss), net of tax	(895)	1,228
Comprehensive income	$ 10,517	$ 13,488

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

PART I – FINANCIAL INFORMATION

FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES

Consolidated Statements of Cash Flows

(Unaudited)

(In thousands)	For the three months ended March 31, 2018	2017
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	$11,412	$12,260
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	153	-
Depreciation and amortization of bank premises and equipment	1,389	1,165
Amortization of premium, net of accretion of discount	2,018	1,903
Net loss from fair value adjustments	100	378
Net loss (gain) from sale of loans	263	(210)
Net gain from sale of OREO	-	(50)
Income from bank owned life insurance	(762)	(795)
Gain from life insurance proceeds	(776)	(1,161)
Stock-based compensation expense	3,452	3,085
Deferred compensation	(1,238)	(1,431)
Deferred income tax expense	350	2,501
Increase in other liabilities	(118)	2,709
Decrease (increase) in other assets	(955)	(4,314)
Net cash provided by operating activities	15,288	16,040
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchases of bank premises and equipment	(1,867)	(630)
Net redemptions of Federal Home Loan Bank of New York shares	6,044	1,789
Purchases of securities held-to-maturity	(353)	-
Proceeds from maturities of securities held-to-maturity	-	1,330
Purchases of securities available for sale	(32,646)	(40,581)
Proceeds from sales and calls of securities available for sale	10,000	-
Proceeds from maturities and prepayments of securities available for sale	20,943	18,691
Proceeds from bank owned life insurance	2,741	651
Net originations of loans	(83,734)	(129,764)
Purchases of loans	(68,818)	(15,621)
Proceeds from sale of real estate owned	-	583
Proceeds from sale of loans	2,464	5,190
Net cash used in investing activities	(145,226)	(158,362)

CASH FLOWS FROM FINANCING ACTIVITIES		
Net (decrease) increase in non-interest bearing deposits	(7,408)	10,865
Net increase in interest-bearing deposits	302,438	172,471
Net increase in mortgagors' escrow deposits	23,373	21,612
Net repayments from short-term borrowed funds	(10,500)	(68,500)
Proceeds from long-term borrowings	-	80,000
Repayment of long-term borrowings	(123,794)	(51,254)
Purchases of treasury stock	(7,963)	(2,268)
Cash dividends paid	(5,795)	(5,246)
Net cash provided by financing activities	170,351	157,680
Net increase in cash and cash equivalents	40,413	15,358
Cash and cash equivalents, beginning of period	51,546	35,857
Cash and cash equivalents, end of period	$91,959	$51,215
SUPPLEMENTAL CASH FLOW DISCLOSURE		
Interest paid	$15,233	$12,491
Income taxes paid	1,103	1,000
Taxes paid if excess tax benefits were not tax deductible	1,691	2,194
Non-cash activities:		
Loans transferred to Other Real Estate Owned or Other Assets	744	-

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

PART I – FINANCIAL INFORMATION

FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES

Consolidated Statements of Changes in Stockholders' Equity

For the three months ended March 31, 2018 and 2017

(Unaudited)

(Dollars in thousands, except per share data)	Total	Common Stock	Additional Paid-in Capital	Retained Earnings	Treasury Stock	Accumulated Other Comprehensive Income (Loss)
Balance at December 31, 2017	$532,608	$ 315	$217,906	$381,048	$(57,675)	$ (8,986)
Reclassification of the Income Tax Effects of the Tax Cuts and Jobs Act from Accumulated Other Comprehensive Income (Loss) to Retained Earnings	-	-	-	2,073	-	(2,073)
Impact of adoption of Accounting Standard Update 2016-01	-	-	-	(775)	-	775
Net Income	11,412	-	-	11,412	-	-
Award of common shares released from Employee Benefit Trust (116,229 shares)	2,488	-	2,488	-	-	-
Vesting of restricted stock unit awards (248,877 shares)	-	-	(4,731)	(170)	4,901	-
Stock-based compensation expense	3,452	-	3,452	-	-	-
Purchase of treasury shares (217,863 shares)	(5,913)	-	-	-	(5,913)	-
Repurchase of shares to satisfy tax obligation (72,837 shares)	(2,050)	-	-	-	(2,050)	-
Dividends on common stock ($0.20 per share)	(5,795)	-	-	(5,795)	-	-
Other comprehensive loss	(895)	-	-	-	-	(895)
Balance at March 31, 2018	$535,307	$ 315	$219,115	$387,793	$(60,737)	$ (11,179)
Balance at December 31, 2016	$513,853	$ 315	$214,462	$361,192	$(53,754)	$ (8,362)
Net Income	12,260	-	-	12,260	-	-
Award of common shares released from Employee Benefit Trust (107,605 shares)	2,280	-	2,280	-	-	-
Vesting of restricted stock unit awards (256,810 shares)	-	-	(4,536)	(262)	4,798	-
Stock-based compensation expense	3,295	-	3,295	-	-	-
Repurchase of shares to satisfy tax obligation (78,554 shares)	(2,268)	-	-	-	(2,268)	-
Dividends on common stock ($0.18 per share)	(5,246)	-	-	(5,246)	-	-
Other comprehensive income	1,228	-	-	-	-	1,228

