

LAKELAND BANCORP INC  
Form 10-K  
March 15, 2016  
Table of Contents

**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, DC 20549

**FORM 10-K**

(Mark One)

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

**FOR THE FISCAL YEAR ENDED DECEMBER 31, 2015.**

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

**FOR THE TRANSITION PERIOD FROM \_\_\_\_\_ TO \_\_\_\_\_.**

**Commission file number: 000-17820**

**LAKELAND BANCORP, INC.**

(Exact name of registrant as specified in its charter)

Edgar Filing: LAKELAND BANCORP INC - Form 10-K

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

**22-2953275**  
(I.R.S. Employer  
Identification No.)

**250 Oak Ridge Road,**  
**Oak Ridge, New Jersey**  
(Address of principal executive offices)

**07438**  
(Zip code)

**Registrant's telephone number, including area code: (973) 697-2000**

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

<b>Title of each class</b>	<b>Name of each exchange on which registered</b>
<b>Common Stock, no par value</b>	<b>NASDAQ</b>

**Securities registered pursuant to Section 12(g) of the Act: None**

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act. Yes  No

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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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	<input type="checkbox"/>	Accelerated filer	<input checked="" type="checkbox"/>
Non-accelerated filer	<input type="checkbox"/>	Smaller Reporting Company	<input type="checkbox"/>

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

As of June 30, 2015, the aggregate market value of the registrant's common stock held by non-affiliates of the registrant was approximately \$417,000,000, based on the closing sale price as reported on the NASDAQ Global Select Market.

Edgar Filing: LAKELAND BANCORP INC - Form 10-K

The number of shares outstanding of the registrant's common stock, as of March 1, 2016, was 41,234,664.

**DOCUMENTS INCORPORATED BY REFERENCE:**

Lakeland Bancorp, Inc.'s Proxy Statement for its 2016 Annual Meeting of Shareholders (Part III).

**Table of Contents**

**LAKELAND BANCORP, INC.**

Form 10-K Index

PART I

	PAGE
Item 1. <u>Business</u>	1
Item 1A. <u>Risk Factors</u>	14
Item 1B. <u>Unresolved Staff Comments</u>	20
Item 2. <u>Properties</u>	20
Item 3. <u>Legal Proceedings</u>	21
Item 3A. <u>Executive Officers of the Registrant</u>	21
Item 4. <u>Mine Safety Disclosures</u>	22

PART II

Item 5. <u>Market for the Registrant's Common Equity, Related Stockholder Matters and Issuer</u>	
	23
Item 6. <u>Purchases of Equity Securities</u>	25
Item 7. <u>Selected Financial Data</u>	27
Item 7A. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	53
Item 8. <u>Quantitative and Qualitative Disclosures About Market Risk</u>	54
Item 9. <u>Financial Statements and Supplementary Data</u>	108
Item 9A. <u>Changes in and Disagreements with Accountants on Accounting and Financial Disclosure</u>	108
Item 9B. <u>Controls and Procedures</u>	111
Item 9B. <u>Other Information</u>	111

PART III

Item 10. <u>Directors, Executive Officers and Corporate Governance</u>	111
Item 11. <u>Executive Compensation</u>	111
Item 12. <u>Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters</u>	111
Item 13. <u>Certain Relationships and Related Transactions, and Director Independence</u>	111
Item 14. <u>Principal Accounting Fees and Services</u>	112

PART IV

Item 15. <u>Exhibits and Financial Statement Schedules</u>	112
<u>Signatures</u>	117

---

**Table of Contents**

**PART I**

**ITEM 1 - Business.**

**GENERAL**

Lakeland Bancorp, Inc. (the Company or Lakeland Bancorp ) is a bank holding company headquartered in Oak Ridge, New Jersey. The Company was organized in March of 1989 and commenced operations on May 19, 1989, upon the consummation of the acquisition of all of the outstanding stock of Lakeland Bank, formerly named Lakeland State Bank ( Lakeland or the Bank or Lakeland Bank ). Through Lakeland, the Company operates 53 banking offices, located in Bergen, Essex, Morris, Passaic, Somerset, Sussex, Union and Warren counties in New Jersey; five New Jersey regional commercial lending centers in Bernardsville, Montville, Newton, Teaneck and Wyckoff/Waldwick; and two commercial loan production offices serving Middlesex and Monmouth counties in New Jersey and the Hudson Valley region of New York. Lakeland offers an extensive suite of financial products and services for businesses and consumers.

The Company has shown substantial growth through a combination of organic growth and acquisitions. Since 1998, Lakeland has opened (including acquired branches) a net total of 32 branch offices, and currently maintains 53 branch offices. The Company has acquired six community banks with an aggregate asset total of approximately \$1.5 billion, including the acquisition of Pascack Community Bank and its parent, Pascack Bancorp, Inc. ( Pascack Bancorp ), which closed on January 7, 2016. All of the acquired banks have been merged into Lakeland and their holding companies, if applicable, have been merged into the Company.

