

Section 1: 10-Q

**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 September 30, 2019

OR

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 0-33203

LANDMARK BANCORP, INC.

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of incorporation or organization)

43-1930755

(I.R.S. Employer Identification Number)

701 Poyntz Avenue, Manhattan, Kansas

(Address of principal executive offices)

66502

(Zip code)

(785) 565-2000

(Registrant's telephone number, including area code)

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

Title of each class:

Trading Symbol(s)

Name of exchange on which registered:

Common Stock, par value \$0.01 per share

LARK

Nasdaq Global Market

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

Indicate by check mark whether the registrant has submitted electronically, every Interactive Data File required to be submitted 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 such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a 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 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 Exchange Act). Yes No

Indicate the number of shares outstanding of each of the issuer's classes of common stock as of the latest practicable date: as of November 7, 2019, the issuer had outstanding 4,376,532 shares of its common stock, \$0.01 par value per share.

LANDMARK BANCORP, INC.
Form 10-Q Quarterly Report

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PART I – FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

**LANDMARK BANCORP, INC. AND SUBSIDIARY
CONSOLIDATED BALANCE SHEETS**

(Dollars in thousands, except per share amounts)

| | <u>September 30, 2019</u> | <u>December 31, 2018</u> |
|--|---------------------------|--------------------------|
| | (Unaudited) | |
| Assets | | |
| Cash and cash equivalents | \$ 21,736 | \$ 19,114 |
| Investment securities available-for-sale, at fair value | 369,317 | 388,345 |
| Bank stocks, at cost | 3,231 | 4,776 |
| Loans, net of allowance for loans losses of \$6,279 at September 30, 2019 and \$5,765 at December 31, 2018 | 520,133 | 489,373 |
| Loans held for sale, at fair value | 15,049 | 4,743 |
| Premises and equipment, net | 21,338 | 21,127 |
| Bank owned life insurance | 24,820 | 24,342 |
| Goodwill | 17,532 | 17,532 |
| Other intangible assets, net | 2,834 | 3,091 |
| Real estate owned, net | 473 | 35 |
| Accrued interest and other assets | 12,268 | 13,306 |
| Total assets | <u>\$ 1,008,731</u> | <u>\$ 985,784</u> |
| Liabilities and Stockholders' Equity | | |
| Liabilities: | | |
| Deposits: | | |
| Non-interest-bearing demand | \$ 184,754 | \$ 168,273 |
| Money market and checking | 352,715 | 393,460 |
| Savings | 98,859 | 94,895 |
| Time | 197,426 | 167,020 |
| Total deposits | <u>833,754</u> | <u>823,648</u> |
| Federal Home Loan Bank borrowings | 17,200 | 20,000 |
| Subordinated debentures | 21,651 | 21,651 |
| Other borrowings | 16,279 | 15,246 |
| Accrued interest, taxes, and other liabilities | 13,809 | 13,338 |
| Total liabilities | <u>902,693</u> | <u>893,883</u> |
| Commitments and contingencies | | |
| Stockholders' equity: | | |
| Preferred stock, \$0.01 par value per share, 200,000 shares authorized; none issued | - | - |
| Common stock, \$0.01 par value per share, 7,500,000 shares authorized; 4,375,532 and 4,372,116 shares issued and outstanding at September 30, 2019 and December 31, 2018, respectively | 44 | 44 |
| Additional paid-in capital | 63,975 | 63,775 |
| Retained earnings | 36,843 | 32,073 |
| Accumulated other comprehensive income (loss) | 5,176 | (3,991) |
| Total stockholders' equity | <u>106,038</u> | <u>91,901</u> |
| Total liabilities and stockholders' equity | <u>\$ 1,008,731</u> | <u>\$ 985,784</u> |

See accompanying notes to consolidated financial statements.

LANDMARK BANCORP, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF EARNINGS
(Unaudited)

(Dollars in thousands, except per share amounts)

| | Three months ended September 30, | | Nine months ended September 30, | |
|---|-------------------------------------|-----------------|------------------------------------|-----------------|
| | 2019 | 2018 | 2019 | 2018 |
| Interest income: | | | | |
| Loans: | | | | |
| Taxable | \$ 7,070 | \$ 6,168 | \$ 20,358 | \$ 17,227 |
| Tax-exempt | 26 | 152 | 78 | 216 |
| Investment securities: | | | | |
| Taxable | 1,444 | 1,341 | 4,430 | 3,843 |
| Tax-exempt | 905 | 985 | 2,756 | 3,044 |
| Total interest income | <u>9,445</u> | <u>8,646</u> | <u>27,622</u> | <u>24,330</u> |
| Interest expense: | | | | |
| Deposits | 1,433 | 833 | 4,144 | 2,005 |
| Borrowings | 353 | 633 | 1,142 | 1,715 |
| Total interest expense | <u>1,786</u> | <u>1,466</u> | <u>5,286</u> | <u>3,720</u> |
| Net interest income | 7,659 | 7,180 | 22,336 | 20,610 |
| Provision for loan losses | 400 | 450 | 1,000 | 900 |
| Net interest income after provision for loan losses | <u>7,259</u> | <u>6,730</u> | <u>21,336</u> | <u>19,710</u> |
| Non-interest income: | | | | |
| Fees and service charges | 2,057 | 1,812 | 5,677 | 5,376 |
| Gains on sales of loans, net | 2,081 | 1,476 | 4,943 | 4,105 |
| Bank owned life insurance | 159 | 160 | 478 | 481 |
| (Losses) gains on sales of investment securities, net | - | (15) | (146) | 20 |
| Other | 258 | 1,134 | 847 | 2,239 |
| Total non-interest income | <u>4,555</u> | <u>4,567</u> | <u>11,799</u> | <u>12,221</u> |
| Non-interest expense: | | | | |
| Compensation and benefits | 4,678 | 4,244 | 13,072 | 11,999 |
| Occupancy and equipment | 1,207 | 1,108 | 3,369 | 3,258 |
| Professional fees | 446 | 386 | 1,285 | 1,204 |
| Data processing | 405 | 394 | 1,233 | 1,135 |
| Amortization of intangibles | 332 | 278 | 887 | 838 |
| Advertising | 166 | 166 | 501 | 498 |
| Federal deposit insurance (credits) premiums | (66) | 73 | 71 | 217 |
| Foreclosure and real estate owned expense | 75 | 24 | 142 | 49 |
| Other | 1,375 | 1,039 | 3,751 | 3,520 |
| Total non-interest expense | <u>8,618</u> | <u>7,712</u> | <u>24,311</u> | <u>22,718</u> |
| Earnings before income taxes | 3,196 | 3,585 | 8,824 | 9,213 |
| Income tax expense | 583 | 565 | 1,430 | 1,249 |
| Net earnings | <u>\$ 2,613</u> | <u>\$ 3,020</u> | <u>\$ 7,394</u> | <u>\$ 7,964</u> |
| Earnings per share: | | | | |
| Basic (1) | <u>\$ 0.60</u> | <u>\$ 0.69</u> | <u>\$ 1.69</u> | <u>\$ 1.83</u> |
| Diluted (1) | <u>\$ 0.60</u> | <u>\$ 0.69</u> | <u>\$ 1.69</u> | <u>\$ 1.83</u> |

(1) Per share amounts for the periods ended September 30, 2018 have been adjusted to give effect to the 5% stock dividend paid during December 2018.

See accompanying notes to consolidated financial statements.

LANDMARK BANCORP, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(Unaudited)

(Dollars in thousands)

| | Three months ended September 30, | | Nine months ended September 30, | |
|---|-------------------------------------|-----------------|------------------------------------|---------------|
| | 2019 | 2018 | 2019 | 2018 |
| Net earnings | \$ 2,613 | \$ 3,020 | \$ 7,394 | \$ 7,964 |
| Net unrealized holding (gains) losses on available-for-sale securities | 1,787 | (2,530) | 11,995 | (9,229) |
| Reclassification adjustment for net losses (gains) included in earnings | - | 15 | 146 | (20) |
| Net unrealized gains (losses) | 1,787 | (2,515) | 12,141 | (9,249) |
| Income tax effect on net (losses) gains included in earnings | - | (4) | (36) | 5 |
| Income tax effect on net unrealized holding (gains) losses | (437) | 621 | (2,938) | 2,262 |
| Other comprehensive income (loss) | 1,350 | (1,898) | 9,167 | (6,982) |
| Total comprehensive income | <u>\$ 3,963</u> | <u>\$ 1,122</u> | <u>\$ 16,561</u> | <u>\$ 982</u> |

See accompanying notes to consolidated financial statements.

LANDMARK BANCORP, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
(Unaudited)

| <i>(Dollars in thousands, except per share amounts)</i> | <u>Common stock</u> | <u>Additional paid-in capital</u> | <u>Retained earnings</u> | <u>Accumulated other comprehensive income (loss)</u> | <u>Total</u> |
|---|---------------------|-----------------------------------|--------------------------|--|-------------------|
| Balance at July 1, 2018 | \$ 41 | \$ 58,356 | \$ 33,514 | \$ (5,496) | \$ 86,415 |
| Net earnings | - | - | 3,020 | - | 3,020 |
| Other comprehensive loss | - | - | - | (1,898) | (1,898) |
| Dividends paid (\$0.19 per share) | - | - | (832) | - | (832) |
| Stock-based compensation | - | 55 | - | - | 55 |
| Exercise of stock options, 4,300 shares | 1 | 49 | - | - | 50 |
| Balance at September 30, 2018 | <u>\$ 42</u> | <u>\$ 58,460</u> | <u>\$ 35,702</u> | <u>\$ (7,394)</u> | <u>\$ 86,810</u> |
| Balance at July 1, 2019 | \$ 44 | \$ 63,904 | \$ 35,105 | \$ 3,826 | \$ 102,879 |
| Net earnings | - | - | 2,613 | - | 2,613 |
| Other comprehensive income | - | - | - | 1,350 | 1,350 |
| Dividends paid (\$0.20 per share) | - | - | (875) | - | (875) |
| Stock-based compensation | - | 71 | - | - | 71 |
| Balance at September 30, 2019 | <u>\$ 44</u> | <u>\$ 63,975</u> | <u>\$ 36,843</u> | <u>\$ 5,176</u> | <u>\$ 106,038</u> |

See accompanying notes to consolidated financial statements.

| <i>(Dollars in thousands, except per share amounts)</i> | <u>Common stock</u> | <u>Additional paid-in capital</u> | <u>Retained earnings</u> | <u>Accumulated other comprehensive income (loss)</u> | <u>Total</u> |
|---|---------------------|-----------------------------------|--------------------------|--|-------------------|
| Balance at January 1, 2018 | \$ 41 | \$ 57,772 | \$ 30,214 | \$ (405) | \$ 87,622 |
| Net earnings | - | - | 7,964 | - | 7,964 |
| Other comprehensive loss | - | - | - | (6,982) | (6,982) |
| Dividends paid (\$0.57 per share) | - | - | (2,483) | - | (2,483) |
| Stock-based compensation | - | 155 | - | - | 155 |
| Adjustment of common stock investments | - | - | 7 | (7) | - |
| Exercise of stock options, 70,587 shares | 1 | 533 | - | - | 534 |
| Balance at September 30, 2018 | <u>\$ 42</u> | <u>\$ 58,460</u> | <u>\$ 35,702</u> | <u>\$ (7,394)</u> | <u>\$ 86,810</u> |
| Balance at January 1, 2019 | \$ 44 | \$ 63,775 | \$ 32,073 | \$ (3,991) | \$ 91,901 |
| Net earnings | - | - | 7,394 | - | 7,394 |
| Other comprehensive income | - | - | - | 9,167 | 9,167 |
| Dividends paid (\$0.60 per share) | - | - | (2,624) | - | (2,624) |
| Stock-based compensation | - | 200 | - | - | 200 |
| Balance at September 30, 2019 | <u>\$ 44</u> | <u>\$ 63,975</u> | <u>\$ 36,843</u> | <u>\$ 5,176</u> | <u>\$ 106,038</u> |

See accompanying notes to consolidated financial statements.

LANDMARK BANCORP, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

(Dollars in thousands)

| | Nine months ended September 30, | |
|--|------------------------------------|------------------|
| | 2019 | 2018 |
| Cash flows from operating activities: | | |
| Net earnings | \$ 7,394 | \$ 7,964 |
| Adjustments to reconcile net earnings to net cash provided by operating activities: | | |
| Provision for loan losses | 1,000 | 900 |
| Valuation allowance on real estate owned | 31 | 12 |
| Amortization of investment security premiums, net | 1,285 | 1,454 |
| Amortization of purchase accounting adjustment on loans | (27) | (184) |
| Amortization of purchase accounting adjustment on subordinated debentures | - | 150 |
| Amortization of intangibles | 887 | 838 |
| Depreciation | 761 | 751 |
| Increase in cash surrender value of bank owned life insurance | (478) | (481) |
| Stock-based compensation | 200 | 155 |
| Deferred income taxes | (430) | (643) |
| Net losses (gains) on sales of investment securities | 146 | (20) |
| Net (gain) loss on sales of premises, equipment and real estate owned | (2) | 41 |
| Net gains on sales of loans | (4,943) | (4,105) |
| Proceeds from sales of loans | 147,620 | 126,745 |
| Origination of loans held for sale | (152,983) | (123,833) |
| Changes in assets and liabilities: | | |
| Accrued interest and other assets | (292) | 188 |
| Accrued expenses, taxes, and other liabilities | (1,208) | 1,122 |
| Net cash (used in) provided by operating activities | <u>(1,039)</u> | <u>11,054</u> |
| Cash flows from investing activities: | | |
| Net increase in loans | (32,377) | (42,630) |
| Maturities and prepayments of investment securities | 54,998 | 40,019 |
| Purchases of investment securities | (34,751) | (58,176) |
| Proceeds from sales of investment securities | 9,491 | 21,125 |
| Proceeds from sales of common stock investments | - | 7 |
| Redemption of bank stocks | 7,498 | 8,226 |
| Purchase of bank stocks | (5,953) | (7,828) |
| Proceeds from sales of premises and equipment and foreclosed assets | 26 | 304 |
| Purchases of premises and equipment, net | (986) | (1,152) |
| Net cash used in investing activities | <u>(2,054)</u> | <u>(40,105)</u> |
| Cash flows from financing activities: | | |
| Net increase in deposits | 10,106 | 1,718 |
| Federal Home Loan Bank advance borrowings | 325,497 | 534,152 |
| Federal Home Loan Bank advance repayments | (328,297) | (505,452) |
| Proceeds from other borrowings | 1,033 | 284 |
| Proceeds from exercise of stock options | - | 534 |
| Payment of dividends | (2,624) | (2,483) |
| Net cash provided by financing activities | <u>5,715</u> | <u>28,753</u> |
| Net increase (decrease) in cash and cash equivalents | 2,622 | (298) |
| Cash and cash equivalents at beginning of period | 19,114 | 16,584 |
| Cash and cash equivalents at end of period | <u>\$ 21,736</u> | <u>\$ 16,286</u> |

(Continued)

LANDMARK BANCORP, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS, CONTINUED
(Unaudited)

(Dollars in thousands)

| | Nine months ended | |
|---|-------------------|------------|
| | September 30, | |
| | 2019 | 2018 |
| | (Unaudited) | |
| Supplemental disclosure of cash flow information: | | |
| Cash payments (refund) for income taxes | \$ 511 | \$ (1,000) |
| Cash paid for interest | 5,156 | 3,442 |
| Cash paid for operating leases | 116 | 107 |
| Supplemental schedule of noncash investing and financing activities: | | |
| Transfer of loans to real estate owned | 482 | 63 |
| Investment securities purchases not yet settled | - | (1,714) |
| Operating lease asset and related lease liability recorded | 353 | - |

See accompanying notes to consolidated financial statements.

**LANDMARK BANCORP, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

1. Interim Financial Statements

The unaudited consolidated financial statements of Landmark Bancorp, Inc. (the “Company”) and its wholly owned subsidiaries, Landmark National Bank (the “Bank”) and Landmark Risk Management, Inc., have been prepared in accordance with the instructions to Form 10-Q. Accordingly, they do not include all the information and footnotes required by U.S. generally accepted accounting principles (“GAAP”) for complete financial statements and should be read in conjunction with the Company’s most recent Annual Report on Form 10-K, containing the latest audited consolidated financial statements and notes thereto. The consolidated financial statements in this report have not been audited by an independent registered public accounting firm, but in the opinion of management, all adjustments, consisting of normal recurring accruals, considered necessary for a fair presentation of financial statements have been reflected herein. The results of the three month and nine month interim periods ended September 30, 2019 are not necessarily indicative of the results expected for the year ending December 31, 2019 or any other future time period. The Company has evaluated subsequent events for recognition and disclosure up to the date the financial statements were issued.

