

FLUSHING FINANCIAL CORP  
Form 10-Q  
August 07, 2018

UNITED STATES

**SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

**FORM 10-Q**

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

For the quarterly period ended **June 30, 2018**

Commission file number **001-33013**

**FLUSHING FINANCIAL CORPORATION**

*(Exact name of registrant as specified in its charter)*

**Delaware**

*(State or other jurisdiction of incorporation or organization)*

**11-3209278**

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

**220 RXR Plaza, Uniondale, New York 11556**

*(Address of principal executive offices)*

**(718) 961-5400**

*(Registrant's telephone number, including area code)*

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).  Yes No

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

Emerging growth company

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

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

The number of shares of the registrant's Common Stock outstanding as of July 31, 2018 was 28,295,441.

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**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Consolidated Statements of Financial Condition**

(Unaudited)

**Item 1. Financial Statements**

|   | June 30,<br>2018                                 | December<br>31,<br>2017 |
|---|--|-------------------------|
|   | (Dollars in thousands,<br>except per share data) |                         |
| Assets  |  |                         |
| Cash and due from banks   | \$42,805   | \$51,546                |
| Securities held-to-maturity:  |  |                         |
| Mortgage-backed securities (including assets pledged of \$4,801 at June 30, 2018 and none pledged at December 31, 2017; fair value of \$7,373 and \$7,810 at June 30, 2018 and December 31, 2017, respectively)   | 7,963  | 7,973                   |
| Other securities (none pledged; fair value of \$21,281 and \$21,889 at June 30, 2018 and December 31, 2017, respectively)   | 23,130   | 22,913                  |
| Securities available for sale, at fair value:   |  |                         |
| Mortgage-backed securities (including assets pledged of \$144,942 and \$148,505 at June 30, 2018 and December 31, 2017, respectively; \$1,426 and \$1,590 at fair value pursuant to the fair value option at June 30, 2018 and December 31, 2017, respectively) | 513,868  | 509,650                 |
| Other securities (including assets pledged of \$25,812 and \$44,052 at June 30, 2018 and December 31, 2017, respectively; \$12,615 and \$12,685 at fair value pursuant to the fair value option at June 30, 2018 and December 31, 2017, respectively)           | 214,755  | 228,704                 |
| Loans:  |  |                         |
| Multi-family residential  | 2,247,852  | 2,273,595               |
| Commercial real estate  | 1,471,894  | 1,368,112               |
| One-to-four family mixed-use property   | 564,474  | 564,206                 |
| One-to-four family residential  | 187,741  | 180,663                 |
| Co-operative apartments   | 7,839  | 6,895                   |
| Construction  | 33,826   | 8,479                   |
| Small Business Administration   | 14,405   | 18,479                  |
| Taxi medallion  | 6,225  | 6,834                   |
| Commercial business and other   | 783,904  | 732,973                 |
| Net unamortized premiums and unearned loan fees   | 15,647   | 16,763                  |
| Allowance for loan losses   | (20,220 )  | (20,351 )               |
| Net loans   | 5,313,587  | 5,156,648               |
| Interest and dividends receivable   | 24,184   | 21,405                  |
| Bank premises and equipment, net  | 30,658   | 30,836                  |

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|   |             |             |
|---|-------------|-------------|
| Federal Home Loan Bank of New York stock, at cost   | 57,384      | 60,089      |
| Bank owned life insurance   | 131,429     | 131,856     |
| Goodwill  | 16,127      | 16,127      |
| Other assets  | 91,726      | 61,527      |
| Total assets  | \$6,467,616 | \$6,299,274 |
| Liabilities   |             |             |
| Due to depositors:  |             |             |
| Non-interest bearing  | \$388,467   | \$385,269   |
| Interest-bearing  | 4,170,411   | 3,955,403   |
| Mortgagors' escrow deposits   | 50,781      | 42,606      |
| Borrowed funds:   |             |             |
| Federal Home Loan Bank advances   | 1,137,318   | 1,198,968   |
| Subordinated debentures   | 73,848      | 73,699      |
| Junior subordinated debentures, at fair value   | 39,566      | 36,986      |
| Total borrowed funds  | 1,250,732   | 1,309,653   |
| Other liabilities   | 69,181      | 73,735      |
| Total liabilities   | 5,929,572   | 5,766,666   |
| Stockholders' Equity  |             |             |
| Preferred stock (\$0.01 par value; 5,000,000 shares authorized; none issued)  | -           | -           |
| Common stock (\$0.01 par value; 100,000,000 shares authorized; 31,530,595 shares issued at June 30, 2018 and December 31, 2017; 28,319,213 shares and 28,588,266 shares outstanding at June 30, 2018 and December 31, 2017, respectively) | 315         | 315         |
| Additional paid-in capital  | 220,432     | 217,906     |
| Treasury stock, at average cost (3,211,382 shares and 2,942,329 shares at June 30, 2018 and December 31, 2017, respectively)  | (66,656 )   | (57,675 )   |
| Retained earnings   | 395,960     | 381,048     |
| Accumulated other comprehensive loss, net of taxes  | (12,007 )   | (8,986 )    |
| Total stockholders' equity  | 538,044     | 532,608     |
| Total liabilities and stockholders' equity  | \$6,467,616 | \$6,299,274 |

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

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Consolidated Statements of Income**

(Unaudited)

| (Dollars in thousands, except per share data)       | For the three<br>months<br>ended June 30, |          | For the six months<br>ended June 30, |           |
|---|---|----------|--------------------------------------|-----------|
|   | 2018                                      | 2017     | 2018                                 | 2017      |
| Interest and dividend income                        |   |          |                                      |           |
| Interest and fees on loans                          | \$57,322                                  | \$51,631 | \$112,339                            | \$102,516 |
| Interest and dividends on securities:               |   |          |                                      |           |
| Interest  | 5,616                                     | 6,432    | 11,084                               | 12,527    |
| Dividends   | 17  | 123      | 31                                   | 244       |
| Other interest income                               | 338                                       | 129      | 625                                  | 282       |
| Total interest and dividend income                  | 63,293                                    | 58,315   | 124,079                              | 115,569   |
| Interest expense                                    |   |          |                                      |           |
| Deposits  | 14,788                                    | 9,510    | 26,898                               | 18,490    |
| Other interest expense                              | 5,865                                     | 5,188    | 11,932                               | 10,073    |
| Total interest expense                              | 20,653                                    | 14,698   | 38,830                               | 28,563    |
| Net interest income                                 | 42,640                                    | 43,617   | 85,249                               | 87,006    |
| Provision for loan losses                           | -   | -        | 153                                  | -         |
| Net interest income after provision for loan losses | 42,640                                    | 43,617   | 85,096                               | 87,006    |
| Non-interest income                                 |   |          |                                      |           |
| Banking services fee income                         | 1,000                                     | 1,014    | 1,948                                | 1,888     |
| Net gain on sale of loans                           | 421                                       | 34       | 158                                  | 244       |
| Net loss from fair value adjustments                | (267 )                                    | (1,159 ) | (367 )                               | (1,537 )  |
| Federal Home Loan Bank of New York stock dividends  | 881                                       | 643      | 1,757                                | 1,466     |
| Gain from life insurance proceeds                   | -   | 6        | 776                                  | 1,167     |
| Bank owned life insurance                           | 776                                       | 807      | 1,538                                | 1,602     |
| Other income  | 357                                       | 603      | 558                                  | 807       |
| Total non-interest income                           | 3,168                                     | 1,948    | 6,368                                | 5,637     |
| Non-interest expense                                |   |          |                                      |           |
| Salaries and employee benefits                      | 15,291                                    | 15,424   | 33,746                               | 32,528    |
| Occupancy and equipment                             | 2,476                                     | 2,654    | 5,053                                | 5,150     |
| Professional services                               | 2,439                                     | 1,919    | 4,624                                | 3,915     |
| FDIC deposit insurance                              | 547                                       | 503      | 1,047                                | 829       |
| Data processing                                     | 1,426                                     | 1,321    | 2,827                                | 2,524     |
| Depreciation and amortization                       | 1,455                                     | 1,155    | 2,844                                | 2,320     |

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|  |          |          |          |          |
|--|----------|----------|----------|----------|
| Other real estate owned/foreclosure expense (income) | 40       | (96 )    | 136      | 255      |
| Net gain from sales of real estate owned             | (27 )    | -        | (27 )    | (50 )    |
| Other operating expenses                             | 3,749    | 3,185    | 8,440    | 8,158    |
| Total non-interest expense                           | 27,396   | 26,065   | 58,690   | 55,629   |
| Income before income taxes                           | 18,412   | 19,500   | 32,774   | 37,014   |
| Provision for income taxes                           |          |          |          |          |
| Federal  | 3,311    | 5,576    | 5,918    | 10,325   |
| State and local                                      | 1,178    | 1,199    | 1,521    | 1,704    |
| Total taxes  | 4,489    | 6,775    | 7,439    | 12,029   |
| Net income   | \$13,923 | \$12,725 | \$25,335 | \$24,985 |
| Basic earnings per common share                      | \$0.48   | \$0.44   | \$0.88   | \$0.86   |
| Diluted earnings per common share                    | \$0.48   | \$0.44   | \$0.88   | \$0.86   |
| Dividends per common share                           | \$0.20   | \$0.18   | \$0.40   | \$0.36   |

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



**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Consolidated Statements of Comprehensive Income**

(Unaudited)

| (In thousands)   | For the three<br>months ended<br>June 30,<br>2018 |           | For the six months<br>ended<br>June 30,<br>2018 |           |
|--|---|-----------|---|-----------|
|  | 2017  | 2017      | 2017  | 2017      |
| Net income   | \$ 13,923   | \$ 12,725 | \$ 25,335                                       | \$ 24,985 |
| Other comprehensive income (loss), net of tax:   |   |           |   |           |
| Amortization of actuarial losses, net of taxes of \$(43) and (\$64) for the three months ended June 30, 2018 and 2017, respectively and of (\$84) and (\$128) for six months ended June 30, 2018 and 2017, respectively.             | 90  | 87        | 181   | 174       |
| Amortization of prior service credits, net of taxes of \$3 and \$5 for the three months ended June 30, 2018 and 2017, respectively and of \$6 and \$9 for six months ended June 30, 2018 and 2017, respectively.                     | (6 )  | (6 )      | (13 )   | (13 )     |
| Net unrealized (losses) gains on securities, net of taxes of \$1,388 and (\$436) for three months ended June 30, 2018 and 2017, respectively and of \$4,443 and (\$1,247) for six months ended June 30, 2018 and 2017, respectively. | (3,014 )  | 601       | (9,654 )  | 1,749     |
| Net unrealized gains (losses) on cash flow hedges, net of taxes of (\$961) and \$90 three months ended June 30, 2018 and 2017, respectively and of (\$3,565) and \$90 for six months ended June 30, 2018 and 2017, respectively.     | 2,085   | (124 )    | 7,746   | (124 )    |
| Change in fair value of liabilities related to instrument-specific credit risk, net of taxes of (\$6) for the three and six months ended June 30, 2018.  | 13  | -         | 13  | -         |
| Total other comprehensive income (loss), net of tax  | (832 )  | 558       | (1,727 )  | 1,786     |
| Comprehensive income   | \$ 13,091   | \$ 13,283 | \$ 23,608                                       | \$ 26,771 |

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

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Consolidated Statements of Cash Flows**

(Unaudited)

| (In thousands)  | For the six months<br>ended<br>June 30, |           |
|---|---|-----------|
|   | 2018                                    | 2017      |
| <b>CASH FLOWS FROM OPERATING ACTIVITIES</b>                                       |   |           |
| Net income  | \$25,335                                | \$24,985  |
| Adjustments to reconcile net income to net cash provided by operating activities: |   |           |
| Provision for loan losses   | 153                                     | -         |
| Depreciation and amortization of bank premises and equipment                      | 2,844                                   | 2,320     |
| Amortization of premium, net of accretion of discount                             | 4,463                                   | 3,657     |
| Net loss from fair value adjustments  | 367                                     | 1,537     |
| Net gain from sale of loans   | (158 )                                  | (244 )    |
| Net gain from sale of OREO  | (27 )                                   | (50 )     |
| Income from bank owned life insurance   | (1,538 )                                | (1,602 )  |
| Gain from life insurance proceeds   | (776 )                                  | (1,167 )  |
| Stock-based compensation expense  | 4,680                                   | 4,190     |
| Deferred compensation   | (1,815 )                                | (1,930 )  |
| Deferred income tax (benefit) provision   | (415 )                                  | 1,005     |
| Increase in other liabilities   | 840                                     | 4         |
| Decrease (increase) in other assets   | 2,747                                   | (21 )     |
| Net cash provided by operating activities   | 36,700                                  | 32,684    |
| <b>CASH FLOWS FROM INVESTING ACTIVITIES</b>                                       |   |           |
| Purchases of bank premises and equipment  | (2,666 )                                | (2,351 )  |
| Net redemptions (purchases) of Federal Home Loan Bank of New York shares          | 2,705                                   | (7,457 )  |
| Purchases of securities held-to-maturity  | (353 )                                  | (8,030 )  |
| Proceeds from maturities of securities held-to-maturity                           | 45                                      | 13,330    |
| Purchases of securities available for sale  | (57,265 )                               | (40,641 ) |
| Proceeds from sales and calls of securities available for sale                    | 10,000                                  | 27,500    |
| Proceeds from maturities and prepayments of securities available for sale         | 40,915                                  | 38,161    |
| Proceeds from bank owned life insurance   | 2,741                                   | 3,911     |
| Net originations of loans   | (81,420 )                               | (201,438) |
| Purchases of loans  | (110,140)                               | (58,431 ) |
| Proceeds from sale of real estate owned   | 665                                     | 583       |
| Proceeds from sale of loans   | 10,200                                  | 21,575    |
| Net cash used in investing activities   | (184,573)                               | (213,288) |
| <b>CASH FLOWS FROM FINANCING ACTIVITIES</b>                                       |   |           |
| Net increase in non-interest bearing deposits                                     | 3,198                                   | 16,139    |

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|   |           |           |
|---|-----------|-----------|
| Net increase in interest-bearing deposits                             | 214,773   | 31,629    |
| Net increase in mortgagors' escrow deposits                           | 8,175     | 1,087     |
| Net proceeds from short-term borrowed funds                           | 73,500    | 66,500    |
| Proceeds from long-term borrowings                                    | 25,000    | 173,066   |
| Repayment of long-term borrowings                                     | (160,084) | (82,049 ) |
| Purchases of treasury stock   | (13,889 ) | (2,599 )  |
| Proceeds from issuance of common stock upon exercise of stock options | 6         | -         |
| Cash dividends paid   | (11,547 ) | (10,487 ) |
| Net cash provided by financing activities                             | 139,132   | 193,286   |
| <br>  |           |           |
| Net (decrease) increase in cash and cash equivalents                  | (8,741 )  | 12,682    |
| Cash and cash equivalents, beginning of period                        | 51,546    | 35,857    |
| Cash and cash equivalents, end of period                              | \$42,805  | \$48,539  |
| <br>  |           |           |
| SUPPLEMENTAL CASH FLOW DISCLOSURE                                     |           |           |
| Interest paid   | \$36,296  | \$27,840  |
| Income taxes paid   | 3,103     | 10,646    |
| Taxes paid if excess tax benefits were not tax deductible             | 3,739     | 9,409     |
| Non-cash activities:  |           |           |
| Loans transferred to Other Real Estate Owned or Other Assets          | 673       | -         |
| Loans held for investment transferred to loans available for sale     | -         | 30,565    |

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

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Consolidated Statements of Changes in Stockholders' Equity****For the six months ended June 30, 2018 and 2017**

(Unaudited)

| (Dollars in thousands, except per share data)   | Total     | Common<br>Stock | Additional<br>Paid-in<br>Capital | Retained<br>Earnings | Treasury<br>Stock | Accumulated<br>Other<br>Comprehensive<br>Income (Loss) |
|---|-----------|-----------------|----------------------------------|----------------------|-------------------|--|
| Balance at December 31, 2017  | \$532,608 | \$ 315          | \$217,906                        | \$381,048            | \$(57,675)        | \$ (8,986 )  |
| Reclassification of the Income Tax Effects of the Tax Cuts and Jobs Act from Accumulated Other Comprehensive Income (Loss) to Retained Earnings | -         | -               | -                                | 2,073                | -                 | (2,073 )   |
| Impact of adoption of Accounting Standard Update 2016-01  | -         | -               | -                                | (779 )               | -                 | 779  |
| Net income  | 25,335    | -               | -                                | 25,335               | -                 | -  |
| Award of common shares released from Employee Benefit Trust (120,684 shares)  | 2,578     | -               | 2,578                            | -                    | -                 | -  |
| Vesting of restricted stock unit awards (248,877 shares)  | -         | -               | (4,731 )                         | (170 )               | 4,901             | -  |
| Exercise of stock options (600 shares)  | 6         | -               | (1 )                             | -                    | 7                 | -  |
| Stock-based compensation expense  | 4,680     | -               | 4,680                            | -                    | -                 | -  |
| Purchase of treasury shares (445,444 shares)  | (11,838 ) | -               | -                                | -                    | (11,838)          | -  |
| Repurchase of shares to satisfy tax obligation (72,869 shares)  | (2,051 )  | -               | -                                | -                    | (2,051 )          | -  |
| Dividends on common stock (\$0.40 per share)  | (11,547 ) | -               | -                                | (11,547 )            | -                 | -  |
| Other comprehensive loss  | (1,727 )  | -               | -                                | -                    | -                 | (1,727 )   |
| Balance at June 30, 2018  | \$538,044 | \$ 315          | \$220,432                        | \$395,960            | \$(66,656)        | \$ (12,007 )   |
| Balance at December 31, 2016  | \$513,853 | \$ 315          | \$214,462                        | \$361,192            | \$(53,754)        | \$ (8,362 )  |
| Net income  | 24,985    | -               | -                                | 24,985               | -                 | -  |
| Award of common shares released from Employee Benefit Trust (111,470 shares)  | 2,363     | -               | 2,363                            | -                    | -                 | -  |
| Vesting of restricted stock unit awards (258,165 shares)  | -         | -               | (4,562 )                         | (262 )               | 4,824             | -  |

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|  |           |        |           |           |            |            |
|--|-----------|--------|-----------|-----------|------------|------------|
| Exercise of stock options (4,400 shares)                       | -         | -      | (6 )      | (40 )     | 46         | -          |
| Stock-based compensation expense                               | 4,190     | -      | 4,190     | -         | -          | -          |
| Purchase of treasury shares (10,000 shares)                    | (278 )    | -      | -         | -         | (278 )     | -          |
| Repurchase of shares to satisfy tax obligation (80,303 shares) | (2,321 )  | -      | -         | -         | (2,321 )   | -          |
| Dividends on common stock (\$0.36 per share)                   | (10,487 ) | -      | -         | (10,487 ) | -          | -          |
| Other comprehensive income                                     | 1,786     | -      | -         | -         | -          | 1,786      |
| Balance at June 30, 2017                                       | \$534,091 | \$ 315 | \$216,447 | \$375,388 | \$(51,483) | \$(6,576 ) |

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

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## **PART I – FINANCIAL INFORMATION**

### **FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES**

#### **Notes to Consolidated Financial Statements**

(Unaudited)

#### **1. Basis of Presentation**

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

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

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

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

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

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

## 2. Use of Estimates

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

## 3. Earnings Per Share

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

|   | For the three months ended<br>June 30,        |          | For the six months ended<br>June 30, |          |
|---|---|----------|--------------------------------------|----------|
|   | 2018  | 2017     | 2018                                 | 2017     |
|   | (Dollars in thousands, except per share data) |          |                                      |          |
| Net income, as reported   | \$13,923                                      | \$12,725 | \$25,335                             | \$24,985 |
| Divided by:   |   |          |                                      |          |
| Weighted average common shares outstanding                                    | 28,845  | 29,135   | 28,909                               | 29,077   |
| Weighted average common stock equivalents                                     | 1   | 1        | 1                                    | 3        |
| Total weighted average common shares outstanding and common stock equivalents | 28,846  | 29,136   | 28,910                               | 29,080   |
| Basic earnings per common share   | \$0.48  | \$0.44   | \$0.88                               | \$0.86   |
| Diluted earnings per common share <sup>(1)</sup>                              | \$0.48  | \$0.44   | \$0.88                               | \$0.86   |
| Dividend payout ratio   | 41.7  | % 40.9   | % 45.5                               | % 41.9   |

(1) For the three and six months ended June 30, 2018 and 2017, there were no common stock equivalents that were anti-dilutive.

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

**4. Securities**

The Company did not hold any trading securities at June 30, 2018 and December 31, 2017. Securities available for sale are recorded at fair value. Securities held-to-maturity are recorded at amortized cost.