Balance at March 31, 2017	$525,402	$ 315	$215,501	$367,944	$(51,224)	$ (7,134)

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

PART I – FINANCIAL INFORMATION

FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES

Notes to Consolidated Financial Statements

(Unaudited)

1. Basis of Presentation

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

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

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

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

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

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

2. Use of Estimates

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

3. Earnings Per Share

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

	For the three months ended March 31,	
	2018	2017
	(Dollars in thousands, except per share data)	
Net income, as reported	$ 11,412	$ 12,260
Divided by:		
Weighted average common shares outstanding	28,974	29,019
Weighted average common stock equivalents	1	4
Total weighted average common shares outstanding and common stock equivalents	28,975	29,023
Basic earnings per common share	$ 0.39	$ 0.42
Diluted earnings per common share [1]	$ 0.39	$ 0.42
Dividend payout ratio	51.3 %	42.9 %

(1) For the three months ended March 31, 2018 and 2017, there were no common stock equivalents that were anti-dilutive.

PART I – FINANCIAL INFORMATION

FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES

Notes to Consolidated Financial Statements

(Unaudited)

4. Debt and Equity Securities

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

The following table summarizes the Company’s portfolio of securities held-to-maturity at March 31, 2018:

	Amortized Cost	Fair Value	Gross Unrealized Gains	Gross Unrealized Losses
	(In thousands)			
Securities held-to-maturity:				
Municipals	$23,267	$21,347	$ -	$ 1,920
Total other securities	23,267	21,347	-	1,920
FNMA	7,968	7,564	-	404
Total mortgage-backed securities	7,968	7,564	-	404
Total	$31,235	$28,911	$ -	$ 2,324

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

	Amortized Cost	Fair Value	Gross Unrealized Gains	Gross Unrealized Losses
	(In thousands)			
Securities held-to-maturity:				

Municipals	$22,913	$21,889	$ -	$ 1,024
Total municipals	22,913	21,889	-	1,024
FNMA	7,973	7,810	-	163
Total mortgage-backed securities	7,973	7,810	-	163
Total	$30,886	$29,699	$ -	$ 1,187

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PART I – FINANCIAL INFORMATION

FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES

Notes to Consolidated Financial Statements

(Unaudited)

The following table summarizes the Company's portfolio of securities available for sale at March 31, 2018:

	Amortized Cost	Fair Value	Gross Unrealized Gains	Gross Unrealized Losses
	(In thousands)			
Corporate	$ 110,000	$ 101,578	$ -	$ 8,422
Municipals	101,129	102,289	1,191	31
Mutual funds	11,451	11,451	-	-
Other	1,162	1,162	-	-
Total other securities	223,742	216,480	1,191	8,453
REMIC and CMO	346,414	338,368	188	8,234
GNMA	940	1,004	64	-
FNMA	131,918	128,535	68	3,451
FHLMC	45,938	44,874	15	1,079
Total mortgage-backed securities	525,210	512,781	335	12,764
Total securities available for sale	$ 748,952	$ 729,261	$ 1,526	$ 21,217

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

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

FHLMC	48,103	47,786	18	335
Total mortgage-backed securities	513,985	509,650	1,015	5,350
Total securities available for sale	$748,350	$738,354	$ 2,587	$ 12,583

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

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

PART I – FINANCIAL INFORMATION

FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES

Notes to Consolidated Financial Statements

(Unaudited)

The following tables detail the amortized cost and fair value of the Company's securities classified as held-to-maturity and available for sale at March 31, 2018, by contractual maturity. Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

Securities held-to-maturity:	Amortized Cost	Fair Value
	(In thousands)	
Due in one year or less	$1,398	$1,398
Due after ten years	21,869	19,949
Total other securities	23,267	21,347
Mortgage-backed securities	7,968	7,564
Total	$31,235	$28,911