On January 1, 2019, the Company adopted ASU 2016-02, Leases (Topic 842). The guidance is intended to increase transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet and requiring more disclosures related to leasing transactions. The amendments in Topic 842 are effective for fiscal years, and interim periods within those years, beginning after December 15, 2018. The Company elected the optional transition method permitted with Topic 842. Under this method, the Company measures leases that exist at the adoption date and prior comparative periods are not adjusted. As a result of the adoption of Topic 842, the Company recorded a right of use asset and a lease liability of \$132,000 as of January 1, 2019 related to three operating leases with an average life of 5.75 years. During the first quarter of 2019, the Company entered into a new operating lease for office space. As a result, the Company recorded a right of use asset and a lease liability of \$221,000 related to this five year lease, which began during the second quarter of 2019. The change in lease accounting did not impact net earnings during the three months and nine months ended September 30, 2019 and was not material to the consolidated financial statements.

In March 2017, the Financial Accounting Standards Board issued ASU 2017-08, Receivables - Nonrefundable Fees and Other Costs (Subtopic 310-20): Premium Amortization on Purchased Callable Debt Securities. The amendments in this update shorten the amortization period for certain callable debt securities held at a premium. Specifically, the amendments require the premium to be amortized to the earliest call date. The amendments do not require an accounting change for securities held at a discount; the discount continues to be amortized to maturity. The provisions of this update become effective for interim and annual periods beginning after December 15, 2018. The Company adopted ASU 2017-08 effective January 1, 2019. Management has concluded that based on the Company’s current portfolio of investment securities that the adoption of these amendments will result in a shorter amortization period for investment security premiums; however, the impact was not material to interest income on investment securities.

2. Investments

A summary of investment securities available-for-sale is as follows:

(Dollars in thousands)

| | As of September 30, 2019 | | | |
|-----------------------------------|--------------------------|------------------------|-------------------------|----------------------|
| | Amortized cost | Gross unrealized gains | Gross unrealized losses | Estimated fair value |
| U. S. treasury securities | \$ 2,298 | \$ 16 | \$ - | \$ 2,314 |
| U. S. federal agency obligations | 4,015 | 98 | - | 4,113 |
| Municipal obligations, tax exempt | 149,193 | 3,565 | (80) | 152,678 |
| Municipal obligations, taxable | 47,479 | 1,620 | (2) | 49,097 |
| Agency mortgage-backed securities | 156,134 | 1,944 | (306) | 157,772 |
| Certificates of deposit | 3,343 | - | - | 3,343 |
| Total | \$ 362,462 | \$ 7,243 | \$ (388) | \$ 369,317 |

(Dollars in thousands)

| | As of December 31, 2018 | | | |
|-----------------------------------|-------------------------|------------------------|-------------------------|----------------------|
| | Amortized cost | Gross unrealized gains | Gross unrealized losses | Estimated fair value |
| U. S. treasury securities | \$ 1,999 | \$ - | \$ (28) | \$ 1,971 |
| U. S. federal agency obligations | 10,370 | 32 | (41) | 10,361 |
| Municipal obligations, tax exempt | 161,529 | 353 | (2,770) | 159,112 |
| Municipal obligations, taxable | 53,178 | 180 | (323) | 53,035 |
| Agency mortgage-backed securities | 158,765 | 264 | (2,953) | 156,076 |
| Certificates of deposit | 7,790 | - | - | 7,790 |
| Total | \$ 393,631 | \$ 829 | \$ (6,115) | \$ 388,345 |

The tables above show that some of the securities in the available-for-sale investment portfolio had unrealized losses, or were temporarily impaired, as of September 30, 2019 and December 31, 2018. This temporary impairment represents the estimated amount of loss that would be realized if the securities were sold on the valuation date. Securities which were temporarily impaired are shown below, along with the length of time in a continuous unrealized loss position.

(Dollars in thousands)

| | No. of securities | As of September 30, 2019 | | | | | |
|-----------------------------------|-------------------|--------------------------|-------------------|---------------------|-------------------|------------------|-------------------|
| | | Less than 12 months | | 12 months or longer | | Total | |
| | | Fair value | Unrealized losses | Fair value | Unrealized losses | Fair value | Unrealized losses |
| Municipal obligations, tax exempt | 35 | \$ 8,105 | \$ (27) | \$ 5,625 | \$ (53) | \$ 13,730 | \$ (80) |
| Municipal obligations, taxable | 7 | - | - | 1,551 | (2) | 1,551 | (2) |
| Agency mortgage-backed securities | 38 | 23,890 | (55) | 19,377 | (251) | 43,267 | (306) |
| Total | 80 | \$ 31,995 | \$ (82) | \$ 26,553 | \$ (306) | \$ 58,548 | \$ (388) |

(Dollars in thousands)

| | No. of securities | As of December 31, 2018 | | | | | |
|-----------------------------------|-------------------|-------------------------|-------------------|---------------------|-------------------|------------------|-------------------|
| | | Less than 12 months | | 12 months or longer | | Total | |
| | | Fair value | Unrealized losses | Fair value | Unrealized losses | Fair value | Unrealized losses |
| U.S. treasury securities | 1 | \$ - | \$ - | \$ 1,971 | \$ (28) | \$ 1,971 | \$ (28) |
| U. S. federal agency obligations | 6 | 145 | (1) | 7,970 | (40) | 8,115 | (41) |
| Municipal obligations, tax exempt | 296 | 35,898 | (367) | 85,921 | (2,403) | 121,819 | (2,770) |
| Municipal obligations, taxable | 86 | 8,293 | (22) | 28,984 | (301) | 37,277 | (323) |
| Agency mortgage-backed securities | 101 | 30,030 | (146) | 96,155 | (2,807) | 126,185 | (2,953) |
| Total | 490 | \$ 74,366 | \$ (536) | \$221,001 | \$ (5,579) | \$295,367 | \$ (6,115) |

The Company's portfolio of municipal obligations consists of both tax-exempt and taxable general obligations securities issued by various municipalities. The Company did not intend to sell and it was more likely than not that the Company will not be required to sell its municipal obligations in an unrealized loss position until the recovery of their costs. Due to the issuers' continued satisfaction of the securities' obligations in accordance with their contractual terms and the expectation that they will continue to do so, the evaluation of the fundamentals of the issuers' financial condition and other objective evidence, the Company believed that the municipal obligations identified in the tables above were temporarily impaired as of September 30, 2019 and December 31, 2018.

The Company's agency mortgage-backed securities portfolio consists of securities underwritten to the standards of and guaranteed by the government-sponsored agencies of Federal Home Loan Mortgage Corporation ("FHLMC"), Federal National Mortgage Association and the Government National Mortgage Association. The receipt of principal, at par, and interest on agency mortgage-backed securities is guaranteed by the respective government-sponsored agency guarantor, such that the Company believed that its agency mortgage-backed securities did not expose the Company to credit-related losses. Based on these factors, along with the Company's intent to not sell the securities and the Company's belief that it was more likely than not that the Company will not be required to sell the securities before recovery of their cost basis, the Company believed that the agency mortgage-backed securities identified in the tables above were temporarily impaired as of September 30, 2019 and December 31, 2018.

The table below sets forth amortized cost and fair value of investment securities at September 30, 2019. The table includes scheduled principal payments and estimated prepayments, based on observable market inputs, for agency mortgage-backed securities. Actual maturities will differ from contractual maturities because borrowers have the right to prepay obligations with or without prepayment penalties.

| <i>(Dollars in thousands)</i> | Amortized cost | Estimated fair value |
|---|-------------------|-------------------------|
| Due in less than one year | \$ 16,778 | \$ 16,796 |
| Due after one year but within five years | 186,606 | 188,671 |
| Due after five years but within ten years | 86,494 | 88,618 |
| Due after ten years | 72,584 | 75,232 |
| Total | <u>\$ 362,462</u> | <u>\$ 369,317</u> |

Sales proceeds and gross realized gains and losses on sales of available-for-sale securities are as follows:

| <i>(Dollars in thousands)</i> | Three months ended September 30, | | Nine months ended September 30, | |
|-------------------------------|-------------------------------------|----------------|------------------------------------|--------------|
| | 2019 | 2018 | 2019 | 2018 |
| Sales proceeds | \$ - | \$ 19,591 | \$ 9,491 | \$ 21,125 |
| Realized gains | \$ - | \$ 49 | \$ 2 | \$ 84 |
| Realized losses | - | (64) | (148) | (64) |
| Net realized losses | <u>\$ -</u> | <u>\$ (15)</u> | <u>\$ (146)</u> | <u>\$ 20</u> |

Securities with carrying values of \$248.0 million and \$249.7 million were pledged to secure public funds on deposit, repurchase agreements and as collateral for borrowings at September 30, 2019 and December 31, 2018, respectively. Except for U.S. federal agency obligations, no investment in a single issuer exceeded 10% of consolidated stockholders' equity.

3. Loans and Allowance for Loan Losses

Loans consisted of the following as of the dates indicated below:

| <i>(Dollars in thousands)</i> | <u>September 30, 2019</u> | <u>December 31, 2018</u> |
|--|---------------------------|--------------------------|
| One-to-four family residential real estate | \$ 141,801 | \$ 136,895 |
| Construction and land | 19,702 | 20,083 |
| Commercial real estate | 135,950 | 138,967 |
| Commercial | 101,150 | 74,289 |
| Agriculture | 100,958 | 96,632 |
| Municipal | 2,728 | 2,953 |
| Consumer | 24,150 | 25,428 |
| Total gross loans | <u>526,439</u> | <u>495,247</u> |
| Net deferred loan costs and loans in process | (27) | (109) |
| Allowance for loan losses | <u>(6,279)</u> | <u>(5,765)</u> |
| Loans, net | <u>\$ 520,133</u> | <u>\$ 489,373</u> |

The following tables provide information on the Company's activity in the allowance for loan losses by loan class:

(Dollars in thousands)

| | Three and nine months ended September 30, 2019 | | | | | | | |
|-------------------------------|--|-----------------------|------------------------|--------------|--------------|-----------|------------|--------------|
| | One-to-four residential real estate | Construction and land | Commercial real estate | Commercial | Agriculture | Municipal | Consumer | Total |
| Allowance for loan losses: | | | | | | | | |
| Balance at July 1, 2019 | \$ 441 | \$ 255 | \$ 1,758 | \$ 1,404 | \$ 2,260 | \$ 7 | \$ 141 | \$ 6,266 |
| Charge-offs | (15) | (31) | - | (284) | - | - | (81) | (411) |
| Recoveries | - | - | - | 1 | - | - | 23 | 24 |
| Provision for loan losses | 249 | (156) | (326) | 490 | 40 | (1) | 104 | 400 |
| Balance at September 30, 2019 | <u>675</u> | <u>68</u> | <u>1,432</u> | <u>1,611</u> | <u>2,300</u> | <u>6</u> | <u>187</u> | <u>6,279</u> |
| Balance at January 1, 2019 | | | | | | | | |
| Balance at January 1, 2019 | \$ 449 | \$ 168 | \$ 1,686 | \$ 1,051 | \$ 2,238 | \$ 7 | \$ 166 | \$ 5,765 |
| Charge-offs | (56) | (31) | - | (324) | - | - | (183) | (594) |
| Recoveries | 1 | - | - | 52 | - | 6 | 49 | 108 |
| Provision for loan losses | 281 | (69) | (254) | 832 | 62 | (7) | 155 | 1,000 |
| Balance at September 30, 2019 | <u>675</u> | <u>68</u> | <u>1,432</u> | <u>1,611</u> | <u>2,300</u> | <u>6</u> | <u>187</u> | <u>6,279</u> |

(Dollars in thousands)

| | Three and nine months ended September 30, 2018 | | | | | | | |
|-------------------------------|--|-----------------------|------------------------|--------------|--------------|-----------|------------|--------------|
| | One-to-four residential real estate | Construction and land | Commercial real estate | Commercial | Agriculture | Municipal | Consumer | Total |
| Allowance for loan losses: | | | | | | | | |
| Balance at July 1, 2018 | \$ 439 | \$ 109 | \$ 1,466 | \$ 1,693 | \$ 2,005 | \$ 7 | \$ 116 | \$ 5,835 |
| Charge-offs | - | - | - | (352) | - | - | (49) | (401) |
| Recoveries | 1 | - | - | 1 | - | - | 3 | 5 |
| Provision for loan losses | 109 | 6 | (19) | 191 | 99 | - | 64 | 450 |
| Balance at September 30, 2018 | <u>549</u> | <u>115</u> | <u>1,447</u> | <u>1,533</u> | <u>2,104</u> | <u>7</u> | <u>134</u> | <u>5,889</u> |
| Balance at January 1, 2018 | | | | | | | | |
| Balance at January 1, 2018 | \$ 542 | \$ 181 | \$ 1,540 | \$ 1,226 | \$ 1,812 | \$ 8 | \$ 150 | \$ 5,459 |
| Charge-offs | - | - | - | (381) | - | - | (126) | (507) |
| Recoveries | 3 | - | 1 | 3 | - | 2 | 28 | 37 |
| Provision for loan losses | 4 | (66) | (94) | 685 | 292 | (3) | 82 | 900 |
| Balance at September 30, 2018 | <u>549</u> | <u>115</u> | <u>1,447</u> | <u>1,533</u> | <u>2,104</u> | <u>7</u> | <u>134</u> | <u>5,889</u> |

The following tables provide information on the Company's activity in the allowance for loan losses by loan class and allowance methodology:

(Dollars in thousands)

| | As of September 30, 2019 | | | | | | | |
|-----------------------------------|--|-----------------------|------------------------|------------|-------------|-----------|-----------|-----------|
| | One-to-four family residential real estate | Construction and land | Commercial real estate | Commercial | Agriculture | Municipal | Consumer | Total |
| Allowance for loan losses: | | | | | | | | |
| Individually evaluated for loss | 316 | 7 | 112 | 228 | - | - | - | 663 |
| Collectively evaluated for loss | 359 | 61 | 1,320 | 1,383 | 2,300 | 6 | 187 | 5,616 |
| Total | 675 | 68 | 1,432 | 1,611 | 2,300 | 6 | 187 | 6,279 |
| Loan balances: | | | | | | | | |
| Individually evaluated for loss | 1,225 | 1,540 | 3,472 | 1,047 | 1,764 | 58 | 4 | 9,110 |
| Collectively evaluated for loss | 140,576 | 18,162 | 132,478 | 100,103 | 99,194 | 2,670 | 24,146 | 517,329 |
| Total | \$ 141,801 | \$ 19,702 | \$ 135,950 | \$ 101,150 | \$ 100,958 | \$ 2,728 | \$ 24,150 | \$526,439 |

(Dollars in thousands)

| | As of December 31, 2018 | | | | | | | |
|-----------------------------------|--|-----------------------|------------------------|------------|-------------|-----------|-----------|-----------|
| | One-to-four family residential real estate | Construction and land | Commercial real estate | Commercial | Agriculture | Municipal | Consumer | Total |
| Allowance for loan losses: | | | | | | | | |
| Individually evaluated for loss | 100 | 103 | 67 | 27 | 13 | - | - | 310 |
| Collectively evaluated for loss | 349 | 65 | 1,619 | 1,024 | 2,225 | 7 | 166 | 5,455 |
| Total | 449 | 168 | 1,686 | 1,051 | 2,238 | 7 | 166 | 5,765 |
| Loan balances: | | | | | | | | |
| Individually evaluated for loss | 623 | 1,808 | 3,912 | 1,528 | 717 | 58 | 45 | 8,691 |
| Collectively evaluated for loss | 136,272 | 18,275 | 135,055 | 72,761 | 95,915 | 2,895 | 25,383 | 486,556 |
| Total | \$ 136,895 | \$ 20,083 | \$ 138,967 | \$ 74,289 | \$ 96,632 | \$ 2,953 | \$ 25,428 | \$495,247 |

The Company's impaired loans increased from \$8.7 million at December 31, 2018 to \$9.1 million at September 30, 2019. The difference between the unpaid contractual principal and the impaired loan balance is a result of charge-offs recorded against impaired loans. The difference in the Company's non-accrual loan balances and impaired loan balances at September 30, 2019 and December 31, 2018, was related to troubled debt restructurings ("TDR") that are current and accruing interest, but still classified as impaired. Interest income recognized on a cash basis on impaired loans was immaterial during the three and nine month periods ended September 30, 2019 and 2018.