The following table summarizes the Company's portfolio of securities held-to-maturity at June 30, 2018:

|                                  | Amortized<br>Cost | Fair<br>Value | Gross<br>Unrealized<br>Gains | Gross<br>Unrealized<br>Losses |
|----------------------------------|-------------------|---------------|------------------------------|-------------------------------|
| (In thousands)                   |                   |               |                              |                               |
| Securities held-to-maturity:     |                   |               |                              |                               |
| Municipals                       | \$23,130          | \$21,281      | \$ -                         | \$ 1,849                      |
| Total other securities           | 23,130            | 21,281        | -                            | 1,849                         |
| FNMA                             | 7,963             | 7,373         | -                            | 590                           |
| Total mortgage-backed securities | 7,963             | 7,373         | -                            | 590                           |
| Total                            | \$31,093          | \$28,654      | \$ -                         | \$ 2,439                      |

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

|                              | Amortized<br>Cost | Fair<br>Value | Gross<br>Unrealized<br>Gains | Gross<br>Unrealized<br>Losses |
|------------------------------|-------------------|---------------|------------------------------|-------------------------------|
| (In thousands)               |                   |               |                              |                               |
| Securities held-to-maturity: |                   |               |                              |                               |
| Municipals                   | \$22,913          | \$21,889      | \$ -                         | \$ 1,024                      |
| Total other securities       | 22,913            | 21,889        | -                            | 1,024                         |
| FNMA                         | 7,973             | 7,810         | -                            | 163                           |



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|                                  |          |          |      |          |
|----------------------------------|----------|----------|------|----------|
| Total mortgage-backed securities | 7,973    | 7,810    | -    | 163      |
| Total                            | \$30,886 | \$29,699 | \$ - | \$ 1,187 |

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**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

The following table summarizes the Company's portfolio of securities available for sale at June 30, 2018:

|                                     | Amortized<br>Cost | Fair Value | Gross<br>Unrealized<br>Gains | Gross<br>Unrealized<br>Losses |
|-------------------------------------|-------------------|------------|------------------------------|-------------------------------|
|                                     | (In thousands)    |            |                              |                               |
| Corporate                           | \$ 110,000        | \$ 100,532 | \$ -                         | \$ 9,468                      |
| Municipals                          | 100,576           | 101,608    | 1,063                        | 31                            |
| Mutual funds                        | 11,427            | 11,427     | -                            | -                             |
| Other                               | 1,188             | 1,188      | -                            | -                             |
| Total other securities              | 223,191           | 214,755    | 1,063                        | 9,499                         |
| REMIC and CMO                       | 342,394           | 332,381    | 80                           | 10,093                        |
| GNMA                                | 847               | 898        | 51                           | -                             |
| FNMA                                | 133,359           | 129,222    | 54                           | 4,191                         |
| FHLMC                               | 52,925            | 51,367     | 12                           | 1,570                         |
| Total mortgage-backed securities    | 529,525           | 513,868    | 197                          | 15,854                        |
| Total securities available for sale | \$ 752,716        | \$ 728,623 | \$ 1,260                     | \$ 25,353                     |

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

|                                     | Amortized<br>Cost | Fair Value | Gross<br>Unrealized<br>Gains | Gross<br>Unrealized<br>Losses |
|-------------------------------------|-------------------|------------|------------------------------|-------------------------------|
|                                     | (In thousands)    |            |                              |                               |
| Corporate                           | \$ 110,000        | \$ 102,767 | \$ -                         | \$ 7,233                      |
| Municipals                          | 101,680           | 103,199    | 1,519                        | -                             |
| Mutual funds                        | 11,575            | 11,575     | -                            | -                             |
| Collateralized loan obligations     | 10,000            | 10,053     | 53                           | -                             |
| Other                               | 1,110             | 1,110      | -                            | -                             |
| Total other securities              | 234,365           | 228,704    | 1,572                        | 7,233                         |
| REMIC and CMO                       | 328,668           | 325,302    | 595                          | 3,961                         |
| GNMA                                | 1,016             | 1,088      | 72                           | -                             |
| FNMA                                | 136,198           | 135,474    | 330                          | 1,054                         |
| FHLMC                               | 48,103            | 47,786     | 18                           | 335                           |
| Total mortgage-backed securities    | 513,985           | 509,650    | 1,015                        | 5,350                         |
| Total securities available for sale | \$ 748,350        | \$ 738,354 | \$ 2,587                     | \$ 12,583                     |

Mortgage-backed securities shown in the table above include one private issue collateralized mortgage obligation (“CMO”) that is collateralized by commercial real estate mortgages with an amortized cost and market value of \$21,000 at December 31, 2017. We did not hold any private issue CMO’s that are collateralized by commercial real estate mortgages at June 30, 2018.

The corporate securities held by the Company at June 30, 2018 and December 31, 2017 are issued by U.S. banking institutions.

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**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

The following tables detail the amortized cost and fair value of the Company's securities classified as held-to-maturity and available for sale at June 30, 2018, by contractual maturity. Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

| Securities held-to-maturity: | Amortized Fair |          |
|------------------------------|----------------|----------|
|                              | Cost           | Value    |
|                              | (In thousands) |          |
| Due in one year or less      | \$1,353        | \$1,353  |
| Due after ten years          | 21,777         | 19,928   |
| Total other securities       | 23,130         | 21,281   |
| Mortgage-backed securities   | 7,963          | 7,373    |
| Total                        | \$31,093       | \$28,654 |

| Securities available for sale:         | Amortized      |            |
|--|----------------|------------|
|  | Cost           | Fair Value |
|  | (In thousands) |            |
| Due in one year or less                | \$-            | \$-        |
| Due after one year through five years  | 4,248          | 4,269      |
| Due after five years through ten years | 125,569        | 116,201    |
| Due after ten years                    | 81,947         | 82,858     |
| Total other securities                 | 211,764        | 203,328    |
| Mutual funds                           | 11,427         | 11,427     |
| Mortgage-backed securities             | 529,525        | 513,868    |
| Total                                  | \$752,716      | \$728,623  |

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

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

|                                      | At June 30, 2018       |            |                      |                     |                      |                   |                      |
|--------------------------------------|------------------------|------------|----------------------|---------------------|----------------------|-------------------|----------------------|
|                                      | Total<br>Coun          | Fair Value | Unrealized<br>Losses | Less than 12 months |                      | 12 months or more |                      |
|                                      |                        |            |                      | Fair Value          | Unrealized<br>Losses | Fair Value        | Unrealized<br>Losses |
|                                      | (Dollars in thousands) |            |                      |                     |                      |                   |                      |
| <b>Held-to-maturity securities</b>   |                        |            |                      |                     |                      |                   |                      |
| Municipals                           | 1                      | \$19,928   | \$1,849              | \$-                 | \$-                  | \$19,928          | \$1,849              |
| Total other securities               | 1                      | 19,928     | 1,849                | -                   | -                    | 19,928            | 1,849                |
| <b>FNMA</b>                          |                        |            |                      |                     |                      |                   |                      |
| Total mortgage-backed securities     | 1                      | 7,373      | 590                  | 7,373               | 590                  | -                 | -                    |
| Total                                | 2                      | \$27,301   | \$2,439              | \$7,373             | \$590                | \$19,928          | \$1,849              |
| <b>Available for sale securities</b> |                        |            |                      |                     |                      |                   |                      |
| Corporate                            | 14                     | \$100,532  | \$9,468              | \$9,394             | \$606                | \$91,138          | \$8,862              |
| Municipals                           | 2                      | 5,088      | 31                   | 5,088               | 31                   | -                 | -                    |
| Total other securities               | 16                     | 105,620    | 9,499                | 14,482              | 637                  | 91,138            | 8,862                |
| <b>REMIC and CMO</b>                 |                        |            |                      |                     |                      |                   |                      |
| FNMA                                 | 23                     | 126,338    | 4,191                | 110,983             | 3,445                | 15,355            | 746                  |
| FHLMC                                | 2                      | 42,830     | 1,570                | 39,920              | 1,438                | 2,910             | 132                  |
| Total mortgage-backed securities     | 73                     | 481,369    | 15,854               | 382,139             | 10,743               | 99,230            | 5,111                |
| Total                                | 89                     | \$586,989  | \$25,353             | \$396,621           | \$11,380             | \$190,368         | \$13,973             |
| <b>At December 31, 2017</b>          |                        |            |                      |                     |                      |                   |                      |
|                                      | Total<br>Coun          | Fair Value | Unrealized<br>Losses | Less than 12 months |                      | 12 months or more |                      |
|                                      |                        |            |                      | Fair Value          | Unrealized<br>Losses | Fair Value        | Unrealized<br>Losses |
|                                      | (Dollars in thousands) |            |                      |                     |                      |                   |                      |
| <b>Held-to-maturity securities</b>   |                        |            |                      |                     |                      |                   |                      |
| Municipals                           | 1                      | \$20,844   | \$1,024              | \$20,844            | \$1,024              | \$-               | \$-                  |

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

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## **PART I – FINANCIAL INFORMATION**

### **FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES**

#### **Notes to Consolidated Financial Statements**

(Unaudited)

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

The Company reviewed each investment that had an unrealized loss at June 30, 2018 and December 31, 2017. The unrealized losses in held-to-maturity municipal securities at June 30, 2018 and December 31, 2017 were caused by illiquidity in the market and movements in interest rates. The unrealized losses in held-to-maturity FNMA securities at June 30, 2018 and December 31, 2017 were caused by movements in interest rates. The unrealized losses in securities available for sale at June 30, 2018 and December 31, 2017 were caused by movements in interest rates.

It is not anticipated that these securities would be settled at a price that is less than the amortized cost of the Company’s investment. Each of these securities is performing according to its terms and, in the opinion of management, will continue to perform according to its terms. The Company does not have the intent to sell these securities and it is more likely than not the Company will not be required to sell the securities before recovery of the securities’ amortized cost basis. This conclusion is based upon considering the Company’s cash and working capital requirements and contractual and regulatory obligations, none of which the Company believes would cause the sale of the securities. Therefore, the Company did not consider these investments to be other-than-temporarily impaired at June 30, 2018 and December 31, 2017.

The Company did not sell any securities during the three and six months ended June 30, 2018 and 2017.

#### **5.Loans**

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

on loans which pay in full prior to their scheduled maturity are included in interest income in the period they are collected.

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

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

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

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





**PART I – FINANCIAL INFORMATION**

**FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES**

**Notes to Consolidated Financial Statements**

(Unaudited)

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

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

The Company considers fair value of collateral dependent loans to be 85% of the appraised or internally estimated value of the property. The 85% is based on the actual net proceeds the Bank has received from the sale of other real estate owned (“OREO”) as a percentage of OREO’s appraised value. For collateral dependent taxi medallion loans, the Company considers fair value to be the value of the underlying medallion based upon the most recently reported arm’s length sales transaction. When there is no recent sale activity, the fair value is calculated using capitalization rates. For both collateral dependent mortgage loans and taxi medallion loans, the amount by which the loan’s book value exceeds fair value is charged-off. During the three months ended June 30, 2018, the fair value of Chicago taxi medallion loans was reduced from \$60,000 per medallion to \$25,000 per medallion, based upon recent sales transactions. At June 30, 2018, our exposure to the Chicago taxi medallion portfolio totals \$0.2 million and to all taxi medallion loans held \$6.2 million, which is 0.12% of total loans.

The Company segregated its loans into two portfolios based on year of origination. One portfolio was reviewed for loans originated after December 31, 2009 and a second portfolio for loans originated prior to January 1, 2010. Our decision to segregate the portfolio based upon origination dates was based on changes made in our underwriting standards during 2009. By the end of 2009, all loans were being underwritten based on revised and tightened underwriting standards. Loans originated prior to 2010 have a higher delinquency rate and loss history. Each of the years in the portfolio for loans originated prior to 2010 has a similar delinquency rate. During the three months ended June 30, 2018, the Loss Emergence Period (“LEP”) used was 1.33 years for the Residential portfolio and 1.58 years for the Commercial portfolio. In the prior quarter, a blended LEP of 1.33 years was used for both portfolios. The Company’s Board of Directors reviews and approves management’s evaluation of the adequacy of the allowance for loan losses on a quarterly basis.

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

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

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

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

The allocation of a portion of the allowance for loan losses for a performing TDR loan is based upon the present value of the future expected cash flows discounted at the loan's original effective rate, or for a non-performing TDR loan which is collateral dependent, the fair value of the collateral. At June 30, 2018, there were no commitments to lend additional funds to borrowers whose loans were modified to a TDR. The modification of loans to a TDR did not have a significant effect on our operating results, nor did it require a significant allocation of the allowance for loan losses.

The Company did not modify any loans as TDR during the three and six months ended June 30, 2018.

The following tables shows loans modified and classified as TDR during the periods indicated:

| (Dollars in thousands) | For the three and six months ended<br>June 30, 2017 |         | Modification description   |
|------------------------|---|---------|--|
|                        | Number  | Balance |  |
| Taxi medallion         | 5   | \$4,289 | Three received a below market interest rate and a loan amortization extension, while two received an amortization extension. |
| Total                  | 5   | \$4,289 |  |

The recorded investment of the loans modified and classified as TDR presented in the table above, were unchanged as there was no principal forgiven in this modification.

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

| (Dollars in thousands) | June 30, 2018           | December 31,<br>2017    |
|------------------------|-------------------------|-------------------------|
|                        | Number<br>of investment | Number<br>of investment |
|                        |                         |                         |

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|   | contracts |           | contracts |           |
|---|-----------|-----------|-----------|-----------|
| Multi-family residential                    | 9         | \$ 2,488  | 9         | \$ 2,518  |
| Commercial real estate                      | -         | -         | 2         | 1,986     |
| One-to-four family - mixed-use property     | 5         | 1,726     | 5         | 1,753     |
| One-to-four family - residential            | 3         | 562       | 3         | 572       |
| Taxi medallion                              | 19        | 5,482     | 20        | 5,916     |
| Commercial business and other               | 2         | 351       | 2         | 462       |
| Total performing troubled debt restructured | 38        | \$ 10,609 | 41        | \$ 13,207 |

During the six months ended June 30, 2018, we sold one commercial real estate TDR loan totaling \$1.8 million, for a loss of \$0.3 million and foreclosed on one taxi medallion TDR loan of \$35,000, which is included in “Other Assets”. There were no TDR loans that defaulted during the period, which were within 12 months of their modification date.

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

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

| (Dollars in thousands)   | June 30, 2018<br>Number<br>of Recorded<br>investment<br>contracts | December 31,<br>2017<br>Number<br>of Recorded<br>investment<br>contracts |
|--|---|--|
| Multi-family residential                                       | 1 \$ 383  | 1 \$ 383   |
| Total troubled debt restructurings that subsequently defaulted | 1 \$ 383  | 1 \$ 383   |

There were no TDR loans transferred to non-performing status during the three months ended June 30, 2018 and 2017 and the six months ended June 30, 2017.

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

| (In thousands)   | June 30,<br>2018 | December<br>31,<br>2017 |
|--|------------------|-------------------------|
| Loans ninety days or more past due and still accruing: |                  |                         |
| Commercial real estate                                 | \$-              | \$2,424                 |
| Construction   | 730              | -                       |
| Total  | 730              | 2,424                   |
| Non-accrual mortgage loans:                            |                  |                         |
| Multi-family residential                               | 2,165            | 3,598                   |
| Commercial real estate                                 | 1,448            | 1,473                   |
| One-to-four family - mixed-use property                | 2,157            | 1,867                   |
| One-to-four family - residential                       | 6,969            | 7,808                   |
| Co-operative apartments                                | 575              | -                       |
| Total  | 13,314           | 14,746                  |

Non-accrual non-mortgage loans:

|                               |          |          |
|-------------------------------|----------|----------|
| Small Business Administration | -        | 46       |
| Taxi medallion                | 743      | 918      |
| Commercial business and other | 2        | -        |
| Total                         | 745      | 964      |
| <br>                          |          |          |
| Total non-accrual loans       | 14,059   | 15,710   |
| <br>                          |          |          |
| Total non-performing loans    | \$14,789 | \$18,134 |

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**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

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

|   | For the three months ended June 30, 2018 |       | For the six months ended June 30, 2017 |       |
|---|--|-------|--|-------|
|   | 2018                                     | 2017  | 2018                                   | 2017  |
|   | (In thousands)                           |       |  |       |
| Interest income that would have been recognized had the loans performed in accordance with their original terms | \$390                                    | \$433 | \$798                                  | \$848 |
| Less: Interest income included in the results of operations   | 156                                      | 141   | 315                                    | 268   |
| Total foregone interest   | \$234                                    | \$292 | \$483                                  | \$580 |

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

| (In thousands)                          | June 30, 2018         |                       |                      |                | Current     | Total Loans |
|---|-----------------------|-----------------------|----------------------|----------------|-------------|-------------|
|   | 30 - 59 Days Past Due | 60 - 89 Days Past Due | Greater than 90 Days | Total Past Due |             |             |
| Multi-family residential                | \$2,887               | \$410                 | \$2,165              | \$5,462        | \$2,242,390 | \$2,247,852 |
| Commercial real estate                  | 4,139                 | 3,206                 | 1,448                | 8,793          | 1,463,101   | 1,471,894   |
| One-to-four family - mixed-use property | 2,080                 | -                     | 2,157                | 4,237          | 560,237     | 564,474     |
| One-to-four family - residential        | 767                   | 400                   | 6,969                | 8,136          | 179,605     | 187,741     |
| Co-operative apartments                 | -                     | -                     | 575                  | 575            | 7,264       | 7,839       |
| Construction loans                      | -                     | -                     | 730                  | 730            | 33,096      | 33,826      |
| Small Business Administration           | 1,537                 | -                     | -                    | 1,537          | 12,868      | 14,405      |
| Taxi medallion                          | -                     | -                     | -                    | -              | 6,225       | 6,225       |
| Commercial business and other           | 562                   | 761                   | 2                    | 1,325          | 782,579     | 783,904     |
| Total                                   | \$11,972              | \$4,777               | \$14,046             | \$30,795       | \$5,287,365 | \$5,318,160 |



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

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**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

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

June 30, 2018

| (In thousands)               | Multi-family residential | Commercial real estate | One-to-four family - mixed-use property | One-to-four family - residential | Construction loans | Small Business Administration | Taxi medallion | Commercial business and other | Unallocated | Total     |
|------------------------------|--------------------------|------------------------|---|----------------------------------|--------------------|-------------------------------|----------------|-------------------------------|-------------|-----------|
| Allowance for credit losses: |                          |                        |   |                                  |                    |                               |                |                               |             |           |
| Beginning balance            | \$ 5,750                 | \$ 4,602               | \$ 2,470                                | \$ 1,041                         | \$ 191             | \$ 675                        | \$ -           | \$ 5,813                      | \$ -        | \$ 20,542 |
| Charge-off's                 | (28 )                    | -                      | -                                       | -                                | -                  | (27 )                         | (353 )         | (8 )                          | -           | (416 )    |
| Recoveries                   | -                        | -                      | 79                                      | 4                                | -                  | 9                             | -              | 2                             | -           | 94        |
| Provision (Benefit)          | (184 )                   | 124                    | (252 )                                  | (42 )                            | 73                 | (108 )                        | 353            | 25                            | 11          | -         |
| Ending balance               | \$ 5,538                 | \$ 4,726               | \$ 2,297                                | \$ 1,003                         | \$ 264             | \$ 549                        | \$ -           | \$ 5,832                      | \$ 11       | \$ 20,220 |

June 30, 2017

| (In thousands)               | Multi-family residential | Commercial real estate | One-to-four family - mixed-use property | One-to-four family - residential | Construction loans | Small Business Administration | Taxi medallion | Commercial business and other | Unallocated | Total     |
|------------------------------|--------------------------|------------------------|---|----------------------------------|--------------------|-------------------------------|----------------|-------------------------------|-------------|-----------|
| Allowance for credit losses: |                          |                        |   |                                  |                    |                               |                |                               |             |           |
| Beginning balance            | \$ 5,907                 | \$ 4,485               | \$ 2,691                                | \$ 979                           | \$ 94              | \$ 315                        | \$ 2,213       | \$ 4,712                      | \$ 815      | \$ 22,211 |
| Charge-off's                 | (148 )                   | (4 )                   | (1 )                                    | (170 )                           | -                  | (24 )                         | -              | (3 )                          | -           | (350 )    |
| Recoveries                   | 201                      | -                      | 68                                      | -                                | -                  | 10                            | -              | 17                            | -           | 296       |
| Provision (Benefit)          | (43 )                    | 207                    | (190 )                                  | 181                              | 36                 | 5                             | 117            | (58 )                         | (255 )      | -         |
| Ending balance               | \$ 5,917                 | \$ 4,688               | \$ 2,568                                | \$ 990                           | \$ 130             | \$ 306                        | \$ 2,330       | \$ 4,668                      | \$ 560      | \$ 22,157 |

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

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

June 30, 2018

| (In thousands)               | Multi-family residential | Commercial real estate | One-to-four family - mixed-use property | One-to-four family - residential | Construction loans | Small Business Administration | Taxi medallion | Commercial business and other | Unallocated | Total     |
|------------------------------|--------------------------|------------------------|---|----------------------------------|--------------------|-------------------------------|----------------|-------------------------------|-------------|-----------|
| Allowance for credit losses: |                          |                        |   |                                  |                    |                               |                |                               |             |           |
| Beginning balance            | \$ 5,823                 | \$ 4,643               | \$ 2,545                                | \$ 1,082                         | \$ 68              | \$ 669                        | \$ -           | \$ 5,521                      | \$ -        | \$ 20,351 |
| Charge-off's                 | (81 )                    | -                      | -                                       | (1 )                             | -                  | (52 )                         | (353 )         | (14 )                         | -           | (501 )    |
| Recoveries                   | 2                        | -                      | 79                                      | 112                              | -                  | 15                            | -              | 9                             | -           | 217       |
| Provision (Benefit)          | (206 )                   | 83                     | (327 )                                  | (190 )                           | 196                | (83 )                         | 353            | 316                           | 11          | 153       |
| Ending balance               | \$ 5,538                 | \$ 4,726               | \$ 2,297                                | \$ 1,003                         | \$ 264             | \$ 549                        | \$ -           | \$ 5,832                      | \$ 11       | \$ 20,220 |

June 30, 2017

| (In thousands)               | Multi-family residential | Commercial real estate | One-to-four family - mixed-use property | One-to-four family - residential | Construction loans | Small Business Administration | Taxi medallion | Commercial business and other | Unallocated | Total     |
|------------------------------|--------------------------|------------------------|---|----------------------------------|--------------------|-------------------------------|----------------|-------------------------------|-------------|-----------|
| Allowance for credit losses: |                          |                        |   |                                  |                    |                               |                |                               |             |           |
| Beginning balance            | \$ 5,923                 | \$ 4,487               | \$ 2,903                                | \$ 1,015                         | \$ 92              | \$ 481                        | \$ 2,243       | \$ 4,492                      | \$ 593      | \$ 22,229 |
| Charge-off's                 | (162 )                   | (4 )                   | (35 )                                   | (170 )                           | -                  | (89 )                         | (54 )          | (15 )                         | -           | (529 )    |
| Recoveries                   | 231                      | 68                     | 68                                      | -                                | -                  | 49                            | -              | 41                            | -           | 457       |
| Provision (Benefit)          | (75 )                    | 137                    | (368 )                                  | 145                              | 38                 | (135 )                        | 141            | 150                           | (33 )       | -         |
| Ending balance               | \$ 5,917                 | \$ 4,688               | \$ 2,568                                | \$ 990                           | \$ 130             | \$ 306                        | \$ 2,330       | \$ 4,668                      | \$ 560      | \$ 22,157 |

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

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

June 30, 2018

| (In thousands)  | Multi-family residential | Commercial real estate | One-to-four family - mixed-use property | One-to-four family-residential | Co-operative apartments | Construction loans | Small Business Administration | Taxi medallion | Commercial business and other | Unallocated | Total       |
|---|--------------------------|------------------------|---|--------------------------------|-------------------------|--------------------|-------------------------------|----------------|-------------------------------|-------------|-------------|
| Financing Receivables:                                |                          |                        |   |                                |                         |                    |                               |                |                               |             |             |
| Ending Balance  | \$2,247,852              | \$1,471,894            | \$564,474                               | \$187,741                      | \$7,839                 | \$33,826           | \$14,405                      | \$6,225        | \$783,904                     | \$-         | \$5,318,421 |
| Ending balance: individually evaluated for impairment | \$6,482                  | \$4,967                | \$5,625                                 | \$8,733                        | \$-                     | \$730              | \$49                          | \$6,225        | \$16,136                      | \$-         | \$48,947    |
| Ending balance: collectively evaluated for impairment | \$2,241,370              | \$1,466,927            | \$558,849                               | \$179,008                      | \$7,839                 | \$33,096           | \$14,356                      | \$-            | \$767,768                     | \$-         | \$5,269,474 |
| Allowance for credit losses:                          |                          |                        |   |                                |                         |                    |                               |                |                               |             |             |
| Ending balance: individually evaluated for impairment | \$147                    | \$-                    | \$159                                   | \$53                           | \$-                     | \$-                | \$-                           | \$-            | \$4                           | \$-         | \$363       |
| Ending balance: collectively evaluated for impairment | \$5,391                  | \$4,726                | \$2,138                                 | \$950                          | \$-                     | \$264              | \$549                         | \$-            | \$5,828                       | \$11        | \$19,857    |