Securities available for sale:	Amortized Cost	Fair Value
	(In thousands)	
Due in one year or less	$-	$-
Due after one year through five years	4,277	4,299
Due after five years through ten years	125,670	117,351
Due after ten years	82,344	83,379
Total other securities	212,291	205,029
Mutual funds	11,451	11,451
Mortgage-backed securities	525,210	512,781
Total	$748,952	$729,261

PART I – FINANCIAL INFORMATION

FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES

Notes to Consolidated Financial Statements

(Unaudited)

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

	At March 31, 2018						
		Total		Less than 12 months		12 months or more	
	Count	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
		(Dollars in thousands)					
Held-to-maturity securities							
Municipals	1	$19,949	$ 1,920	$-	$ -	$19,949	$ 1,920
Total other securities	1	19,949	1,920	-	-	19,949	1,920
FNMA	1	7,564	404	7,564	404	-	-
Total mortgage-backed securities	1	7,564	404	7,564	404	-	-
Total	2	$27,513	$ 2,324	$7,564	$ 404	$19,949	$ 1,920
Available for sale securities							
Corporate	14	$101,578	$ 8,422	$9,469	$ 531	$92,109	$ 7,891
Municipals	3	5,107	31	5,107	31	-	-
Total other securities	17	106,685	8,453	14,576	562	92,109	7,891
REMIC and CMO	46	306,808	8,234	223,172	4,458	83,636	3,776
FNMA	20	126,645	3,451	116,149	2,971	10,496	480
FHLMC	2	44,001	1,079	41,061	961	2,940	118
Total mortgage-backed securities	68	477,454	12,764	380,382	8,390	97,072	4,374
Total	85	$584,139	$ 21,217	$394,958	$ 8,952	$189,181	$ 12,265

	At December 31, 2017						
		Total		Less than 12 months		12 months or more	
	Count	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
	(Dollars in thousands)						

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

PART I – FINANCIAL INFORMATION

FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES

Notes to Consolidated Financial Statements

(Unaudited)

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

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

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

The Company did not sell any securities during the three months ended March 31, 2018 and 2017.

5. Loans

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

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

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

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

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

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

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

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

The Company segregated its loans into two portfolios based on year of origination. One portfolio was reviewed for loans originated after December 31, 2009 and a second portfolio for loans originated prior to January 1, 2010. Our decision to segregate the portfolio based upon origination dates was based on changes made in our underwriting standards during 2009. By the end of 2009, all loans were being underwritten based on revised and tightened underwriting standards. Loans originated prior to 2010 have a higher delinquency rate and loss history. Each of the years in the portfolio for loans originated prior to 2010 has a similar delinquency rate. For the three months ended March 31, 2018, the Company used a loss emergence period of 1.33 years. The Company's Board of Directors reviews and approves management's evaluation of the adequacy of the allowance for loan losses on a quarterly basis.

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

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

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

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The allocation of a portion of the allowance for loan losses for a performing TDR loan is based upon the present value of the future expected cash flows discounted at the loan's original effective rate, or for a non-performing TDR which is collateral dependent, the fair value of the collateral. At March 31, 2018, there were no commitments to lend additional funds to borrowers whose loans were modified to a TDR. The modification of loans to a TDR did not have a significant effect on our operating results, nor did it require a significant allocation of the allowance for loan losses.

The Company did not modify any loans as TDR during the three months ended March 31, 2018 and March 31, 2017.

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

	March 31, 2018		December 31, 2017	
(Dollars in thousands)	Number of contracts	Recorded investment	Number of contracts	Recorded investment
Multi-family residential	9	$ 2,503	9	$ 2,518
Commercial real estate	-	-	2	1,986
One-to-four family - mixed-use property	5	1,740	5	1,753
One-to-four family - residential	3	567	3	572
Taxi medallion	19	5,712	20	5,916
Commercial business and other	2	407	2	462
Total performing troubled debt restructured	38	$ 10,929	41	$ 13,207

During the three months ended March 31, 2018, we sold one commercial real estate TDR totaling $1.8 million, for a loss of $0.3 million and foreclosed on one taxi medallion TDR of $0.1 million, which is included in "Other Assets". There were no TDRs that defaulted during the period, which were within 12 months of their modification date.

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

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

During the three months ended March 31, 2018, one taxi medallion TDR was foreclosed upon and transferred to non-performing status. There were no TDR loans transferred to non-performing status during the three months ended March 31, 2017.