Lakeland Bancorp, Lakeland Bank and Harmony Bank signed a merger agreement on February 17, 2016, pursuant to which Harmony Bank will be merged with and into Lakeland Bank, with Lakeland Bank as the surviving bank. The merger agreement provides that shareholders of Harmony Bank will receive 1.25 shares of Lakeland Bancorp common stock for each share of Harmony Bank common stock that they own at the effective time of the merger. Lakeland Bancorp expects to issue an aggregate of approximately 3.0 million shares of its common stock in the merger and will cash out Harmony Bank options that remain outstanding at the effective time of the merger. The closing of the merger is subject to receipt of approvals from regulators, approval of the merger by Harmony Bank s shareholders and other customary conditions. Harmony Bank, a New Jersey state-chartered commercial bank that focuses on serving consumers and small-to-medium-size businesses, is headquartered in Jackson, New Jersey, with additional branch offices in Lakewood and Toms River, New Jersey. As of December 31, 2015, Harmony Bank had total assets, total loans, total deposits and total stockholders equity of \$295 million, \$241 million, \$257 million and \$28 million, respectively.

At December 31, 2015, Lakeland Bancorp had total consolidated assets of \$3.9 billion, total consolidated deposits of \$3.0 billion, total consolidated loans, net of the allowance for loan and lease losses, of \$2.9 billion and total consolidated stockholders equity of \$400.5 million. Following the closing of Lakeland Bancorp s acquisition of Pascack Bancorp, Inc. and its subsidiary, Pascack Community Bank, on January 7, 2016, Lakeland Bancorp s total assets approximated \$4.3 billion.

This Annual Report on Form 10-K contains certain forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 ( Forward-Looking Statements ). Such statements are subject to risks and uncertainties that could cause actual results to differ materially from those projected in such Forward-Looking Statements. Certain factors which could materially affect such results and the future performance of the Company are described in Item 1A - Risk Factors of this Annual Report on Form 10-K.

Unless otherwise indicated, all weighted average, actual shares and per share information contained in this Annual Report on Form 10-K have been adjusted retroactively for the effect of stock dividends, including the Company s 5% stock dividend which was distributed on June 17, 2014.

## **Table of Contents**

### **Commercial Bank Services**

Through Lakeland, the Company offers a broad range of lending, depository, and related financial services to individuals and small to medium sized businesses located primarily in northern and central New Jersey, the Hudson Valley region in New York, and surrounding areas. In the lending area, these services include short and medium term loans, lines of credit, letters of credit, inventory and accounts receivable financing, real estate construction loans, mortgage loans and merchant credit card services. In addition to commercial real estate loans, Lakeland makes commercial and industrial loans. These types of loans can diversify the Company's exposure in a depressed real estate market. Lakeland's equipment financing division provides a solution to small and medium sized companies who prefer to lease equipment over other financial alternatives. Lakeland's asset based loan department provides commercial borrowers with another lending alternative.

Depository products include demand deposits, as well as savings, money market and time accounts. The Company also offers wire transfer, internet banking, mobile banking and night depository services to the business community and municipal relationships. In addition, Lakeland offers cash management services, such as remote capture of deposits and overnight sweep repurchase agreements.

### **Consumer Banking**

Lakeland also offers a broad range of consumer banking services, including checking accounts, savings accounts, NOW accounts, money market accounts, certificates of deposit, internet banking, secured and unsecured loans, consumer installment loans, mortgage loans, and safe deposit services.

As a result of the merger with Somerset Hills Bancorp in 2013, Lakeland expanded its mortgage division by acquiring a mortgage company subsidiary, which originates and sells residential mortgage loans, and a 50% interest in a title company.

### **Other Services**

Investment and advisory services for individuals and businesses are also available.

### **Competition**

Lakeland faces considerable competition in its market areas for deposits and loans from other depository institutions. Many of Lakeland's depository institution competitors have substantially greater resources, broader geographic markets, and higher lending limits than Lakeland and are also able to provide more services and make greater use of media advertising. In recent years, intense market demands, economic pressures, increased customer awareness of products and services, and the availability of electronic services have forced banking institutions to diversify their services and become more cost-effective.

Lakeland also competes with credit unions, brokerage firms, insurance companies, money market mutual funds, consumer finance companies, mortgage companies and other financial companies, some of which are not subject to the same degree of regulation and restrictions as Lakeland in attracting deposits and making loans. Interest rates on deposit accounts, convenience of facilities, products and services, and marketing are all significant factors in the competition for deposits. Competition for loans comes from other commercial banks, savings institutions, insurance companies, consumer finance companies, credit unions, mortgage banking firms and other institutional lenders. Lakeland primarily competes for loan originations through its structuring of loan transactions and the overall quality of service it provides. Competition is affected by the availability of lendable funds, general and local economic conditions, interest rates, and other factors that are not readily predictable.

The Company expects that competition will continue in the future.

---

## **Table of Contents**

### **Concentration**

The Company is not dependent for deposits or exposed by loan concentrations to a single customer or a small group of customers the loss of any one or more of which would have a material adverse effect upon the financial condition of the Company.

### **Employees**

At December 31, 2015, the Company had 551 full-time equivalent employees. None of these employees is covered by a collective bargaining agreement. The Company considers relations with its employees to be good.