December 31, 2017

Unallocated

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| (In thousands)  | Multi-family residential | Commercial real estate | One-to-four family - mixed-use property | One-to-four family- residential | Co-operative apartments | Construction loans | Small Business Administration | Taxi medallions | Commercial business and other |     |             |
|---|--------------------------|------------------------|---|---------------------------------|-------------------------|--------------------|-------------------------------|-----------------|-------------------------------|-----|-------------|
| Financing Receivables:                                |                          |                        |   |                                 |                         |                    |                               |                 |                               |     |             |
| Ending Balance  | \$2,273,595              | \$1,368,112            | \$564,206                               | \$180,663                       | \$6,895                 | \$8,479            | \$18,479                      | \$6,834         | \$732,973                     | \$- | \$5,160,230 |
| Ending balance: individually evaluated for impairment | \$7,311                  | \$9,089                | \$5,445                                 | \$9,686                         | \$-                     | \$-                | \$137                         | \$6,834         | \$661                         | \$- | \$39,163    |
| Ending balance: collectively evaluated for impairment | \$2,266,284              | \$1,359,023            | \$558,761                               | \$170,977                       | \$6,895                 | \$8,479            | \$18,342                      | \$-             | \$732,312                     | \$- | \$5,121,067 |
| Allowance for credit losses:                          |                          |                        |   |                                 |                         |                    |                               |                 |                               |     |             |
| Ending balance: individually evaluated for impairment | \$205                    | \$177                  | \$198                                   | \$56                            | \$-                     | \$-                | \$-                           | \$-             | \$6                           | \$- | \$642       |
| Ending balance: collectively evaluated for impairment | \$5,618                  | \$4,466                | \$2,347                                 | \$1,026                         | \$-                     | \$68               | \$669                         | \$-             | \$5,515                       | \$- | \$19,709    |

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

The following table shows our recorded investment, unpaid principal balance and allocated allowance for loan losses for impaired loans at the periods indicated:

|  | June 30, 2018          |                                |                      | December 31, 2017      |                                |                      |
|--|------------------------|--------------------------------|----------------------|------------------------|--------------------------------|----------------------|
|  | Recorded<br>Investment | Unpaid<br>Principal<br>Balance | Related<br>Allowance | Recorded<br>Investment | Unpaid<br>Principal<br>Balance | Related<br>Allowance |
|  | (In thousands)         |                                |                      |                        |                                |                      |
| With no related allowance recorded:            |                        |                                |                      |                        |                                |                      |
| Mortgage loans:                                |                        |                                |                      |                        |                                |                      |
| Multi-family residential                       | \$4,285                | \$4,814                        | \$ -                 | \$5,091                | \$5,539                        | \$ -                 |
| Commercial real estate                         | 4,967                  | 4,967                          | -                    | 7,103                  | 7,103                          | -                    |
| One-to-four family mixed-use property          | 4,419                  | 4,676                          | -                    | 4,218                  | 4,556                          | -                    |
| One-to-four family residential                 | 8,326                  | 9,281                          | -                    | 9,272                  | 10,489                         | -                    |
| Construction                                   | 730                    | 730                            | -                    | -                      | -                              | -                    |
| Non-mortgage loans:                            |                        |                                |                      |                        |                                |                      |
| Small Business Administration                  | 49                     | 58                             | -                    | 137                    | 151                            | -                    |
| Taxi medallion                                 | 6,225                  | 17,450                         | -                    | 6,834                  | 18,063                         | -                    |
| Commercial business and other                  | 15,829                 | 16,198                         | -                    | 313                    | 682                            | -                    |
| Total loans with no related allowance recorded | 44,830                 | 58,174                         | -                    | 32,968                 | 46,583                         | -                    |
| With an allowance recorded:                    |                        |                                |                      |                        |                                |                      |
| Mortgage loans:                                |                        |                                |                      |                        |                                |                      |
| Multi-family residential                       | 2,197                  | 2,197                          | 147                  | 2,220                  | 2,220                          | 205                  |
| Commercial real estate                         | -                      | -                              | -                    | 1,986                  | 1,986                          | 177                  |
| One-to-four family mixed-use property          | 1,206                  | 1,206                          | 159                  | 1,227                  | 1,227                          | 198                  |
| One-to-four family residential                 | 407                    | 407                            | 53                   | 414                    | 414                            | 56                   |
| Non-mortgage loans:                            |                        |                                |                      |                        |                                |                      |
| Commercial business and other                  | 307                    | 307                            | 4                    | 348                    | 348                            | 6                    |
| Total loans with an allowance recorded         | 4,117                  | 4,117                          | 363                  | 6,195                  | 6,195                          | 642                  |
| Total Impaired Loans:                          |                        |                                |                      |                        |                                |                      |
| Total mortgage loans                           | \$26,537               | \$28,278                       | \$ 359               | \$31,531               | \$33,534                       | \$ 636               |
| Total non-mortgage loans                       | \$22,410               | \$34,013                       | \$ 4                 | \$7,632                | \$19,244                       | \$ 6                 |



**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

The following table shows our average recorded investment and interest income recognized for impaired loans for the three months ended:

|  | June 30, 2018  |                | June 30, 2017  |                |
|--|----------------|----------------|----------------|----------------|
|  | Average        | Interest       | Average        | Interest       |
|  | Recorded       | Recognized     | Recorded       | Recognized     |
|  | Investmen      | Investmen      | Investmen      | Investmen      |
|  | (In thousands) | (In thousands) | (In thousands) | (In thousands) |
| With no related allowance recorded:            |                |                |                |                |
| Mortgage loans:                                |                |                |                |                |
| Multi-family residential                       | \$4,431        | \$ 16          | \$2,730        | \$ 22          |
| Commercial real estate                         | 5,847          | 52             | 6,438          | 59             |
| One-to-four family mixed-use property          | 4,397          | 39             | 5,560          | 41             |
| One-to-four family residential                 | 8,382          | 10             | 10,263         | 30             |
| Construction                                   | 365            | 10             | 602            | -              |
| Non-mortgage loans:                            |                |                |                |                |
| Small Business Administration                  | 74             | 1              | 160            | 2              |
| Taxi medallion                                 | 6,421          | 86             | 4,352          | 25             |
| Commercial business and other                  | 7,954          | 308            | 2,187          | 43             |
| Total loans with no related allowance recorded | 37,871         | 522            | 32,292         | 222            |
| With an allowance recorded:                    |                |                |                |                |
| Mortgage loans:                                |                |                |                |                |
| Multi-family residential                       | 2,203          | 30             | 2,471          | 50             |
| Commercial real estate                         | -              | -              | 2,043          | 24             |
| One-to-four family mixed-use property          | 1,212          | 15             | 1,450          | 16             |
| One-to-four family residential                 | 409            | 4              | 424            | 4              |
| Non-mortgage loans:                            |                |                |                |                |
| Small Business Administration                  | -              | -              | -              | -              |
| Taxi medallion                                 | -              | -              | 14,216         | 50             |
| Commercial business and other                  | 318            | 4              | 391            | 6              |
| Total loans with an allowance recorded         | 4,142          | 53             | 20,995         | 150            |
| Total Impaired Loans:                          |                |                |                |                |
| Total mortgage loans                           | \$27,246       | \$ 176         | \$31,981       | \$ 246         |
| Total non-mortgage loans                       | \$14,767       | \$ 399         | \$21,306       | \$ 126         |





**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

The following table shows our average recorded investment and interest income recognized for impaired loans for the six months ended:

|  | June 30, 2018  |                | June 30, 2017  |                |
|--|----------------|----------------|----------------|----------------|
|  | Average        | Interest       | Average        | Interest       |
|  | Recorded       | Recognized     | Recorded       | Recognized     |
|  | Investmen      | Investmen      | Investmen      | Investmen      |
|  | (In thousands) | (In thousands) | (In thousands) | (In thousands) |
| With no related allowance recorded:            |                |                |                |                |
| Mortgage loans:                                |                |                |                |                |
| Multi-family residential                       | \$4,651        | \$ 36          | \$3,040        | \$ 45          |
| Commercial real estate                         | 6,266          | 126            | 5,788          | 154            |
| One-to-four family mixed-use property          | 4,337          | 80             | 5,851          | 78             |
| One-to-four family residential                 | 8,678          | 25             | 10,028         | 56             |
| Construction                                   | 243            | 10             | 401            | 7              |
| Non-mortgage loans:                            |                |                |                |                |
| Small Business Administration                  | 95             | 2              | 245            | 4              |
| Taxi medallion                                 | 6,559          | 168            | 3,679          | 55             |
| Commercial business and other                  | 5,407          | 310            | 2,148          | 87             |
| Total loans with no related allowance recorded | 36,236         | 757            | 31,180         | 486            |
| With an allowance recorded:                    |                |                |                |                |
| Mortgage loans:                                |                |                |                |                |
| Multi-family residential                       | 2,208          | 59             | 2,401          | 79             |
| Commercial real estate                         | 662            | -              | 2,049          | 48             |
| One-to-four family mixed-use property          | 1,217          | 24             | 1,758          | 34             |
| One-to-four family residential                 | 411            | 8              | 425            | 8              |
| Non-mortgage loans:                            |                |                |                |                |
| Small Business Administration                  | -              | -              | 507            | -              |
| Taxi medallion                                 | -              | -              | 14,126         | 93             |
| Commercial business and other                  | 328            | 9              | 401            | 12             |
| Total loans with an allowance recorded         | 4,826          | 100            | 21,667         | 274            |
| Total Impaired Loans:                          |                |                |                |                |
| Total mortgage loans                           | \$28,673       | \$ 368         | \$31,741       | \$ 509         |
| Total non-mortgage loans                       | \$12,389       | \$ 489         | \$21,106       | \$ 251         |



**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

In accordance with our policy and the current regulatory guidelines, we designate loans as “Special Mention,” which are considered “Criticized Loans,” and “Substandard,” “Doubtful,” or “Loss,” which are considered “Classified Loans”. If a loan does not fall within one of the previous mentioned categories then the loan would be considered “Pass.” Loans that are non-accrual are designated as Substandard, Doubtful or Loss. These loan designations are updated quarterly. We designate a loan as Substandard when a well-defined weakness is identified that may jeopardize the orderly liquidation of the debt. We designate a loan Doubtful when it displays the inherent weakness of a Substandard loan with the added provision that collection of the debt in full, on the basis of existing facts, is highly improbable. We designate a loan as Loss if it is deemed the debtor is incapable of repayment. The Company does not hold any loans designated as Loss, as loans that are designated as Loss are charged to the Allowance for Loan Losses. We designate a loan as Special Mention if the asset does not warrant classification within one of the other classifications, but does contain a potential weakness that deserves closer attention.

The following table sets forth the recorded investment in loans designated as Criticized or Classified at the periods indicated:

| (In thousands)                          | June 30, 2018      |             |          |      |          |
|---|--------------------|-------------|----------|------|----------|
|   | Special<br>Mention | Substandard | Doubtful | Loss | Total    |
| Multi-family residential                | \$3,432            | \$ 3,994    | \$ -     | \$ - | \$7,426  |
| Commercial real estate                  | 4,475              | 4,206       | -        | -    | 8,681    |
| One-to-four family - mixed-use property | 1,223              | 3,899       | -        | -    | 5,122    |
| One-to-four family - residential        | 883                | 7,597       | -        | -    | 8,480    |
| Co-operative apartments                 | -                  | 575         | -        | -    | 575      |
| Construction loans                      | -                  | 730         | -        | -    | 730      |
| Small Business Administration           | 879                | 45          | -        | -    | 924      |
| Taxi medallion                          | -                  | 6,225       | -        | -    | 6,225    |
| Commercial business and other           | 10,927             | 16,852      | -        | -    | 27,779   |
| Total loans                             | \$21,819           | \$ 44,123   | \$ -     | \$ - | \$65,942 |

| (In thousands)           | December 31, 2017  |             |          |      |          |
|--------------------------|--------------------|-------------|----------|------|----------|
|                          | Special<br>Mention | Substandard | Doubtful | Loss | Total    |
| Multi-family residential | \$6,389            | \$ 4,793    | \$ -     | \$ - | \$11,182 |
| Commercial real estate   | 2,020              | 8,871       | -        | -    | 10,891   |

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|   |          |           |      |      |          |
|---|----------|-----------|------|------|----------|
| One-to-four family - mixed-use property | 2,835    | 3,691     | -    | -    | 6,526    |
| One-to-four family - residential        | 2,076    | 9,115     | -    | -    | 11,191   |
| Small Business Administration           | 548      | 108       | -    | -    | 656      |
| Taxi medallion                          | -        | 6,834     | -    | -    | 6,834    |
| Commercial business and other           | 14,859   | 545       | -    | -    | 15,404   |
| Total loans                             | \$28,727 | \$ 33,957 | \$ - | \$ - | \$62,684 |

Commitments to extend credit (principally real estate mortgage loans) and lines of credit (principally home equity lines of credit and business lines of credit) amounted to \$25.2 million and \$300.8 million, respectively, at June 30, 2018.

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**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

**6. Loans held for sale**

Loans held for sale are carried at the lower of cost or estimated fair value. At June 30, 2018 and December 31, 2017, the Bank did not have any loans held for sale.

The Company has implemented a strategy of selling certain delinquent and non-performing loans. Once the Company has decided to sell a loan, the sale usually closes in a short period of time, generally within the same quarter. Loans designated held for sale are reclassified from loans held for investment to loans held for sale. Terms of sale include cash due upon the closing of the sale, no contingencies or recourse to the Company and servicing is released to the buyer. Additionally, at times the Company may sell participating interests in performing loans.

The following tables show loans sold during the period indicated:

| (Dollars in thousands)              | For the three months ended June 30, 2018 |          |          |
|-------------------------------------|--|----------|----------|
|                                     | Loans sold                               | Proceeds | Net gain |
| Delinquent and non-performing loans |  |          |          |
| Commercial real estate              | 2  | \$ 2,065 | \$ 28    |
| Total                               | 2  | \$ 2,065 | \$ 28    |
| Performing loans                    |  |          |          |
| Small Business Administration       | 9  | \$ 5,671 | \$ 393   |
| Total                               | 9  | \$ 5,671 | \$ 393   |

  

| (Dollars in thousands) | For the three months ended June 30, 2017 |          |                 |                 |
|------------------------|--|----------|-----------------|-----------------|
|                        | Loans sold                               | Proceeds | Net charge-offs | Net gain (loss) |

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Delinquent and non-performing loans

|            |   |       |         |     |
|------------|---|-------|---------|-----|
| Commercial | 1 | \$335 | \$ (4 ) | \$- |
|------------|---|-------|---------|-----|

|       |   |       |         |     |
|-------|---|-------|---------|-----|
| Total | 1 | \$335 | \$ (4 ) | \$- |
|-------|---|-------|---------|-----|

Performing loans

|                          |   |         |      |        |
|--------------------------|---|---------|------|--------|
| Multi-family residential | 2 | \$6,080 | \$ - | \$(14) |
|--------------------------|---|---------|------|--------|

|                        |   |       |   |      |
|------------------------|---|-------|---|------|
| Commercial real estate | 5 | 8,451 | - | (21) |
|------------------------|---|-------|---|------|

|                               |   |       |   |    |
|-------------------------------|---|-------|---|----|
| Small Business Administration | 4 | 1,519 | - | 69 |
|-------------------------------|---|-------|---|----|

|       |    |          |      |      |
|-------|----|----------|------|------|
| Total | 11 | \$16,050 | \$ - | \$34 |
|-------|----|----------|------|------|

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**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

| (Dollars in thousands)                 | For the six months ended June 30, 2018 |           |                 |                 |
|--|--|-----------|-----------------|-----------------|
|  | Loans sold                             | Proceeds  | Net gain (loss) |                 |
| Delinquent and non-performing loans    |  |           |                 |                 |
| Multi-family - residential             | 3                                      | \$ 964    | \$-             |                 |
| Commercial real estate                 | 3                                      | 3,565     | (235)           |                 |
| Total                                  | 6                                      | \$ 4,529  | \$(235)         |                 |
| Performing loans                       |  |           |                 |                 |
| Small Business Administration          | 9                                      | \$ 5,671  | \$ 393          |                 |
| Total                                  | 9                                      | \$ 5,671  | \$ 393          |                 |
| For the six months ended June 30, 2017 |  |           |                 |                 |
| (Dollars in thousands)                 | Loans sold                             | Proceeds  | Net charge-offs | Net gain (loss) |
| Delinquent and non-performing loans    |  |           |                 |                 |
| One-to-four family- residential        | 5                                      | \$ 1,790  | \$ (33 )        | \$-             |
| Commercial real estate                 | 1                                      | 335       | (4 )            | -               |
| Total                                  | 6                                      | \$ 2,125  | \$ (37 )        | \$-             |
| Performing loans                       |  |           |                 |                 |
| Multi-family residential               | 2                                      | \$ 6,080  | \$ -            | \$(14 )         |
| Commercial real estate                 | 5                                      | 8,451     | -               | (21 )           |
| Small Business Administration          | 7                                      | 4,919     | -               | 250             |
| Total                                  | 14                                     | \$ 19,450 | \$ -            | \$ 216          |

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**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

**7. Other Real Estate Owned**

OREO are included in other assets on the Company's Consolidated Statements of Financial Condition. The following table shows changes in OREO during the periods indicated:

|                                | For the three<br>months<br>ended<br>June 30,<br>2018 |      | For the six<br>months ended<br>June 30,<br>2017 |       |
|--------------------------------|--|------|---|-------|
|                                | 2018   | 2017 | 2018  | 2017  |
|                                | (In thousands)                                       |      |   |       |
| Balance at beginning of period | \$638  | \$ - | \$-   | \$533 |
| Acquisitions                   | -  | -    | 638   | -     |
| Sales                          | (638)  | -    | (638)   | (533) |
| Balance at end of period       | \$-  | \$ - | \$-   | \$-   |

The following table shows the gross gains, gross losses and write-downs of OREO reported in the Consolidated Statements of Income during the periods indicated:

|             | For the<br>three<br>months<br>ended<br>June 30,<br>2018 |      | For the six<br>months<br>ended<br>June 30,<br>2017 |      |
|-------------|---|------|--|------|
|             | 2018  | 2017 | 2018   | 2017 |
|             | (In thousands)  |      |  |      |
| Gross gains | \$ 27   | \$ - | \$27   | \$50 |

During the six months ended June 30, 2018 we foreclosed on one residential real estate property for \$0.6 million. During the three months ended June 30, 2018 and the three and six months ended June 30, 2017, we did not foreclose

on any consumer mortgages through in-substance repossession. We did not hold any foreclosed residential real estate properties at June 30, 2018 and December 31, 2017. Included within net loans as of June 30, 2018 and December 31, 2017 was a recorded investment of \$9.8 million and \$10.5 million, respectively, of consumer mortgage loans secured by residential real estate properties for which formal foreclosure proceedings were in process according to local requirements of the applicable jurisdiction.

## **8. Stock-Based Compensation**

For the three months ended June 30, 2018 and 2017, the Company's net income, as reported, includes \$1.2 million and \$1.0 million, respectively, of stock-based compensation costs and \$0.3 million and \$0.4 million of income tax benefits, respectively, related to the stock-based compensation plans in each of the periods. For the six months ended June 30, 2018 and 2017, the Company's net income, as reported, includes \$4.6 million and \$4.1 million, respectively, of stock-based compensation costs and \$1.0 million and \$1.2 million of income tax benefits, respectively, related to the stock-based compensation plans in each of the periods. During the three months ended June 30, 2018, the Company granted 5,600 restricted stock units. The Company did not grant any restricted stock units during the three months ended June 30, 2017. During the six months ended June 30, 2018 and 2017, the Company granted 280,590 and 276,900 restricted stock units, respectively. There were 600 stock options exercised during the three and six months ended June 30, 2018 and 4,400 stock options exercised during the three and six months ended June 30, 2017. The Company has not granted stock options since 2009. At June 30, 2018, the Company had 600 stock options, all 100% vested, outstanding, at an average exercise price of \$8.44 per share.

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

The Company uses the fair value of the common stock on the date of award to measure compensation cost for restricted stock unit awards. Compensation cost is recognized over the vesting period of the award using the straight-line method.

The following table summarizes the Company’s restricted stock unit (“RSU”) awards at or for the six months ended June 30, 2018:

|                                      | Shares    | Weighted-Average<br>Grant-Date<br>Fair Value |
|--------------------------------------|-----------|--|
| Non-vested at December 31, 2017      | 497,322   | \$ 22.46                                     |
| Granted                              | 280,590   | 28.19  |
| Vested                               | (239,599) | 23.64  |
| Forfeited                            | (7,110 )  | 25.27  |
| Non-vested at June 30, 2018          | 531,203   | \$ 24.91                                     |
| Vested but unissued at June 30, 2018 | 234,799   | \$ 25.14                                     |

As of June 30, 2018, there was \$10.8 million of total unrecognized compensation cost related to RSU awards granted. That cost is expected to be recognized over a weighted-average period of 3.1 years. The total fair value of awards vested for the three months ended June 30, 2018 and 2017 was \$28,000 and \$40,000, respectively. The total fair value of awards vested for the six months ended June 30, 2018 and 2017 was \$6.7 and \$4.8 million, respectively. The vested but unissued RSU awards consist of awards made to employees and directors who are eligible for retirement. According to the terms of these awards, which provide for vesting upon retirement, these employees and directors have no risk of forfeiture. These shares will be issued at the original contractual vesting and settlement dates.

*Phantom Stock Plan:* The Company maintains a non-qualified phantom stock plan as a supplement to its profit sharing plan for officers who have achieved the designated level and completed one year of service. The Company adjusts its liability under this plan to the fair value of the shares at the end of each period.

The following table summarizes the Phantom Stock Plan at or for the six months ended June 30, 2018:

| Phantom Stock Plan               | Shares | Fair Value |
|----------------------------------|--------|------------|
| Outstanding at December 31, 2017 | 89,180 | \$27.50    |
| Granted                          | 8,946  | 27.75      |
| Forfeited                        | -      | -          |
| Distributions                    | (32 )  | 27.18      |
| Outstanding at June 30, 2018     | 98,094 | \$26.10    |
| Vested at June 30, 2018          | 97,515 | \$26.10    |

The Company recorded stock-based compensation benefit for the Phantom Stock Plan of \$0.1 million for the each of the three month periods ended June 30, 2018 and 2017. The total fair value of the distributions from the Phantom Stock Plan was less than \$1,000 for each of the three month periods ended June 30, 2018 and 2017.

