

CHOICEONE FINANCIAL SERVICES INC
Form 10-Q
May 17, 2010

**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, 2010

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

For the transition period from _____ to _____

Commission File Number: **000-19202**

ChoiceOne Financial Services, Inc.
(Exact Name of Registrant as Specified in its Charter)

Michigan
(State or Other Jurisdiction of
Incorporation or Organization)

38-2659066
(I.R.S. Employer Identification No.)

**109 East Division
Sparta, Michigan**
(Address of Principal Executive Offices)

49345
(Zip Code)

(616) 887-7366

(Registrant's Telephone Number, including Area Code)

Indicate by checkmark whether the Registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Website, 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, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer," and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

As of April 30, 2010, the Registrant had outstanding 3,270,288 shares of common stock.

PART I. FINANCIAL INFORMATIONItem 1. Financial Statements.ChoiceOne Financial Services, Inc.
CONSOLIDATED BALANCE SHEETS

(Dollars in thousands)	March 31, 2010 (Unaudited)	December 31 2009 (Audited)
	<u> </u>	<u> </u>
Assets		
Cash and due from banks	\$ 7,480	\$ 9,957
Federal funds sold	9,644	9,793
	<u> </u>	<u> </u>
Cash and cash equivalents	17,124	19,750
Securities available for sale	78,433	74,413
Federal Home Loan Bank stock	3,304	3,304
Federal Reserve Bank stock	1,270	1,270
Loans held for sale	68	322
Loans	316,620	322,716
Allowance for loan losses	(4,687)	(4,322)
	<u> </u>	<u> </u>
Loans, net	311,933	318,394
Premises and equipment, net	12,329	11,918
Other real estate owned, net	1,851	2,201
Cash value of life insurance policies	9,281	9,201
Intangible assets, net	2,956	3,068
Goodwill	13,728	13,728
Other assets	8,758	8,346
	<u> </u>	<u> </u>
Total assets	\$ 461,035	\$ 465,915
Liabilities		
Deposits - noninterest-bearing	\$ 60,708	\$ 60,802
Deposits - interest-bearing	305,762	304,208
	<u> </u>	<u> </u>
Total deposits	366,470	365,010
Advances from Federal Home Loan Bank	18,480	21,980
Securities sold under agreements to repurchase	17,435	20,684
Other liabilities	5,283	5,315
	<u> </u>	<u> </u>
Total liabilities	407,668	412,989

Shareholders' Equity

Edgar Filing: CHOICEONE FINANCIAL SERVICES INC - Form 10-Q

Preferred stock; shares authorized: 100,000; shares outstanding: none	-	-
Common stock and paid in capital, no par value; shares authorized: 7,000,000; shares outstanding: 3,269,103 at March 31, 2010 and 3,265,714 at December 31, 2009	46,358	46,326
Retained earnings	6,064	5,813
Accumulated other comprehensive income, net	945	787
<hr/>	<hr/>	<hr/>
Total shareholders' equity	53,367	52,926
<hr/>	<hr/>	<hr/>
Total liabilities and shareholders' equity	\$ 461,035	\$ 465,915
<hr/>	<hr/>	<hr/>

See accompanying notes to consolidated financial statements.

ChoiceOne Financial Services, Inc.
CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME (Unaudited)

(Dollars in thousands, except per share data)	Three Months Ended March 31,	
	2010	2009
Interest income		
Loans, including fees	\$ 4,724	\$ 5,064
Securities:		
Taxable	345	464
Tax exempt	366	383
Other	3	2
	5,438	5,913
Interest expense		
Deposits	1,065	1,583
Advances from Federal Home Loan Bank	233	339
Other	80	93
	1,378	2,015
Net interest income	4,060	3,898
Provision for loan losses	1,050	600
	3,010	3,298
Net interest income after provision for loan losses	3,010	3,298
Noninterest income		
Customer service charges	729	717
Insurance and investment commissions	147	195
Gains on sales of loans	106	170
Gains on sales of securities	389	103
Losses on sales of other assets	(92)	(57)
Earnings on life insurance policies	90	92
Other income	138	156
	1,507	1,376
Total noninterest income	1,507	1,376
Noninterest expense		
Salaries and benefits	1,680	1,774
Occupancy and equipment	551	546
Data processing	426	376
Professional fees	172	181
Supplies and postage	126	152
Advertising and promotional	31	21

