

CHOICEONE FINANCIAL SERVICES INC  
Form 10-Q  
November 16, 2009

**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, 2009

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number: **000-19202**

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

**Michigan**  
(State or Other Jurisdiction of  
Incorporation or Organization)

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

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

**49345**  
(Zip Code)

**(616) 887-7366**

(Registrant's Telephone Number, including Area Code)

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

Yes ☒ No ☐

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes ☐ No ☐

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

Large accelerated filer ☐

Accelerated filer ☐

Non-accelerated filer ☐

Smaller reporting company ☒

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

Yes ☐ No ☒

As of October 31, 2009, the Registrant had outstanding 3,263,430 shares of common stock.



**PART I. FINANCIAL INFORMATION****Item 1. Financial Statements.**

ChoiceOne Financial Services, Inc.  
**CONSOLIDATED BALANCE SHEETS**

(Dollars in thousands)	September 30, 2009 (Unaudited)	December 31, 2008 (Audited)
	<hr/>	<hr/>
<b>Assets</b>		
Cash and due from banks	\$ 7,355	\$ 9,252
Federal funds sold	5,229	1,908
	<hr/>	<hr/>
Cash and cash equivalents	12,584	11,160
Securities available for sale	75,511	77,368
Federal Home Loan Bank stock	3,304	3,304
Federal Reserve Bank stock	1,270	1,269
Loans held for sale	245	316
Loans	320,524	325,977
Allowance for loan losses	(4,103)	(3,600)
	<hr/>	<hr/>
Loans, net	316,421	322,377
Premises and equipment, net	11,863	11,745
Other real estate owned, net	4,154	3,692
Cash value of life insurance policies	9,119	8,873
Intangible assets, net	3,182	3,537
Goodwill	13,728	13,728
Other assets	5,933	6,182
	<hr/>	<hr/>
Total assets	\$ 457,314	\$ 463,551
<hr/>		
<b>Liabilities</b>		
Deposits - noninterest-bearing	\$ 55,575	\$ 54,511
Deposits - interest-bearing	303,506	292,487
	<hr/>	<hr/>
Total deposits	359,081	346,998
Advances from Federal Home Loan Bank	22,476	39,957
Securities sold under agreements to repurchase	16,992	18,786
Other liabilities	4,973	5,625
	<hr/>	<hr/>
Total liabilities	403,522	411,366

**Shareholders' Equity**

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Preferred stock; shares authorized: 100,000;

shares outstanding: none

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Common stock and paid in capital, no par value;

shares authorized: 7,000,000; shares outstanding:

3,262,311 at Sept 30, 2009 and 3,246,109 at December 31, 2008

**46,302**

46,171

Retained earnings

**6,181**

5,898

Accumulated other comprehensive income, net

**1,309**

116

Total shareholders' equity

**53,792**

52,185

Total liabilities and shareholders' equity

\$ **457,314**

\$ 463,551

See accompanying notes to consolidated financial statements.

## ChoiceOne Financial Services, Inc.

**CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME (Unaudited)**

(Dollars in thousands, except per share data)	Three Months Ended September 30,		Nine Months Ended September 30,	
	2009	2008	2009	2008
<b>Interest income</b>				
Loans, including fees	\$ 5,010	\$ 5,633	\$ 15,106	\$ 17,120
Securities:				
Taxable	284	526	1,063	1,642
Tax exempt	499	426	1,348	1,284
Other	1	15	6	65
Total interest income	5,794	6,600	17,523	20,111
<b>Interest expense</b>				
Deposits	1,348	2,054	4,347	6,950
Advances from Federal Home Loan Bank	277	437	910	1,314
Other	85	123	266	435
Total interest expense	1,710	2,614	5,523	8,699
<b>Net interest income</b>	4,084	3,986	12,000	11,412
<b>Provision for loan losses</b>	1,225	750	3,175	1,750
<b>Net interest income after provision for loan losses</b>	2,859	3,236	8,825	9,662
<b>Noninterest income</b>				
Deposit service charges	846	880	2,349	2,487
Insurance and investment commissions	166	141	566	538
Gains on sales of loans	89	45	504	179
Gains on sales of securities	35	-	158	33
Loan servicing fees, net	20	19	9	52
Earnings on life insurance policies	92	94	274	281
Other	84	(75)	337	116
Total noninterest income	1,332	1,104	4,197	3,686
<b>Noninterest expense</b>				
Compensation and benefits	1,732	1,739	5,234	5,389
Occupancy and equipment	536	543	1,614	1,625
Data processing	407	355	1,182	1,012
Professional fees	148	159	510	472
Supplies and postage	133	137	416	385
Advertising and promotional	35	43	72	103