The following tables present information on impaired loans:

(Dollars in thousands)

| | As of September 30, 2019 | | | | | | |
|--|-------------------------------------|------------------------------|--|---|-----------------------------------|--|--|
| | <u>Unpaid contractual principal</u> | <u>Impaired loan balance</u> | <u>Impaired loans without an allowance</u> | <u>Impaired loans with an allowance</u> | <u>Related allowance recorded</u> | <u>Year-to-date average loan balance</u> | <u>Year-to-date interest income recognized</u> |
| One-to-four family residential real estate | \$ 1,266 | \$ 1,225 | \$ 855 | \$ 370 | \$ 316 | \$ 1,253 | \$ 8 |
| Construction and land | 3,275 | 1,540 | 1,348 | 192 | 7 | 195 | 28 |
| Commercial real estate | 3,472 | 3,472 | 3,269 | 203 | 112 | 3,504 | 357 |
| Commercial | 1,047 | 1,047 | 128 | 919 | 228 | 1,107 | 11 |
| Agriculture | 1,979 | 1,764 | 1,764 | - | - | 1,753 | 35 |
| Municipal | 58 | 58 | 58 | - | - | 58 | 1 |
| Consumer | 4 | 4 | 4 | - | - | 4 | - |
| Total impaired loans | <u>\$ 11,101</u> | <u>\$ 9,110</u> | <u>\$ 7,426</u> | <u>\$ 1,684</u> | <u>\$ 663</u> | <u>\$ 7,874</u> | <u>\$ 440</u> |

(Dollars in thousands)

| | As of December 31, 2018 | | | | | | |
|--|-------------------------------------|------------------------------|--|---|-----------------------------------|--|--|
| | <u>Unpaid contractual principal</u> | <u>Impaired loan balance</u> | <u>Impaired loans without an allowance</u> | <u>Impaired loans with an allowance</u> | <u>Related allowance recorded</u> | <u>Year-to-date average loan balance</u> | <u>Year-to-date interest income recognized</u> |
| One-to-four family residential real estate | \$ 623 | \$ 623 | \$ 413 | \$ 210 | \$ 100 | \$ 640 | \$ 10 |
| Construction and land | 3,543 | 1,808 | 1,383 | 425 | 103 | 2,689 | 53 |
| Commercial real estate | 3,912 | 3,912 | 2,120 | 1,792 | 67 | 3,928 | 487 |
| Commercial | 1,528 | 1,528 | 1,446 | 82 | 27 | 1,537 | - |
| Agriculture | 932 | 717 | 529 | 188 | 13 | 844 | 52 |
| Municipal | 58 | 58 | 58 | - | - | 58 | 1 |
| Consumer | 45 | 45 | 45 | - | - | 49 | - |
| Total impaired loans | <u>\$ 10,641</u> | <u>\$ 8,691</u> | <u>\$ 5,994</u> | <u>\$ 2,697</u> | <u>\$ 310</u> | <u>\$ 9,745</u> | <u>\$ 603</u> |

The Company's key credit quality indicator is a loan's performance status, defined as accruing or non-accruing. Performing loans are considered to have a lower risk of loss. Non-accrual loans are those which the Company believes have a higher risk of loss. The accrual of interest on non-performing loans is discontinued at the time the loan is ninety days delinquent, unless the credit is well secured and in process of collection. Loans are placed on non-accrual or are charged off at an earlier date if collection of principal or interest is considered doubtful. There were no loans 90 days or more delinquent and accruing interest at September 30, 2019 or December 31, 2018.

The following tables present information on the Company's past due and non-accrual loans by loan class:

(Dollars in thousands)

| | As of September 30, 2019 | | | | | | |
|--|------------------------------------|------------------------------------|---|-------------------------------|-------------------|--------------------------------------|--------------------------|
| | 30-59 days delinquent and accruing | 60-89 days delinquent and accruing | 90 days or more delinquent and accruing | Total past due loans accruing | Non-accrual loans | Total past due and non-accrual loans | Total loans not past due |
| One-to-four family residential real estate | \$ 71 | \$ 564 | \$ - | \$ 635 | \$ 1,053 | \$ 1,688 | \$140,113 |
| Construction and land | - | - | - | - | 904 | 904 | 18,798 |
| Commercial real estate | 15 | 328 | - | 343 | 1,449 | 1,792 | 134,158 |
| Commercial | 16 | 392 | - | 408 | 1,019 | 1,427 | 99,723 |
| Agriculture | 510 | 106 | - | 616 | 1,509 | 2,125 | 98,833 |
| Municipal | - | - | - | - | - | - | 2,728 |
| Consumer | 35 | 47 | - | 82 | 4 | 86 | 24,064 |
| Total | <u>\$ 647</u> | <u>\$ 1,437</u> | <u>\$ -</u> | <u>\$ 2,084</u> | <u>\$ 5,938</u> | <u>\$ 8,022</u> | <u>\$518,417</u> |
| Percent of gross loans | 0.12% | 0.28% | 0.00% | 0.40% | 1.13% | 1.53% | 98.47% |

(Dollars in thousands)

| | As of December 31, 2018 | | | | | | |
|--|------------------------------------|------------------------------------|---|-------------------------------|-------------------|--------------------------------------|--------------------------|
| | 30-59 days delinquent and accruing | 60-89 days delinquent and accruing | 90 days or more delinquent and accruing | Total past due loans accruing | Non-accrual loans | Total past due and non-accrual loans | Total loans not past due |
| One-to-four family residential real estate | \$ 131 | \$ 206 | \$ - | \$ 337 | \$ 442 | \$ 779 | \$136,116 |
| Construction and land | - | 134 | - | 134 | 948 | 1,082 | 19,001 |
| Commercial real estate | 465 | - | - | 465 | 1,791 | 2,256 | 136,711 |
| Commercial | 398 | 20 | - | 418 | 1,528 | 1,946 | 72,343 |
| Agriculture | 100 | 88 | - | 188 | 482 | 670 | 95,962 |
| Municipal | - | - | - | - | - | - | 2,953 |
| Consumer | 106 | 23 | - | 129 | 45 | 174 | 25,254 |
| Total | <u>\$ 1,200</u> | <u>\$ 471</u> | <u>\$ -</u> | <u>\$ 1,671</u> | <u>\$ 5,236</u> | <u>\$ 6,907</u> | <u>\$488,340</u> |
| Percent of gross loans | 0.24% | 0.10% | 0.00% | 0.34% | 1.06% | 1.40% | 98.60% |

Under the original terms of the Company's non-accrual loans, interest earned on such loans for the nine months ended September 30, 2019 and 2018 would have increased interest income by \$171,000 and \$205,000, respectively. No interest income related to non-accrual loans was included in interest income for the nine months ended September 30, 2019 and 2018.

The Company also categorizes loans into risk categories based on relevant information about the ability of the borrowers to service their debt such as current financial information, historical payment experience, credit documentation, public information and current economic trends, among other factors. The Company analyzes loans individually by classifying the loans as to credit risk. This analysis is performed on a quarterly basis. Non-classified loans generally include those loans that are expected to be repaid in accordance with contractual loan terms. Classified loans are those that are assigned a special mention, substandard or doubtful risk rating using the following definitions:

Special Mention: Loans are currently protected by the current net worth and paying capacity of the obligor or of the collateral pledged but such protection is potentially weak. These loans constitute an undue and unwarranted credit risk, but not to the point of justifying a classification of substandard. The credit risk may be relatively minor, yet constitutes an unwarranted risk in light of the circumstances surrounding a specific asset.

Substandard: Loans are inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged. Loans have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. Loans are characterized by the distinct possibility that the Company will sustain some loss if the deficiencies are not corrected.

Doubtful: Loans classified doubtful have all the weaknesses inherent in those classified as substandard, with the added characteristic that weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions and values, highly questionable and improbable.

The following table provides information on the Company's risk categories by loan class:

(Dollars in thousands)

| | As of September 30, 2019 | | As of December 31, 2018 | |
|--|--------------------------|------------------|-------------------------|------------------|
| | Non-classified | Classified | Non-classified | Classified |
| One-to-four family residential real estate | \$ 140,596 | \$ 1,205 | \$ 135,947 | \$ 948 |
| Construction and land | 18,798 | 904 | 19,135 | 948 |
| Commercial real estate | 130,913 | 5,037 | 126,619 | 12,348 |
| Commercial | 93,125 | 8,025 | 66,490 | 7,799 |
| Agriculture | 92,120 | 8,838 | 86,917 | 9,715 |
| Municipal | 2,728 | - | 2,953 | - |
| Consumer | 24,146 | 4 | 25,383 | 45 |
| Total | <u>\$ 502,426</u> | <u>\$ 24,013</u> | <u>\$ 463,444</u> | <u>\$ 31,803</u> |

At September 30, 2019, the Company had nine loan relationships consisting of 13 outstanding loans that were classified as TDRs. There were no loans classified as TDRs during the first nine months of 2019.

There were no loans classified as TDRs during the third quarter of 2018. An agriculture loan relationship consisting of two loans that were originally classified as TDRs during 2015 and a municipal loan that was classified as a TDR in 2010 were both paid off in the third quarter of 2018. During the second quarter of 2018, the Company classified an agriculture loan totaling \$64,000 as a TDR after originating a loan to an existing loan relationship that was classified as a TDR in 2016. As part of the restructuring the borrower paid off three loans previously classified as TDRs. Since the agriculture loan relationship was adequately secured, no impairments were recorded against the principal as of September 30, 2018. The Company also classified a \$41,000 commercial loan as a TDR after extending the maturity of the loan during the second quarter of 2018. The commercial loan had an \$11,000 impairment recorded against the principal balance as of September 30, 2018. There were no new loans classified as TDRs during the first three months of 2018.

The Company evaluates each TDR individually and returns the loan to accrual status when a payment history is established after the restructuring and future payments are reasonably assured. There were no loans modified as TDRs for which there was a payment default within 12 months of modification as of September 30, 2019 and 2018. The Company did not record any charge-offs against loans classified as TDRs in the first nine months of 2019 or 2018. No provision for loan losses related to TDRs was recorded in the three months ended September 30, 2019. A credit provision for loan losses of \$25,000 related to TDRs was recorded in the three months ended September 30, 2018. A credit provision for loan losses of \$1,000 and \$116,000 related to TDRs was recorded in the nine months ended September 30, 2019 and 2018, respectively. The Company allocated \$9,000 and \$10,000 of the allowance for loan losses against loans classified as TDRs at September 30, 2019 and December 31, 2018, respectively.

The following table presents information on loans that are classified as TDRs:

(Dollars in thousands)

| | As of September 30, 2019 | | | As of December 31, 2018 | | |
|--|--------------------------|---------------------|------------------|-------------------------|---------------------|------------------|
| | Number of loans | Non-accrual balance | Accruing balance | Number of loans | Non-accrual balance | Accruing balance |
| One-to-four family residential real estate | 2 | \$ - | \$ 172 | 2 | \$ - | \$ 181 |
| Construction and land | 4 | 513 | 636 | 4 | 523 | 860 |
| Commercial real estate | 1 | - | 2,023 | 2 | - | 2,121 |
| Commercial | 1 | - | 28 | 1 | 36 | - |
| Agriculture | 4 | - | 255 | 4 | 23 | 235 |
| Municipal | 1 | - | 58 | 1 | - | 58 |
| Total troubled debt restructurings | <u>13</u> | <u>\$ 513</u> | <u>\$ 3,172</u> | <u>14</u> | <u>\$ 582</u> | <u>\$ 3,455</u> |

4. Goodwill and Other Intangible Assets

The Company tests goodwill for impairment annually or more frequently if circumstances warrant. The Company's annual step one impairment test as of December 31, 2018 concluded that its goodwill was not impaired. The Company concluded there were no triggering events during the first nine months of 2019 that required an interim goodwill impairment test.

Lease intangible assets are amortized over the life of the lease. Core deposit intangible assets are amortized over the estimated useful life of ten years on an accelerated basis. Mortgage servicing rights are amortized over the estimated life of the mortgage loan serviced for others. A summary of the other intangible assets that continue to be subject to amortization is as follows:

(Dollars in thousands)

| | As of September 30, 2019 | | |
|--------------------------------|--------------------------|--------------------------|---------------------|
| | Gross carrying amount | Accumulated amortization | Net carrying amount |
| Core deposit intangible assets | \$ 2,018 | \$ (1,669) | \$ 349 |
| Lease intangible asset | 350 | (267) | 83 |
| Mortgage servicing rights | 6,783 | (4,381) | 2,402 |
| Total other intangible assets | <u>\$ 9,151</u> | <u>\$ (6,317)</u> | <u>\$ 2,834</u> |

(Dollars in thousands)

| | As of December 31, 2018 | | |
|--------------------------------|-------------------------|--------------------------|---------------------|
| | Gross carrying amount | Accumulated amortization | Net carrying amount |
| Core deposit intangible assets | \$ 2,067 | \$ (1,588) | \$ 479 |
| Lease intangible asset | 350 | (233) | 117 |
| Mortgage servicing rights | 6,545 | (4,050) | 2,495 |
| Total other intangible assets | <u>\$ 8,962</u> | <u>\$ (5,871)</u> | <u>\$ 3,091</u> |

The following sets forth estimated amortization expense for core deposit and lease intangible assets for the remainder of 2019 and in successive years ending December 31:

(Dollars in thousands)

| | Amortization expense |
|-------------------|----------------------|
| Remainder of 2019 | \$ 50 |
| 2020 | 177 |
| 2021 | 121 |
| 2022 | 58 |
| 2023 | 26 |
| Total | <u>\$ 432</u> |

Mortgage loans serviced for others are not reported as assets. The following table provides information on the principal balances of mortgage loans serviced for others:

(Dollars in thousands)

| | September 30, 2019 | December 31, 2018 |
|-------|--------------------|-------------------|
| FHLMC | \$ 512,167 | \$ 521,489 |
| FHLB | 28,878 | 10,603 |
| Total | <u>\$ 541,045</u> | <u>\$ 532,092</u> |

Custodial escrow balances maintained in connection with serviced loans were \$8.3 million and \$4.5 million at September 30, 2019 and December 31, 2018, respectively. Gross service fee income related to such loans was \$344,000 and \$337,000 for the three months ended September 30, 2019 and 2018, respectively, and is included in fees and service charges in the consolidated statements of earnings. Gross service fee income related to such loans was \$1.0 million for the nine months ended September 30, 2019 and 2018.

Activity for mortgage servicing rights and the related valuation allowance was as follows:

(Dollars in thousands)

| | Three months ended September 30, | | Nine months ended September 30, | |
|-----------------------------------|-------------------------------------|-----------------|------------------------------------|-----------------|
| | 2019 | 2018 | 2019 | 2018 |
| Mortgage servicing rights: | | | | |
| Balance at beginning of period | \$ 2,372 | \$ 2,639 | \$ 2,495 | \$ 2,811 |
| Additions | 308 | 150 | 630 | 409 |
| Amortization | (278) | (214) | (723) | (645) |
| Balance at end of period | <u>\$ 2,402</u> | <u>\$ 2,575</u> | <u>\$ 2,402</u> | <u>\$ 2,575</u> |

The fair value of mortgage servicing rights was \$4.9 million and \$6.2 million at September 30, 2019 and December 31, 2018, respectively. Fair value at September 30, 2019 was determined using discount rates ranging from 9.00% to 11.00%; prepayment speeds ranging from 6.00% to 24.13%, depending on the stratification of the specific mortgage servicing right; and a weighted average default rate of 1.40%. Fair value at December 31, 2018 was determined using discount rates ranging from 9.00% to 11.00%, prepayment speeds ranging from 6.00% to 22.40%, depending on the stratification of the specific mortgage servicing right, and a weighted average default rate of 1.37%.

The Company had a mortgage repurchase reserve of \$235,000 at both September 30, 2019 and December 31, 2018, which represents the Company's best estimate of probable losses that the Company will incur related to the repurchase of one-to-four family residential real estate loans previously sold or to reimburse investors for credit losses incurred on loans previously sold where a breach of the contractual representations and warranties occurred. The Company did not incur any losses charged against the reserve or make any provisions to the reserve during the first nine months of 2019 and 2018. As of September 30, 2019, the Company did not have any outstanding mortgage repurchase requests.

5. Earnings per Share

Basic earnings per share have been computed based upon the weighted average number of common shares outstanding during each period. Diluted earnings per share include the effect of all potential common shares outstanding during each period. The shares used in the calculation of basic and diluted earnings per share are shown below:

| | Three months ended September 30, | | Nine months ended September 30, | |
|--|-------------------------------------|------------------|------------------------------------|------------------|
| | 2019 | 2018 | 2019 | 2018 |
| <i>(Dollars in thousands, except per share amounts)</i> | | | | |
| Net earnings (1) | \$ 2,613 | \$ 3,020 | \$ 7,394 | \$ 7,964 |
| Weighted average common shares outstanding - basic (1) | 4,374,344 | 4,365,917 | 4,372,867 | 4,342,896 |
| Assumed exercise of stock options (1) | 14,924 | 17,846 | 14,503 | 17,140 |
| Weighted average common shares outstanding - diluted (1) | <u>4,389,268</u> | <u>4,383,763</u> | <u>4,387,370</u> | <u>4,360,036</u> |
| Net earnings per share (1): | | | | |
| Basic | \$ 0.60 | \$ 0.69 | \$ 1.69 | \$ 1.83 |
| Diluted | \$ 0.60 | \$ 0.69 | \$ 1.69 | \$ 1.83 |

(1) Share and per share values for the periods ended September 30, 2018 have been adjusted to give effect to the 5% stock dividend paid during December 2018.

The diluted earnings per share computations for the three months ended September 30, 2019 and 2018 excluded 95,264 and 30,859, respectively, of unexercised stock options because their inclusion would have been anti-dilutive during such periods. The diluted earnings per share computations for the nine months ended September 30, 2019 and 2018 excluded 95,264 and 30,859, respectively, of unexercised stock options because their inclusion would have been anti-dilutive during such periods.