Edgar Filing: CHOICEONE FINANCIAL SERVICES INC - Form 10-Q

Intangible amortization	112	118
FDIC insurance	156	149
Other expense	444	480
	<hr/>	<hr/>
Total noninterest expense	3,698	3,797
	<hr/>	<hr/>
Income before income tax	819	877
Income tax expense	175	136
	<hr/>	<hr/>
Net income	\$ 644	\$ 741
<hr/>		
Basic earnings per share	\$ 0.20	\$ 0.23
<hr/>		
Diluted earnings per share	\$ 0.20	\$ 0.23
<hr/>		
Dividends declared per share	\$ 0.12	\$ 0.12
<hr/>		

See accompanying notes to consolidated financial statements.

ChoiceOne Financial Services, Inc.
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY (Unaudited)

(Dollars in thousands)	Number of Shares	Common Stock and Paid in Capital	Retained Earnings	Accumulated Other Comprehensive Income, Net	Total
Balance, January 1, 2009	3,246,109	\$ 46,171	\$ 5,898	\$ 116	\$ 52,185
Comprehensive income					
Net income			741		741
Net change in unrealized gain on securities available for sale, net of tax of \$134				260	260
Total comprehensive income					1,001
Shares issued	4,641	27			27
Effect of stock options granted		9			9
Effect of employee stock purchases		3			3
Cash dividends declared (\$0.12 per share)			(390)		(390)
Balance, March 31, 2009	3,250,750	\$ 46,210	\$ 6,249	\$ 376	\$ 52,835
Balance, January 1, 2010	3,265,714	\$ 46,326	\$ 5,813	\$ 787	\$ 52,926
Comprehensive income					
Net income			644		644
Net change in unrealized gain on securities available for sale, net of tax of \$81				158	158
Total comprehensive income					802
Shares issued	3,389	25			25
Effect of stock options granted		3			3
Effect of employee stock purchases		4			4
Cash dividends declared (\$0.12 per share)			(393)		(393)
Balance, March 31, 2010	3,269,103	\$ 46,358	\$ 6,064	\$ 945	\$ 53,367

See accompanying notes to consolidated financial statements.

ChoiceOne Financial Services, Inc.
CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)

(Dollars in thousands)	Three Months Ended March 31,	
	2010	2009
Cash flows from operating activities:		
Net income	\$ 644	\$ 741
Adjustments to reconcile net income to net cash from operating activities:		
Provision for loan losses	1,050	600
Depreciation	208	228
Amortization	233	271
Compensation expense on stock options and employee stock purchases	7	12
Gains on sales of securities	(389)	(103)
Gains on sales of loans	(106)	(170)
Loans originated for sale	(4,320)	(8,946)
Proceeds from loan sales	4,657	8,428
Earnings on bank-owned life insurance	(90)	(92)
Losses on sales of other real estate owned	100	47
Write-downs of other real estate owned	107	119
Proceeds from sales of other real estate owned	291	490
Deferred federal income tax expense/(benefit)	(128)	-
Net changes in other assets	(431)	(198)
Net changes in other liabilities	17	176
	1,850	1,603
Net cash from operating activities		
Cash flows from investing activities:		
Securities available for sale:		
Sales	2,063	2,698
Maturities, prepayments and calls	6,567	6,638
Purchases	(12,087)	(3,984)
Loan originations and payments, net	5,263	5,637
Additions to premises and equipment	(619)	(39)
	1,187	10,950
Net cash from investing activities		
Cash flows from financing activities:		
Net change in deposits	1,460	6,424
Net change in repurchase agreements	(3,249)	(1,593)
Proceeds from Federal Home Loan Bank advances	-	5,000
Payments on Federal Home Loan Bank advances	(3,506)	(18,500)
Issuance of common stock	25	27
Cash dividends	(393)	(390)
	(5,663)	(9,032)
Net cash used in financing activities		

Edgar Filing: CHOICEONE FINANCIAL SERVICES INC - Form 10-Q

Net change in cash and cash equivalents	(2,626)	3,521
Beginning cash and cash equivalents	19,750	11,160
<hr/>		
Ending cash and cash equivalents	\$ 17,124	\$ 14,681
<hr/>		
Supplemental disclosures of cash flow information:		
Cash paid for interest	\$ 1,462	\$ 2,150
Loans transferred to other real estate	\$ 148	\$ 1,266

See accompanying notes to consolidated financial statements.