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Intangible amortization	<b>118</b>	125	<b>355</b>	374
Director fees	<b>56</b>	74	<b>182</b>	217
FDIC insurance	<b>122</b>	72	<b>630</b>	201
Other	<b>522</b>	399	<b>1,358</b>	1,113
	<hr/>	<hr/>	<hr/>	<hr/>
Total noninterest expense	<b>3,809</b>	3,646	<b>11,553</b>	10,891
	<hr/>	<hr/>	<hr/>	<hr/>
<b>Income before income tax</b>	<b>382</b>	694	<b>1,469</b>	2,457
<b>Income tax expense (benefit)</b>	<b>(27)</b>	82	<b>14</b>	363
	<hr/>	<hr/>	<hr/>	<hr/>
<b>Net income</b>	<b>\$ 409</b>	<b>\$ 612</b>	<b>\$ 1,455</b>	<b>\$ 2,094</b>
	<hr/>	<hr/>	<hr/>	<hr/>
<b>Comprehensive income</b>	<b>\$ 1,212</b>	<b>\$ 661</b>	<b>\$ 2,648</b>	<b>\$ 1,639</b>
	<hr/>	<hr/>	<hr/>	<hr/>
<b>Basic earnings per share</b>	<b>\$ 0.13</b>	<b>\$ 0.19</b>	<b>\$ 0.45</b>	<b>\$ 0.65</b>
	<hr/>	<hr/>	<hr/>	<hr/>
<b>Diluted earnings per share</b>	<b>\$ 0.13</b>	<b>\$ 0.19</b>	<b>\$ 0.45</b>	<b>\$ 0.65</b>
	<hr/>	<hr/>	<hr/>	<hr/>
<b>Dividends declared per share</b>	<b>\$ 0.12</b>	<b>\$ 0.17</b>	<b>\$ 0.36</b>	<b>\$ 0.51</b>
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See accompanying notes to consolidated financial statements.

## ChoiceOne Financial Services, Inc.

**CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY (Unaudited)**

(Dollars in thousands)	Number of Shares	Common Stock and Paid in Capital	Retained Earnings	Accumulated Other Comprehensive Income, Net	Total
Balance, January 1, 2008	3,229,814	\$ 45,956	\$ 6,665	\$ 521	\$ 53,142
Comprehensive income					
Net income			2,094		2,094
Net change in unrealized gain on securities available for sale				(455)	(455)
Total comprehensive income					1,639
Shares issued	12,504	119			119
Change in ESOP repurchase obligation		19			19
Effect of stock options granted		24			24
Effect of employee stock purchases		10			10
Cash dividends declared (\$0.51 per share)			(1,650)		(1,650)
Balance, September 30, 2008	3,242,318	\$ 46,128	\$ 7,109	\$ 66	\$ 53,303
Balance, January 1, 2009	3,246,109	\$ 46,171	\$ 5,898	\$ 116	\$ 52,185
Comprehensive income					
Net income			1,455		1,455
Net change in unrealized gain on securities available for sale				1,193	1,193
Total comprehensive income					2,648
Shares issued	16,202	102			102
Change in ESOP repurchase obligation		2			2
Effect of stock options granted		18			18
Effect of employee stock purchases		9			9
Cash dividends declared (\$0.36 per share)			(1,172)		(1,172)
Balance, September 30, 2009	3,262,311	\$ 46,302	\$ 6,181	\$ 1,309	\$ 53,792

See accompanying notes to consolidated financial statements.



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

(Dollars in thousands)	Nine Months Ended September 30,	
	<u>2009</u>	<u>2008</u>
Cash flows from operating activities:		
Net income	\$ 1,455	\$ 2,094
Adjustments to reconcile net income to net cash from operating activities:		
Provision for loan losses	3,175	1,750
Depreciation	674	629
Amortization	835	742
Expense related to employee stock options and stock purchases	27	34
Gains on sales of securities	(158)	(33)
Gains on sales of loans	(504)	(179)
Loans originated for sale	(23,411)	(9,621)
Proceeds from loan sales	23,801	9,503
Earnings on bank-owned life insurance	(274)	(281)
Proceeds from sales of other real estate owned	1,928	1,133
Net changes in other assets	391	154
Net changes in other liabilities	(1,264)	(1,000)
Net cash from operating activities	6,675	4,925
Cash flows from investing activities:		
Securities available for sale:		
Sales	4,258	1,740
Maturities, prepayments and calls	18,505	17,864
Purchases	(19,117)	(16,606)
Loan repayments, net	(155)	(1,136)
Purchases of premises and equipment, net of disposals/sales	(461)	(722)
Net cash from investing activities	3,030	1,140
Cash flows from financing activities:		
Net change in deposits	12,083	(14,153)
Net change in securities sold under agreements to repurchase	(1,794)	(4,910)
Net change in federal funds purchased	-	5,209
Proceeds from Federal Home Loan Bank advances	29,500	30,000
Payments on Federal Home Loan Bank advances	(47,000)	(24,000)
Issuance of common stock	102	119
Cash dividends	(1,172)	(1,650)
Net cash used in financing activities	(8,281)	(9,385)
Net change in cash and cash equivalents	1,424	(3,320)