For the six months ended June 30, 2018 and 2017, the company recorded stock-based compensation benefit for the Phantom Stock Plan of \$0.1 million for each of the six month periods ended June 30, 2018 and 2017. The total fair value of the distributions from the Phantom Stock Plan was \$1,000 and \$6,000 for the six months ended June 30, 2018 and 2017, respectively.

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

**9. Pension and Other Postretirement Benefit Plans**

The following table sets forth information regarding the components of net expense for the pension and other postretirement benefit plans.

| (In thousands)                             | Three months<br>ended<br>June 30,<br>2018 |       | Six months<br>ended<br>June 30,<br>2017 |       |
|--|---|-------|---|-------|
|  | 2018                                      | 2017  | 2018                                    | 2017  |
| <b>Employee Pension Plan:</b>              |   |       |   |       |
| Interest cost                              | \$195                                     | \$216 | \$390                                   | \$432 |
| Amortization of unrecognized loss          | 156                                       | 174   | 311                                     | 348   |
| Expected return on plan assets             | (363)                                     | (348) | (726)                                   | (696) |
| Net employee pension (benefit) expense     | \$(12)                                    | \$42  | \$(25)                                  | \$84  |
| <b>Outside Director Pension Plan:</b>      |   |       |   |       |
| Service cost                               | \$11                                      | \$10  | \$22                                    | \$20  |
| Interest cost                              | 20  | 23    | 40                                      | 46    |
| Amortization of unrecognized gain          | (23)                                      | (23)  | (46)                                    | (46)  |
| Amortization of past service liability     | 3   | 10    | 6                                       | 20    |
| Net outside director pension expense       | \$11                                      | \$20  | \$22                                    | \$40  |
| <b>Other Postretirement Benefit Plans:</b> |   |       |   |       |
| Service cost                               | \$88                                      | \$79  | \$176                                   | \$158 |
| Interest cost                              | 77  | 76    | 154                                     | 152   |
| Amortization of past service credit        | (12)                                      | (21)  | (25)                                    | (42)  |
| Net other postretirement expense           | \$153                                     | \$134 | \$305                                   | \$268 |

The Company previously disclosed in its Consolidated Financial Statements for the year ended December 31, 2017 that it expects to contribute \$0.2 million to each of the Outside Director Pension Plan (the “Outside Director Pension Plan”) and the other postretirement benefit plans (the “Other Postretirement Benefit Plans”), during the year ending December 31, 2018. The Company does not expect to make a contribution to the Employee Pension Plan (the “Employee Pension Plan”). As of June 30, 2018, the Company has contributed \$48,000 to the Outside Director Pension Plan and \$56,000 in contributions were made to the Other Postretirement Benefit Plans. As of June 30, 2018, the Company has not revised its expected contributions for the year ending December 31, 2018.

## **10. Fair Value of Financial Instruments**

The Company carries certain financial assets and financial liabilities at fair value in accordance with GAAP which defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date, establishes a framework for measuring fair value and expands disclosures about fair value measurements. GAAP permits entities to choose to measure many financial instruments and certain other items at fair value. At June 30, 2018, the Company carried financial assets and financial liabilities under the fair value option with fair values of \$14.0 million and \$39.6 million, respectively. At December 31, 2017, the Company carried financial assets and financial liabilities under the fair value option with fair values of \$14.3 million and \$37.0 million, respectively. The Company did not elect to carry any additional financial assets or financial liabilities under the fair value option during the three and six months ended June 30, 2018.

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(Unaudited)

The following table presents the financial assets and financial liabilities reported at fair value under the fair value option, and the changes in fair value included in the Consolidated Statement of Income – Net gain (loss) from fair value adjustments, at or for the periods ended as indicated:

|  | Fair Value<br>Measurements<br>at June 30,<br>2018 | Fair Value<br>Measurements<br>at December<br>31,<br>2017 | Changes in Fair Values For Items<br>Measured at Fair Value<br>Pursuant to Election of the Fair<br>Value Option |               |                                      |               |
|--|---|--|--|---------------|--------------------------------------|---------------|
|  |   |  | Three Months<br>Ended<br>June 30,<br>2018  |               | Six Months Ended<br>June 30,<br>2017 |               |
| (In thousands)   |   |  | June 30, 2018  | June 30, 2017 | June 30, 2018                        | June 30, 2017 |
| Mortgage-backed securities                             | \$ 1,426  | \$ 1,590   | \$-  | \$(3 )        | \$(11 )                              | \$(10 )       |
| Other securities                                       | 12,615  | 12,685   | (62 )  | 112           | (200 )                               | 144           |
| Borrowed funds   | 39,566  | 36,986   | (867)  | (595)         | (2,548)                              | (1,165)       |
| Net loss from fair value adjustments <sup>(1)(2)</sup> |   |  | \$(929)  | \$(486)       | \$(2,759)                            | \$(1,031)     |

The net loss from fair value adjustments presented in the above table does not include net gains (losses) of \$0.7 (1) million and (\$0.7) million for the three months ended June 30, 2018 and 2017, respectively, from the change in the fair value of interest rate swaps.

The net loss from fair value adjustments presented in the above table does not include net gains (losses) of \$2.4 (2) million and (\$0.5) million for the six months ended June 30, 2018 and 2017, respectively, from the change in the fair value of interest rate swaps.

Included in the fair value of the financial assets and financial liabilities selected for the fair value option is the accrued interest receivable or payable for the related instrument. The Company reports as interest income or interest expense in the Consolidated Statement of Income, the interest receivable or payable on the financial instruments selected for the fair value option at their respective contractual rates.

The borrowed funds had a contractual principal amount of \$61.9 million at both June 30, 2018 and December 31, 2017. The fair value of borrowed funds includes accrued interest payable of \$0.2 million at June 30, 2018 and

December 31, 2017.

The Company generally holds its earning assets, other than securities available for sale, to maturity and settles its liabilities at maturity. However, fair value estimates are made at a specific point in time and are based on relevant market information. These estimates do not reflect any premium or discount that could result from offering for sale at one time the Company's entire holdings of a particular instrument. Accordingly, as assumptions change, such as interest rates and prepayments, fair value estimates change and these amounts may not necessarily be realized in an immediate sale.

Disclosure of fair value does not require fair value information for items that do not meet the definition of a financial instrument or certain other financial instruments specifically excluded from its requirements. These items include core deposit intangibles and other customer relationships, premises and equipment, leases, income taxes and equity.

Further, fair value disclosure does not attempt to value future income or business. These items may be material and accordingly, the fair value information presented does not purport to represent, nor should it be construed to represent, the underlying "market" or franchise value of the Company.

Financial assets and financial liabilities reported at fair value are required to be measured based on either: (1) quoted prices in active markets for identical financial instruments (Level 1); (2) significant other observable inputs (Level 2); or (3) significant unobservable inputs (Level 3).

A description of the methods and significant assumptions utilized in estimating the fair value of the Company's assets and liabilities that are carried at fair value on a recurring basis are as follows:

Level 1 – where quoted market prices are available in an active market. At June 30, 2018 and December 31, 2017, Level 1 included one mutual fund.

Level 2 – when quoted market prices are not available, fair value is estimated using quoted market prices for similar financial instruments and adjusted for differences between the quoted instrument and the instrument being valued. Fair value can also be estimated by using pricing models, or discounted cash flows. Pricing models primarily use market-based or independently sourced market parameters as inputs, including, but not limited to, yield curves, interest rates, equity or debt prices and credit spreads. In addition to observable market information, models also incorporate maturity and cash flow assumptions. At June 30, 2018 and December 31, 2017, Level 2 included mortgage related securities, corporate debt, municipals and interest rate swaps.





**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

Level 3 – when there is limited activity or less transparency around inputs to the valuation, financial instruments are classified as Level 3. At June 30, 2018 and December 31, 2017, Level 3 included trust preferred securities owned and junior subordinated debentures issued by the Company.

The methods described above may produce fair values that may not be indicative of net realizable value or reflective of future fair values. While the Company believes, its valuation methods are appropriate and consistent with those of other market participants, the use of different methodologies, assumptions and models to determine fair value of certain financial instruments could produce different estimates of fair value at the reporting date.

The following table sets forth the assets and liabilities that are carried at fair value on a recurring basis and their respective category in the fair value hierarchy, at June 30, 2018 and December 31, 2017:

|                            | Quoted Prices<br>in Active Markets<br>for Identical Assets<br>(Level 1) |                 | Significant Other<br>Observable Inputs<br>(Level 2) |                  | Significant Other<br>Unobservable<br>Inputs<br>(Level 3) |                 | Total carried at fair<br>value<br>on a recurring basis |                  |
|----------------------------|---|-----------------|---|------------------|--|-----------------|--|------------------|
|                            | 2018  | 2017            | 2018  | 2017             | 2018   | 2017            | 2018   | 2017             |
| (In thousands)             |   |                 |   |                  |  |                 |  |                  |
| <b>Assets:</b>             |   |                 |   |                  |  |                 |  |                  |
| Mortgage-backed Securities | \$-   | \$-             | \$513,868   | \$509,650        | \$-  | \$-             | \$513,868  | \$509,650        |
| Other securities           | 11,427  | 11,575          | 202,140   | 216,019          | 1,188  | 1,110           | 214,755  | 228,704          |
| Interest rate swaps        | -   | -               | 27,398  | 7,388            | -  | -               | 27,398   | 7,388            |
| <b>Total assets</b>        | <b>\$11,427</b>   | <b>\$11,575</b> | <b>\$743,406</b>                                    | <b>\$733,057</b> | <b>\$1,188</b>   | <b>\$1,110</b>  | <b>\$756,021</b>                                       | <b>\$745,742</b> |
| <b>Liabilities:</b>        |   |                 |   |                  |  |                 |  |                  |
| Borrowings                 | \$-   | \$-             | \$-   | \$-              | \$39,566   | \$36,986        | \$39,566   | \$36,986         |
| Interest rate swaps        | -   | -               | 1,128   | 3,758            | -  | -               | 1,128  | 3,758            |
| <b>Total liabilities</b>   | <b>\$-</b>  | <b>\$-</b>      | <b>\$1,128</b>                                      | <b>\$3,758</b>   | <b>\$39,566</b>  | <b>\$36,986</b> | <b>\$40,694</b>  | <b>\$40,744</b>  |

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The following tables sets forth the Company's assets and liabilities that are carried at fair value on a recurring basis, classified within Level 3 of the valuation hierarchy for the periods indicated:

|   | For the three months ended |              |               |              |
|---|----------------------------|--------------|---------------|--------------|
|   | June 30, 2018              |              | June 30, 2017 |              |
|   | Trust                      | Junior       | Trust         | Junior       |
|   | preferred                  | subordinated | preferred     | subordinated |
|   | securities                 | debentures   | securities    | debentures   |
|   | (In thousands)             |              |               |              |
| Beginning balance   | \$1,162                    | \$ 38,692    | \$7,394       | \$ 34,536    |
| Net gain from fair value adjustment of financial assets <sup>(1)</sup>      | 25                         | -            | 48            | -            |
| Net loss from fair value adjustment of financial liabilities <sup>(1)</sup> | -                          | 867          | -             | 594          |
| Increase in accrued interest receivable                                     | 1                          | -            | -             | -            |
| Increase in accrued interest payable  | -                          | 26           | -             | 7            |
| Change in unrealized gains (losses) included in other comprehensive income  | -                          | (19 )        | 2             | -            |
| Ending balance  | \$1,188                    | \$ 39,566    | \$7,444       | \$ 35,137    |
| Changes in unrealized gains (losses) held at period end                     | \$-                        | \$ (19 )     | \$2           | \$ -         |

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**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

|   | For the six months ended   |                                |                            |                                |
|---|----------------------------|--------------------------------|----------------------------|--------------------------------|
|   | June 30, 2018              |                                | June 30, 2017              |                                |
|   | Trust preferred securities | Junior subordinated debentures | Trust preferred securities | Junior subordinated debentures |
|   | (In thousands)             |                                |                            |                                |
| Beginning balance   | \$1,110                    | \$ 36,986                      | \$7,361                    | \$ 33,959                      |
| Net gain from fair value adjustment of financial assets <sup>(1)</sup>      | 77                         | -                              | 81                         | -                              |
| Net loss from fair value adjustment of financial liabilities <sup>(1)</sup> |                            | 2,548                          | -                          | 1,165                          |
| Increase in accrued interest receivable                                     | 1                          | -                              | -                          | -                              |
| Increase in accrued interest payable  | -                          | 51                             | -                          | 13                             |
| Change in unrealized gains (losses) included in other comprehensive income  | -                          | (19 )                          | 2                          | -                              |
| Ending balance  | \$1,188                    | \$ 39,566                      | \$7,444                    | \$ 35,137                      |
| Changes in unrealized gains (losses) held at period end                     | \$-                        | \$ (19 )                       | \$2                        | \$ -                           |

<sup>(1)</sup> Totals in the table above are presented in the Consolidated Statement of Income under net gains (losses) from fair value adjustments.

During the three and six months ended June 30, 2018 and 2017, there were no transfers between Levels 1, 2 and 3.

The following tables present the quantitative information about recurring Level 3 fair value of financial instruments and the fair value measurements at the periods indicated:

|                            | June 30, 2018 |                       |                    |       | Weighted Average |
|----------------------------|---------------|-----------------------|--------------------|-------|------------------|
|                            | Fair Value    | Valuation Technique   | Unobservable Input | Range |                  |
| (Dollars in thousands)     |               |                       |                    |       |                  |
| Assets:                    |               |                       |                    |       |                  |
| Trust preferred securities | \$1,188       | Discounted cash flows | Discount rate      | n/a   | 5.5 %            |
| Liabilities:               |               |                       |                    |       |                  |

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|                                |          |                       |               |     |       |
|--------------------------------|----------|-----------------------|---------------|-----|-------|
| Junior subordinated debentures | \$39,566 | Discounted cash flows | Discount rate | n/a | 5.5 % |
|--------------------------------|----------|-----------------------|---------------|-----|-------|

December 31, 2017

| Fair Value | Valuation Technique | Unobservable Input | Range | Weighted Average |
|------------|---------------------|--------------------|-------|------------------|
|------------|---------------------|--------------------|-------|------------------|

(Dollars in thousands)

Assets:

|                            |         |                       |               |     |       |
|----------------------------|---------|-----------------------|---------------|-----|-------|
| Trust preferred securities | \$1,110 | Discounted cash flows | Discount rate | n/a | 5.7 % |
|----------------------------|---------|-----------------------|---------------|-----|-------|

Liabilities:

|                                |          |                       |               |     |       |
|--------------------------------|----------|-----------------------|---------------|-----|-------|
| Junior subordinated debentures | \$36,986 | Discounted cash flows | Discount rate | n/a | 5.7 % |
|--------------------------------|----------|-----------------------|---------------|-----|-------|

The significant unobservable inputs used in the fair value measurement of the Company's trust preferred securities and junior subordinated debentures valued under Level 3 at June 30, 2018 and December 31, 2017, are the effective yields used in the cash flow models. Significant increases or decreases in the effective yield in isolation would result in a significantly lower or higher fair value measurement.

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The following table sets forth the Company's assets and liabilities that are carried at fair value on a non-recurring basis and their respective category in the fair value hierarchy at June 30, 2018 and December 31, 2017:

|                          | Quoted<br>Prices<br>in Active<br>Markets<br>for<br>Identical<br>Assets<br>(Level 1) | Significant<br>Other<br>Observable<br>Inputs<br>(Level 2) | Significant<br>Other<br>Unobservable<br>Inputs<br>(Level 3) | Total carried at fair<br>value<br>on a recurring basis |          |          |
|--------------------------|---|---|---|--|----------|----------|
|                          | 2018  | 2017  | 2018  | 2017   | 2018     | 2017     |
| (In thousands)           |   |   |   |  |          |          |
| Assets:                  |   |   |   |  |          |          |
| Impaired loans           | \$-   | \$-   | \$-   | \$-  | \$14,102 | \$16,027 |
| Other repossessed assets | -   | -   | -   | -  | 35       | -        |
| Total assets             | \$-   | \$-   | \$-   | \$-  | \$14,137 | \$16,027 |

The following tables present the qualitative information about non-recurring Level 3 fair value of financial instruments and the fair value measurements at the periods indicated:

|                | June 30, 2018<br>Fair Value<br>(Dollars in thousands) | Valuation<br>Technique | Unobservable Input   | Range                  | Weighted<br>Average                |
|----------------|---|------------------------|--|------------------------|------------------------------------|
| Assets:        |   |                        |  |                        |                                    |
| Impaired loans | \$1,531   | Income approach        | Capitalization rate<br>Reduction for planned expedited<br>disposal                           | 6.5% to<br>15.0%       | 7.0 %<br>15.0 %                    |
| Impaired loans | \$8,655   | Sales approach         | Adjustment to sales comparison value<br>to reconcile differences between<br>comparable sales | -50.0% to<br>-40.6% to | 16.2%<br>15.0%<br>-1.5 %<br>10.4 % |

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|                          |         |                                   |  |           |       |      |   |
|--------------------------|---------|-----------------------------------|--|-----------|-------|------|---|
|                          |         |                                   | Reduction for planned expedited disposal   |           |       |      |   |
| Impaired loans           | \$3,916 | Blended income and sales approach | Adjustment to sales comparison value to reconcile differences between comparable sales | -30.0% to | 25.0% | -0.8 | % |
|                          |         |                                   | Capitalization rate  | 5.0% to   | 9.8%  | 7.1  | % |
|                          |         |                                   | Reduction for planned expedited disposal   | 15.0%     |       | 15.0 | % |
| Other repossessed assets | \$35    | Sales approach                    | Reduction for planned expedited disposal   | 15.0%     |       | 15.0 | % |

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(Unaudited)

|                | December 31, 2017<br>Fair Value<br>(Dollars in thousands) | Valuation<br>Technique            | Unobservable Input   | Range           | Weighted<br>Average |
|----------------|---|-----------------------------------|--|-----------------|---------------------|
| <b>Assets:</b> |   |                                   |  |                 |                     |
| Impaired loans | \$1,818   | Income approach                   | Capitalization rate  | 6.5% to 7.5%    | 6.8 %               |
|                |   |                                   | Reduction planned for expedited disposal   | 15.0%           | 15.0 %              |
| Impaired loans | \$10,003  | Sales approach                    | Adjustment to sales comparison value to reconcile differences between comparable sales | -50.0% to 16.2% | -0.8 %              |
|                |   |                                   | Reduction planned for expedited disposal   | -30.9% to 15.0% | 8.7 %               |
| Impaired loans | \$4,206   | Blended income and sales approach | Adjustment to sales comparison value to reconcile differences between comparable sales | -30.0% to 25.0% | -1.2 %              |
|                |   |                                   | Capitalization rate  | 5.0% to 9.8%    | 7.2 %               |
|                |   |                                   | Reduction planned for expedited disposal   | 15.0%           | 15.0 %              |

The Company did not have any liabilities that were carried at fair value on a non-recurring basis at June 30, 2018 and December 31, 2017.

The methods and assumptions used to estimate fair value at June 30, 2018 and December 31, 2017 are as follows:

**Securities:**

The fair values of securities are contained in Note 4 of Notes to Consolidated Financial Statements. Fair value is based upon quoted market prices, where available. If a quoted market price is not available, fair value is estimated using quoted market prices for similar securities and adjusted for differences between the quoted instrument and the instrument being valued. When there is limited activity or less transparency around inputs to the valuation, securities are valued using discounted cash flows.



**Impaired Loans:**

For non-accruing loans, fair value is generally estimated by discounting management's estimate of future cash flows with a discount rate commensurate with the risk associated with such assets or, for collateral dependent loans, 85% of the appraised or internally estimated value of the property, except for taxi medallion loans. The fair value of the underlying collateral of taxi medallion loans is the most recent reported arm's length transaction. When there is no recent sale activity, the fair value is calculated using capitalization rates.

**Other Real Estate Owned and Other Repossessed Assets:**

OREO and other repossessed assets are carried at fair value less selling costs. The fair value for OREO is based on appraised value through a current appraisal, or sometimes through an internal review, additionally adjusted by the estimated costs to sell the property. The fair value for other repossessed assets are based upon the most recently reported arm's length sales transaction. When there is no recent sale activity, the fair value is calculated using capitalization rates.

**Junior Subordinated Debentures:**

The fair value of the junior subordinated debentures was developed using a credit spread based on the subordinated debt issued by the Company adjusting for differences in the junior subordinated debt's credit rating, liquidity and time to maturity. The unrealized net gain/loss attributable to changes in our own credit risk was determined by adjusting the fair value as determined in the proceeding sentence by the average rate of default on debt instruments with a similar debt rating as our junior subordinated debentures, with the difference from the original calculation and this calculation resulting in the instrument-specific unrealized gain/loss.

**Interest Rate Swaps:**

The fair value of interest rate swaps is based upon broker quotes.

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

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The following tables set forth the carrying amounts and estimated fair values of selected financial instruments based on the assumptions described above used by the Company in estimating fair value at the periods indicated:

|                               | June 30, 2018      |               |             |             |           |
|-------------------------------|--------------------|---------------|-------------|-------------|-----------|
|                               | Carrying<br>Amount | Fair<br>Value | Level 1     | Level 2     | Level 3   |
|                               | (In thousands)     |               |             |             |           |
| <b>Assets:</b>                |                    |               |             |             |           |
| Cash and due from banks       | \$42,805           | \$42,805      | \$42,805    | \$-         | \$-       |
| Securities held-to-maturity   |                    |               |             |             |           |
| Mortgage-backed securities    | 7,963              | 7,373         | -           | 7,373       | -         |
| Other securities              | 23,130             | 21,281        | -           | -           | 21,281    |
| Securities available for sale |                    |               |             |             |           |
| Mortgage-backed securities    | 513,868            | 513,868       | -           | 513,868     | -         |
| Other securities              | 214,755            | 214,755       | 11,427      | 202,140     | 1,188     |
| Loans                         | 5,333,807          | 5,291,398     | -           | -           | 5,291,398 |
| FHLB-NY stock                 | 57,384             | 57,384        | -           | 57,384      | -         |
| Accrued interest receivable   | 24,184             | 24,184        | 38          | 1,980       | 22,166    |
| Interest rate swaps           | 27,398             | 27,398        | -           | 27,398      | -         |
| <b>Liabilities:</b>           |                    |               |             |             |           |
| Deposits                      | \$4,609,659        | \$4,601,283   | \$3,157,643 | \$1,443,640 | \$-       |
| Borrowings                    | 1,250,732          | 1,241,294     | -           | 1,201,728   | 39,566    |
| Accrued interest payable      | 4,573              | 4,573         | -           | 4,573       | -         |
| Interest rate swaps           | 1,128              | 1,128         | -           | 1,128       | -         |

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|                               | December 31, 2017  |               |             |             |           |
|-------------------------------|--------------------|---------------|-------------|-------------|-----------|
|                               | Carrying<br>Amount | Fair<br>Value | Level 1     | Level 2     | Level 3   |
|                               | (In thousands)     |               |             |             |           |
| <b>Assets:</b>                |                    |               |             |             |           |
| Cash and due from banks       | \$51,546           | \$51,546      | \$51,546    | \$-         | \$-       |
| Securities held-to-maturity   |                    |               |             |             |           |
| Mortgage-backed securities    | 7,973              | 7,810         | -           | 7,810       | -         |
| Other securities              | 22,913             | 21,889        | -           | -           | 21,889    |
| Securities available for sale |                    |               |             |             |           |
| Mortgage-backed securities    | 509,650            | 509,650       | -           | 509,650     | -         |
| Other securities              | 228,704            | 228,704       | 11,575      | 216,019     | 1,110     |
| Loans                         | 5,176,999          | 5,169,108     | -           | -           | 5,169,108 |
| FHLB-NY stock                 | 60,089             | 60,089        | -           | 60,089      | -         |
| Accrued interest receivable   | 21,405             | 21,405        | 16          | 1,916       | 19,473    |
| Interest rate swaps           | 7,388              | 7,388         | -           | 7,388       | -         |
| <b>Liabilities:</b>           |                    |               |             |             |           |
| Deposits                      | \$4,383,278        | \$4,380,174   | \$3,031,345 | \$1,348,829 | \$-       |
| Borrowings                    | 1,309,653          | 1,310,487     | -           | 1,273,501   | 36,986    |
| Accrued interest payable      | 2,659              | 2,659         | -           | 2,659       | -         |
| Interest rate swaps           | 3,758              | 3,758         | -           | 3,758       | -         |

**11. Derivative Financial Instruments**

At June 30, 2018 and December 31, 2017, the Company's derivative financial instruments consist of interest rate swaps. The Company's interest rate swaps are used for three purposes: 1) to mitigate the Company's exposure to rising interest rates on a portion (\$18.0 million) of its floating rate junior subordinated debentures that have a contractual value of \$61.9 million, at June 30, 2018 and December 31, 2017; 2) to mitigate the Company's exposure to rising interest rates on certain fixed rate loans totaling \$279.8 million and \$280.2 million at June 30, 2018 and December 31, 2017, respectively; and 3) to mitigate exposure to rising interest rates on certain short-term advances totaling \$441.5 million at June 30, 2018 and December 31, 2017.