6. Repurchase Agreements

The Company has overnight repurchase agreements with certain deposit customers whereby the Company uses investment securities as collateral for non-insured funds. These balances are accounted for as collateralized financing and included in other borrowings on the balance sheet. The following is a summary of the balances of and collateral for the Company's repurchase agreements:

| | As of September 30, 2019 | | | | |
|-----------------------------------|-----------------------------|------------------|-------------|-------------------------|------------------|
| | Overnight and Continuous | Up to 30 days | 30-90 days | Greater than 90 days | Total |
| Repurchase agreements: | | | | | |
| U.S. federal treasury obligations | \$ 649 | \$ - | \$ - | \$ - | \$ 649 |
| U.S. federal agency obligations | 1,895 | - | - | - | 1,895 |
| Agency mortgage-backed securities | 13,735 | - | - | - | 13,735 |
| Total | <u>\$ 16,279</u> | <u>\$ -</u> | <u>\$ -</u> | <u>\$ -</u> | <u>\$ 16,279</u> |

| | As of December 31, 2018 | | | | |
|-----------------------------------|-----------------------------|------------------|-------------|-------------------------|------------------|
| | Overnight and Continuous | Up to 30 days | 30-90 days | Greater than 90 days | Total |
| Repurchase agreements: | | | | | |
| U.S. federal treasury obligations | \$ 416 | \$ - | \$ - | \$ - | \$ 416 |
| U.S. federal agency obligations | 5,626 | - | - | - | 5,626 |
| Agency mortgage-backed securities | 9,204 | - | - | - | 9,204 |
| Total | <u>\$ 15,246</u> | <u>\$ -</u> | <u>\$ -</u> | <u>\$ -</u> | <u>\$ 15,246</u> |

Repurchase agreements are comprised of non-insured customer funds, totaling \$16.3 million at September 30, 2019, and \$15.2 million at December 31, 2018, which were secured by \$19.7 million and \$18.6 million of the Company's investment portfolio at the same dates, respectively.

The investment securities are held by a third-party financial institution in the customer's custodial account. The Company is required to maintain adequate collateral for each repurchase agreement. Changes in the fair value of the investment securities impact the amount of collateral required. If the Company were to default, the investment securities would be used to settle the repurchase agreement with the deposit customer.

7. Revenue from Contracts with Customers

All of the Company's revenue from contracts with customers in the scope of ASC 606 is recognized within non-interest income. Items outside the scope of ASC 606 are noted as such.

| <i>(Dollars in thousands)</i> | Three months ended | | Nine months ended | |
|--|--------------------|-----------------|-------------------|------------------|
| | September 30, | | September 30, | |
| | 2019 | 2018 | 2019 | 2018 |
| Non-interest income: | | | | |
| Service charges on deposits | | | | |
| Overdraft fees | \$ 979 | \$ 828 | \$ 2,633 | \$ 2,408 |
| Other | 165 | 113 | 435 | 386 |
| Interchange income | 532 | 494 | 1,505 | 1,452 |
| Loan servicing fees (1) | 344 | 337 | 1,017 | 1,010 |
| Office lease income (1) | 158 | 160 | 481 | 468 |
| Gains on sales of loans (1) | 2,081 | 1,476 | 4,943 | 4,105 |
| Bank owned life insurance income (1) | 159 | 160 | 478 | 481 |
| Gains (losses) on sales of investment securities (1) | - | (15) | (146) | 20 |
| Gains (losses) on sales of real estate owned | (2) | (42) | 2 | (41) |
| Other | 139 | 1,056 | 451 | 1,932 |
| Total non-interest income | \$ 4,555 | \$ 4,567 | \$ 11,799 | \$ 12,221 |

(1) Not within the scope of ASC 606.

A description of the Company's revenue streams within the scope of ASC 606 follows:

Service Charges on Deposit Accounts

The Company earns fees from its deposit customers for transaction-based, account maintenance, and overdraft services. Transaction-based fees, which include services such as ATM usage fees, stop payment charges, statement rendering, and ACH fees, are recognized at the time the transaction is executed as that is the point in time the Company fulfills the customer's request. Account maintenance fees, which relate primarily to monthly maintenance, are earned over the course of a month, representing the period during which the Company satisfies the performance obligation. Overdraft fees are recognized at the point in time that the overdraft occurs. Service charges on deposits are withdrawn from the customer's account balance.

Interchange Income

The Company earns interchange fees from debit cardholder transactions conducted through the interchange payment network. Interchange fees from cardholder transactions represent a percentage of the underlying transaction value and are recognized daily, concurrently with the transaction processing services provided to the cardholder.

Gains (Losses) on Sales of Real Estate Owned

The Company records a gain or loss from the sale of real estate owned when control of the property transfers to the buyer, which generally occurs at the time of an executed deed. When the Company finances the sale of real estate owned to the buyer, the Company assesses whether the buyer is committed to perform their obligations under the contract and whether collectability of the transaction price is probable. Once these criteria are met, the real estate owned asset is derecognized, and the gain or loss on sale is recorded upon the transfer of control of the property to the buyer. In determining the gain or loss on the sale, the Company adjusts the transaction price and related gain (loss) on sale if a significant financing component is present. There were no sales of real estate owned that were financed by the Company during the first nine months of 2019 or 2018.

8. Fair Value of Financial Instruments and Fair Value Measurements

Fair value is the exchange price that would be received for an asset or paid to transfer a liability (exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. There are three levels of inputs that may be used to measure fair values:

Level 1 – Quoted prices (unadjusted) for identical assets or liabilities in active markets that the entity has the ability to access as of the measurement date.

Level 2 – Significant other observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data.

Level 3 – Significant unobservable inputs that reflect a company’s own assumptions about the assumptions that market participants would use in pricing an asset or liability.

Fair value estimates of the Company’s financial instruments as of September 30, 2019 and December 31, 2018, including methods and assumptions utilized, are set forth below:

(Dollars in thousands)

| | As of September 30, 2019 | | | | |
|--|--------------------------|--------------|-----------|---------|--------------|
| | Carrying amount | Level 1 | Level 2 | Level 3 | Total |
| Financial assets: | | | | | |
| Cash and cash equivalents | \$ 21,736 | \$ 21,736 | \$ - | \$ - | \$ 21,736 |
| Investment securities available-for-sale | 369,317 | 2,314 | 367,003 | - | 369,317 |
| Bank stocks, at cost | 3,231 | n/a | n/a | n/a | n/a |
| Loans, net | 520,133 | - | - | 526,049 | 526,049 |
| Loans held for sale, net | 15,049 | - | 15,049 | - | 15,049 |
| Accrued interest receivable | 4,958 | 11 | 1,977 | 2,970 | 4,958 |
| Derivative financial instruments | 858 | - | 858 | - | 858 |
| Financial liabilities: | | | | | |
| Non-maturity deposits | \$ (636,328) | \$ (636,328) | \$ - | \$ - | \$ (636,328) |
| Time deposits | (197,426) | - | (196,600) | - | (196,600) |
| FHLB borrowings | (17,200) | - | (17,200) | - | (17,200) |
| Subordinated debentures | (21,651) | - | (19,563) | - | (19,563) |
| Other borrowings | (16,279) | - | (16,279) | - | (16,279) |
| Accrued interest payable | (572) | - | (572) | - | (572) |
| Derivative financial instruments | (20) | - | (20) | - | (20) |

| | As of December 31, 2018 | | | | |
|--|-------------------------|-----------|-----------|---------|-----------|
| | Carrying amount | Level 1 | Level 2 | Level 3 | Total |
| Financial assets: | | | | | |
| Cash and cash equivalents | \$ 19,114 | \$ 19,114 | \$ - | \$ - | \$ 19,114 |
| Investment securities available-for-sale | 388,345 | 1,971 | 386,374 | - | 388,345 |
| Bank stocks, at cost | 4,776 | n/a | n/a | n/a | n/a |
| Loans, net | 489,373 | - | - | 494,473 | 494,473 |
| Loans held for sale | 4,743 | - | 4,743 | - | 4,743 |
| Accrued interest receivable | 4,631 | - | 2,194 | 2,437 | 4,631 |
| Derivative financial instruments | 522 | - | 522 | - | 522 |
| Financial liabilities: | | | | | |
| Non-maturity deposits | (656,628) | (656,628) | - | - | (656,628) |
| Time deposits | (167,020) | - | (164,994) | - | (164,994) |
| FHLB borrowings | (20,000) | - | (20,000) | - | (20,000) |
| Subordinated debentures | (21,651) | - | (19,678) | - | (19,678) |
| Other borrowings | (15,246) | - | (15,246) | - | (15,246) |
| Accrued interest payable | (442) | - | (442) | - | (442) |
| Derivative financial instruments | (25) | - | (25) | - | (25) |

Transfers

The Company did not transfer any assets or liabilities among levels during the nine months ended September 30, 2019 or during the year ended December 31, 2018.

Valuation Methods for Instruments Measured at Fair Value on a Recurring Basis

The following tables represent the Company's financial instruments that are measured at fair value on a recurring basis at September 30, 2019 and December 31, 2018 allocated to the appropriate fair value hierarchy:

(Dollars in thousands)

| | As of September 30, 2019 | | | |
|---|--------------------------|----------------------|---------|---------|
| | Total | Fair value hierarchy | | |
| | | Level 1 | Level 2 | Level 3 |
| Assets: | | | | |
| Available-for-sale investment securities: | | | | |
| U. S. treasury securities | \$ 2,314 | \$ 2,314 | \$ - | \$ - |
| U. S. federal agency obligations | 4,113 | - | 4,113 | - |
| Municipal obligations, tax exempt | 152,678 | - | 152,678 | - |
| Municipal obligations, taxable | 49,097 | - | 49,097 | - |
| Agency mortgage-backed securities | 157,772 | - | 157,772 | - |
| Certificates of deposit | 3,343 | - | 3,343 | - |
| Loans held for sale | 15,049 | - | 15,049 | - |
| Derivative financial instruments | 858 | - | 858 | - |
| Liability: | | | | |
| Derivative financial instruments | (20) | - | (20) | - |
| | As of December 31, 2018 | | | |
| | Total | Fair value hierarchy | | |
| | | Level 1 | Level 2 | Level 3 |
| Assets: | | | | |
| Available-for-sale investment securities: | | | | |
| U. S. treasury securities | \$ 1,971 | \$ 1,971 | \$ - | \$ - |
| U. S. federal agency obligations | 10,361 | - | 10,361 | - |
| Municipal obligations, tax exempt | 159,112 | - | 159,112 | - |
| Municipal obligations, taxable | 53,035 | - | 53,035 | - |
| Agency mortgage-backed securities | 156,076 | - | 156,076 | - |
| Certificates of deposit | 7,790 | - | 7,790 | - |
| Loans held for sale | 4,743 | - | 4,743 | - |
| Derivative financial instruments | 522 | - | 522 | - |
| Liabilities: | | | | |
| Derivative financial instruments | (25) | - | (25) | - |

The Company's investment securities classified as available-for-sale include U.S. treasury securities, U.S. federal agency obligations, municipal obligations, agency mortgage-backed securities and certificates of deposits. Quoted exchange prices are available for the Company's U.S. treasury securities, which are classified as Level 1. U.S. federal agency securities and agency mortgage-backed securities are priced utilizing industry-standard models that consider various assumptions, including time value, yield curves, volatility factors, prepayment speeds, default rates, loss severity, current market and contractual prices for the underlying financial instruments, as well as other relevant economic measures. Substantially all of these assumptions are observable in the marketplace, can be derived from observable data, or are supported by observable levels at which transactions are executed in the marketplace. These measurements are classified as Level 2. Municipal obligations are valued using a type of matrix, or grid, pricing in which securities are benchmarked against U.S. treasury rates based on credit rating. These model and matrix measurements are classified as Level 2 in the fair value hierarchy.

Changes in the fair value of available-for-sale securities are included in other comprehensive income to the extent the changes are not considered other-than-temporary impairments. Other-than-temporary impairment tests are performed on a quarterly basis and any decline in the fair value of an individual security below its cost that is deemed to be other-than-temporary results in a write-down of that security's cost basis.

Mortgage loans originated and intended for sale in the secondary market are carried at fair value. The mortgage loan valuations are based on quoted secondary market prices for similar loans and are classified as Level 2. Changes in the fair value of mortgage loans originated and intended for sale in the secondary market and derivative financial instruments are included in gains on sales of loans.

The aggregate fair value, contractual balance (including accrued interest), and gain on loans held for sale were as follows:

| <i>(Dollars in thousands)</i> | As of September 30, 2019 | As of December 31, 2018 |
|-------------------------------|-----------------------------|----------------------------|
| Aggregate fair value | \$ 15,049 | \$ 4,743 |
| Contractual balance | 14,906 | 4,687 |
| Gain | <u>\$ 143</u> | <u>\$ 56</u> |

The Company's derivative financial instruments consist of interest rate lock commitments and corresponding forward sales contracts on mortgage loans held for sale. The fair values of these derivatives are based on quoted prices for similar loans in the secondary market. The market prices are adjusted by a factor, based on the Company's historical data and its judgment about future economic trends, which considers the likelihood that a commitment will ultimately result in a closed loan. These instruments are classified as Level 2. The amounts are included in other assets or other liabilities on the consolidated balance sheets and gains on sales of loans, net in the consolidated statements of earnings. The total amount of gains from changes in fair value of loans held for sale included in earnings were as follows:

| <i>(Dollars in thousands)</i> | Three months ended September 30, | | Nine months ended September 30, | |
|-------------------------------|-------------------------------------|----------------|------------------------------------|---------------|
| | 2019 | 2018 | 2019 | 2018 |
| Interest income | \$ 139 | \$ 100 | \$ 309 | \$ 246 |
| Change in fair value | (115) | (185) | 87 | (20) |
| Total change in fair value | <u>\$ 24</u> | <u>\$ (85)</u> | <u>\$ 396</u> | <u>\$ 226</u> |

Valuation Methods for Instruments Measured at Fair Value on a Non-recurring Basis

The Company does not value its loan portfolio at fair value. Collateral-dependent impaired loans are generally carried at the lower of cost or fair value of the collateral, less estimated selling costs. Collateral values are determined based on appraisals performed by qualified licensed appraisers hired by the Company and then further adjusted if warranted based on relevant facts and circumstances. The appraisals may utilize a single valuation approach or a combination of approaches including the comparable sales and income approach. Adjustments are routinely made in the appraisal process by the appraisers to adjust for differences between the comparable sales and income data available. Such adjustments are typically significant and result in a Level 3 classification of the inputs for determining fair value. Impaired loans are reviewed and evaluated at least quarterly for additional impairment and adjusted accordingly, based on the same factors identified above. The carrying value of the Company's impaired loans was \$9.1 million and \$8.7 million, with an allocated allowance of \$663,000 and \$310,000, at September 30, 2019 and December 31, 2018, respectively.

Real estate owned includes assets acquired through, or in lieu of, foreclosure and land previously acquired for expansion. Real estate owned is initially recorded at the fair value of the collateral less estimated selling costs. Subsequent valuations are updated periodically and are based upon independent appraisals, third party price opinions or internal pricing models. The appraisals may utilize a single valuation approach or a combination of approaches including the comparable sales and income approach. Adjustments are routinely made in the appraisal process by the appraisers to adjust for differences between the comparable sales and income data available. Such adjustments are typically significant and result in a Level 3 classification of the inputs for determining fair value. Real estate owned is reviewed and evaluated at least annually for additional impairment and adjusted accordingly, based on the same factors identified above.

The following tables represent the Company's financial instruments that are measured at fair value on a non-recurring basis as of September 30, 2019 and December 31, 2018 allocated to the appropriate fair value hierarchy:

(Dollars in thousands)

| | As of September 30, 2019 | | | | Total (losses)/ gains |
|--|--------------------------|----------------------|---------|---------|-----------------------------|
| | Total | Fair value hierarchy | | | |
| | | Level 1 | Level 2 | Level 3 | |
| Assets: | | | | | |
| Impaired loans: | | | | | |
| One-to-four family residential real estate | \$ 54 | \$ - | \$ - | \$ 54 | \$ (222) |
| Construction and land | 185 | - | - | 185 | (6) |
| Commercial real estate | 91 | - | - | 91 | (112) |
| Commercial | 691 | - | - | 691 | (164) |
| Real estate owned: | | | | | |
| One-to-four family residential real estate | 14 | - | - | 14 | (6) |
| | As of December 31, 2018 | | | | Total (losses)/ gains |
| | Total | Fair value hierarchy | | | |
| | | Level 1 | Level 2 | Level 3 | |
| Assets: | | | | | |
| Impaired loans: | | | | | |
| One-to-four family residential real estate | \$ 110 | \$ - | \$ - | \$ 110 | \$ (29) |
| Construction and land | 322 | - | - | 322 | (103) |
| Commercial real estate | 1,725 | - | - | 1,725 | 377 |
| Commercial | 55 | - | - | 55 | (51) |
| Agriculture | 175 | - | - | 175 | 11 |

The following table presents quantitative information about Level 3 fair value measurements for impaired loans measured at fair value on a non-recurring basis as of September 30, 2019 and December 31, 2018.