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

(In thousands)	March 31, 2018	December 31, 2017
Loans ninety days or more past due and still accruing:		
Commercial real estate	$ 1,668	$ 2,424
Total	1,668	2,424
Non-accrual mortgage loans:		
Multi-family residential	2,193	3,598
Commercial real estate	1,894	1,473
One-to-four family - mixed-use property	2,396	1,867

One-to-four family - residential	7,542	7,808
Total	14,025	14,746
Non-accrual non-mortgage loans:		
Small Business Administration	41	46
Taxi medallion	906	918
Total	947	964
Total non-accrual loans	14,972	15,710
Total non-performing loans	$16,640	$18,134

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

	For the three months ended March 31,	
	2018	2017
	(In thousands)	
Interest income that would have been recognized had the loans performed in accordance with their original terms	$406	$414
Less: Interest income included in the results of operations	158	127
Total foregone interest	$248	$287

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

	March 31, 2018					
(In thousands)	30 - 59 Days Past Due	60 - 89 Days Past Due	Greater than 90 Days	Total Past Due	Current	Total Loans
Multi-family residential	$2,748	$-	$2,193	$4,941	$2,281,862	$2,286,803
Commercial real estate	-	-	3,563	3,563	1,423,284	1,426,847
One-to-four family - mixed-use property	2,659	-	2,396	5,055	561,875	566,930
One-to-four family - residential	1,449	151	7,542	9,142	180,973	190,115
Co-operative apartments	-	-	-	-	6,826	6,826
Construction loans	-	730	-	730	23,157	23,887
Small Business Administration	-	-	-	-	20,004	20,004

Taxi medallion	-	-	-	-	6,617	6,617
Commercial business and other	200	5	-	205	768,235	768,440
Total	$7,056	$886	$15,694	$23,636	$5,272,833	$5,296,469

	December 31, 2017					
(In thousands)	30 - 59 Days Past Due	60 - 89 Days Past Due	Greater than 90 Days	Total Past Due	Current	Total Loans
Multi-family residential	$2,533	$279	$3,598	$6,410	$2,267,185	$2,273,595
Commercial real estate	1,680	2,197	3,897	7,774	1,360,338	1,368,112
One-to-four family - mixed-use property	1,570	860	1,867	4,297	559,909	564,206
One-to-four family - residential	1,921	680	7,623	10,224	170,439	180,663
Co-operative apartments	-	-	-	-	6,895	6,895
Construction loans	-	-	-	-	8,479	8,479
Small Business Administration	-	-	-	-	18,479	18,479
Taxi medallion	-	108	-	108	6,726	6,834
Commercial business and other	2	-	-	2	732,971	732,973
Total	$7,706	$4,124	$16,985	$28,815	$5,131,421	$5,160,236

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

March 31, 2018

(In thousands)	Multi-family residential	Commercial real estate	One-to-four family - mixed-use property	One-to-four family - residential	Construction loans	Small Business Administration	Taxi medallion	Commercial business and other	Total
Allowance for credit losses:									
Beginning balance	$ 5,823	$ 4,643	$ 2,545	$ 1,082	$ 68	$ 669	$ -	$ 5,521	$ 20,351
Charge-off's	(53)	-	-	(1)	-	(25)	-	(6)	(85)
Recoveries	2	-	-	108	-	6	-	7	123
Provision (benefit)	(22)	(41)	(75)	(148)	123	25	-	291	153
Ending balance	$ 5,750	$ 4,602	$ 2,470	$ 1,041	$ 191	$ 675	$ -	$ 5,813	$ 20,542

March 31, 2017

(In thousands)	Multi-family residential	Commercial real estate	One-to-four family - mixed-use property	One-to-four family - residential	Construction loans	Small Business Administration	Taxi medallion	Commercial business and other	Unallocated	Total
Allowance for credit losses:										
Beginning balance	$ 5,923	$ 4,487	$ 2,903	$ 1,015	$ 92	$ 481	$ 2,243	$ 4,492	$ 593	$ 22,229
Charge-off's	(14)	-	(34)	-	-	(65)	(54)	(12)	-	(179)
Recoveries	30	68	-	-	-	41	-	22	-	161
Provision (benefit)	(32)	(70)	(178)	(36)	2	(140)	24	208	222	-
Ending balance	$ 5,907	$ 4,485	$ 2,691	$ 979	$ 94	$ 317	$ 2,213	$ 4,710	$ 815	$ 22,211

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

March 31, 2018

(In thousands)	Multi-family residential	Commercial real estate	One-to-four family - mixed-use property	One-to-four family-residential	Co-operative apartments	Construction loans	Small Business Administration	Taxi medallion	Commercial business and other	Total
Financing Receivables:										
Ending Balance	$2,286,803	$								