At June 30, 2018 and December 31, 2017, we held derivatives designated as cash flow hedges, fair value hedges and certain derivatives not designated as hedges.

The Company's derivative instruments are carried at fair value in the Company's financial statements as part of Other Assets for derivatives with positive fair values and Other Liabilities for derivatives with negative fair values. The accounting for changes in the fair value of a derivative instrument is dependent upon whether or not it qualifies and has been designated as a hedge for accounting purposes, and further, by the type of hedging relationship.

At June 30, 2018 and December 31, 2017, derivatives with a combined notional amount of \$36.3 million were not designated as hedges. At June 30, 2018 and December 31, 2017, derivatives with a combined notional amount of \$261.4 million and \$261.9 million were designated as fair value hedges. At June 30, 2018 and December 31, 2017, derivatives with a combined notional amount of \$441.5 million were designated as cash flow hedges.

For cash flow hedges, the effective portion of changes in the fair value of the derivative is reported in AOCL, net of tax, with the ineffective portion of changes in the fair value of the derivative is recognized directly in earnings. Amounts in accumulated other comprehensive income are reclassified into earnings in the same period during which the hedged forecasted transaction effects earnings. During the three and six months ended June 30, 2018, \$0.3 million and \$0.4 million, respectively, was reclassified from accumulated other comprehensive loss to interest expense.

Changes in the fair value of interest rate swaps not designated as hedges are reflected in "Net gain/loss from fair value adjustments" in the Consolidated Statements of Income.

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

The following table sets forth information regarding the Company's derivative financial instruments at the periods indicated:

| (In thousands)                         | June 30, 2018   |                                   | December 31, 2017 |                                   |
|--|-----------------|-----------------------------------|-------------------|-----------------------------------|
|  | Notional Amount | Net Carrying Value <sup>(1)</sup> | Notional Amount   | Net Carrying Value <sup>(1)</sup> |
| Interest rate swaps (fair value hedge) | \$259,747       | \$15,677                          | \$199,341         | \$6,971                           |
| Interest rate swaps (fair value hedge) | 1,694           | (12 )                             | 62,564            | (921 )                            |
| Interest rate swaps (cash flow hedge)  | 441,500         | 11,721                            | 250,000           | 417                               |
| Interest rate swaps (cash flow hedge)  | -               | -                                 | 191,500           | (7 )                              |
| Interest rate swaps (non-hedge)        | 36,321          | (1,116 )                          | 36,321            | (2,830 )                          |
| Total derivatives                      | \$739,262       | \$26,270                          | \$739,726         | \$3,630                           |

<sup>(1)</sup> Derivatives in a net positive position are recorded as "Other assets" and derivatives in a net negative position are recorded as "Other liabilities" in the Consolidated Statements of Financial Condition.

The following table sets forth the effect of derivative instruments on the Consolidated Statements of Income for the periods indicated:

| (In thousands)         | For the three months ended |               | For the six months ended |               |
|------------------------|----------------------------|---------------|--------------------------|---------------|
|                        | June 30, 2018              | June 30, 2017 | June 30, 2018            | June 30, 2017 |
| Financial Derivatives: |                            |               |                          |               |

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|  |       |         |         |         |
|--|-------|---------|---------|---------|
| Interest rate swaps (non-hedge)        | \$438 | \$(493) | \$1,714 | \$(260) |
| Interest rate swaps (fair value hedge) | 224   | (180)   | 678     | (246)   |
| Net gain (1)                           | \$662 | \$(673) | \$2,392 | \$(506) |

(1) Net gains and losses are recorded as part of “Net gain/loss from fair value adjustments” in the Consolidated Statements of Income.

During the three and six months ended June 30, 2018 and 2017, the Company did not record any hedge ineffectiveness.

The Company’s interest rate swaps are subject to master netting arrangements between the Company and its two designated counterparties. The Company has not made a policy election to offset its derivative positions.

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The following tables present the effect of the master netting arrangements on the presentation of the derivative assets and liabilities in the Consolidated Statements of Condition as of the dates indicated:

| June 30, 2018       |                                   |   |  |   |                          |            |
|---------------------|-----------------------------------|---|--|---|--------------------------|------------|
| (In thousands)      | Gross Amount of Recognized Assets | Gross Amount Offset in the Statement of Condition | Net Amount of Assets Presented in the Statement of Condition | Gross Amounts Not Offset in the Consolidated Statement of Condition |                          | Net Amount |
|                     |                                   |   |  | Financial Instruments   | Cash Collateral Received |            |
| Interest rate swaps | \$ 27,398                         | \$ -  | \$ 27,398  | \$ -  | \$ 25,440                | \$ 1,958   |

  

| (In thousands)      | Gross Amount of Recognized Liabilities | Gross Amount Offset in the Statement of Condition | Net Amount of Liabilities Presented in the Statement of Condition | Gross Amounts Not Offset in the Consolidated Statement of Condition |                         | Net Amount |
|---------------------|--|---|---|---|-------------------------|------------|
|                     |  |   |   | Financial Instruments   | Cash Collateral Pledged |            |
| Interest rate swaps | \$ 1,128                               | \$ -  | \$ 1,128  | \$ -  | \$ -                    | \$ 1,128   |

December 31, 2017

| (In thousands)      | Gross Amount of Recognized Assets | Gross Amount Offset in the Statement of Condition | Net Amount of Assets Presented in the Statement of Condition | Gross Amounts Not Offset in the Consolidated Statement of Condition |                          | Net Amount |
|---------------------|-----------------------------------|---|--|---|--------------------------|------------|
|                     |                                   |   |  | Financial Instruments   | Cash Collateral Received |            |
| Interest rate swaps | \$7,388                           | \$ -  | \$ 7,388   | \$ -  | \$ 3,660                 | \$ 3,728   |

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| (In thousands)      | Gross<br>Amount of<br>Recognized<br>Liabilities | Gross<br>Amount<br>Offset in<br>the<br>Statement<br>of<br>Condition | Net<br>Amount of<br>Liabilities<br>Presented<br>in the<br>Statement<br>of<br>Condition | Gross Amounts<br>Not Offset in the<br>Consolidated<br>Statement of<br>Condition |                               | Net<br>Amount |
|---------------------|---|---|--|---|-------------------------------|---------------|
|                     |   |   |  | Financial<br>Instruments  | Cash<br>Collateral<br>Pledged |               |
| Interest rate swaps | \$ 3,758  | \$ -  | \$ 3,758   | \$ -  | \$ -                          | \$ 3,758      |

**12. Income Taxes**

Flushing Financial Corporation files consolidated Federal and combined New York State and New York City income tax returns with its subsidiaries, with the exception of the Company's trusts, which file separate Federal income tax returns as trusts, and Flushing Preferred Funding Corporation, which files a separate Federal income tax return as a real estate investment trust. Additionally, the Bank files New Jersey State tax returns.

Income tax provisions are summarized as follows:

| (In thousands)              | For the three<br>months<br>ended June 30, |         | For the six<br>months<br>ended June 30, |         |
|-----------------------------|---|---------|---|---------|
|                             | 2018                                      | 2017    | 2018                                    | 2017    |
| Federal:                    |   |         |   |         |
| Current                     | \$3,755                                   | \$6,653 | \$6,165                                 | \$9,605 |
| Deferred                    | (444 )                                    | (1,077) | (247 )                                  | 720     |
| Total federal tax provision | 3,311                                     | 5,576   | 5,918                                   | 10,325  |
| State and Local:            |   |         |   |         |
| Current                     | 1,499                                     | 1,618   | 1,689                                   | 1,419   |

|                                     |         |         |         |          |
|-------------------------------------|---------|---------|---------|----------|
| Deferred                            | (321 )  | (419 )  | (168 )  | 285      |
| Total state and local tax provision | 1,178   | 1,199   | 1,521   | 1,704    |
| Total income tax provision          | \$4,489 | \$6,775 | \$7,439 | \$12,029 |

**13. Accumulated Other Comprehensive Income (Loss):**

The following tables sets forth the changes in accumulated other comprehensive income (loss) by component for the periods indicated:

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(Unaudited)

|  | For the three months ended June 30, 2018   |  |  |   | Total      |
|--|--|--|--|---|------------|
|  | Unrealized<br>Gains<br>(Losses)<br>on<br>Available<br>for Sale<br>Securities<br>(In thousands) | Unrealized<br>Gains<br>(Losses)<br>on<br>Cash flow<br>Hedges | Defined<br>Benefit<br>Pension<br>Items | Fair<br>Value<br>Option<br>Elected<br>on<br>Liabilities |            |
| Beginning balance, net of tax  | \$(13,487)   | \$ 5,942   | \$(4,409)                              | \$ 779  | \$(11,175) |
| Other comprehensive income before reclassifications, net of tax              | (3,014 )   | 1,898  | -                                      | 13  | (1,103 )   |
| Amounts reclassified from accumulated other comprehensive income, net of tax | -  | 187  | 84                                     | -   | 271        |
| Net current period other comprehensive income (loss), net of tax             | (3,014 )   | 2,085  | 84                                     | 13  | (832 )     |
| Ending balance, net of tax   | \$(16,501)   | \$ 8,027   | \$(4,325)                              | \$ 792  | \$(12,007) |

|   | For the three months ended June 30, 2017   |  |  |   | Total     |
|---|--|--|--|---|-----------|
|   | Unrealized<br>Gains<br>(Losses)<br>on<br>Available<br>for Sale<br>Securities<br>(In thousands) | Unrealized<br>Gains<br>(Losses)<br>on<br>Cash flow<br>Hedges | Defined<br>Benefit<br>Pension<br>Items | Fair<br>Value<br>Option<br>Elected<br>on<br>Liabilities |           |
| Beginning balance, net of tax                                   | \$(2,711)  | \$ -   | \$(4,423)                              |   | \$(7,134) |
| Other comprehensive income before reclassifications, net of tax | 601  | (124 )   | -                                      |   | 477       |
|   | -  | -  | 81                                     |   | 81        |

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Amounts reclassified from accumulated other comprehensive income, net of tax

|  |           |          |           |           |
|--|-----------|----------|-----------|-----------|
| Net current period other comprehensive income (loss), net of tax | 601       | (124 )   | 81        | 558       |
| Ending balance, net of tax                                       | \$(2,110) | \$(124 ) | \$(4,342) | \$(6,576) |

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|  | For the six months ended June 30, 2018   |  |  |   |            |
|--|--|--|--|---|------------|
|  | Unrealized<br>Gains<br>(Losses)<br>on<br>Available<br>for Sale<br>Securities<br>(In thousands) | Unrealized<br>Gains<br>(Losses)<br>on<br>Cash flow<br>Hedges | Defined<br>Benefit<br>Pension<br>Items | Fair<br>Value<br>Option<br>Elected<br>on<br>Liabilities | Total      |
| Beginning balance, net of tax  | \$(5,522 )   | \$ 231   | \$(3,695)                              | \$ -  | \$(8,986 ) |
| Reclassification of the Income Tax Effects of the Tax Cuts and Jobs Act from AOCL to Retained Earnings | (1,325 )   | 50   | (798 )                                 | -   | (2,073 )   |
| Impact of adoption of Accounting Standard Update 2016-01   | -  | -  | -                                      | 779   | 779        |
| Other comprehensive income before reclassifications, net of tax  | (9,654 )   | 7,505  | -                                      | 13  | (2,136 )   |
| Amounts reclassified from accumulated other comprehensive income (loss), net of tax                    | -  | 241  | 168                                    | -   | 409        |
| Net current period other comprehensive income, net of tax  | (9,654 )   | 7,746  | 168                                    | 13  | (1,727 )   |
| Ending balance, net of tax   | \$(16,501)   | \$ 8,027   | \$(4,325)                              | \$ 792  | \$(12,007) |

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|  | For the six months ended June 30, 2017   |  |  |            |
|--|--|--|--|------------|
|  | Unrealized<br>Gains<br>(Losses)<br>on<br>Available<br>for Sale<br>Securities<br>(In thousands) | Unrealized<br>Gains<br>(Losses)<br>on<br>Cash flow<br>Hedges | Defined<br>Benefit<br>Pension<br>Items | Total      |
| Beginning balance, net of tax  | \$ (3,859)   | \$ -   | \$ (4,503)                             | \$ (8,362) |
| Other comprehensive income before reclassifications, net of tax              | 1,749  | (124 )   | -                                      | 1,625      |
| Amounts reclassified from accumulated other comprehensive income, net of tax | -  | -  | 161                                    | 161        |
| Net current period other comprehensive income (loss), net of tax             | 1,749  | (124 )   | 161                                    | 1,786      |
| Ending balance, net of tax   | \$ (2,110)   | \$ (124 )  | \$ (4,342)                             | \$ (6,576) |

The following tables set forth significant amounts reclassified from accumulated other comprehensive income (loss) by component for the periods indicated:

For the three months ended June 30, 2018

| Details about Accumulated Other Comprehensive Loss Components | Amounts<br>Reclassified<br>from<br>Accumulated<br>Other<br>Comprehensive<br>Loss<br>(In thousands) | Affected Line Item in the Statement<br>Where Net Income is Presented |
|---|--|--|
|---|--|--|

|  |           |                         |
|--|-----------|-------------------------|
| Cash flow hedges:                              |           |                         |
| Interest rate swaps                            | \$ (273 ) | Other interest expense  |
|  | 86        | Tax expense             |
|  | \$ (187 ) | Net of tax              |
| Amortization of defined benefit pension items: |           |                         |
| Actuarial losses                               | \$ (133 ) | Other operating expense |
| Prior service credits                          | 9 (1)     | Other operating expense |
|  | (124 )    | Total before tax        |
|  | 40        | Tax expense             |
|  | \$ (84 )  | Net of tax              |

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For the three months ended June 30, 2017

| Details about Accumulated Other Comprehensive Loss Components | Amounts<br>Reclassified<br>from<br>Accumulated<br>Other<br>Comprehensive<br>Loss<br>(In thousands) | Affected Line Item in the Statement<br>Where Net Income is Presented |
|---|--|--|
| Amortization of defined benefit pension items:                |  |  |
| Actuarial losses  | \$ (151 )  | Other operating expense  |
| Prior service credits   | 11 (1)   | Other operating expense  |
|   | (140 )   | Total before tax   |
|   | 59   | Tax benefit  |
|   | \$ (81 )   | Net of tax   |

For the six months ended June 30, 2018

| Details about Accumulated Other Comprehensive Loss Components | Amounts<br>Reclassified<br>from<br>Accumulated<br>Other<br>Comprehensive<br>Loss<br>(In thousands) | Affected Line Item in the Statement<br>Where Net Income is Presented |
|---|--|--|
| Cash flow hedges:   |  |  |
| Interest rate swaps   | \$ (351 )  | Interest expense   |
|   | 110  | Tax benefit  |
|   | \$ (241 )  | Net of tax   |
| Amortization of defined benefit pension items:                |  |  |
| Actuarial losses  | \$ (265 )  | Other operating expense  |
| Prior service credits   | 19 (1)   | Other operating expense  |
|   | (246 )   | Total before tax   |



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|           |             |
|-----------|-------------|
| 78        | Tax benefit |
| \$ (168 ) | Net of tax  |

For the six months ended June 30, 2017

| Details about Accumulated Other Comprehensive Loss Components | Amounts<br>Reclassified<br>from<br>Accumulated<br>Other<br>Comprehensive<br>Loss<br>(In thousands) | Affected Line Item in the Statement<br>Where Net Income is Presented |
|---|--|--|
| Amortization of defined benefit pension items:                |  |  |
| Actuarial losses  | \$ (302 )  | Other operating expense  |
| Prior service credits   | 22 (1)   | Other operating expense  |
|   | (280 )   | Total before tax   |
|   | 119  | Tax benefit  |
|   | \$ (161 )  | Net of tax   |

These accumulated other comprehensive loss components are included in the computation of net periodic pension (1) cost (See Note 9 of the Notes to Consolidated Financial Statements “Pension and Other Postretirement Benefit Plans”.)

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

**14. Regulatory Capital**

Under current capital regulations, the Bank is required to comply with four separate capital adequacy standards. As of June 30, 2018, the Bank continues to be categorized as “well-capitalized” under the prompt corrective action regulations and continues to exceed all regulatory capital requirements. In 2016, a Capital Conservation Buffer (“CCB”) requirement became effective for banks. The CCB is designed to establish a capital range above minimum capital requirements and impose constraints on dividends, share buybacks and discretionary bonus payments when capital levels fall below prescribed levels. The minimum CCB in 2018 is 1.875% and increases 0.625% annually through 2019 to 2.5%. The CCB for the Bank at June 30, 2018 was 5.79%.

Set forth below is a summary of the Bank’s compliance with banking regulatory capital standards.

|  | June 30, 2018          |                         | December 31, 2017 |                         |
|--|------------------------|-------------------------|-------------------|-------------------------|
|  | Amount                 | Percent<br>of<br>Assets | Amount            | Percent<br>of<br>Assets |
|  | (Dollars in thousands) |                         |                   |                         |
| Tier I (leverage) capital:               |                        |                         |                   |                         |
| Capital level                            | \$644,880              | 9.90 %                  | \$631,285         | 10.11 %                 |
| Requirement to be well capitalized       | 325,697                | 5.00                    | 312,343           | 5.00                    |
| Excess                                   | 319,183                | 4.90                    | 318,942           | 5.11                    |
| Common Equity Tier I risk-based capital: |                        |                         |                   |                         |
| Capital level                            | \$644,880              | 13.37 %                 | \$631,285         | 13.87 %                 |
| Requirement to be well capitalized       | 313,524                | 6.50                    | 295,937           | 6.50                    |
| Excess                                   | 331,356                | 6.87                    | 335,348           | 7.37                    |
| Tier 1 risk-based capital:               |                        |                         |                   |                         |
| Capital level                            | \$644,880              | 13.37 %                 | \$631,285         | 13.87 %                 |
| Requirement to be well capitalized       | 385,876                | 8.00                    | 364,230           | 8.00                    |
| Excess                                   | 259,004                | 5.37                    | 267,055           | 5.87                    |
| Total risk-based capital:                |                        |                         |                   |                         |
| Capital level                            | \$665,100              | 13.79 %                 | \$651,636         | 14.31 %                 |
| Requirement to be well capitalized       | 482,345                | 10.00                   | 455,288           | 10.00                   |

|        |         |      |         |      |
|--------|---------|------|---------|------|
| Excess | 182,755 | 3.79 | 196,348 | 4.31 |
|--------|---------|------|---------|------|

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**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Notes to Consolidated Financial Statements**

(Unaudited)

The Holding Company is subject to the same regulatory capital requirements as the Bank. As of June 30, 2018, the Holding Company continues to be categorized as “well-capitalized” under the prompt corrective action regulations and continues to exceed all regulatory capital requirements. The CCB for the Holding Company at June 30, 2018 was 5.84%.

Set forth below is a summary of the Holding Company’s compliance with banking regulatory capital standards.

|  | June 30, 2018          |                         | December 31, 2017 |                         |
|--|------------------------|-------------------------|-------------------|-------------------------|
|  | Amount                 | Percent<br>of<br>Assets | Amount            | Percent<br>of<br>Assets |
|  | (Dollars in thousands) |                         |                   |                         |
| Tier I (leverage) capital:               |                        |                         |                   |                         |
| Capital level                            | \$572,189              | 8.79 %                  | \$563,426         | 9.02 %                  |
| Requirement to be well capitalized       | 325,615                | 5.00                    | 312,278           | 5.00                    |
| Excess                                   | 246,574                | 3.79                    | 251,148           | 4.02                    |
| Common Equity Tier I risk-based capital: |                        |                         |                   |                         |
| Capital level                            | \$534,036              | 11.07 %                 | \$527,727         | 11.59 %                 |
| Requirement to be well capitalized       | 313,460                | 6.50                    | 295,865           | 6.50                    |
| Excess                                   | 220,576                | 4.57                    | 231,862           | 5.09                    |
| Tier 1 risk-based capital:               |                        |                         |                   |                         |
| Capital level                            | \$572,189              | 11.87 %                 | \$563,426         | 12.38 %                 |
| Requirement to be well capitalized       | 385,797                | 8.00                    | 364,141           | 8.00                    |
| Excess                                   | 186,392                | 3.87                    | 199,285           | 4.38                    |
| Total risk-based capital:                |                        |                         |                   |                         |
| Capital level                            | \$667,409              | 13.84 %                 | \$658,777         | 14.47 %                 |
| Requirement to be well capitalized       | 482,246                | 10.00                   | 455,177           | 10.00                   |
| Excess                                   | 185,163                | 3.84                    | 203,600           | 4.47                    |

## **PART I – FINANCIAL INFORMATION**

### **FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES**

#### **Notes to Consolidated Financial Statements**

(Unaudited)

#### **15. New Authoritative Accounting Pronouncements**

##### *Accounting Standards Adopted in 2018:*

In February 2018, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) No. 2018-02, “Income Statement – Reporting Comprehensive Income (Topic 220).” As a result of the Tax Cuts and Jobs Act (the “TCJA”), concerns arose regarding the guidance which requires deferred tax assets and liabilities to be adjusted for the effect of a change in tax laws or rates with the effect included in income from continuing operations in the reporting period that includes the enactment date. The amendments in this ASU require a reclassification for stranded tax effects from accumulated other comprehensive income to retained earnings, furthermore eliminating the stranded tax effects resulting from the TCJA. The amount of the reclassification is the difference between the previous corporate income tax rate of 35% and the newly enacted corporate income tax rate of 21%. The amendments of this ASU are effective for fiscal years beginning after December 15, 2018, and interim periods within those fiscal years, with early adoption permitted in any interim period or fiscal year before the effective date. We have elected to early adopt this guidance as of January 1, 2018. Our Consolidated Statements of Financial Condition reflect adoption of this ASU and reclassification of \$2.1 million in stranded tax effects from accumulated other comprehensive income to retained earnings. See Note 12 “Income Taxes” for additional information.