ChoiceOne Financial Services, Inc.
NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation

The consolidated financial statements include ChoiceOne Financial Services, Inc. (the "Registrant") and its wholly-owned subsidiary, ChoiceOne Bank (the "Bank"), and the Bank's wholly-owned subsidiary ChoiceOne Insurance Agencies, Inc. Intercompany transactions and balances have been eliminated in consolidation.

The consolidated financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information, prevailing practices within the banking industry and the instructions to Form 10-Q. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements.

The accompanying consolidated financial statements reflect all adjustments ordinary in nature which are, in the opinion of management, necessary for a fair presentation of the Consolidated Balance Sheets as of March 31, 2010 and December 31, 2009, the Consolidated Statements of Income for the three-month periods ended March 31, 2010 and March 31, 2009, the Consolidated Statements of Changes in Shareholders' Equity for the three-month periods ended March 31, 2010 and March 31, 2009, and the Consolidated Statements of Cash Flows for the three-month periods ended March 31, 2010 and March 31, 2009. Operating results for the three months ended March 31, 2010 are not necessarily indicative of the results that may be expected for the year ending December 31, 2010.

The accompanying consolidated financial statements should be read in conjunction with the consolidated financial statements and footnotes thereto included in the Registrant's Annual Report on Form 10-K for the year ended December 31, 2009.

Allowance for Loan Losses

The allowance for loan losses is maintained at a level believed adequate by management to absorb probable incurred losses inherent in the consolidated loan portfolio. Management's evaluation of the adequacy of the allowance is an estimate based on reviews of individual loans, assessments of the impact of current economic conditions on the portfolio and historical loss experience of seasoned loan portfolios. See Note 2 to the interim consolidated financial statements for additional information.

Management believes the accounting estimate related to the allowance for loan losses is a "critical accounting estimate" because (1) the estimate is highly susceptible to change from period to period because of assumptions concerning the changes in the types and volumes of the portfolios and economic conditions and (2) the impact of recognizing an impairment or loan loss could have a material effect on ChoiceOne's assets reported on the balance sheet as well as its net income.

Stock Transactions

A total of 1,234 shares of common stock were issued to the Registrant's Board of Directors for a cash price of \$10,000 under the terms of the Directors' Stock Purchase Plan in the first quarter of 2010. A total of 2,155 shares were issued to employees for a cash price of \$15,000 under the Employee Stock Purchase Plan for the quarter ended March 31, 2010.

Reclassifications

Certain amounts presented in prior periods have been reclassified to conform to the current presentation.

ChoiceOne Financial Services, Inc.
NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS (Continued)

NOTE 2 - ALLOWANCE FOR LOAN LOSSES

An analysis of changes in the allowance for loan losses follows:

(Dollars in thousands)	Three Months Ended March 31,	
	2010	2009
Balance at beginning of period	\$ 4,322	\$ 3,600
Provision charged to expense	1,050	600
Recoveries credited to the allowance	91	138
Loans charged off	(776)	(279)
	4,687	4,059
Balance at end of period	\$ 4,687	\$ 4,059

Information regarding impaired loans follows:

(Dollars in thousands)	March 31, 2010	December 31, 2009
Loans with no allowance allocated	\$ 4,945	\$ 5,062
Loans with allowance allocated	3,958	4,685
Amount of allowance for loan losses allocated	953	1,096

(Dollars in thousands)	Three Months Ended March 31,	
	2010	2009
Average balance during the period	\$ 9,325	\$ 6,950

NOTE 3 - EARNINGS PER SHARE

Earnings per share are based on the weighted average number of shares outstanding during the period. A computation of basic earnings per share and diluted earnings per share follows:

	Three Months Ended March 31,	
	2010	2009
(Dollars in thousands, except per share data)		
<u>Basic Earnings Per Share</u>		
Net income available to common shareholders	\$ 644	\$ 741
Weighted average common shares outstanding	3,266,899	3,247,365
Basic earnings per share	\$ 0.20	\$ 0.23
<u>Diluted Earnings Per Share</u>		
Net income available to common shareholders	\$ 644	\$ 741
Weighted average common shares outstanding	3,266,899	3,247,365
Plus dilutive stock options	-	-
Weighted average common shares outstanding and potentially dilutive shares	3,266,899	3,247,365
Diluted earnings per share	\$ 0.20	\$ 0.23

As of March 31, 2010 and 2009, there were 48,732 stock options that are considered to be anti-dilutive to earnings per share for the three-month periods ended March 31, 2010 and 2009. These stock options have been excluded from the calculation above.

NOTE 4 - FINANCIAL INSTRUMENTS

Financial instruments as of the dates indicated were as follows:

	March 31, 2010		December 31, 2009	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
(Dollars in thousands)				

Edgar Filing: CHOICEONE FINANCIAL SERVICES INC - Form 10-Q

Assets:

Cash and due from banks	\$	7,480	\$	7,480	\$	9,957	\$	9,957
Federal funds sold		9,644		9,644		9,793		9,793
Securities available for sale		78,433		78,433		74,413		74,413
Federal Home Loan Bank and Federal Reserve		4,574		4,574		4,574		4,574
Bank stock								
Loans held for sale		68		68		322		322
Loans, net		311,933		301,024		318,394		314,491
Accrued interest receivable		2,362		2,362		2,091		2,091

Liabilities:

Demand, savings and money market deposits		209,773		209,773		199,418		199,418
Time deposits		156,697		155,990		165,592		165,597
Repurchase agreements		17,435		17,432		20,684		20,686
Advances from Federal Home Loan Bank		18,480		19,080		21,980		21,986
Accrued interest payable		293		293		377		377

The estimated fair values approximate the carrying amounts for all assets and liabilities except those described later in this paragraph. The methodology for determining the estimated fair value for securities available for sale is described in Note 5. The estimated fair value for loans is based on the rates charged at March 31, 2010 for new loans with similar maturities, applied until the loan is assumed to reprice or be paid. The allowance for loan losses is considered to be a reasonable estimate of discount for credit quality concerns. The estimated fair values for time deposits and Federal Home Loan Bank advances are based on the rates paid at March 31, 2010 for new deposits or FHLB advances, applied until maturity. The estimated fair values for other financial instruments and off-balance sheet loan commitments are considered nominal.

NOTE 5 - FAIR VALUE MEASUREMENTS

The following tables present information about the Bank's assets and liabilities measured at fair value on a recurring basis and the valuation techniques used by the Bank to determine those fair values.

In general, fair values determined by Level 1 inputs use quoted prices in active markets for identical assets or liabilities that the Bank has the ability to access.

Fair values determined by Level 2 inputs use other inputs that are observable, either directly or indirectly. These Level 2 inputs include quoted prices for similar assets and liabilities in active markets, and other inputs such as interest rates and yield curves that are observable at commonly quoted intervals.

Level 3 inputs are unobservable inputs, including inputs that are available in situations where there is little, if any, market activity for the related asset or liability.

In instances where inputs used to measure fair value fall into different levels in the above fair value hierarchy, fair value measurements in their entirety are categorized based on the lowest level input that is significant to the valuation. The Bank's assessment of the significance of particular inputs to these fair value measurements requires judgment and considers factors specific to each asset or liability.

There were no liabilities measured at fair value as of March 31, 2010 or December 31, 2009. Disclosures concerning assets measured at fair value are as follows:

Assets Measured at Fair Value on a Recurring Basis (Dollars in Thousands)

	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance at Date Indicated
<u>Investment Securities, Available for Sale - March 31, 2010</u>				
U.S. Government and federal agency	\$ 22,460	\$ -	\$ -	\$ 22,460
State and municipal	918	42,053	2,174	45,145