(Dollars in thousands)

| | Fair value | Valuation technique | Unobservable inputs | Range |
|--|------------|---------------------|--------------------------------|--------|
| As of September 30, 2019 | | | | |
| Impaired loans: | | | | |
| One-to-four family residential real estate | \$ 54 | Sales comparison | Adjustment to appraised value | 0%-25% |
| Construction and land | 185 | Sales comparison | Adjustment to appraised value | 25% |
| Commercial real estate | 91 | Sales comparison | Adjustment to appraised value | 20% |
| Commercial | 691 | Sales comparison | Adjustment to comparable sales | 0%-75% |
| Real estate owned: | | | | |
| One-to-four family residential real estate | 14 | Sales comparison | Adjustment to appraised value | 15% |
| As of December 31, 2018 | | | | |
| Impaired loans: | | | | |
| One-to-four family residential real estate | \$ 110 | Sales comparison | Adjustment to appraised value | 0%-20% |
| Construction and land | 322 | Sales comparison | Adjustment to appraised value | 0%-25% |
| Commercial real estate | 1,725 | Sales comparison | Adjustment to appraised value | 0% |
| Commercial | 55 | Sales comparison | Adjustment to comparable sales | 0%-15% |
| Agriculture | 175 | Sales comparison | Adjustment to appraised value | 0% |

9. Regulatory Capital Requirements

Banks and bank holding companies are subject to regulatory capital requirements administered by federal banking agencies. Capital adequacy guidelines and, additionally for banks, prompt corrective action regulations involve quantitative measures of assets, liabilities, and certain off-balance-sheet items calculated under regulatory accounting practices. Capital amounts and classifications are also subject to qualitative judgments by regulators. Failure to meet capital requirements can initiate regulatory action. Management believed that as of September 30, 2019, the Company and the Bank met all capital adequacy requirements to which they were subject at that time.

Prompt corrective action regulations provide five classifications: well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized, and critically undercapitalized, although these terms are not used to represent overall financial condition. If adequately capitalized, regulatory approval is required to accept brokered deposits. If undercapitalized, capital distributions are limited, as is asset growth and expansion, and capital restoration plans are required. The Company and the Bank are subject to the Basel III Rule, which is applicable to all U.S. banks that are subject to minimum capital requirements, as well as to bank and savings and loan holding companies other than “small bank holding companies” (generally, non-public bank holding companies with consolidated assets of less than \$3.0 billion).

The Basel III Rule includes a common equity Tier 1 capital to risk-weighted assets minimum ratio of 4.5%, a minimum ratio of Tier 1 capital to risk-weighted assets of 6.0%, a minimum ratio of Total Capital to risk-weighted assets of 8.0%, and a minimum Tier 1 leverage ratio of 4.0%. A capital conservation buffer, comprised of common equity Tier 1 capital, is also established above the regulatory minimum capital requirements. This capital conservation buffer was 1.875% for 2018, and increased to its final level of 2.5% on January 1, 2019. The capital conservation buffer increases the common equity Tier 1 capital ratio, and Tier 1 capital and total risk based capital ratios.

As of September 30, 2019 and December 31, 2018, the most recent regulatory notifications categorized the Bank as well capitalized under the regulatory framework for prompt corrective action then in effect. There are no conditions or events since that notification that management believes have changed the institution’s category.

The following is a comparison of the Company’s regulatory capital to minimum capital requirements at September 30, 2019 and December 31, 2018:

(Dollars in thousands)

| | Actual | | For capital adequacy purposes | |
|---------------------------------|------------|--------|-------------------------------|-----------|
| | Amount | Ratio | Amount | Ratio (1) |
| As of September 30, 2019 | | | | |
| Leverage | \$ 104,358 | 10.63% | \$ 39,263 | 4.0% |
| Common Equity Tier 1 Capital | 83,358 | 12.92% | 45,158 | 7.0% |
| Tier 1 Capital | 104,358 | 16.18% | 54,835 | 8.5% |
| Total Risk Based Capital | 110,777 | 17.17% | 67,737 | 10.5% |
| As of December 31, 2018 | | | | |
| Leverage | \$ 99,150 | 10.34% | \$ 38,373 | 4.0% |
| Common Equity Tier 1 Capital | 78,150 | 13.12% | 37,982 | 6.4% |
| Tier 1 Capital | 99,150 | 16.64% | 46,919 | 7.9% |
| Total Risk Based Capital | 105,055 | 17.63% | 58,835 | 9.9% |

- (1) The required ratios for capital adequacy purposes include a capital conservation buffer of 2.5% for September 30, 2019 and 1.875% for December 31, 2018

The following is a comparison of the Bank's regulatory capital to minimum capital requirements at September 30, 2019 and December 31, 2018:

(Dollars in thousands)

| | Actual | | For capital adequacy purposes | | To be well-capitalized under prompt corrective action provisions | |
|---------------------------------|------------|--------|-------------------------------|----------|--|-------|
| | Amount | Ratio | Amount | Ratio(1) | Amount | Ratio |
| As of September 30, 2019 | | | | | | |
| Leverage | \$ 101,965 | 10.42% | \$ 39,141 | 4.0% | \$ 48,927 | 5.0% |
| Common Equity Tier 1 Capital | 101,965 | 15.83% | 45,089 | 7.0% | 41,869 | 6.5% |
| Tier 1 Capital | 101,965 | 15.83% | 54,751 | 8.5% | 51,531 | 8.0% |
| Total Risk Based Capital | 108,384 | 16.83% | 67,634 | 10.5% | 64,413 | 10.0% |
| As of December 31, 2018 | | | | | | |
| Leverage | \$ 97,112 | 10.15% | \$ 38,254 | 4.0% | \$ 47,818 | 5.0% |
| Common Equity Tier 1 Capital | 97,112 | 16.33% | 37,922 | 6.4% | 38,665 | 6.5% |
| Tier 1 Capital | 97,112 | 16.33% | 46,844 | 7.9% | 47,588 | 8.0% |
| Total Risk Based Capital | 103,017 | 17.32% | 58,741 | 9.9% | 59,485 | 10.0% |

(1) The required ratios for capital adequacy purposes include a capital conservation buffer of 2.5% for September 30, 2019 and 1.875% for December 31, 2018.

10. Impact of Recent Accounting Pronouncements

In June 2016, the FASB issued ASU 2016-13, Financial Instruments - Credit Losses (Topic 326), commonly referred to as "CECL." The provisions of the update eliminate the probable initial recognition threshold under current GAAP which requires reserves to be based on an incurred loss methodology. Under CECL, reserves required for financial assets measured at amortized cost will reflect an organization's estimate of all expected credit losses over the expected term of the financial asset and thereby require the use of reasonable and supportable forecasts to estimate future credit losses. Because CECL encompasses all financial assets carried at amortized cost, the requirement that reserves be established based on an organization's reasonable and supportable estimate of expected credit losses extends to held to maturity debt securities. Under the provisions of the update, credit losses recognized on available for sale debt securities will be presented as an allowance as opposed to a write-down. In addition, CECL will modify the accounting for purchased loans so that reserves are established at the date of acquisition for purchased loans. Under current GAAP a purchased loan's contractual balance is adjusted to fair value through a credit discount, and no reserve is recorded on the purchased loan upon acquisition. Since under CECL reserves will be established for purchased loans at the time of acquisition, the accounting for purchased loans is made more comparable to the accounting for originated loans. Finally, increased disclosure requirements under CECL oblige organizations to present the currently required credit quality disclosures disaggregated by the year of origination or vintage. FASB expects that the evaluation of underwriting standards and credit quality trends by financial statement users will be enhanced with the additional vintage disclosures. For public entities, the amendments of the update are effective beginning January 1, 2020. In October 2019, the FASB approved a change in the effective dates for CECL which would delay the effective date to fiscal years beginning after December 15, 2022 for smaller reporting companies. Because the Company is a smaller reporting company, the proposed delay is applicable to the Company, and the Company plans to delay the implementation of CECL until January 1, 2023. Management has initiated an implementation committee that has implemented a process to collect the data and is developing a system for the new standard. Initial calculations estimate the effect will be an increase to the allowance for loan losses upon adoption. However, the size of the overall increase is uncertain at this time. Management will utilize the delay to continue to refine and back test the CECL calculation.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Overview. Landmark Bancorp, Inc. is a financial holding company incorporated under the laws of the State of Delaware and is engaged in the banking business through its wholly-owned subsidiary, Landmark National Bank, and in the insurance business through its wholly-owned subsidiary, Landmark Risk Management, Inc. References to the "Company," "we," "us," and "our" refer collectively to Landmark Bancorp, Inc., Landmark National Bank and Landmark Risk Management, Inc. The Company is listed on the Nasdaq Global Market under the symbol "LARK." The Bank is dedicated to providing quality financial and banking services to its local communities. Our strategy includes continuing a tradition of holding and acquiring quality assets while growing our commercial, commercial real estate and agriculture loan portfolios. We are committed to developing relationships with our borrowers and providing a total banking service.

The Bank is principally engaged in the business of attracting deposits from the general public and using such deposits, together with borrowings and other funds, to originate one-to-four family residential real estate, construction and land, commercial real estate, commercial, agriculture, municipal and consumer loans. Although not our primary business function, we do invest in certain investment and mortgage-related securities using deposits and other borrowings as funding sources.

Landmark Risk Management, Inc., which was formed and began operations in 2017, is a Nevada-based captive insurance company which provides supplemental property and casualty insurance coverage to the Company and the Bank for which insurance may not be currently available or economically feasible in today's insurance marketplace. Landmark Risk Management, Inc. pools resources with several other similar insurance company subsidiaries of financial institutions to spread a limited amount of risk among themselves. Landmark Risk Management, Inc. is subject to the regulations of the State of Nevada and undergoes periodic examinations by the Nevada Division of Insurance. As of May 31, 2019, Landmark Risk Management, Inc. exited the pool resources relationship of which it was previously a member, and its management is evaluating other alternatives. Landmark Risk Management, Inc. is not currently providing insurance coverage to the Company or the Bank.

Our results of operations depend generally on net interest income, which is the difference between interest income from interest-earning assets and interest expense on interest-bearing liabilities. Net interest income is affected by regulatory, economic and competitive factors that influence interest rates, loan demand and deposit flows. In addition, we are subject to interest rate risk to the degree that our interest-earning assets mature or reprice at different times, or at different speeds, than our interest-bearing liabilities. Our results of operations are also affected by non-interest income, such as service charges, loan fees, gains from the sale of newly originated loans, gains or losses on investments and certain other non-interest related items. Our principal operating expenses, aside from interest expense, consist of compensation and employee benefits, occupancy costs, professional fees, federal deposit insurance costs, data processing expenses, provision for loan losses, and certain other non-interest expenses.

We are significantly impacted by prevailing economic conditions, including federal monetary and fiscal policies, and federal regulations of financial institutions. Deposit balances are influenced by numerous factors such as competing investments, the level of income and the personal rate of savings within our market areas. Factors influencing lending activities include the demand for housing and the interest rate pricing competition from other lending institutions.

Currently, our business consists of ownership of the Bank, with its main office in Manhattan, Kansas and twenty- nine additional branch offices in central, eastern, southeast and southwest Kansas, and our ownership of Landmark Risk Management, Inc. In May 2019, we opened a loan production office in Prairie Village, Kansas. We converted the loan production office to a branch office during the third quarter of 2019.

Critical Accounting Policies. Critical accounting policies are those which are both most important to the portrayal of our financial condition and results of operations and require our management's most difficult, subjective or complex judgments, often as a result of the need to make estimates about the effect of matters that are inherently uncertain. Our critical accounting policies relate to the allowance for loan losses, accounting for income taxes and the accounting for goodwill and other intangible assets, all of which involve significant judgment by our management. Information about our critical accounting policies is included under Item 7 "Management's Discussion and Analysis of Financial Condition and Results of Operations" in our Annual Report on Form 10-K for the year ended December 31, 2018.

Summary of Results. During the third quarter of 2019, we recorded net earnings of \$2.6 million, which was a decrease of \$407,000, or 13.5%, from the \$3.0 million of net earnings in the third quarter of 2018. During the first nine months of 2019, we recorded net earnings of \$7.4 million, which was a decrease of \$570,000, or 7.2%, from the \$8.0 million of net earnings in the first nine months of 2018.

The following table summarizes earnings and key performance measures for the periods presented.

(Dollars in thousands, except per share amounts)

| | Three months ended | | Nine months ended | |
|--------------------------------|--------------------|----------|-------------------|----------|
| | September 30, | | September 30, | |
| | 2019 | 2018 | 2019 | 2018 |
| Net earnings: | | | | |
| Net earnings | \$ 2,613 | \$ 3,020 | \$ 7,394 | \$ 7,964 |
| Basic earnings per share (1) | \$ 0.60 | \$ 0.69 | \$ 1.69 | \$ 1.83 |
| Diluted earnings per share (1) | \$ 0.60 | \$ 0.69 | \$ 1.69 | \$ 1.83 |
| Earnings ratios: | | | | |
| Return on average assets (2) | 1.03% | 1.24% | 1.00% | 1.12% |
| Return on average equity (2) | 9.90% | 13.73% | 10.02% | 12.39% |
| Equity to total assets | 10.51% | 9.32% | 10.51% | 9.32% |
| Net interest margin (2) | 3.44% | 3.42% | 3.43% | 3.36% |
| Dividend payout ratio | 33.33% | 27.40% | 47.34% | 31.25% |

(1) Per share values for the periods ended September 30, 2018 have been adjusted to give effect to the 5% stock dividend paid during December 2018.

(2) Ratios have been annualized and are not necessarily indicative of the results for the entire year.

Interest Income. Interest income of \$9.4 million for the quarter ended September 30, 2019 increased \$799,000, or 9.2%, as compared to the same period of 2018. Interest income on loans increased \$776,000, or 12.3%, to \$7.1 million for the quarter ended September 30, 2019, compared to the same period of 2018 due primarily to an increase in our average loan balances, which increased from \$474.8 million in the third quarter of 2018 to \$529.6 million in the third quarter of 2019. Interest income on investment securities increased \$23,000, or 1.0%, to \$2.3 million for the third quarter of 2019, as compared to the same period of 2018. The increase in interest income on investment securities was primarily the result of higher yields on investments, which increased from 2.60% in the third quarter of 2018 to 2.68% in the third quarter of 2019, which was partially offset by lower average balances.

Interest income of \$27.6 million for the nine months ended September 30, 2019 increased \$3.3 million, or 13.5%, as compared to the same period of 2018. Interest income on loans increased \$3.0 million, or 17.2%, to \$20.4 million for the nine months ended September 30, 2019, compared to the same period of 2018 due primarily to an increase in our average loan balances, which increased from \$455.2 million during the first nine months of 2018 to \$511.3 million during the first nine months of 2019. Also contributing to the increase in interest income were higher yields on loans, which increased from 5.14% in the first nine months of 2018 to 5.35% in the first nine months of 2019. Interest income on investment securities increased \$299,000, or 4.3%, to \$7.2 million for the first nine months of 2019, as compared to \$6.9 million in the same period of 2018. The increase in interest income on investment securities was primarily the result of higher yields on investments, which increased from 2.58% in the first nine months of 2018 to 2.72% in the first nine months of 2019, which was partially offset by lower average balances.

Interest Expense. Interest expense during the quarter ended September 30, 2019 increased \$320,000, or 21.8%, to \$1.8 million as compared to the same period of 2018. Interest expense on interest-bearing deposits increased \$600,000, or 72.0%, to \$1.4 million for the quarter ended September 30, 2019 as compared to the same period of 2018. The increase in interest expense on interest-bearing deposits was the result of deposits repricing higher and an increase in average interest-bearing deposit balances, which increased from \$605.2 million in the third quarter of 2018 to \$652.4 million in the third quarter of 2019. The average rate of interest-bearing deposits increased 0.32% to 0.87% for the third quarter of 2019 as compared to 0.55% in the same period of 2018. Our deposit growth primarily consisted of brokered certificates of deposit which have higher rates than our typical retail and commercial deposits. The brokered certificates of deposits were utilized to fund loan growth at lower rates than our borrowings. For the third quarter of 2019, interest expense on borrowings decreased \$280,000, or 44.2%, to \$353,000 as compared to the same period of 2018, due primarily to a decrease in our average outstanding borrowings, which decreased from \$88.8 million in the third quarter of 2018 to \$52.3 million in the same period of 2019. Also contributing to the decline in interest expense were lower average rates on our borrowings, which decreased to 2.68% for the third quarter of 2019 compared to 2.83% for the same period of 2018.