In August 2016, the FASB issued ASU No. 2016-15 “Classification of Certain Cash Receipts and Cash Payments”, to clarify how certain cash receipts and cash payments are presented and classified in the statements of cash flows. The amendments are intended to reduce diversity in practice by clarifying whether the following items should be categorized as operating, investing or financing in the statement of cash flows: (i) debt prepayments and extinguishment costs, (ii) settlement of zero-coupon debt, (iii) settlement of contingent consideration, (iv) insurance proceeds, (v) settlement of corporate-owned life insurance (COLI) and bank-owned life insurance (BOLI) policies, (vi) distributions from equity method investees, (vii) beneficial interests in securitization transactions, and (viii) receipts and payments with aspects of more than one class of cash flows. The ASU will be effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2017. Early adoption is permitted. If an entity early adopts the amendments in an interim period, any adjustments should be reflected as of the beginning of the fiscal year that includes that interim period. An entity that elects early adoption must adopt all of the amendments in the same period. This ASU was adopted on January 1, 2018 and did not have a significant impact on the presentation of our cash flows.

In January 2016, FASB issued ASU No. 2016-01 “Financial Instruments” which requires an entity to: (i) measure equity investments at fair value through net income, with certain exceptions; (ii) present in other comprehensive income the

changes in instrument-specific credit risk for financial liabilities measured using the fair value option; (iii) present financial assets and financial liabilities by measurement category and form of financial asset; (iv) calculate the fair value of financial instruments for disclosure purposes based on an exit price and; (v) assess a valuation allowance on deferred tax assets related to unrealized losses of available for sale debt securities in combination with other deferred tax assets. The ASU provides an election to subsequently measure certain nonmarketable equity investments at cost less any impairment and adjusted for certain observable price changes. The ASU also requires a qualitative impairment assessment of such equity investments and amends certain fair value disclosure requirements. This ASU became effective for us on January 1, 2018. The adoption of the guidance resulted in a cumulative-effect adjustment totaling \$0.8 million and did not have a significant impact on our results of operations, financial condition and cash flows.

In May 2014, the FASB issued ASU 2014-09, "Revenue from Contracts with Customers (Topic 606)". This ASU establishes a comprehensive revenue recognition standard for virtually all industries under GAAP, including those that previously followed industry-specific guidance such as real estate, construction and software industries. The revenue standard's core principle is built on the contract between a vendor and a customer for the provision of goods and services. It attempts to depict the exchange of rights and obligations between the parties in the pattern of revenue recognition based on the consideration to which the vendor is entitled. The guidance in this ASU for public companies is effective for the annual periods beginning after December 15, 2016, including interim periods therein. In August 2015, the FASB approved a one-year delay of the effective date of this standard to reporting periods beginning after December 15, 2017. This ASU allows for either full retrospective adoption or modified retrospective adoption. This ASU became effective for us on January 1, 2018. We adopted this standard through the modified retrospective transition method. The modified retrospective method requires application of ASU 2014-09 to uncompleted contracts at the date of adoption; however, periods prior to the date of adoption have not been retrospectively revised as the impact of the new standard on uncompleted contracts as the date of adoption was not material as such a cumulative effective adjustment to opening retained earnings was not deemed necessary.

## **PART I – FINANCIAL INFORMATION**

### **FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES**

#### **Notes to Consolidated Financial Statements**

(Unaudited)

Topic 606 does not apply to the majority of our revenue streams which are primarily comprised of interest and dividend income and associated fees within those revenue streams. The revenue streams derived by the Company that are within the scope of Topic 606 are primarily certain banking service fees, including wire transfer fees, ATM fees, account maintenance fees, overdraft fees and other deposit fees. We generally satisfy our performance obligations on contracts with customers as services are rendered, and the transaction prices are typically fixed and charged either on a periodic basis or based on activity. Being that performance obligations are satisfied as services are rendered and the transaction prices are fixed, there is little judgment involved in applying Topic 606 that significantly affects the determination of the amount and timing of revenue from contracts with customers. Additionally, the Company will receive revenue from the sale of investment products through a third party as part of a revenue sharing agreement. This revenue is included in “Other Income” in the Consolidated Statements of Income. These fees are remitted to the Company monthly as our performance obligation is satisfied. We have evaluated the nature of our contracts with customers and determined that further disaggregation of revenue from contracts with customers into more granular categories beyond what is present in the Consolidated Statements of Income was not necessary.

#### *Accounting Standards Pending Adoption:*

In August 2017, the FASB issued ASU No. 2017-12, “Derivatives and Hedging (Topic 815)” providing targeted improvements to the accounting for hedging activities, which is effective January 1, 2019, with early adoption permitted in any interim period or fiscal year before the effective date. The guidance introduces a number of amendments, several of which are optional, that are designed to simplify the application of hedge accounting, improve financial statement transparency and more closely align hedge accounting with an entity’s risk management strategies. This ASU eliminates the requirement to separately measure and report hedge ineffectiveness and changes the presentation so that all items that affect earnings are in the same income statement line as the hedged item. We are currently evaluating the impact of adopting this new guidance on our consolidated results of operations, financial condition and cash flows.

In March 2017, the FASB issued ASU No. 2017-08, “Premium Amortization on Purchased Callable Debt Securities” which shortens the amortization period for premiums on purchased callable debt securities to the earliest call date, rather than amortizing over the full contractual term. The ASU does not change the accounting for securities held at a discount. The amendments in this ASU require companies to reset the effective yield using the payment terms of the debt security if the call option is not exercised on the earliest call date. If the security has additional future call dates, any excess of the amortized cost basis over the amount repayable by the issuer at the next call date should be amortized to the next call date. The amendments in this update are effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. Early adoption is permitted, including adoption in an interim period. If an entity early adopts the amendments in an interim period, any adjustments should be reflected as

of the beginning of the fiscal year that includes that interim period. The guidance is not expected to have an impact on the Company's financial positions, results of operations or disclosures.

In January 2017, the FASB issued ASU No. 2017-04, "Intangibles - Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment." The ASU simplifies the subsequent measurement of goodwill and eliminates Step 2 from the goodwill impairment test. Under this ASU, the Company should perform its goodwill impairment test by comparing the fair value of a reporting unit with its carrying amount. An impairment charge should be recognized for the amount by which the carrying amount exceeds the reporting unit's fair value. The impairment charge is limited to the amount of goodwill allocated to that reporting unit. The amendments in this update are effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. Early adoption is permitted for goodwill impairment tests performed on testing dates after January 1, 2017. The guidance is not expected to have a significant impact on the Company's financial positions, results of operations or disclosures.

In June 2016, the FASB issued ASU No. 2016-13, "Financial Instruments – Credit Losses" which sets forth a "current expected credit loss" ("CECL") model which requires the Company to measure all expected credit losses for financial instruments held at the reporting date based on historical experience, current conditions and reasonable supportable forecasts. This replaces the existing incurred loss model and will apply to the measurement of credit losses on financial assets measured at amortized cost and to some off-balance sheet credit exposures. This ASU will be effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. The Company has begun collecting and evaluating data and system requirements to implement this standard. The adoption of this update could have a material impact on the Company's consolidated results of operations and financial condition. The extent of the impact is still unknown and will depend on many factors, such as the composition of the Company's loan portfolio and expected loss history at adoption. Management has engaged consultants to assess the preparedness of the Company and has developed inter-departmental steering and working committees to evaluate and implement CECL.



**PART I – FINANCIAL INFORMATION**

**FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES**

**Notes to Consolidated Financial Statements**

(Unaudited)

In February 2016, the FASB issued ASU No. 2016-02, “Leases”. From the lessee's perspective, the new standard establishes a right-of-use (“ROU”) model that requires a lessee to record a ROU asset and a lease liability on the balance sheet for all leases with terms longer than 12 months. Leases will be classified as either finance or operating, with classification affecting the pattern of expense recognition in the income statement for a lessee. From the lessor's perspective, the new standard requires a lessor to classify leases as either sales-type, finance or operating. A lease will be treated as a sale if it transfers all of the risks and rewards, as well as control of the underlying asset, to the lessee. If risks and rewards are conveyed without the transfer of control, the lease is treated as a financing. If the lessor doesn't convey risks and rewards or control, an operating lease results. The new standard is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. A modified retrospective transition approach is required for lessees for capital and operating leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements, with certain practical expedients available. A modified retrospective transition approach is required for lessors for sales-type, direct financing, and operating leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements, with certain practical expedients available. The Company has not adopted a new accounting policy as of the filing date. Management is continuing to evaluate the standard and the Company's outstanding inventory of leases determining the effect of recognizing most operating leases on the Consolidated Statements of Financial Condition is expected to be material. The Company expects to recognize right-of-use assets and lease liabilities for substantially all of its operating lease commitments based on the present value of unpaid lease payments as of the date of adoption.

**PART I – FINANCIAL INFORMATION**

**FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES**

**Management’s Discussion and Analysis of**

**Financial Condition and Results of Operations**

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

*This Quarterly Report should be read in conjunction with the more detailed and comprehensive disclosures included in our Annual Report on Form 10-K for the year ended December 31, 2017. In addition, please read this section in conjunction with our Consolidated Financial Statements and Notes to Consolidated Financial Statements contained herein.*

*As used in this Quarterly Report, the words “we,” “us,” “our” and the “Company” are used to refer to Flushing Financial Corporation and its direct and indirect wholly owned subsidiaries, Flushing Bank (the “Bank”), Flushing Preferred Funding Corporation, Flushing Service Corporation, and FSB Properties Inc.*

Statements contained in this Quarterly Report relating to plans, strategies, objectives, economic performance and trends, projections of results of specific activities or investments and other statements that are not descriptions of historical facts may be forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. Forward-looking information is inherently subject to risks and uncertainties and actual results could differ materially from those currently anticipated due to a number of factors, which include, but are not limited to, factors discussed elsewhere in this Quarterly Report and in other documents filed by us with the Securities and Exchange Commission from time to time, including, without limitation, our Annual Report on Form 10-K for the year ended December 31, 2017. Forward-looking statements may be identified by terms such as “may,” “will,” “should,” “could,” “expects,” “plans,” “intends,” “anticipates,” “believes,” “estimates,” “predicts,” “forecast,” “potential” or “continue” or similar terms or the negative of these terms. Although we believe that the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee future results, levels of activity, performance or achievements. We have no obligation to update these forward-looking statements.

**Executive Summary**

We are a Delaware corporation organized in May 1994. The Bank was organized in 1929 as a New York State-chartered mutual savings bank. Today the Bank operates as a full-service New York State commercial bank. The Bank’s primary regulator is the New York State Department of Financial Services, and its primary federal regulator is the Federal Deposit Insurance Corporation (“FDIC”). Deposits are insured to the maximum allowable amount by the

FDIC. Additionally, the Bank is a member of the Federal Home Loan Bank system. The primary business of Flushing Financial Corporation has been the operation of the Bank. The Bank owns three subsidiaries: Flushing Preferred Funding Corporation, Flushing Service Corporation, and FSB Properties Inc. The Bank also operates an internet branch, which operates under the brands of iGObanking.com® and BankPurely® (the “Internet Branch”). The activities of Flushing Financial Corporation are primarily funded by dividends, if any, received from the Bank, issuances of subordinated debt, junior subordinated debt, and issuances of equity securities. Flushing Financial Corporation’s common stock is traded on the NASDAQ Global Select Market under the symbol “FFIC.”

Our principal business is attracting retail deposits from the general public and investing those deposits together with funds generated from ongoing operations and borrowings, primarily in (1) originations and purchases of multi-family residential loans, commercial business loans, commercial real estate mortgage loans and, to a lesser extent, one-to-four family loans (focusing on mixed-use properties, which are properties that contain both residential dwelling units and commercial units); (2) Small Business Administration (“SBA”) loans and other small business loans; (3) construction loans, primarily for residential properties; (4) mortgage loan surrogates such as mortgage-backed securities; and (5) U.S. government securities, corporate fixed-income securities and other marketable securities. We also originate certain other consumer loans including overdraft lines of credit. Our results of operations depend primarily on net interest income, which is the difference between the income earned on our interest-earning assets and the cost of our interest-bearing liabilities. Net interest income is the result of our interest rate margin, which is the difference between the average yield earned on interest-earning assets and the average cost of interest-bearing liabilities, adjusted for the difference in the average balance of interest-earning assets as compared to the average balance of interest-bearing liabilities. We also generate non-interest income primarily from loan fees, service charges on deposit accounts, mortgage servicing fees, and other fees, income earned on Bank Owned Life Insurance (“BOLI”), dividends on Federal Home Loan Bank of New York stock and net gains and losses on sales of securities and loans. Our operating expenses consist principally of employee compensation and benefits, occupancy and equipment costs, other general and administrative expenses and income tax expense. Our results of operations also can be significantly affected by changes in the fair value of financial assets and financial liabilities for which changes in value are recorded through earnings, our periodic provision for loan losses and specific provision for losses on real estate owned.

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**FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES**

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**Financial Condition and Results of Operations**

Our strategy is to continue our focus on being an institution serving consumers, businesses, and governmental units in our local markets. In furtherance of this objective, we intend to:

- increase core deposits and continue to improve funding mix to manage cost of funds;
- increase net interest income by leveraging loan pricing opportunities and portfolio mix;
- enhance earnings power by improving scalability and efficiency;
- manage credit risk;
- remain well capitalized;
- increase our commitment to the multi-cultural marketplace, with a particular focus on the Asian community in Queens;
- manage enterprise-wide risk.

There can be no assurance that we will be able to effectively implement this strategy. Our strategy is subject to change by the Board of Directors.

Our investment policy, which is approved by the Board of Directors, is designed primarily to manage the interest rate sensitivity of our overall assets and liabilities, to generate a favorable return without incurring undue interest rate risk and credit risk, to complement our lending activities and to provide and maintain liquidity. In establishing our investment strategies, we consider our business and growth strategies, the economic environment, our interest rate risk exposure, our interest rate sensitivity “gap” position, the types of securities to be held and other factors. We classify our investment securities as available for sale or held-to-maturity.

We carry a portion of our financial assets and financial liabilities at fair value and record changes in their fair value through earnings in non-interest income on our Consolidated Statements of Income and Comprehensive Income. A description of the financial assets and financial liabilities that are carried at fair value through earnings can be found in Note 10 of the Notes to the Consolidated Financial Statements.

One of the Company's strategic objectives is the emphasis of rate over volume regarding loan originations. To that end, we decided to allow over \$70 million of loan participations with another financial institution to prepay as the rates being offered through the refinancing process did not meet our lending criteria. Consequently, during the three months ended June 30, 2018, our loan growth was 0.4% compared to loan growth of 2.6% for the three months ended March 31, 2018. We believe emphasizing rate over volume is a long-term winning strategy and we are beginning to see tangible results as the yield in the loan portfolio has risen 10 basis points to 4.31% for the three months ended June 30, 2018 from 4.21% for the three months ended March 31, 2018.

However during the three months ended June 30, 2018, deposit pressures outstripped the gains on the loan side as net interest margin pressure continued. The cost of funds increased 14 basis points to 1.41% for the three months ended June 30, 2018, from 1.27% for the three months ended March 31, 2018. However the combination of improved loan yields and mitigation strategies that we put in place on the liability side of the balance sheet have decelerated the pace of net interest margin compression from 11 basis points experienced in the first quarter of 2018 compared to the fourth quarter of 2017, to three basis points experienced in the three months ended June 30, 2018, compared to the three months ended March 31, 2018.

As we've continued to improve loan yields we have retained our focus on credit quality. Non-performing assets decreased by 18.3% since December 31, 2017. At June 30, 2018, the allowance for loan losses to gross loans was 0.38% while the allowance for loan losses to non-performing was 136.7%. The loan-to-value ratio on our non-performing real estate loans at June 30, 2018 remains conservative at 35.1%. The net charge offs of \$322,000 for the quarter reflect the change in the fair value of Chicago taxi medallions from \$60,000 to \$25,000 per medallion, based upon recent sales transactions. Currently, the Chicago taxi medallion portfolio totals \$0.2 million. Our exposure to taxi medallion loans in Chicago and NYC totals \$6.2 million, which is 0.12% of total loans.

The Bank and Company are subject to the same regulatory capital requirements. See Note 14 of the Notes to the Consolidated Financial Statements "Regulatory Capital."

## **PART I – FINANCIAL INFORMATION**

### **FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES**

#### **Management’s Discussion and Analysis of**

#### **Financial Condition and Results of Operations**

### **COMPARISON OF OPERATING RESULTS FOR THE THREE MONTHS ENDED**

#### **JUNE 30, 2018 AND 2017**

**General.** Net income for the three months ended June 30, 2018 was \$13.9 million, an increase of \$1.2 million, or 9.4%, compared to \$12.7 million for the three months ended June 30, 2017. Diluted earnings per common share were \$0.48 for the three months ended June 30, 2018, an increase of \$0.04, or 9.1%, from \$0.44 for the three months ended June 30, 2017.

Return on average equity increased to 10.5% for the three months ended June 30, 2018 from 9.6% for the three months ended June 30, 2017. Return on average assets increased to 0.9% for the three months ended June 30, 2018 from 0.8% for the three months ended June 30, 2017.

**Interest Income.** Total interest and dividend income increased \$5.0 million, or 8.5%, to \$63.3 million for the three months ended June 30, 2018 from \$58.3 million for the three months ended June 30, 2017. The increase in interest income was primarily attributable to an increase of 16 basis points in the yield of interest-earning assets to 4.10% for the three months ended June 30, 2018 from 3.94% in the comparable prior year period, combined with an increase of \$262.2 million in the average balance of interest-earning assets to \$6,181.2 million for the three months ended June 30, 2018 from \$5,919.0 million for the comparable prior year period. The increase in the yield on interest-earning assets of 16 basis points was primarily due to an increase of 15 basis points in the yield of total loans, net to 4.31% for the three months ended June 30, 2018 from 4.16% for the comparable prior year period. Additionally, interest income increased due to an increase of \$353.3 million in the average balance of total loans, net, which have a higher yield than the yield of total interest-earning assets. Excluding prepayment penalty income and recovered interest from loans, the yield on total loans, net, would have increased 14 basis points to 4.19% for the three months ended June 30, 2018 from 4.05% for the three months ended June 30, 2017.

**Interest Expense.** Interest expense increased \$6.0 million, or 40.5%, to \$20.7 million for the three months ended June 30, 2018 from \$14.7 million for the three months ended June 30, 2017. The increase in interest expense was primarily due to an increase of 39 basis points in the average cost of interest-bearing liabilities to 1.50% for the three months ended June 30, 2018 from 1.11% for the three months ended June 30, 2017, combined with an increase of \$227.9 million in the average balance of interest-bearing liabilities to \$5,515.6 million for the three months ended June 30, 2018, from \$5,287.7 million for the comparable prior year period. The 39 basis point increase in the cost of interest-bearing liabilities was primarily due to the Bank raising the rates we pay on some of our deposit products to

stay competitive within our market and an increase in borrowing costs from recent increases in the Fed Funds rate.

**Net Interest Income.** For the three months ended June 30, 2018, net interest income was \$42.6 million, a decrease of \$1.0 million, or 2.2%, from \$43.6 million for the three months ended June 30, 2017. The decrease in net interest income was primarily due to the 39 basis point increase in the cost of interest-bearing liabilities to 1.50% for the three months ended June 30, 2018 from 1.11% for the comparable prior year period, partially offset by an increase of 16 basis points in the yield of interest-earning assets to 4.10% for the three months ended June 30, 2018 as compared to 3.94% for the three months ended June 30, 2017. The effects of the above on both the net interest spread and net interest margin were decreases of 23 basis points to 2.60% and 19 basis points to 2.76%, respectively, for the quarter ended June 30, 2018, compared to the quarter ended June 30, 2017. Included in net interest income was prepayment penalty income from loans for the three months ended June 30, 2018 and 2017 totaling \$1.6 million and \$1.0 million, respectively, recovered interest from non-accrual loans totaling \$0.2 million and \$0.3 million, respectively, and accelerated accretion of discount upon the call of CLO securities totaling none and \$0.4 million, respectively. Without the prepayment penalty income, recovered interest and accelerated discount upon call, the net interest margin for the three months ended June 30, 2018 would have been 2.64%, a decrease of 19 basis points, as compared to 2.83% for the three months ended June 30, 2017.

**Provision for Loan Losses.** There was no provision for loan losses recorded for the three months ended June 30, 2018 and 2017. No provision was recorded due to the Company's analysis of the adequacy of the allowance for loan losses indicating that the reserve was at an appropriate level. During the three months ended June 30, 2018, the Bank recorded net charge-offs totaling \$0.3 million, while non-accrual loans decreased \$1.7 million to \$14.1 million at June 30, 2018 from \$15.7 million at December 31, 2017. The current average loan-to-value ratio for our non-performing loans collateralized by real estate was 35.1% at June 30, 2018. The Bank continues to maintain conservative underwriting standards. We anticipate that we will continue to see low loss content in our loan portfolio. See Note 5 of the Notes to the Consolidated Financial Statements "Loans" and "ALLOWANCE FOR LOAN LOSSES."

## PART I – FINANCIAL INFORMATION

### FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES

#### Management’s Discussion and Analysis of

#### Financial Condition and Results of Operations

**Non-Interest Income.** Non-interest income for the three months ended June 30, 2018 was \$3.2 million, an increase of \$1.2 million, or 62.6%, from \$1.9 million for the three months ended June 30, 2017. The increase in non-interest income was primarily due to a decline of \$0.9 million in net losses from fair value adjustments to \$0.3 million for the three months ended June 30, 2018 from \$1.2 million for the comparable prior year period and an increase in net gains from the sale of loans of \$0.4 million to \$0.4 million for the three months ended June 30, 2018 from \$34,000 for the comparable prior year period.