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Beginning cash and cash equivalents	<b>11,160</b>	11,140
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Ending cash and cash equivalents	<b>\$ 12,584</b>	<b>\$ 7,820</b>
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Supplemental disclosures of cash flow information:

Cash paid for interest	<b>\$ 5,721</b>	<b>\$ 9,044</b>
Cash paid for income taxes	<b>\$ 21</b>	<b>\$ 300</b>
Loans transferred to other real estate	<b>\$ 2,936</b>	<b>\$ 2,201</b>
Other real estate transferred to premises and equipment	<b>\$ 331</b>	<b>\$ -</b>

See accompanying notes to consolidated financial statements.

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

**NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

Principles of Consolidation

The consolidated financial statements include ChoiceOne Financial Services, Inc. (the "Registrant") and its wholly-owned subsidiary, ChoiceOne Bank (the "Bank"), and the Bank's wholly-owned subsidiaries ChoiceOne Insurance Agencies, Inc., and, with respect to 2008, ChoiceOne Mortgage Company of Michigan (the "Mortgage Company"). Intercompany transactions and balances have been eliminated in consolidation. Effective December 31, 2008, ChoiceOne consolidated the operations of the Mortgage Company into the Bank and eliminated the mortgage company subsidiary.

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

The accompanying consolidated financial statements reflect all adjustments ordinary in nature which are, in the opinion of management, necessary for a fair presentation of the Consolidated Balance Sheets as of September 30, 2009 and December 31, 2008, the Consolidated Statements of Income for the three- and nine-month periods ended September 30, 2009 and September 30, 2008, the Consolidated Statements of Changes in Shareholders' Equity for the nine-month periods ended September 30, 2009 and September 30, 2008, and the Consolidated Statements of Cash Flows for the nine-month periods ended September 30, 2009 and September 30, 2008. Operating results for the nine months ended September 30, 2009 are not necessarily indicative of the results that may be expected for the year ending December 31, 2009.

The accompanying consolidated financial statements should be read in conjunction with the consolidated financial statements and footnotes thereto included in the Registrant's Annual Report on Form 10-K for the year ended December 31, 2008.

Allowance for Loan Losses

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

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

Stock Transactions

A total of 7,135 shares of common stock were issued to the Registrant's Board of Directors for a cash price of \$53,000 under the terms of the Directors' Stock Purchase Plan in the first nine months of 2009. A total of 9,067 shares were

issued to employees for a cash price of \$49,000 under the Employee Stock Purchase Plan in the first three quarters of 2009.

Reclassifications

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

Subsequent Events

In accordance with Statement of Financial Accounting Standards No. 165, *Subsequent Events*, we have evaluated events through the date of this filing of November 16, 2009. Other than the transfer of other real estate owned disclosed in the Other Real Estate Owned section in Management's Discussion and Analysis, we do not believe there are any material subsequent events which would require further disclosure.

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

**NOTE 2 - ALLOWANCE FOR LOAN LOSSES**

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

(Dollars in thousands)	Three Months Ended September 30,		Nine Months Ended September 30,	
	2009	2008	2009	2008
Balance at beginning of period	\$ 3,832	\$ 3,710	\$ 3,600	\$ 3,600
Provision charged to expense	1,225	750	3,175	1,750
Recoveries credited to the allowance	164	110	417	300
Loans charged off	(1,118)	(485)	(3,089)	(1,565)
Balance at end of period	\$ 4,103	\$ 4,085	\$ 4,103	\$ 4,085

Information regarding impaired loans follows:

(Dollars in thousands)	Sept 30, 2009	December 31, 2008
Loans with no allowance allocated	\$ 5,788	\$ 5,576
Loans with allowance allocated	3,495	2,087
Amount of allowance for loan losses allocated	688	520

(Dollars in thousands)	Three Months Ended September 30,	
	2009	2008
Average balance during the period	\$ 8,797	\$ 5,568

(Dollars in thousands)	Nine Months Ended September 30,	
	2009	2008

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Average balance during the period	\$	<b>7,874</b>	\$	5,009
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**NOTE 3 - EARNINGS PER SHARE**

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

(Dollars in thousands, except per share data)	Three Months Ended September 30,		Nine Months Ended September 30,	
	<u>2009</u>	<u>2008</u>	<u>2009</u>	<u>2008</u>
<u>Basic Earnings Per Share</u>				
Net income available to common shareholders	\$ <b>409</b>	\$ 612	\$ <b>1,455</b>	\$ 2,094
<hr/>				
Weighted average common shares outstanding	<b>3,259,521</b>	3,239,451	<b>3,253,497</b>	3,234,915
<hr/>				
Basic earnings per share				