Interest expense during the nine months ended September 30, 2019 increased \$1.6 million, or 42.1%, to \$5.3 million as compared to the same period of 2018. Interest expense on interest-bearing deposits increased \$2.1 million, or 106.7%, to \$4.1 million for the nine months ended September 30, 2019 as compared to the same period of 2018. The increase in interest expense on interest-bearing deposits was the result of deposits repricing higher and an increase in average interest-bearing deposit balances, which increased from \$601.7 million in the first nine months of 2018 to \$647.9 million in the same period of 2019. The average rate of interest-bearing deposits increased 0.41% to 0.86% for the first nine months of 2019 as compared to 0.45% in the same period of 2018. For the first nine months of 2019, interest expense on borrowings decreased \$573,000, or 33.4%, to \$1.1 million as compared to the same period of 2018, due to a decrease in our average outstanding borrowings, which decreased from \$82.7 million in the first nine months of 2018 to \$53.6 million in the first nine months of 2019. Partially offsetting the lower average outstanding borrowings were higher average rates on our borrowings, which increased to 2.85% for the first nine months of 2019 compared to 2.77% for the same period of 2018.

Net Interest Income. Net interest income increased \$479,000, or 6.7%, to \$7.7 million for the third quarter of 2019 compared to the same period of 2018. The increase in net interest income was primarily a result of an increase of 5.0% in average interest-earning assets, from \$867.5 million in the third quarter of 2018 to \$911.1 million for the same period of 2019. Our net interest margin, on a tax-equivalent basis, increased from 3.42% during the third quarter of 2018 to 3.44% in the same period of 2019.

Net interest income increased \$1.7 million, or 8.4%, to \$22.3 million for the first nine months of 2019 compared to the same period of 2018. The increase was primarily a result of a 5.4% increase in average interest-earning assets, from \$852.5 million in the first nine months of 2018 to \$898.5 million in the first nine months of 2019. Net interest margin, on a tax-equivalent basis, increased from 3.36% in the first nine months of 2018 to 3.43% in the same period of 2019.

Our net interest income and net interest margin have increased primarily as a result of higher average outstanding loan balances. We may not be able to continue to increase our net interest income and net interest margin if loan growth slows or if a decline in interest rates causes the yields on our loans and investment securities to decline faster than the rates on our interest-bearing deposits and borrowings. An increase in interest rates may not result in higher net interest income and net interest margin if we are unable to reprice our loans faster than our cost of interest-bearing deposits and borrowings increase. See the Average Assets/Liabilities and Rate/Volume tables at the end of Item 2 “Management’s Discussion and Analysis of Financial Condition and Results of Operations” for additional details on volumes of assets and liabilities, asset yields, liability rates and net interest margin.

Provision for Loan Losses. We maintain, and our Board of Directors monitors, an allowance for losses on loans. The allowance is established based upon management’s periodic evaluation of known and inherent risks in the loan portfolio, review of significant individual loans and collateral, review of delinquent loans, past loss experience, adverse situations that may affect the borrowers’ ability to repay, current and expected market conditions, and other factors management deems important. Determining the appropriate level of reserves involves a high degree of management judgment and is based upon historical and projected losses in the loan portfolio and the collateral value or discounted cash flows of specifically identified impaired loans. Additionally, allowance policies are subject to periodic review and revision in response to a number of factors, including current market conditions, actual loss experience, management’s expectations and review by our regulators.

During the third quarter of 2019, we recorded a provision for loan losses of \$400,000 compared to \$450,000 in the third quarter of 2018. We recorded net loan charge-offs of \$387,000 during the third quarter of 2019 compared to net loan charge-offs of \$396,000 during the third quarter of 2018.

During the first nine months of 2019, we recorded a provision for loan losses of \$1.0 million compared to \$900,000 during the same period of 2018. We recorded net loan charge-offs of \$486,000 during the nine months ended September 30, 2019 compared to \$470,000 during the same period of 2018.

For further discussion of the allowance for loan losses, refer to the “Asset Quality and Distribution” section below.

Non-interest Income. Total non-interest income was \$4.6 million in the third quarter of 2019, a decrease of \$12,000, or 0.3%, from the same period in 2018, primarily as a result of a decrease of \$876,000 in other non-interest income between the periods. Results for the third quarter of 2018 included \$888,000 of recoveries on a deposit-related loss that occurred in the third quarter of 2017, which were included in other non-interest income. Partially offsetting that decline was an increase of \$605,000 in gains on sales of loans, driven by higher volumes of one-to-four family residential real estate loans originated, and an increase of \$245,000 in fees and service charges, due to higher fee income on deposit accounts.

Total non-interest income was \$11.8 million in the first nine months of 2019, a decrease of \$422,000, or 3.5%, from the first nine months of 2018, including a decline of \$1.4 million in other non-interest income, primarily due to the 2018 period's \$1.4 million in recoveries on the deposit-related loss. The first nine months of 2019 included losses on sales of investment securities totaling \$146,000 compared to gains on sales of investments totaling \$20,000 in the first nine months of 2018. Partially offsetting those declines were increases of \$838,000 in gains on sales of loans and \$301,000 in fees and service charges.

Non-interest Expense. Non-interest expense totaled \$8.6 million for the third quarter of 2019, an increase of \$906,000, or 11.7%, from \$7.7 million for the third quarter of 2018. The increase was primarily due to increases of \$434,000 in compensation and benefits as a result of the addition of bank employees and increased compensation costs. Also contributing to the increase were increases of \$336,000 in other non-interest expense, \$99,000 in occupancy and equipment and \$60,000 in professional fees in the third quarter of 2019 as compared to the third quarter of 2018. Partially offsetting the increases was a decrease in federal deposit insurance premiums of \$139,000 due to the receipt of small bank assessment credits. The small bank assessment credits will offset our premiums for the rest of 2019 as long as the Deposit Insurance Fund continues to exceed 1.35%.

Non-interest expense totaled \$24.3 million for the first nine months of 2019, an increase of \$1.6 million, or 7.0%, from \$22.7 million for the first nine months of 2018. The increase was primarily due to increases of \$1.1 million in compensation and benefits as a result of the addition of bank employees and increased compensation costs. Also contributing to the increase were increases of \$231,000 in other non-interest expenses, \$111,000 in occupancy and equipment, \$98,000 in data processing, \$93,000 in foreclosure and real estate owned expense and \$81,000 in professional fees in the first nine months of 2019 as compared to the first nine months of 2018. Partially offsetting the increases was a decrease in federal deposit insurance premiums of \$146,000 due to receipt of small bank assessment credits.

Income Tax Expense. During the third quarter of 2019, we recorded income tax expense of \$583,000, compared to \$565,000 during the same period of 2018. Our effective tax rate increased from 15.8% in the third quarter of 2018 to 18.2% in the third quarter of 2019. The increase in our effective tax rate was primarily due to a decrease in tax-exempt income as a proportion of earnings before income taxes.

We recorded income tax expense of \$1.4 million for the first nine months of 2019 compared to \$1.2 million in the same period of 2018. Our effective tax rate increased from 13.6% in the first nine months of 2018 to 16.2% in the first nine months of 2019 primarily as a result of the recognition of \$139,000 of excess tax benefits from the exercise of stock options during the first nine months of 2018.

Financial Condition. Despite measured improvement in certain metrics, general uncertainty with respect to economic conditions in the United States continues to affect our asset quality and performance. The geographic markets in which the Company operates have also been impacted by an economic downturn in the agriculture sector. However, our loan portfolio is diversified across various types of loans and collateral throughout the markets in which we operate. Aside from a few problem loans that management is working to resolve, our asset quality has generally improved over the past few years. Aside from these identified problem assets, management believes that the Company continues to have a high quality asset base and solid core earnings, and anticipates that its efforts to maintain these quality features will continue to provide a strong foundation for continued growth and profitability in the future.

Asset Quality and Distribution. Our primary investing activities are the origination of one-to-four family residential real estate, construction and land, commercial real estate, commercial, agriculture, municipal and consumer loans and the purchase of investment securities. Total assets increased \$22.9 million, or 2.3%, to \$1.0 billion at September 30, 2019, compared to \$985.8 million at December 31, 2018. Net loans increased \$30.8 million, or 6.3%, to \$520.1 million at September 30, 2019, compared to \$489.4 million at year-end 2018. Investment securities decreased \$20.6 million, or 5.2%, to \$372.5 million at September 30, 2019, from \$393.1 million at December 31, 2018.

The allowance for loan losses is established through a provision for loan losses based on our evaluation of the risk inherent in the loan portfolio and changes in the nature and volume of our loan activity. This evaluation, which includes a review of all loans with respect to which full collectability may not be reasonably assured, considers the fair value of the underlying collateral, economic conditions, historical loan loss experience, level of classified loans and other factors that warrant recognition in providing for an appropriate allowance for loan losses. At September 30, 2019, our allowance for loan losses totaled \$6.3 million, or 1.19% of gross loans outstanding, compared to \$5.8 million, or 1.16% of gross loans outstanding, at December 31, 2018.

As of September 30, 2019 and December 31, 2018, approximately \$24.0 million and \$31.8 million, respectively, of loans were considered classified and assigned a risk rating of special mention, substandard or doubtful. These ratings indicate that these loans were identified as potential problem loans having more than normal risk which raised doubts as to the ability of the borrower to comply with present loan repayment terms. Even though borrowers were experiencing moderate cash flow problems as well as some deterioration in collateral value, management believed the allowance for loan losses was sufficient to cover the risks and probable incurred losses related to such loans at September 30, 2019 and December 31, 2018, respectively.

Loans past due 30-89 days and still accruing interest totaled \$2.1 million, or 0.40% of gross loans, at September 30, 2019, compared to \$1.7 million, or 0.34% of gross loans, at December 31, 2018. At September 30, 2019, \$5.9 million in loans were on non-accrual status, or 1.13% of gross loans, compared to \$5.2 million, or 1.06% of gross loans, at December 31, 2018. Non-accrual loans typically consist of loans 90 or more days past due and certain impaired loans. There were no loans 90 days delinquent and accruing interest at September 30, 2019 or December 31, 2018. Our impaired loans totaled \$9.1 million at September 30, 2019 compared to \$8.7 million at December 31, 2018. The difference in the Company's non-accrual loan balances and impaired loan balances at September 30, 2019 and December 31, 2018 was related to TDRs that were accruing interest but still classified as impaired.

As part of our credit risk management, we continue to manage the loan portfolio to identify problem loans and have placed additional emphasis on agriculture, commercial real estate and construction and land relationships. We are working to resolve the remaining problem credits or move the non-performing credits out of the loan portfolio. At September 30, 2019, we had \$473,000 of real estate owned compared to \$35,000 at December 31, 2018. As of September 30, 2019, real estate owned consisted of residential real estate and agriculture land. The Company is currently marketing all of the remaining properties in real estate owned.

Liability Distribution. Our primary ongoing sources of funds are deposits, FHLB borrowings, proceeds from principal and interest payments on loans and investment securities and proceeds from the sale of mortgage loans and investment securities. While maturities and scheduled amortization of loans are a predictable source of funds, deposit flows and mortgage prepayments are greatly influenced by general interest rates and economic conditions. We experienced an increase of \$10.2 million in total deposits during the first nine months of 2019, to \$833.8 million at September 30, 2019, from \$823.6 million at December 31, 2018. The increase in deposits was primarily due to increased balances of non-interest bearing, savings and time deposit accounts. This increase was partially offset by lower balances of money market and checking deposit accounts.

Non-interest-bearing deposits at September 30, 2019, were \$184.8 million, or 22.1% of deposits, compared to \$168.3 million, or 20.4% of deposits, at December 31, 2018. Money market and checking deposit accounts were 42.3% of our deposit portfolio and totaled \$352.7 million at September 30, 2019, compared to \$393.5 million, or 47.8% of deposits, at December 31, 2018. Savings accounts increased to \$98.9 million, or 11.9% of deposits, at September 30, 2019, from \$94.9 million, or 11.5% of deposits, at December 31, 2018. Certificates of deposit totaled \$197.4 million, or 23.7% of deposits, at September 30, 2019, compared to \$167.0 million, or 20.3% of deposits, at December 31, 2018.

Certificates of deposit at September 30, 2019, scheduled to mature in one year or less, totaled \$171.8 million. Historically, maturing deposits have generally remained with the Bank, and we believe that a significant portion of the deposits maturing in one year or less will remain with us upon maturity in some type of deposit account.

Total borrowings decreased \$1.8 million to \$55.1 million at September 30, 2019, from \$56.9 million at December 31, 2018. The decrease in total borrowings was primarily due to a decrease in our FHLB borrowings from \$20.0 million at December 31, 2018 to \$17.2 million at September 30, 2019.

Cash Flows. During the nine months ended September 30, 2019, our cash and cash equivalents increased by \$2.6 million. Our operating activities used cash of \$1.0 million during the first nine months of 2019 primarily as a result of the origination of loans held for sale. Our investing activities used net cash of \$2.1 million during the first nine months of 2019, primarily as a result of an increase in our loan balances. Financing activities provided net cash of \$5.7 million during the first nine months of 2019, primarily as a result of increased deposits.

Liquidity. Our most liquid assets are cash and cash equivalents and investment securities available for sale. The levels of these assets are dependent on the operating, financing, lending and investing activities during any given period. These liquid assets totaled \$391.1 million at September 30, 2019 and \$407.5 million at December 31, 2018. During periods in which we are not able to originate a sufficient amount of loans and/or periods of high principal prepayments, we generally increase our liquid assets by investing in short-term, high-grade investments.

Liquidity management is both a daily and long-term function of our strategy. Excess funds are generally invested in short-term investments. Excess funds are typically generated as a result of increased deposit balances, while uses of excess funds are generally deposit withdrawals and loan advances. In the event we require funds beyond our ability to generate them internally, additional funds are generally available through the use of FHLB advances, a line of credit with the FHLB, other borrowings or through sales of investment securities. At September 30, 2019, we had \$17.2 million of borrowings against our line of credit with the FHLB. At September 30, 2019, we had collateral pledged to the FHLB that would allow us to borrow an additional \$95.0 million, subject to FHLB credit requirements and policies. At September 30, 2019, we had no borrowings through the Federal Reserve discount window, while our borrowing capacity with the Federal Reserve was \$17.9 million. We also have various other federal funds agreements, both secured and unsecured, with correspondent banks totaling approximately \$30.0 million in available credit under which we had no outstanding borrowings at September 30, 2019. At September 30, 2019, we had subordinated debentures totaling \$21.7 million and other borrowings of \$16.3 million, which consisted of \$16.3 million in repurchase agreements. The Company has a \$7.5 million line of credit from an unrelated financial institution maturing on November 1, 2020, with an interest rate that adjusts daily based on the prime rate less 0.25%. This line of credit has covenants specific to capital and other financial ratios, with which the Company was in compliance at September 30, 2019.

Off Balance Sheet Arrangements. As a provider of financial services, we routinely issue financial guarantees in the form of financial and performance standby letters of credit. Standby letters of credit are contingent commitments issued by us generally to guarantee the payment or performance obligation of a customer to a third party. While these standby letters of credit represent a potential outlay by us, a significant amount of the commitments may expire without being drawn upon. We have recourse against the customer for any amount the customer is required to pay to a third party under a standby letter of credit. The letters of credit are subject to the same credit policies, underwriting standards and approval process as loans made by us. Most of the standby letters of credit are secured, and in the event of nonperformance by the customers, we have the right to the underlying collateral, which could include commercial real estate, physical plant and property, inventory, receivables, cash and marketable securities. The contract amount of these standby letters of credit, which represents the maximum potential future payments guaranteed by us, was \$1.8 million at September 30, 2019.

At September 30, 2019, we had outstanding loan commitments, excluding standby letters of credit, of \$114.9 million. We anticipate that sufficient funds will be available to meet current loan commitments. These commitments consist of unfunded lines of credit and commitments to finance real estate loans.

Capital. Current regulatory capital regulations require financial institutions (including banks and bank holding companies) to meet certain regulatory capital requirements. The Company and the Bank are subject to the Basel III Rules that implemented the Basel III regulatory capital reforms from the Basel Committee on Banking Supervision and certain changes required by the Dodd-Frank Wall Street Reform and Consumer Protection Act. The Basel III Rules are applicable to all U.S. banks that are subject to minimum capital requirements, as well as to bank and savings and loan holding companies other than “small bank holding companies” (generally, non-public bank holding companies with consolidated assets of less than \$3.0 billion).

The Basel III Rules require a common equity Tier 1 capital to risk-weighted assets minimum ratio of 4.5%, a Tier 1 capital to risk-weighted assets minimum ratio of 6.0%, a Total Capital to risk-weighted assets minimum ratio of 8.0%, and a Tier 1 leverage minimum ratio of 4.0%. A capital conservation buffer, comprised of common equity Tier 1 capital, is also established above the regulatory minimum capital requirements. This capital conservation buffer was 1.875% for 2018, and increased to its final level of 2.5% on January 1, 2019. As of September 30, 2019 and December 31, 2018, the Bank’s capital ratios were in excess of the requirements to be “well capitalized,” which is the highest rating available under the regulatory capital regulations framework for prompt corrective action. Management believed that as of September 30, 2019, the Company and the Bank met all capital adequacy requirements to which we were subject.