**Non-Interest Expense.** Non-interest expense was \$27.4 million for the three months ended June 30, 2018, an increase of \$1.3 million, or 5.1%, from \$26.1 million for the three months ended June 30, 2017. The increase in non-interest expense was primarily due increased legal consulting and depreciation expense due to the growth of the Bank.

**Income before Income Taxes.** Income before the provision for income taxes decreased \$1.1 million, or 5.6%, to \$18.4 million for the three months ended June 30, 2018 from \$19.5 million for the three months ended June 30, 2017, for the reasons discussed above.

**Provision for Income Taxes.** The provision for income taxes was \$4.5 million for the three months ended June 30, 2018, a decrease of \$2.3 million, or 33.7%, from \$6.8 million for the three months ended June 30, 2017. The effective tax rate decreased to 24.4% for the three months ended June 30, 2018 from 34.7% in the comparable prior year period primarily due to the impact of the top federal tax rate declining to 21% in 2018 from 35% in 2017, as a result of the Tax Cuts and Jobs Act (the “TCJA”).

## COMPARISON OF OPERATING RESULTS FOR THE SIX MONTHS ENDED

### JUNE 30, 2017 AND 2016

**General.** Net income for the six months ended June 30, 2018 was \$25.3 million, an increase of \$0.4 million, or 1.4%, compared to \$25.0 million for the six months ended June 30, 2017. Diluted earnings per common share were \$0.88 for the six months ended June 30, 2018, an increase of \$0.02, or 2.3%, from \$0.86 for the six months ended June 30, 2017.



Return on average equity was 9.5% for the six months ended June 30, 2018 and 2017. Return on average assets was 0.8% for the six months ended June 30, 2018 and 2017.

**Interest Income.** Total interest and dividend income increased \$8.5 million, or 7.4%, to \$124.1 million for the six months ended June 30, 2018 from \$115.6 million for the six months ended June 30, 2017. The increase in interest income was primarily attributable to an increase of \$243.7 million in the average balance of interest-earning assets to \$6,140.2 million for the six months ended June 30, 2018 from \$5,896.5 million for the comparable prior year period, combined with an increase of 12 basis points in the yield of interest-earning assets to 4.04% for the six months ended June 30, 2018. The increase in the yield on interest-earning assets was primarily due to a nine basis point increase in the yield of total loans, net to 4.26% for the six months ended June 30, 2018 from 4.17% for the six months ended June 30, 2017. The yield on interest-earning assets was also positively impacted by an increase of \$358.3 million in the average balance of total loans, net, which have a higher yield than the yield of total interest-earning assets, combined with a decrease of \$126.2 million in the average balance of total securities, which have a lower yield than the yield of total interest-earning assets. In addition, the yield of interest-earning assets improved due to increases of three basis points in the yield of total securities to 2.85% for the six months ended June 30, 2018 from 2.82% for the comparable prior year period and 70 basis points in the yield of interest-earning deposits and federal funds sold to 1.45% for the six months ended June 30, 2018 from 0.75% for the comparable prior year period. The nine basis point increase in the yield on the total loans, net was primarily due to new loans being originated at a higher rate than the average yield of the existing loan portfolio and adjustable rate loans repricing higher. Excluding prepayment penalty income and recovered interest from loans, the yield on total loans, net, would have increased nine basis points to 4.15% for the six months ended June 30, 2018 from 4.06% for the six months ended June 30, 2017.

**Interest Expense.** Interest expense increased \$10.3 million, or 35.9%, to \$38.8 million for the six months ended June 30, 2018 from \$28.6 million for the six months ended June 30, 2017. The increase in interest expense was primarily due to an increase of 34 basis points in the average cost of interest-bearing liabilities to 1.42% for the six months ended June 30, 2018 from 1.08% for the six months ended June 30, 2017, combined with an increase of \$208.0 million in the average balance of interest-bearing liabilities to \$5,479.3 million for the six months ended June 30, 2018 from \$5,271.3 million for the comparable prior year period. The 34 basis point increase in the cost of interest-bearing liabilities was primarily due to the Bank raising the rates we pay on some of our deposit products to stay competitive within our market and an increase in borrowing costs from recent increases in the Fed Funds rate.

## PART I – FINANCIAL INFORMATION

### FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES

#### Management’s Discussion and Analysis of

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**Net Interest Income.** For the six months ended June 30, 2018, net interest income was \$85.2 million, a decrease of \$1.8 million, or 2.0%, from \$87.0 million for the six months ended June 30, 2017. The decrease in net interest income was primarily due to the 34 basis point increase in the cost of interest-bearing liabilities to 1.42% for the six months ended June 30, 2018 from 1.08% for the comparable prior year period, partially offset by an increase of 12 basis points in the yield of interest-earning assets to 4.04% for the six months ended June 30, 2018 as compared to 3.92% for the six months ended June 30, 2017. The effects of the above on both the net interest spread and net interest margin were decreases of 22 basis points to 2.62% and 17 basis points to 2.78%, respectively, for the six months ended June 30, 2018, compared to the six months ended June 30, 2017. Included in net interest income was prepayment penalty income from loans and securities for the six months ended June 30, 2018 and 2017 totaling \$2.5 million and \$2.1 million, respectively, recovered interest from non-accrual loans totaling \$0.4 million and \$0.8 million, respectively, and accelerated accretion of discount upon the call of CLO securities totaling none and \$0.4 million respectively. Without the prepayment penalty income, recovered interest and accelerated discount upon call, the net interest margin for the six months ended June 30, 2018 would have been 2.67%, a decrease of 17 basis points, as compared to 2.84% for the six months ended June 30, 2017.

**Provision for Loan Losses.** During the six month ended June 30, 2018, a provision of \$0.2 million was recorded compared to no provision for loan losses recorded during the comparable prior year period. The \$0.2 million provision was recorded during the six months ended June 30, 2018 due to the quarterly analysis of the adequacy of the allowance for loan losses indicating that the provision was necessary to maintain the reserve at an appropriate level. During the six months ended June 30, 2018, the Bank recorded net charge-offs totaling \$0.3 million, while non-accrual loans decreased \$1.7 million to \$14.1 million at June 30, 2018 from \$15.7 million at December 31, 2017. The current average loan-to-value ratio for our non-performing loans collateralized by real estate was 35.1% at June 30, 2018. The Bank continues to maintain conservative underwriting standards. We anticipate that we will continue to see low loss content in our loan portfolio. See Note 5 of the Notes to the Consolidated Financial Statements “Loans” and “ALLOWANCE FOR LOAN LOSSES.”

**Non-Interest Income.** Non-interest income for the six months ended June 30, 2018 was \$6.4 million, an increase of \$0.7 million, or 13.0%, from \$5.6 million for the six months ended June 30, 2017. The increase in non-interest income was primarily due to a decline of \$1.2 million in net losses from fair value adjustments to \$0.4 million for the three months ended June 30, 2018 from \$1.5 million for the comparable prior year period, partially offset by a decrease of \$0.4 million in gains from life insurance claims to \$0.8 million for the six months ended June 30, 2018 from \$1.2 million for the comparable prior year period.

**Non-Interest Expense.** Non-interest expense was \$58.7 million for the six months ended June 30, 2018, an increase of \$3.1 million, or 5.5%, from \$55.6 million for the six months ended June 30, 2017. The increase in non-interest

expense was primarily due to increases in salaries and benefits, legal, consulting, depreciation, data processing and FDIC insurance premiums all due to the growth of the Bank.

***Income before Income Taxes.*** Income before the provision for income taxes decreased \$4.2 million, or 11.5%, to \$32.8 million for the six months ended June 30, 2018 from \$37.0 million for the six months ended June 30, 2017 for the reasons discussed above.

***Provision for Income Taxes.*** The provision for income taxes for the six months ended June 30, 2018 was \$7.4 million, a decrease of \$4.6 million, or 38.2%, from \$12.0 million for the comparable prior year period. The decrease was primarily due to a decrease in the effective tax rate to 22.7% for the six months ended June 30, 2018 from 32.5% in the comparable prior year period and the \$4.2 million decrease in income before income taxes. The decrease in the effective tax rate reflects the impact of the TCJA on the tax provision for the six months ended June 30, 2018.

## **FINANCIAL CONDITION**

***Assets.*** Total assets at June 30, 2018 were \$6,467.6 million, an increase of \$168.3 million, or 2.7%, from \$6,299.3 million at December 31, 2017. Total loans, net increased \$156.9 million, or 3.0%, during the six months ended June 30, 2018 to \$5,313.6 million from \$5,156.6 million at December 31, 2017. Loan originations and purchases were \$597.2 million for the six months ended June 30, 2018, an increase of \$69.5 million, or 13.2%, from \$527.7 million for the six months ended June 30, 2017. During the six months ended June 30, 2018, we continued to focus on the origination of multi-family residential, commercial real estate and commercial business loans with a full banking relationship. The loan pipeline totaled \$322.9 million at June 30, 2018 compared to \$359.8 million at December 31, 2017.

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The following table shows loan originations and purchases for the periods indicated:

| (In thousands)   | For the three months<br>ended June 30, |           | For the six months<br>ended June 30, |           |
|--|--|-----------|--------------------------------------|-----------|
|  | 2018                                   | 2017      | 2018                                 | 2017      |
| Multi-family residential <sup>(1)</sup>                | \$70,972                               | \$63,469  | \$152,153                            | \$190,177 |
| Commercial real estate <sup>(2)</sup>                  | 64,890                                 | 123,559   | 136,444                              | 159,291   |
| One-to-four family – mixed-use property <sup>(3)</sup> | 12,294                                 | 13,656    | 28,362                               | 32,198    |
| One-to-four family – residential <sup>(4)</sup>        | 6,974                                  | 4,860     | 23,942                               | 10,780    |
| Co-operative apartments                                | 1,500                                  | -         | 1,500                                | -         |
| Construction   | 9,940                                  | 4,429     | 24,619                               | 6,973     |
| Small Business Administration                          | 228                                    | 1,870     | 2,195                                | 2,511     |
| Commercial business and other <sup>(5)</sup>           | 88,612                                 | 49,312    | 228,019                              | 125,796   |
| Total  | \$255,410                              | \$261,155 | \$597,234                            | \$527,726 |

Includes purchases of \$0.8 million and \$15.8 million for the three months ended June 30, 2018 and 2017, (1) respectively. Includes purchases of \$14.1 million and \$22.5 million for the six months ended June 30, 2018 and 2017, respectively.

(2) Includes purchases of \$5.8 million for the three and six-month periods ended June 30, 2018 and \$25.9 million for the three and six-month periods ended June 30, 2017, respectively.

(3) Includes purchases of \$0.7 million for the three and six-month periods ended June 30, 2018, respectively.

(4) Includes purchases of \$0.9 million for six months ended June 30, 2018.

Includes purchases of \$34.0 million and \$1.1 million for the three months ended June 30, 2018 and 2017, (5) respectively. Includes purchases of \$88.7 million and \$10.0 million for the six months ended June 30, 2018 and 2017, respectively.

The Bank maintains its conservative underwriting standards that include, among other things, a loan-to-value ratio of 75% or less and a debt coverage ratio of at least 125%. Multi-family residential (excluding underlying co-operative mortgages), commercial real estate and one-to-four family mixed-use property mortgage loans originated and purchased during the three months ended June 30, 2018 had an average loan-to-value ratio of 46.3% and an average debt coverage ratio of 186%.

The Bank’s non-performing assets totaled \$14.8 million at June 30, 2018, a decrease of \$3.3 million, or 18.3%, from \$18.1 million at December 31, 2017. Total non-performing assets as a percentage of total assets were 0.23% at June 30, 2018 compared to 0.29% at December 31, 2017. The ratio of allowance for loan losses to total non-performing

loans was 136.72% at June 30, 2018 and 112.23% at December 31, 2017.

During the six months ended June 30, 2018, mortgage-backed securities including held-to-maturity increased \$4.2 million, or 0.8%, to \$521.8 million from \$517.6 million at December 31, 2017. The increase in mortgage-backed securities during the six months ended June 30, 2018 was primarily due to purchases of \$57.1 million at an average yield of 3.39%, partially offset by principal repayments of \$40.8 million and a decline in the fair value of \$11.3 million.

During the six months ended June 30, 2018, other securities, including held-to-maturity, decreased \$13.7 million, or 5.5%, to \$237.9 million from \$251.6 million at December 31, 2017. The decrease in other securities during the six months ended June 30, 2018 was primarily due to the call of one CLO security at par for \$10.0 million and a decline in fair value of \$3.0 million. At June 30, 2018, other securities primarily consist of securities issued by mutual or bond funds that invest in government and government agency securities, municipal bonds and corporate bonds.

**Liabilities.** Total liabilities were \$5,929.6 million at June 30, 2018, an increase of \$162.9 million, or 2.8%, from \$5,766.7 million at December 31, 2017. During the six months ended June 30, 2018, due to depositors increased \$218.2 million, or 5.0%, to \$4,558.9 million, due to increases of \$118.1 million in non-maturity deposits and \$100.1 million in certificates of deposit. The increase in non-maturity deposits was due to increases of \$89.9 million, \$89.5 million and \$3.2 million in money market, NOW and demand accounts, respectively, partially offset by a decrease of \$64.5 million savings accounts. Borrowed funds decreased \$58.9 million during the six months ended June 30, 2018. The decrease in borrowed funds was primarily due to a decrease in FHLB short-term borrowings as funding needs were provided by increased deposits.

**Equity.** Total stockholders' equity increased \$5.4 million, or 1.0%, to \$538.0 million at June 30, 2018 from \$532.6 million at December 31, 2017. Stockholders' equity increased primarily due to net income of \$25.3 million and the net impact of vesting and exercising of shares of employee and director stock plans totaling \$5.2 million. These increases were partially offset by the purchase of 445,444 treasury shares, at an average cost of \$26.58 per share, totaling \$11.8 million, the declaration and payment of dividends on the Company's common stock of \$0.40 per common share totaling \$11.5 million and a decrease of \$3.0 million in other comprehensive loss. Book value per common share was \$19.00 at June 30, 2018 compared to \$18.63 at December 31, 2017.

## **PART I – FINANCIAL INFORMATION**

### **FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES**

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**Cash flow.** During the six months ended June 30, 2018, funds provided by the Company's operating activities amounted to \$36.7 million. These funds, combined with \$139.1 million provided from financing activities and \$51.5 million available from the beginning of the period, were utilized to fund net investing activities of \$184.6 million. The Company's primary business objective is the origination and purchase of multi-family residential loans, commercial business loans and commercial real estate mortgage loans and to a lesser extent one-to-four family (including mixed-use properties) and SBA loans. During the six months ended June 30, 2018, the net total of loan originations and purchases less loan repayments and sales was \$181.4 million. During the six months ended June 30, 2018, the Company also funded \$57.3 million in purchases of securities available for sale and \$0.4 million of securities held-to-maturity. During the six months ended June 30, 2018, funds were provided by net increases in total deposits of \$226.1 million and short-term borrowed funds of \$73.5 million, as well as proceeds from new long-term borrowing of \$25.0 million. In addition to funding loan growth, these funds were used to repay \$160.1 million in long-term borrowings. The Company also used funds of \$13.9 million and \$11.6 million for purchases of treasury stock and dividend payments, respectively, during the six months ended June 30, 2018.

#### **INTEREST RATE RISK**

The Consolidated Statements of Financial Position have been prepared in accordance with generally accepted accounting principles in the United States of America, which require the measurement of financial position and operating results in terms of historical dollars without considering the changes in fair value of certain investments due to changes in interest rates. Generally, the fair value of financial investments such as loans and securities fluctuates inversely with changes in interest rates. As a result, increases in interest rates could result in decreases in the fair value of the Company’s interest-earning assets which could adversely affect the Company’s results of operations if such assets were sold, or, in the case of securities classified as available for sale, decreases in the Company’s stockholders’ equity, if such securities were retained.

The Company manages the mix of interest-earning assets and interest-bearing liabilities on a continuous basis to maximize return and adjust its exposure to interest rate risk. On a quarterly basis, management prepares the “Earnings and Economic Exposure to Changes in Interest Rate” report for review by the Asset Liability Committee of the Board of Directors, as summarized below. This report quantifies the potential changes in net interest income and net portfolio value should interest rates go up or down (shocked) 200 basis points, assuming the yield curves of the rate shocks will be parallel to each other. The Company’s regulators currently place focus on the net portfolio value, focusing on a rate shock up or down of 200 basis points. Net portfolio value is defined as the market value of assets net of the market value of liabilities. The market value of assets and liabilities is determined using a discounted cash flow calculation. The net portfolio value ratio is the ratio of the net portfolio value to the market value of assets. All changes in income and value are measured as percentage changes from the projected net interest income and net

portfolio value at the base interest rate scenario. The base interest rate scenario assumes interest rates at June 30, 2018. Various estimates regarding prepayment assumptions are made at each level of rate shock. However, prepayment penalty income is excluded from this analysis. Actual results could differ significantly from these estimates. At June 30, 2018, the Company was within the guidelines set forth by the Board of Directors for each interest rate level.

The following table presents the Company's interest rate shock as of June 30, 2018:

| Change in Interest Rate | Projected<br>Percentage<br>Change In |                           |                                    |
|-------------------------|--------------------------------------|---------------------------|------------------------------------|
|                         | Net<br>Interest<br>Income            | Net<br>Portfolio<br>Value | Net<br>Portfolio<br>Value<br>Ratio |
| -200 Basis points       | 4.90 %                               | 9.97 %                    | 13.41 %                            |
| -100 Basis points       | 3.17                                 | 3.81                      | 13.06                              |
| Base interest rate      | 0.00                                 | 0.00                      | 12.92                              |
| +100 Basis points       | -4.04                                | -4.87                     | 12.63                              |
| +200 Basis points       | -7.93                                | -9.44                     | 12.34                              |

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Management’s Discussion and Analysis of****Financial Condition and Results of Operations****AVERAGE BALANCES**

Net interest income represents the difference between income on interest-earning assets and expense on interest-bearing liabilities. Net interest income depends upon the relative amount of interest-earning assets and interest-bearing liabilities and the interest rate earned or paid on them. The following tables sets forth certain information relating to the Company’s Consolidated Statements of Financial Condition and Consolidated Statements of Income for the three and six months ended June 30, 2018 and 2017, and reflects the average yield on assets and average cost of liabilities for the periods indicated. Such yields and costs are derived by dividing income or expense by the average balance of assets or liabilities, respectively, for the periods shown. Average balances are derived from average daily balances. The yields include amortization of fees which are considered adjustments to yields.

|  | For the three months ended June 30, |          |                |                    |          |                |
|--|-------------------------------------|----------|----------------|--------------------|----------|----------------|
|  | 2018                                |          |                | 2017               |          |                |
|  | Average<br>Balance                  | Interest | Yield/<br>Cost | Average<br>Balance | Interest | Yield/<br>Cost |
| Assets   | (Dollars in thousands)              |          |                |                    |          |                |
| Interest-earning assets:                         |                                     |          |                |                    |          |                |
| Mortgage loans, net                              | \$4,509,778                         | 47,673   | 4.23 %         | \$4,297,697        | \$44,879 | 4.18 %         |
| Other loans, net                                 | 806,255                             | 9,649    | 4.79           | 665,037            | 6,752    | 4.06           |
| Total loans, net <sup>(1)</sup>                  | 5,316,033                           | 57,322   | 4.31           | 4,962,734          | 51,631   | 4.16           |
| Taxable securities:                              |                                     |          |                |                    |          |                |
| Mortgage-backed securities                       | 533,088                             | 3,754    | 2.82           | 532,938            | 3,418    | 2.57           |
| Other securities                                 | 122,601                             | 1,023    | 3.34           | 217,599            | 2,171    | 3.99           |
| Total taxable securities                         | 655,689                             | 4,777    | 2.91           | 750,537            | 5,589    | 2.98           |
| Tax-exempt securities: <sup>(2)</sup>            |                                     |          |                |                    |          |                |
| Other securities                                 | 124,058                             | 856      | 2.76           | 145,812            | 966      | 2.65           |
| Total tax-exempt securities                      | 124,058                             | 856      | 2.76           | 145,812            | 966      | 2.65           |
| Interest-earning deposits and federal funds sold | 85,406                              | 338      | 1.58           | 59,898             | 129      | 0.86           |
| Total interest-earning assets                    | 6,181,186                           | 63,293   | 4.10           | 5,918,981          | 58,315   | 3.94           |
| Other assets                                     | 303,696                             |          |                | 299,091            |          |                |
| Total assets                                     | \$6,484,882                         |          |                | \$6,218,072        |          |                |
| Liabilities and Equity                           |                                     |          |                |                    |          |                |
| Interest-bearing liabilities:                    |                                     |          |                |                    |          |                |
| Deposits:  |                                     |          |                |                    |          |                |
| Savings accounts                                 | \$235,564                           | 285      | 0.48           | \$279,723          | 399      | 0.57           |



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|   |             |          |       |             |          |       |
|---|-------------|----------|-------|-------------|----------|-------|
| NOW accounts  | 1,444,889   | 3,364    | 0.93  | 1,517,726   | 2,331    | 0.61  |
| Money market accounts   | 1,110,690   | 3,983    | 1.43  | 858,066     | 1,651    | 0.77  |
| Certificate of deposit accounts                                     | 1,519,348   | 7,118    | 1.87  | 1,410,295   | 5,099    | 1.45  |
| Total due to depositors   | 4,310,491   | 14,750   | 1.37  | 4,065,810   | 9,480    | 0.93  |
| Mortgagors' escrow accounts   | 77,343      | 38       | 0.20  | 73,838      | 30       | 0.16  |
| Total deposits  | 4,387,834   | 14,788   | 1.35  | 4,139,648   | 9,510    | 0.92  |
| Borrowed funds  | 1,127,746   | 5,865    | 2.08  | 1,148,072   | 5,188    | 1.81  |
| Total interest-bearing liabilities                                  | 5,515,580   | 20,653   | 1.50  | 5,287,720   | 14,698   | 1.11  |
| Non interest-bearing deposits                                       | 370,790     |          |       | 336,036     |          |       |
| Other liabilities   | 66,485      |          |       | 64,865      |          |       |
| Total liabilities   | 5,952,855   |          |       | 5,688,621   |          |       |
| Equity  | 532,027     |          |       | 529,451     |          |       |
| Total liabilities and equity  | \$6,484,882 |          |       | \$6,218,072 |          |       |
| Net interest income /<br>net interest rate spread                   |             | \$42,640 | 2.60% |             | \$43,617 | 2.83% |
| Net interest-earning assets /<br>net interest margin                | \$665,606   |          | 2.76% | \$631,261   |          | 2.95% |
| Ratio of interest-earning assets to<br>interest-bearing liabilities |             |          | 1.12X |             |          | 1.12X |

Loan interest income includes loan fee income (which includes net amortization of deferred fees and costs, late (1) charges, and prepayment penalties) of approximately \$0.3 million for the three months ended June 30, 2018 and 2017.

(2) Interest income on tax-exempt securities does not include the tax benefit of the tax-exempt securities.