Dividends. During the quarter ended September 30, 2019, we paid a quarterly cash dividend of \$0.20 per share to our stockholders.

The payment of dividends by any financial institution or its holding company is affected by the requirement to maintain adequate capital pursuant to applicable capital adequacy guidelines and regulations. In addition, under the Basel III Rules, financial institutions have to maintain 2.5% in common equity Tier 1 capital attributable to the capital conservation buffer in order to pay dividends and make other capital distributions. As described above, the Bank exceeded its minimum capital requirements under applicable guidelines as of September 30, 2019. The National Bank Act imposes limitations on the amount of dividends that a national bank may pay without prior regulatory approval. Generally, the amount is limited to the bank’s current year’s net earnings plus the adjusted retained earnings for the two preceding years. As of September 30, 2019, approximately \$12.6 million was available to be paid as dividends to the Company by the Bank without prior regulatory approval.

Additionally, our ability to pay dividends is limited by the subordinated debentures that are held by three business trusts that we control. Interest payments on the debentures must be paid before we pay dividends on our capital stock, including our common stock. We have the right to defer interest payments on the debentures for up to 20 consecutive quarters. However, if we elect to defer interest payments, all deferred interest must be paid before we may pay dividends on our capital stock.

Average Assets/Liabilities. The following tables reflect the tax-equivalent yields earned on average interest-earning assets and costs of average interest-bearing liabilities for the periods indicated (derived by dividing income or expense by the monthly average balance of assets or liabilities, respectively) as well as “net interest margin” (which reflects the effect of the net earnings balance) for the periods shown:

(Dollars in thousands)

| | Three months ended September 30, 2019 | | | Three months ended September 30, 2018 | | |
|--|--|----------|-----------------------|--|----------|-----------------------|
| | Average balance | Interest | Average yield/rate | Average balance | Interest | Average yield/rate |
| Assets | | | | | | |
| Interest-earning assets: | | | | | | |
| Interest-bearing deposits at banks | \$ 304 | \$ 4 | 5.22% | \$ 578 | \$ 7 | 4.80% |
| Investment securities (1) | 381,217 | 2,570 | 2.68% | 392,141 | 2,566 | 2.60% |
| Loans receivable, net (2) | 529,552 | 7,103 | 5.32% | 474,801 | 6,361 | 5.32% |
| Total interest-earning assets | 911,073 | 9,677 | 4.21% | 867,520 | 8,934 | 4.09% |
| Non-interest-earning assets | 92,886 | | | 95,910 | | |
| Total | \$1,003,959 | | | \$ 963,430 | | |
| Liabilities and Stockholders' Equity | | | | | | |
| Interest-bearing liabilities: | | | | | | |
| Money market and checking | \$ 362,500 | \$ 630 | 0.69% | \$ 368,360 | \$ 489 | 0.53% |
| Savings accounts | 98,802 | 9 | 0.04% | 95,579 | 7 | 0.03% |
| Time deposit | 191,063 | 794 | 1.65% | 141,285 | 337 | 0.95% |
| Total deposits | 652,365 | 1,433 | 0.87% | 605,224 | 833 | 0.55% |
| FHLB advances and other borrowings | 52,264 | 353 | 2.68% | 88,846 | 633 | 2.83% |
| Total interest-bearing liabilities | 704,629 | 1,786 | 1.01% | 694,070 | 1,466 | 0.84% |
| Non-interest-bearing liabilities | 194,655 | | | 182,073 | | |
| Stockholders' equity | 104,675 | | | 87,287 | | |
| Total | \$1,003,959 | | | \$ 963,430 | | |
| Interest rate spread (3) | | | 3.20% | | | 3.25% |
| Net interest margin (4) | | \$ 7,891 | 3.44% | | \$ 7,468 | 3.42% |
| Tax-equivalent interest - imputed | | 232 | | | 288 | |
| Net interest income | | \$ 7,659 | | | \$ 7,180 | |
| Ratio of average interest-earning assets to average interest-bearing liabilities | | | 129.3% | | | 125.0% |

- (1) Income on tax exempt securities is presented on a fully tax-equivalent basis, using a 21% federal tax rate.
- (2) Includes loans classified as non-accrual. Income on tax-exempt loans is presented on a fully tax-equivalent basis, using a 21% federal tax rate.
- (3) Interest rate spread represents the difference between the average yield earned on interest-earning assets and the average rate paid on interest-bearing liabilities.
- (4) Net interest margin represents annualized, tax-equivalent net interest income divided by average interest-earning assets.

(Dollars in thousands)

| | Nine months ended September 30, 2019 | | | Nine months ended September 30, 2018 | | |
|--|---|------------------|-----------------------|---|------------------|-----------------------|
| | Average balance | Interest | Average yield/rate | Average balance | Interest | Average yield/rate |
| Assets | | | | | | |
| Interest-earning assets: | | | | | | |
| Interest-bearing deposits at banks | \$ 814 | \$ 23 | 3.78% | \$ 874 | \$ 16 | 2.45% |
| Investment securities (1) | 386,416 | 7,850 | 2.72% | 396,381 | 7,642 | 2.58% |
| Loans receivable, net (2) | 511,312 | 20,456 | 5.35% | 455,242 | 17,500 | 5.14% |
| Total interest-earning assets | <u>898,542</u> | <u>28,329</u> | 4.22% | <u>852,497</u> | <u>25,158</u> | 3.95% |
| Non-interest-earning assets | 93,011 | | | 94,920 | | |
| Total | <u>\$ 991,553</u> | | | <u>\$ 947,417</u> | | |
| Liabilities and Stockholders' Equity | | | | | | |
| Interest-bearing liabilities: | | | | | | |
| Money market and checking | \$ 373,608 | \$ 2,024 | 0.72% | \$ 375,636 | \$ 1,293 | 0.46% |
| Savings accounts | 97,590 | 26 | 0.04% | 95,664 | 21 | 0.03% |
| Time deposit | 176,655 | 2,094 | 1.58% | 130,421 | 691 | 0.71% |
| Total deposits | 647,853 | 4,144 | 0.86% | 601,721 | 2,005 | 0.45% |
| FHLB advances and other borrowings | 53,567 | 1,142 | 2.85% | 82,671 | 1,715 | 2.77% |
| Total interest-bearing liabilities | <u>701,420</u> | <u>5,286</u> | 1.01% | <u>684,392</u> | <u>3,720</u> | 0.73% |
| Non-interest-bearing liabilities | 191,465 | | | 177,082 | | |
| Stockholders' equity | 98,668 | | | 85,943 | | |
| Total | <u>\$ 991,553</u> | | | <u>\$ 947,417</u> | | |
| Interest rate spread (3) | | | 3.21% | | | 3.22% |
| Net interest margin (4) | | <u>\$ 23,043</u> | 3.43% | | <u>\$ 21,438</u> | 3.36% |
| Tax-equivalent interest - imputed | | <u>707</u> | | | <u>828</u> | |
| Net interest income | | <u>\$ 22,336</u> | | | <u>\$ 20,610</u> | |
| Ratio of average interest-earning assets to average interest-bearing liabilities | | | 128.1% | | | 124.6% |

- (1) Income on tax exempt securities is presented on a fully tax-equivalent basis, using a 21% federal tax rate.
- (2) Includes loans classified as non-accrual. Income on tax-exempt loans is presented on a fully tax-equivalent basis, using a 21% federal tax rate.
- (3) Interest rate spread represents the difference between the average yield earned on interest-earning assets and the average rate paid on interest-bearing liabilities.
- (4) Net interest margin represents annualized, tax-equivalent net interest income divided by average interest-earning assets.

Rate/Volume Table. The following table describes the extent to which changes in tax-equivalent interest income and interest expense for major components of interest-earning assets and interest-bearing liabilities affected the Company's interest income and expense for the periods indicated. The table distinguishes between (i) changes attributable to rate (changes in rate multiplied by prior volume), (ii) changes attributable to volume (changes in volume multiplied by prior rate), and (iii) net change (the sum of the previous columns). The net changes attributable to the combined effect of volume and rate that cannot be segregated have been allocated proportionately to the change due to volume and the change due to rate.

(Dollars in thousands)

| | Three months ended September 30, | | | Nine months ended September 30, | | |
|------------------------------------|-------------------------------------|------------|------------|-------------------------------------|--------------|--------------|
| | 2019 vs 2018 | | | 2019 vs 2018 | | |
| | Increase/(decrease) attributable to | | | Increase/(decrease) attributable to | | |
| | Volume | Rate | Net | Volume | Rate | Net |
| Interest income: | | | | | | |
| Interest-bearing deposits at banks | \$ (4) | \$ 1 | \$ (3) | \$ (1) | \$ 8 | \$ 7 |
| Investment securities | (48) | 53 | 5 | (179) | 387 | 208 |
| Loans | 742 | - | 742 | 2,220 | 736 | 2,956 |
| Total | 690 | 54 | 744 | 2,040 | 1,131 | 3,171 |
| Interest expense: | | | | | | |
| Deposits | 71 | 529 | 600 | 166 | 1,973 | 2,139 |
| Borrowings | (248) | (32) | (280) | (624) | 51 | (573) |
| Total | (177) | 497 | 320 | (458) | 2,024 | 1,566 |
| Net interest income | \$ 867 | \$ (443) | \$ 424 | \$ 2,498 | \$ (893) | \$ 1,605 |

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Our assets and liabilities are principally financial in nature, and the resulting net interest income thereon is subject to changes in market interest rates and the mix of various assets and liabilities. Interest rates in the financial markets affect our decisions relating to pricing our assets and liabilities, which impact net interest income, a significant cash flow source for us. As a result, a substantial portion of our risk management activities relates to managing interest rate risk.

Our Asset/Liability Management Committee monitors the interest rate sensitivity of our balance sheet using earnings simulation models. We have set policy limits of interest rate risk to be assumed in the normal course of business and monitor such limits through our simulation process.

We have been successful in meeting the interest rate sensitivity objectives set forth in our policy. Simulation models are prepared to determine the impact on net interest income for the coming twelve months, including one using rates at September 30, 2019, and forecasting volumes for the twelve-month projection. This position is then subjected to a shift in interest rates of 100 and 200 basis points with an impact to our net interest income on a one-year horizon as follows:

| Scenario | Dollar change in net interest income (\$000's) | Percent change in net interest income |
|-------------------------|--|---------------------------------------|
| 200 basis point rising | \$ (1,450) | (4.7)% |
| 100 basis point rising | \$ (720) | (2.3)% |
| 100 basis point falling | \$ 683 | 2.2% |
| 200 basis point falling | \$ 1,236 | 4.0% |

SAFE HARBOR STATEMENT UNDER THE PRIVATE SECURITIES LITIGATION REFORM ACT OF 1995

Forward-Looking Statements

This document (including information incorporated by reference) contains, and future oral and written statements by us and our management may contain, forward-looking statements, within the meaning of such term in the Private Securities Litigation Reform Act of 1995, with respect to our financial condition, results of operations, plans, objectives, future performance and business. Forward-looking statements, which may be based upon beliefs, expectations and assumptions of our management and on information currently available to management, are generally identifiable by the use of words such as “believe,” “expect,” “anticipate,” “plan,” “intend,” “estimate,” “may,” “will,” “would,” “could,” “should” or other similar expressions. Additionally, all statements in this document, including forward-looking statements, speak only as of the date they are made, and we undertake no obligation to update any statement in light of new information or future events.

Our ability to predict results or the actual effect of future plans or strategies is inherently uncertain. Factors which could have a material adverse effect on operations and future prospects by us and our subsidiaries include, but are not limited to, the following:

- The strength of the United States economy in general and the strength of the local economies in which we conduct our operations, which may be less favorable than expected and may result in, among other things, a deterioration in the credit quality and value of our assets.
- The effects of, and changes in, federal, state and local laws, regulations and policies affecting banking, securities, insurance, tax, trade and monetary and financial matters.
- The effects of changes in interest rates (including the effects of changes in the rate of prepayments of our assets) and the policies of the Board of Governors of the Federal Reserve System.
- Our ability to compete with other financial institutions due to increases in competitive pressures in the financial services sector.
- Our inability to obtain new customers or to retain existing customers.
- The timely development and acceptance of products and services, including products and services offered through alternative delivery channels such as the Internet.
- Technological changes implemented by us and by other parties, including third-party vendors, which may be more difficult or more expensive than anticipated or which may have unforeseen consequences to us and our customers.
- Our ability to develop and maintain secure and reliable electronic systems.
- Our ability to retain key executives and employees and the difficulty that we may experience in replacing key executives and employees in an effective manner.
- Consumer spending and saving habits which may change in a manner that affects our business adversely.
- Our ability to successfully integrate acquired businesses and future growth.
- The costs, effects and outcomes of existing or future litigation.
- Changes in accounting policies and practices, as may be adopted by state and federal regulatory agencies and the FASB.
- The economic impact of past and any future terrorist attacks, acts of war or threats thereof, and the response of the United States to any such threats and attacks.
- Our ability to effectively manage our credit risk.
- Our ability to forecast probable loan losses and maintain an adequate allowance for loan losses.
- The effects of declines in the value of our investment portfolio.
- Our ability to raise additional capital if needed.
- The effects of cyber-attacks.
- The effects of declines in real estate markets.
- The effects of fraudulent activity on the part of our employees, customers, vendors, or counterparties.

These risks and uncertainties should be considered in evaluating forward-looking statements and undue reliance should not be placed on such statements. Additional information concerning us and our business, including other factors that could materially affect our financial results, is included in our filings with the Securities and Exchange Commission, including the “Risk Factors” section in our Annual Report on Form 10-K for the year ended December 31, 2018.

ITEM 4. CONTROLS AND PROCEDURES

An evaluation was performed under the supervision and with the participation of the Company’s management, including the Chief Executive Officer and Chief Financial Officer, of the effectiveness of the Company’s disclosure controls and procedures (as defined in Rule 13a-15 (e) promulgated under the Securities Exchange Act of 1934, as amended) as of September 30, 2019. Based on that evaluation, the Company’s management, including the Chief Executive Officer and Chief Financial Officer, concluded that the Company’s disclosure controls and procedures were effective as of September 30, 2019.

There were no changes in the Company’s internal control over financial reporting during the quarter ended September 30, 2019 that materially affected or are reasonably likely to materially affect the Company’s internal control over financial reporting.

PART II – OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

There are no material pending legal proceedings to which the Company or its subsidiaries is a party or which any of their property is subject, other than ordinary routine litigation incidental to their respective businesses.

ITEM 1A. RISK FACTORS

There have been no material changes in the risk factors applicable to the Company from those disclosed in Part I, Item 1A. “Risk Factors,” in the Company’s 2018 Annual Report on Form 10-K.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

ITEM 5. OTHER INFORMATION

None.

ITEM 6. EXHIBITS

- | | |
|--------------|--|
| Exhibit 10.1 | <u>Change in Terms Agreement dated November 1, 2019, between Landmark Bancorp, Inc. and First National Bank of Omaha</u> |
| Exhibit 31.1 | <u>Certificate of Chief Executive Officer Pursuant to Rule 13a-14(a)/15d-14(a)</u> |
| Exhibit 31.2 | <u>Certificate of Chief Financial Officer Pursuant to Rule 13a-14(a)/15d-14(a)</u> |
| Exhibit 32.1 | <u>Certification of Chief Executive Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002</u> |
| Exhibit 32.2 | <u>Certification of Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002</u> |
| Exhibit 101 | Interactive data files pursuant to Rule 405 of Regulation S-T: (i) Consolidated Balance Sheets as of September 30, 2019 and December 31, 2018; (ii) Consolidated Statements of Earnings for the three and nine months ended September 30, 2019 and September 30, 2018; (iii) Consolidated Statements of Comprehensive Income for the three and nine months ended September 30, 2019 and September 30, 2018; (iv) Consolidated Statements of Stockholders’ Equity for the three and nine months ended September 30, 2019 and September 30, 2018; (v) Consolidated Statements of Cash Flows for the nine months ended September 30, 2019 and September 30, 2018; and (vi) Notes to Consolidated Financial Statements |

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

LANDMARK BANCORP, INC.

Date: November 8, 2019

/s/ Michael E. Scheopner

Michael E. Scheopner
President and Chief Executive Officer
(Principal Executive Officer)

Date: November 8, 2019

/s/ Mark A. Herpich

Mark A. Herpich
Vice President, Secretary, Treasurer and Chief Financial Officer
(Principal Financial and Accounting Officer)

Section 2: EX-10.1

Exhibit 10.1

CHANGE IN TERMS AGREEMENT

| <i>Principal</i> | <i>Loan Date</i> | <i>Maturity</i> | <i>Loan No</i> | <i>Call/Coll</i> | <i>Account</i> | <i>Officer</i> | <i>Initials</i> |
|------------------|------------------|-----------------|----------------|------------------|----------------|----------------|-----------------|
| \$7,500,000.00 | 11-01-2019 | 11-01-2020 | xxxxxxx | | | *** | |

Borrower: Landmark Bancorp, Inc.
701 Poyntz Ave
Manhattan KS 66502-6055

Lender: First National Bank of Omaha
Downtown-Corporate Banking Group
1620 Dodge St SC 1031
Omaha, NE 68197

Principal Amount: \$7,500,000.00

Date of Agreement: November 1, 2019

DESCRIPTION OF EXISTING INDEBTEDNESS. This Change in Terms Agreement is an amendment and/or modification of the terms and conditions of indebtedness of Borrower as set forth in a Promissory Note dated November 1, 2016, in the amount of \$7,500,000.00, and most recently documented in a Change in Terms Agreement dated November 1, 2018, and shall include all renewals, modifications and extensions of such documents.

DESCRIPTION OF CHANGE IN TERMS. As fully set forth herein below, this Change in Terms Agreement generally modifies the terms applicable to the existing indebtedness by extending the maturity date. Any sums due and owing hereunder shall take into account any principal and interest payments made by the Borrower in accordance with regular established billing cycles.

PROMISE TO PAY. Landmark Bancorp, Inc. (“Borrower”) promises to pay to First National Bank of Omaha (“Lender”), or order, in lawful money of the United States of America, the principal amount of Seven Million Five Hundred Thousand & 00/100 Dollars (\$7,500,000.00) or so much as may be outstanding, together with interest on the unpaid outstanding principal balance of each advance. Interest shall be calculated from the date of each advance until repayment of each advance.

PAYMENT. Borrower will pay this loan in one payment of all outstanding principal plus all accrued unpaid interest on November 1, 2020. In addition, Borrower will pay regular quarterly payments of all accrued unpaid interest due as of each payment date, beginning February 1, 2020, with all subsequent interest payments to be due on the same day of each quarter after that. Unless otherwise agreed or required by applicable law, payments will be applied to interest, principal, and expenses owing under the Note in an order determined by Lender. Borrower will pay Lender at Lender’s address shown above or at such other place as Lender may designate in writing.

VARIABLE INTEREST RATE. The interest rate on this loan is subject to change from time to time based on changes in an independent index which is the U.S. Prime Rate as published by the Wall Street Journal and currently is determined by the base rate on corporate loans posted by at least seventy percent (70%) of the nations ten (10) largest banks (the “Index”). The Index is not necessarily the lowest rate charged by Lender on its loans. If the Index becomes unavailable during the term of this loan, Lender may designate a substitute index after notifying Borrower. Lender will tell Borrower the current Index rate upon Borrower’s request. The interest rate change will not occur more often than each day during the term of the loan. If at any time the Index is less than zero, then it shall be deemed to be zero for the purpose of calculating the interest rate on this Note. Borrower understands that Lender may make loans based on other rates as well. **The Index currently is 4.750% per annum.** Interest on the unpaid principal balance of this loan will be calculated as described in the “INTEREST CALCULATION METHOD” paragraph using a rate of 0.250 percentage points under the Index, resulting in an initial rate of 4.500% per annum based on a year of 360 days. NOTICE: Under no circumstances will the interest rate on this loan be more than the maximum rate allowed by applicable law.

INTEREST CALCULATION METHOD. Interest on this loan is computed on a 365/360 basis; that is, by applying the ratio of the interest rate over a year of 360 days, multiplied by the outstanding principal balance, multiplied by the actual number of days the principal balance is outstanding. All interest payable under this loan is computed using this method.

PREPAYMENT. Borrower may pay without penalty all or a portion of the amount owed earlier than it is due. Early payments will not, unless agreed to by Lender in writing, relieve Borrower of Borrower's obligation to continue to make payments of accrued unpaid interest. Rather, early payments will reduce the principal balance due. Borrower agrees not to send Lender payments marked "paid in full", "without recourse", or similar language. If Borrower sends such a payment, Lender may accept it without losing any of Lender's rights under this Agreement, and Borrower will remain obligated to pay any further amount owed to Lender. **All written communications concerning disputed amounts, including any check or other payment instrument that indicates that the payment constitutes "payment in full" of the amount owed or that is tendered with other conditions or limitations or as full satisfaction of a disputed amount must be mailed or delivered to: First National Bank of Omaha, Downtown- Corporate Banking Group, 1620 Dodge St SC 1031, Omaha, NE 68197.**

LATE CHARGE. If a payment is 10 days or more late, Borrower will be charged **5.000% of the regularly scheduled payment.**

INTEREST AFTER DEFAULT. Upon default, including failure to pay upon final maturity, the interest rate on this loan shall be increased by adding an additional 6.000 percentage point margin ("Default Rate Margin"). The Default Rate Margin shall also apply to each succeeding interest rate change that would have applied had there been no default. However, in no event will the interest rate exceed the maximum interest rate limitations under applicable law.

DEFAULT. Each of the following shall constitute an Event of Default under this Agreement:

Payment Default. Borrower fails to make any payment when due under this Indebtedness.

Other Defaults. Borrower fails to comply with or to perform any other term, obligation, covenant or condition contained in this Agreement or in any of the Related Documents or to comply with or to perform any term, obligation, covenant or condition contained in any other agreement between Lender and Borrower.

Default in Favor of Third Parties. Borrower defaults under any loan, extension of credit, security agreement, purchase or sales agreement, or any other agreement, in favor of any other creditor or person that may materially affect any of Borrower's property or ability to perform Borrower's obligations under this Agreement or any of the Related Documents.

False Statements. Any warranty, representation or statement made or furnished to Lender by Borrower or on Borrower's behalf, or made by Guarantor, or any other guarantor, endorser, surety, or accommodation party, under this Agreement or the Related Documents in connection with the obtaining of the indebtedness evidenced by this Agreement or any security document directly or indirectly securing repayment of this Agreement is false or misleading in any material respect, either now or at the time made or furnished or becomes false or misleading at any time thereafter.

Insolvency. The dissolution or termination of Borrower's existence as a going business, the insolvency of Borrower, the appointment of a receiver for any part of Borrower's property, any assignment for the benefit of creditors, any type of creditor workout, or the commencement of any proceeding under any bankruptcy or insolvency laws by or against Borrower.

Creditor or Forfeiture Proceedings. Commencement of foreclosure or forfeiture proceedings, whether by judicial proceeding, self-help, repossession or any other method, by any creditor of Borrower or by any governmental agency against any collateral securing the indebtedness. This includes a garnishment of any of Borrower's accounts, including deposit accounts, with Lender. However, this Event of Default shall not apply if there is a good faith dispute by Borrower as to the validity or reasonableness of the claim which is the basis of the creditor or forfeiture proceeding and if Borrower gives Lender written notice of the creditor or forfeiture proceeding and deposits with Lender monies or a surety bond for the creditor or forfeiture proceeding, in an amount determined by Lender, in its sole discretion, as being an adequate reserve or bond for the dispute.

Execution; Attachment. Any execution or attachment is levied against the Collateral, and such execution or attachment is not set aside, discharged or stayed within thirty (30) days after the same is levied.

Change in Zoning or Public Restriction. Any change in any zoning ordinance or regulation or any other public restriction is enacted, adopted or implemented, that limits or defines the uses which may be made of the Collateral such that the present or intended use of the Collateral, as specified in the Related Documents, would be in violation of such zoning ordinance or regulation or public restriction, as changed.

Default Under Other Lien Documents. A default occurs under any other mortgage, deed of trust or security agreement covering all or any portion of the Collateral.

Judgment. Unless adequately covered by insurance in the opinion of Lender, the entry of a final judgment for the payment of money involving more than ten thousand dollars (\$10,000.00) against Borrower and the failure by Borrower to discharge the same, or cause it to be discharged, or bonded off to Lenders satisfaction, within thirty (30) days from the date of the order, decree or process under which or pursuant to which such judgment was entered.

Events Affecting Guarantor. Any of the preceding events occurs with respect to any Guarantor, or any other guarantor, endorser, surely, or accommodation party of any of the Indebtedness or any Guarantor, or any other guarantor, endorser, surely, or accommodation party dies or becomes incompetent, or revokes or disputes the validity of, or liability under, any Guaranty of the Indebtedness evidenced by this Note.

Change In Ownership. Any change in ownership of twenty-five percent (25%) or more of the common stock of Borrower.

Adverse Change. A material adverse change occurs in Borrowers financial condition, or Lender believes the prospect of payment or performance of the Indebtedness is impaired.

Insecurity. Lender in good faith believes itself insecure.

LENDER'S RIGHTS. Upon default, Lender may declare the entire unpaid principal balance under this Agreement and all accrued unpaid interest immediately due, and then Borrower will pay that amount.

ATTORNEYS' FEES; EXPENSES. Lender may hire or pay someone else to help collect this Agreement if Borrower does not pay. Borrower will pay Lender that amount. This includes, subject to any limits under applicable law, Lender's attorneys' fees and Lender's legal expenses, whether or not there is a lawsuit, including attorneys' fees, expenses for bankruptcy proceedings (including efforts to modify or vacate any automatic stay or injunction), and appeals. If not prohibited by applicable law, Borrower also will pay any court costs, in addition to all other sums provided by law.

JURY WAIVER. Lender and Borrower hereby waive the right to any jury trial in any action, proceeding, or counterclaim brought by either Lender or Borrower against the other.

GOVERNING LAW. This Agreement will be governed by federal law applicable to Lender and, to the extent not preempted by federal law, the laws of the State of Nebraska without regard to its conflicts of law provisions. This Agreement has been accepted by Lender in the State of Nebraska.

CHOICE OF VENUE. If there is a lawsuit, Borrower agrees upon Lenders request to submit to the jurisdiction of the courts of Douglas County, State of Nebraska.

DISHONORED ITEM FEE. Borrower will pay a fee to Lender of \$30.00 if Borrower makes a payment on Borrower's loan and the check or preauthorized charge with which Borrower pays is later dishonored.

RIGHT OF SETOFF. To the extent permitted by applicable law, Lender reserves a right of setoff in all Borrower's accounts with Lender (whether checking, savings, or some other account). This includes all accounts Borrower holds jointly with someone else and all accounts Borrower may open in the future. However, this does not include any IRA or Keogh accounts, or any trust accounts for which setoff would be prohibited by law. Borrower authorizes Lender, to the extent permitted by applicable law, to charge or setoff all sums owing on the indebtedness against any and all such accounts, and, at Lender's option, to administratively freeze all such accounts to allow Lender to protect Lender's charge and setoff rights provided in this paragraph.

COLLATERAL. Borrower acknowledges this Agreement is secured by a Commercial Pledge Agreement dated November 1, 2016, and any and all other security agreements or documents and any and all other collateral agreements or documents associated with this Loan or Note whether now existing or hereafter arising.

LINE OF CREDIT. This Agreement evidences a revolving line of credit. Advances under this Agreement may be requested either orally or in writing by Borrower or as provided in this paragraph. Lender may, but need not, require that all oral requests be confirmed in writing. All communications, instructions, or directions by telephone or otherwise to Lender are to be directed to Lender's office shown above. Borrower agrees to be liable for all sums either: (A) advanced in accordance with the instructions of an authorized person or (B) credited to any of Borrower's accounts with Lender. The unpaid principal balance owing on this Agreement at any time may be evidenced by endorsements on this Agreement or by Lenders internal records, including daily computer print-outs.

CONTINUING VALIDITY. Except as expressly changed by this Agreement, the terms of the original obligation or obligations, including all agreements evidenced or securing the obligation(s), remain unchanged and in full force and effect. Consent by Lender to this Agreement does not waive Lender's right to strict performance of the obligation(s) as changed, nor obligate Lender to make any future change in terms. Nothing in this Agreement will constitute a satisfaction of the obligation(s). It is the intention of Lender to retain as liable parties all makers and endorser of the original obligation(s), including accommodation parties, unless a party is expressly released by Lender in writing. Any maker or endorser, including accommodation makers, will not be released by virtue of this Agreement. If any person who signed the original obligation does not sign this Agreement below, then all persons signing below acknowledge that this Agreement is given conditionally, based on the representation to Lender that the non-signing party consents to the changes and provisions of this Agreement or otherwise will not be released by it. This waiver applies not only to any initial extension, modification or release, but also to all such subsequent actions.

U.S.A. PATRIOT ACT. To help the government fight the funding of terrorism and money laundering activities, the USA PATRIOT Act requires all banks to obtain and verify the identity of each person or business that opens an account. When Borrower opens an account Lender will ask Borrower for information that will allow Lender to properly identify Borrower and Lender will verify that information. If Lender cannot properly verify identity within 30 calendar days, Lender reserves the right to deem all of the balance and accrued interest due and payable immediately.

ELECTRONIC COPIES. Lender may copy, electronically or otherwise, and thereafter destroy, the originals of this Agreement and/or Related Documents in the regular course of Lender's business. All such copies produced from an electronic form or by any other reliable means (i.e., photographic image or facsimile) shall in all respects be considered equivalent to an original, and Borrower hereby waives any rights or objections to the use of such copies.

CHANGE IN MEMBERSHIP. If Borrower or Guarantor is a limited liability company, any change in ownership of twenty-five percent (25%) or more of the membership interest of Borrower or Guarantor is an Event of Default.

CROSS DEFAULT. An Event of Default, beyond the applicable cure period, if any, or an Event of Default under any other Loan or any Related Document will constitute an Event of Default under this Agreement and a default and an Event of Default under any other agreement by Borrower or any affiliate or subsidiary of Borrower with or in favor of Lender and under any evidence of any Loan or Indebtedness held by Lender, whether or not such is specified therein. Borrower acknowledges that some Loan Documents will be preprinted forms and that it is the intent of Borrower and Lender that all Loans and Guaranties by Borrower or any affiliate or subsidiary of Borrower with or in favor of Lender be cross-defaulted with each other.

SUCCESSORS AND ASSIGNS. Subject to any limitations stated in this Agreement on transfer of Borrower's interest, this Agreement shall be binding upon and inure to the benefit of the parties, their successors and assigns. If ownership of the Collateral becomes vested in a person other than Borrower, Lender, without notice to Borrower, may deal with Borrower's successors with reference to this Agreement and the Indebtedness by way of forbearance or extension without releasing Borrower from the obligations of this Agreement or liability under the Indebtedness.

MISCELLANEOUS PROVISIONS. If any part of this Agreement cannot be enforced, this fact will not affect the rest of the Agreement. Lender may delay or forgo enforcing any of its rights or remedies under this Agreement without losing them. Borrower and any other person who signs, guarantees or endorses this Agreement, to the extent allowed by law, waive presentment, demand for payment, and notice of dishonor. Upon any change in the terms of this Agreement, and unless otherwise expressly stated in writing, no party who signs this Agreement, whether as maker, guarantor, accommodation maker or endorser, shall be released from liability. All such parties agree that Lender may renew or extend (repeatedly and for any length of time) this loan or release any party or guarantor or collateral; or impair, fail to realize upon or perfect Lenders security interest in the collateral; and take any other action deemed necessary by Lender without the consent of or notice to anyone. All such parties also agree that Lender may modify this loan without the consent of or notice to anyone other than the party with whom the modification is made. The obligations under this Agreement are joint and several.

PRIOR TO SIGNING THIS AGREEMENT, BORROWER READ AND UNDERSTOOD ALL THE PROVISIONS OF THIS AGREEMENT, INCLUDING THE VARIABLE INTEREST RATE PROVISIONS. BORROWER AGREES TO THE TERMS OF THE AGREEMENT.

BORROWER:

LANDMARK BANCORP, INC

/s/ Mark A Herpich

Mark A Herpich, Chief Fin. Officer/Secretary of
Landmark Bancorp, Inc.

FIRST NATIONAL BANK OF OMAHA

/s/ Blake J Suing

Blake J Suing, Vice President

Section 3: EX-31.1

Exhibit 31.1

CERTIFICATION PURSUANT TO RULE 13a-14(a)/15d-14(a)

I, Michael E. Scheopner, certify that:

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

Date: November 8, 2019

/s/ Michael E. Scheopner

Michael E. Scheopner
Chief Executive Officer

Section 4: EX-31.2

Exhibit 31.2

CERTIFICATION PURSUANT TO RULE 13a-14(a)/15d-14(a)

I, Mark A. Herpich, certify that:

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

Date: November 8, 2019

/s/ Mark A. Herpich

Mark A. Herpich
Chief Financial Officer

Section 5: EX-32.1

Exhibit 32.1

**CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of Landmark Bancorp, Inc. (the “Company”) on Form 10-Q for the period ended September 30, 2019 as filed with the Securities and Exchange Commission on the date hereof (the “Report”), I, Michael E. Scheopner, Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Michael E. Scheopner

Michael E. Scheopner
Chief Executive Officer
November 8, 2019

Section 6: EX-32.2

Exhibit 32.2

**CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of Landmark Bancorp, Inc. (the "Company") on Form 10-Q for the period ended September 30, 2019 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Mark A. Herpich, Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Mark A. Herpich

Mark A. Herpich
Chief Financial Officer
November 8, 2019

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