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|  | For the six months ended June 30, |          |                |             |          |                |
|--|-----------------------------------|----------|----------------|-------------|----------|----------------|
|  | 2018                              |          |                | 2017        |          |                |
|  | Average                           | Interest | Yield/<br>Cost | Average     | Interest | Yield/<br>Cost |
|  | Balance                           |          |                | Balance     |          |                |
|  | (Dollars in thousands)            |          |                |             |          |                |
| <b>Assets</b>                                    |                                   |          |                |             |          |                |
| Interest-earning assets:                         |                                   |          |                |             |          |                |
| Mortgage loans, net                              | \$4,476,509                       | 93,785   | 4.19%          | \$4,255,822 | \$89,308 | 4.20%          |
| Other loans, net                                 | 797,430                           | 18,554   | 4.65           | 659,830     | 13,208   | 4.00           |
| Total loans, net <sup>(1)</sup>                  | 5,273,939                         | 112,339  | 4.26           | 4,915,652   | 102,516  | 4.17           |
| Taxable securities:                              |                                   |          |                |             |          |                |
| Mortgage-backed securities                       | 528,922                           | 7,261    | 2.75           | 531,448     | 6,784    | 2.55           |
| Other securities                                 | 126,816                           | 2,144    | 3.38           | 228,412     | 4,053    | 3.55           |
| Total taxable securities                         | 655,738                           | 9,405    | 2.87           | 759,860     | 10,837   | 2.85           |
| Tax-exempt securities: <sup>(2)</sup>            |                                   |          |                |             |          |                |
| Other securities                                 | 124,091                           | 1,710    | 2.76           | 146,155     | 1,934    | 2.65           |
| Total tax-exempt securities                      | 124,091                           | 1,710    | 2.76           | 146,155     | 1,934    | 2.65           |
| Interest-earning deposits and federal funds sold |                                   |          |                |             |          |                |
|  | 86,405                            | 625      | 1.45           | 74,847      | 282      | 0.75           |
| Total interest-earning assets                    | 6,140,173                         | 124,079  | 4.04           | 5,896,514   | 115,569  | 3.92           |
| Other assets                                     | 304,191                           |          |                | 297,082     |          |                |
| Total assets                                     | \$6,444,364                       |          |                | \$6,193,596 |          |                |
| <b>Liabilities and Equity</b>                    |                                   |          |                |             |          |                |
| Interest-bearing liabilities:                    |                                   |          |                |             |          |                |
| Deposits:  |                                   |          |                |             |          |                |
| Savings accounts                                 | \$250,646                         | 674      | 0.54           | \$267,059   | 706      | 0.53           |
| NOW accounts                                     | 1,492,413                         | 6,512    | 0.87           | 1,542,857   | 4,538    | 0.59           |
| Money market accounts                            | 1,068,443                         | 7,058    | 1.32           | 859,415     | 3,150    | 0.73           |
| Certificate of deposit accounts                  | 1,432,342                         | 12,581   | 1.76           | 1,407,528   | 10,039   | 1.43           |
| Total due to depositors                          | 4,243,844                         | 26,825   | 1.26           | 4,076,859   | 18,433   | 0.90           |
| Mortgagors' escrow accounts                      | 68,202                            | 73       | 0.21           | 64,280      | 57       | 0.18           |
| Total deposits                                   | 4,312,046                         | 26,898   | 1.25           | 4,141,139   | 18,490   | 0.89           |
| Borrowed funds                                   | 1,167,222                         | 11,932   | 2.04           | 1,130,132   | 10,073   | 1.78           |
| Total interest-bearing liabilities               | 5,479,268                         | 38,830   | 1.42           | 5,271,271   | 28,563   | 1.08           |
| Non interest-bearing deposits                    |                                   |          |                |             |          |                |
|  | 367,903                           |          |                | 333,142     |          |                |
| Other liabilities                                |                                   |          |                |             |          |                |
|  | 66,531                            |          |                | 65,525      |          |                |
| Total liabilities                                | 5,913,702                         |          |                | 5,669,938   |          |                |
| Equity   |                                   |          |                |             |          |                |
|  | 530,662                           |          |                | 523,658     |          |                |
| Total liabilities and equity                     | \$6,444,364                       |          |                | \$6,193,596 |          |                |

Net interest income /

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|   |           |       |           |       |
|---|-----------|-------|-----------|-------|
| net interest rate spread  | \$85,249  | 2.62% | \$87,006  | 2.84% |
| Net interest-earning assets /<br>net interest margin                | \$660,905 | 2.78% | \$625,243 | 2.95% |
| Ratio of interest-earning assets to<br>interest-bearing liabilities |           | 1.12X |           | 1.12X |

Loan interest income includes loan fee income (which includes net amortization of deferred fees and costs, late (1) charges, and prepayment penalties) of approximately \$0.4 million and \$1.0 million for the six months ended June 30, 2018 and 2017, respectively.

(2) Interest income on tax-exempt securities does not include the tax benefit of the tax-exempt securities.

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**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Management’s Discussion and Analysis of****Financial Condition and Results of Operations****LOANS**

The following table sets forth the Company’s loan originations (including the net effect of refinancing) and the changes in the Company’s portfolio of loans, including purchases, sales and principal reductions for the periods indicated.

| (In thousands)                          | For the six months ended |             |
|---|--------------------------|-------------|
|   | June 30,<br>2018         | 2017        |
| Mortgage Loans                          |                          |             |
| At beginning of period                  | \$4,401,950              | \$4,187,818 |
| Mortgage loans originated:              |                          |             |
| Multi-family residential                | 138,064                  | 167,647     |
| Commercial real estate                  | 130,644                  | 133,364     |
| One-to-four family – mixed-use property | 27,677                   | 32,198      |
| One-to-four family – residential        | 23,067                   | 10,780      |
| Co-operative apartments                 | 1,500                    | -           |
| Construction                            | 24,619                   | 6,973       |
| Total mortgage loans originated         | 345,571                  | 350,962     |
| Mortgage loans purchased:               |                          |             |
| Multi-family residential                | 14,089                   | 22,530      |
| Commercial real estate                  | 5,800                    | 25,927      |
| One-to-four family – mixed-use property | 685                      | -           |
| One-to-four family – residential        | 875                      | -           |
| Total mortgage loans purchased          | 21,449                   | 48,457      |
| Less:                                   |                          |             |
| Principal and other reductions          | 249,996                  | 184,858     |
| Loans transferred to held for sale      | -                        | 30,565      |
| Loans transferred to OREO               | 638                      | -           |
| Sales                                   | 4,710                    | 16,508      |
| At end of period                        | \$4,513,626              | \$4,355,306 |

## Non-Mortgage Loans

|                                |           |           |
|--------------------------------|-----------|-----------|
| At beginning of period         | \$758,286 | \$631,316 |
| Other loans originated:        |           |           |
| Small Business Administration  | 2,195     | 2,511     |
| Commercial business            | 138,229   | 114,628   |
| Other                          | 1,099     | 1,194     |
| Total other loans originated   | 141,523   | 118,333   |
| Other loans purchased:         |           |           |
| Commercial business            | 88,691    | 9,974     |
| Total other loans purchased    | 88,691    | 9,974     |
| Less:                          |           |           |
| Principal and other reductions | 178,640   | 81,764    |
| Sales                          | 5,266     | 4,703     |
| Other                          | 60        | -         |
| At end of period               | \$804,534 | \$673,156 |

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**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Management’s Discussion and Analysis of****Financial Condition and Results of Operations****TROUBLED DEBT RESTRUCUTURED (“TDR”) AND NON-PERFORMING ASSETS**

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

| (In thousands)                              | June 30,<br>2018 | March<br>31,<br>2018 | December<br>31,<br>2017 |
|---|------------------|----------------------|-------------------------|
| Accrual Status:                             |                  |                      |                         |
| Multi-family residential                    | \$2,488          | \$2,503              | \$2,518                 |
| Commercial real estate                      | -                | -                    | 1,986                   |
| One-to-four family - mixed-use property     | 1,726            | 1,740                | 1,753                   |
| One-to-four family - residential            | 562              | 567                  | 572                     |
| Commercial business and other               | 351              | 407                  | 462                     |
| Total                                       | 5,127            | 5,217                | 7,291                   |
| Non-Accrual Status:                         |                  |                      |                         |
| Taxi medallion                              | 5,482            | 5,712                | 5,916                   |
| Total                                       | 5,482            | 5,712                | 5,916                   |
| Total performing troubled debt restructured | \$10,609         | \$10,929             | \$13,207                |



**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Management’s Discussion and Analysis of****Financial Condition and Results of Operations**

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

| (In thousands)  | June 30,<br>2018 | March 31,<br>2018 | December<br>31,<br>2017 |
|---|------------------|-------------------|-------------------------|
| Loans 90 days or more past due<br>and still accruing: |                  |                   |                         |
| Commercial real estate                                | \$-              | \$1,668           | \$2,424                 |
| Construction  | 730              | -                 | -                       |
| Total   | 730              | 1,668             | 2,424                   |
| Non-accrual loans:                                    |                  |                   |                         |
| Multi-family residential                              | 2,165            | 2,193             | 3,598                   |
| Commercial real estate                                | 1,448            | 1,894             | 1,473                   |
| One-to-four family - mixed-use property               | 2,157            | 2,396             | 1,867                   |
| One-to-four family - residential                      | 6,969            | 7,542             | 7,808                   |
| Co-operative apartments                               | 575              | -                 | -                       |
| Small business administration                         | -                | 41                | 46                      |
| Taxi medallion  | 743              | 906               | 918                     |
| Commercial business and other                         | 2                | -                 | -                       |
| Total   | 14,059           | 14,972            | 15,710                  |
| Total non-performing loans                            | 14,789           | 16,640            | 18,134                  |
| Other non-performing assets:                          |                  |                   |                         |
| Real estate acquired through foreclosure              | -                | 638               | -                       |
| Other assets acquired through foreclosure             | 35               | 106               | -                       |
| Total   | 35               | 744               | -                       |
| Total non-performing assets                           | \$14,824         | \$17,384          | \$18,134                |
| Non-performing assets to total assets                 | 0.23 %           | 0.27 %            | 0.29 %                  |
| Allowance for loan losses to non-performing loans     | 136.72 %         | 123.45 %          | 112.23 %                |

Included in loans over 90 days past due and still accruing were one loan for \$0.7 million, two loans totaling \$1.7 million and three loans totaling \$2.4 million at June 30, 2018, March 31, 2018 and December 31, 2017, respectively, which are past their respective maturity dates and are still remitting payments. The Bank actively works with borrowers to extend the loans maturity or have the loan repaid when loans go past their contractual maturity date.



Included in non-performing loans was one multi-family loan totaling \$0.4 million at June 30, 2018, March 31, 2018 and December 31, 2017 which was restructured as TDR and not performing in accordance with its restructured terms.

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## **PART I – FINANCIAL INFORMATION**

### **FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES**

#### **Management’s Discussion and Analysis of**

#### **Financial Condition and Results of Operations**

### **CRITICIZED AND CLASSIFIED ASSETS**

Our policy is to review our assets, focusing primarily on the loan portfolio, OREO and the investment portfolios, to ensure that credit quality is maintained at the highest levels. See Note 5 of the Notes to the Consolidated Financial Statements “Loans” for a description of how loans are determined to be criticized or classified and a table displaying criticized and classified loans at June 30, 2018 and December 31, 2017. The Company had classified other assets acquired through foreclosure totaling \$35,000 at June 30, 2018 and none at December 31, 2017. The Company did not hold any criticized or classified investment securities at June 30, 2018 and December 31, 2017. Our total Criticized and Classified assets were \$65.9 million at June 30, 2018, an increase of \$3.3 million from \$62.7 million at December 31, 2017.

On a quarterly basis, all collateral dependent loans that are classified as Substandard or Doubtful are internally reviewed for impairment, based on updated cash flows for income producing properties, or updated independent appraisals. The loan balances of collateral dependent loans reviewed for impairment are then compared to the loans updated fair value. We consider fair value of collateral dependent loans to be 85% of the appraised or internally estimated value of the property, except for taxi medallion loans. The fair value of the underlying collateral of taxi medallion loans is the value of the underlying medallion based upon the most recently reported arm’s length transaction. When there is no recent sale activity, the fair value is calculated using the income approach. All taxi medallion loans are classified impaired. For collateral dependent mortgage loans and taxi medallion loans, the portion of the loan balance which exceeds fair value is generally charged-off. At June 30, 2018, the current average loan-to-value ratio on our collateral dependent loans reviewed for impairment was 46.5%.

### **ALLOWANCE FOR LOAN LOSSES**

The ALL represents the expense charged to earnings based upon management’s quarterly analysis of credit risk. The amount of the ALL is based upon multiple factors that reflect management’s assessment of the credit quality of the loan portfolio. The factors are both quantitative and qualitative in nature including, but not limited to, historical losses, economic conditions, trends in delinquencies, value and adequacy of underlying collateral, volume and portfolio mix, and internal loan processes.

Management has developed a comprehensive analytical process to monitor the adequacy of the ALL. The process and guidelines were developed using, among other factors, the guidance from federal banking regulatory agencies and GAAP. The results of this process, along with the conclusions of our independent loan review officer, support management's assessment as to the adequacy of the ALL at each balance sheet date. See Note 5 of the Notes to the Consolidated Financial Statements "Loans" for a detailed explanation of management's methodology and policy.

As a component of the credit risk assessment, the Bank has established an Asset Classification Committee which carefully evaluates loans which are past due 90 days and/or are classified. The Asset Classification Committee thoroughly assesses the condition and circumstances surrounding each loan meeting the criteria. The Bank also has a Delinquency Committee that evaluates loans meeting specific criteria. The Bank's loan policy requires loans to be placed into non-accrual status once the loan becomes 90 days delinquent unless there is, in our opinion, compelling evidence the borrower will bring the loan current in the immediate future.

During the three months ended June 30, 2018, the portion of the ALL related to the loss history declined, while the qualitative factors increased slightly, primarily due to growth in the loan portfolio. Charge-offs recorded in the past twelve quarters were minimal, with the exception of taxi medallion charge-offs recorded in the fourth quarter of 2017, as credit conditions remained stable. The percentage of loans originated prior to 2009, compared to the total loan portfolio, decreased as scheduled amortization and repayments occurred. As disclosed in Note 5 of the Notes to the Consolidated Financial Statements "Loans", the loans originated prior to 2009 have a higher delinquency and loss rate. The impact from the above resulted in the ALL totaling \$20.2 million, a decrease of \$0.1 million, or 0.6%, from December 31, 2017. Based upon management consistently applying the ALL methodology and review of the loan portfolio, management concluded a charge to earnings to increase the ALL was not warranted. The ALL at June 30, 2018 and December 31, 2017, represented 0.38% and 0.39% of gross loans outstanding, respectively. The ALL represented 136.7% of non-performing loans at June 30, 2018 compared to 112.2% at December 31, 2017.

Management recommends to the Board of Directors the amount of the ALL quarterly. The Board of Directors approves the ALL.

**PART I – FINANCIAL INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****Management’s Discussion and Analysis of****Financial Condition and Results of Operations**

The following table sets forth the activity in the Company's allowance for loan losses for the periods indicated:

| (Dollars in thousands)   | At or for the six<br>months ended June<br>30, |          |
|--|---|----------|
|  | 2018  | 2017     |
| Balance at beginning of period   | \$20,351                                      | \$22,229 |
| Provision for loan losses  | 153   | -        |
| Loans charged-off:   |   |          |
| Multi-family residential   | (81 )   | (162 )   |
| Commercial real estate   | -   | (4 )     |
| One-to-four family – mixed-use property  | -   | (35 )    |
| One-to-four family – residential   | (1 )  | (170 )   |
| Small Business Administration  | (52 )   | (89 )    |
| Taxi medallion   | (353 )  | (54 )    |
| Commercial business and other  | (14 )   | (15 )    |
| Total loans charged-off  | (501 )  | (529 )   |
| Recoveries:  |   |          |
| Multi-family residential   | 2   | 231      |
| Commercial real estate   | -   | 68       |
| One-to-four family – mixed-use property  | 79  | 68       |
| One-to-four family – residential   | 112   | -        |
| Small Business Administration  | 15  | 49       |
| Commercial business and other  | 9   | 41       |
| Total recoveries   | 217   | 457      |
| Net charge-offs  | (284 )  | (72 )    |
| Balance at end of period   | \$20,220                                      | \$22,157 |
| Ratio of net charge-offs during the period to<br>average loans outstanding during the period | 0.01 %  | - %      |
| Ratio of allowance for loan losses to gross loans at end of period                           | 0.38 %  | 0.44 %   |
| Ratio of allowance for loan losses to non-performing<br>assets at end of period              | 136.40 %                                      | 143.33 % |

Ratio of allowance for loan losses to non-performing  
loans at end of period

136.72% 143.33%

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**PART I – FINANCIAL INFORMATION**

**FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES**

**ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

For a discussion of the qualitative and quantitative disclosures about market risk, see the information under the caption "Management's Discussion and Analysis of Financial Condition and Results of Operations - Interest Rate Risk."

**ITEM 4. CONTROLS AND PROCEDURES**

The Company carried out, under the supervision and with the participation of the Company's management, including its Chief Executive Officer and Chief Financial Officer, an evaluation of the effectiveness of the design and operation of the Company's disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934) as of the end of the period covered by this Quarterly Report. Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that, as of June 30, 2018, the design and operation of these disclosure controls and procedures were effective. During the period covered by this Quarterly Report, there have been no changes in the Company's internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

**PART II – OTHER INFORMATION****FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES****ITEM 1. LEGAL PROCEEDINGS**

The Company is a defendant in various lawsuits. Management of the Company, after consultation with outside legal counsel, believes that the resolution of these various matters will not result in any material adverse effect on the Company's consolidated financial condition, results of operations and cash flows.

**ITEM 1A. RISK FACTORS**

There have been no material changes from the risk factors disclosed in the Company's Annual Report on Form 10-K for the year ended December 31, 2017.

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

The following table sets forth information regarding the shares of common stock repurchased by the Company during the three months ended June 30, 2018:

| Period                    | Total<br>Number<br>of Shares<br>Purchased | Average<br>Price<br>Paid per<br>Share | Total<br>Number of<br>Shares<br>Purchased<br>as Part of<br>Publicly<br>Announced<br>or<br>Programs | Maximum<br>Number of<br>Shares That<br>May<br>Yet Be<br>Purchased<br>Under the<br>Plans<br>or<br>Programs |
|---------------------------|---|---------------------------------------|--|---|
| April 1 to April 30, 2018 | 24,422                                    | \$26.28                               | 24,422   | 1,011,995   |
| May 1 to May 31, 2018     | 193,348                                   | 25.97                                 | 193,348  | 818,647   |
| June 1 to June 30, 2018   | 9,811                                     | 26.75                                 | 9,811  | 808,836   |
| Total                     | 227,581                                   | 26.04                                 | 227,581  |   |

During the quarter ended June 30, 2018, the Company repurchased 227,581 shares of the Company's common stock at an average cost of \$26.04 per share. On June 30, 2018, 808,836 shares may still be repurchased under the currently authorized stock repurchase program. Stock will be purchased under the current stock repurchase programs from time to time, in the open market or through private transactions, subject to market conditions. There is no expiration or maximum dollar amount under these authorizations.

**ITEM 3. DEFAULTS UPON SENIOR SECURITIES**

None.

**ITEM 4. MINE SAFETY DISCLOSURES**

Not applicable.

**ITEM 5. OTHER INFORMATION**

None.





**PART II – OTHER INFORMATION**

**FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES**

**ITEM 6. EXHIBITS**

| Exhibit No. | Description   |
|-------------|---|
| 3.1 P       | Certificate of Incorporation of Flushing Financial Corporation (1)  |
| <u>3.2</u>  | <u>Certificate of Amendment to Certificate of Incorporation of Flushing Financial Corporation (3)</u>   |
| <u>3.3</u>  | <u>Certificate of Amendment to Certificate of Incorporation of Flushing Financial Corporation (5)</u>   |
| <u>3.4</u>  | <u>Certificate of Designations of Series A Junior Participating Preferred Stock of Flushing Financial Corporation (4)</u>   |
| <u>3.5</u>  | <u>Certificate of Increase of Shares Designated as Series A Junior Participating Preferred Stock of Flushing Financial Corporation (2)</u>  |
| <u>3.6</u>  | <u>Amended and Restated By-Laws of Flushing Financial Corporation (6)</u>   |
| 4.1         | Flushing Financial Corporation has outstanding certain long-term debt. None of such debt exceeds ten percent of Flushing Financial Corporation's total assets; therefore, copies of constituent instruments defining the rights of the holders of such debt are not included as exhibits. Copies of instruments with respect to such long-term debt will be furnished to the Securities and Exchange Commission upon request. |
| <u>31.1</u> | <u>Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 by the Chief Executive Officer (filed herewith)</u>  |
| <u>31.2</u> | <u>Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 by the Chief Financial Officer (filed herewith)</u>  |
| <u>32.1</u> | <u>Certification Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes Oxley Act of 2002 by the Chief Executive Officer (furnished herewith)</u>   |
| <u>32.2</u> | <u>Certification Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes Oxley Act of 2002 by the Chief Financial Officer (furnished herewith)</u>   |
| 101.INS     | XBRL Instance Document (filed herewith)   |
| 101.SCH     | XBRL Taxonomy Extension Schema Document (filed herewith)  |
| 101.CAL     | XBRL Taxonomy Extension Calculation Linkbase Document (filed herewith)  |
| 101.DEF     | XBRL Taxonomy Extension Definition Linkbase Document (filed herewith)   |
| 101.LAB     | XBRL Taxonomy Extension Label Linkbase Document (filed herewith)  |
| 101.PRE     | XBRL Taxonomy Extension Presentation Linkbase Document (filed herewith)   |
| (1)         | Incorporated by reference to Exhibits filed with the Registration Statement on Form S-1 filed September 1, 1995, Registration No. 33-96488. (P: Indicates a filing submitted in paper)  |
| (2)         | Incorporated by reference to Exhibit filed with Form 8-K filed September 27, 2006.  |
| (3)         | Incorporated by reference to Exhibits filed with Form S-8 filed May 31, 2002.   |
| (4)         | Incorporated by reference to Exhibits filed with Form 10-Q for the quarter ended September 30, 2002.  |
| (5)         | Incorporated by reference to Exhibit filed with Form 10-K for the year ended December 31, 2011.   |
| (6)         | Incorporated by reference to Exhibit filed with Form 10-Q for the quarter ended June 30, 2014.  |



**FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES**

**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.

Flushing Financial Corporation,

Dated: August 7, 2018 By: /s/John R. Buran  
John R. Buran  
President and Chief Executive Officer

Dated: August 7, 2018 By: /s/Susan K. Cullen  
Susan K. Cullen  
Senior Executive Vice President, Treasurer and  
Chief Financial Officer

**FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES**

**EXHIBIT INDEX**

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