## **SUPERVISION AND REGULATION**

### **General**

The Company is a registered bank holding company under the federal Bank Holding Company Act of 1956, as amended (the Holding Company Act ), and is required to file with the Federal Reserve Board an annual report and such additional information as the Federal Reserve Board may require pursuant to the Holding Company Act. The Company is subject to examination by the Federal Reserve Board.

Lakeland is a state chartered banking association subject to supervision and examination by the Department of Banking and Insurance of the State of New Jersey (the Department ) and the Federal Deposit Insurance Corporation (the FDIC ). The regulations of the State of New Jersey and FDIC govern most aspects of Lakeland s business, including reserves against deposits, loans, investments, mergers and acquisitions, borrowings, dividends, and location of branch offices. Lakeland is subject to certain restrictions imposed by law on, among other things, (i) the maximum amount of obligations of any one person or entity which may be outstanding at any one time, (ii) investments in stock or other securities of the Company or any subsidiary of the Company, and (iii) the taking of such stock or securities as collateral for loans to any borrower.

### **The Holding Company Act**

The Holding Company Act limits the activities which may be engaged in by the Company and its subsidiaries to those of banking, the ownership and acquisition of assets and securities of banking organizations, and the management of banking organizations, and to certain non-banking activities which the Federal Reserve Board finds, by order or regulation, to be so closely related to banking or managing or controlling a bank as to be a proper incident thereto. The Federal Reserve Board is empowered to differentiate between activities by a bank holding company or a subsidiary thereof and activities commenced by acquisition of a going concern.

With respect to non-banking activities, the Federal Reserve Board has by regulation determined that several non-banking activities are closely related to banking within the meaning of the Holding Company Act and thus may be performed by bank holding companies. Although the Company s management periodically reviews other avenues of business opportunities that are included in that regulation, the Company has no present plans to engage in any of these activities other than providing investment brokerage services.

With respect to the acquisition of banking organizations, the Company is required to obtain the prior approval of the Federal Reserve Board before it may, by merger, purchase or otherwise, directly or indirectly acquire all or substantially all of the assets of any bank or bank holding company, if, after such acquisition, it will own or control more than 5% of the voting shares of such bank or bank holding company.

### **Regulation of Bank Subsidiaries**

There are various legal limitations, including Sections 23A and 23B of the Federal Reserve Act, which govern the extent to which a bank subsidiary may finance or otherwise supply funds to its holding company or its

## **Table of Contents**

holding company's non-bank subsidiaries. Under federal law, no bank subsidiary may, subject to certain limited exceptions, make loans or extensions of credit to, or investments in the securities of, its parent or the non-bank subsidiaries of its parent (other than direct subsidiaries of such bank which are not financial subsidiaries) or take their securities as collateral for loans to any borrower. Each bank subsidiary is also subject to collateral security requirements for any loans or extensions of credit permitted by such exceptions.

### **Commitments to Affiliated Institutions**

The policy of the Federal Reserve Board provides that a bank holding company is expected to act as a source of financial strength to its subsidiary banks and to commit resources to support such subsidiary banks in circumstances in which it might not do so absent such policy.

### **Interstate Banking**

The Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994 permits bank holding companies to acquire banks in states other than their home state, regardless of applicable state law. New Jersey enacted legislation to authorize interstate banking and branching and the entry into New Jersey of foreign country banks. New Jersey did not authorize de novo branching into the state. However, under federal law, federal savings banks, which meet certain conditions, may branch de novo into a state, regardless of state law. The Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act) removes the restrictions on interstate branching contained in the Riegle-Neal Act, and allows national banks and state banks to establish branches in any state if, under the laws of the state in which the branch is to be located, a state bank chartered by that state would be permitted to establish the branch.

### **Gramm-Leach-Bliley Act of 1999**

The Gramm-Leach-Bliley Financial Services Modernization Act of 1999 (the Modernization Act) became effective in early 2000. The Modernization Act:

allows bank holding companies meeting management, capital, and Community Reinvestment Act standards to engage in a substantially broader range of non-banking activities than previously was permissible, including insurance underwriting and making merchant banking investments in commercial and financial companies; if a bank holding company elects to become a financial holding company, it files a certification, effective in 30 days, and thereafter may engage in certain financial activities without further approvals (Lakeland Bancorp is such a financial holding company);

allows insurers and other financial services companies to acquire banks;

removes various restrictions that previously applied to bank holding company ownership of securities firms and mutual fund advisory companies; and

establishes the overall regulatory structure applicable to bank holding companies that also engage in insurance and securities operations.

The Modernization Act also modified other financial laws, including laws related to financial privacy and community reinvestment.

### **The USA PATRIOT Act**

As part of the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001, Congress adopted the International Money Laundering Abatement and Financial Anti-Terrorism Act of 2001 (collectively, the USA PATRIOT Act). By way of amendments to the Bank Secrecy Act, Title III of the USA PATRIOT Act encourages information sharing among bank regulatory agencies and law enforcement bodies. Further, certain provisions of Title III impose affirmative obligations on a





## **Table of Contents**

broad range of financial institutions, including banks, thrifts, brokers, dealers, credit unions, money transfer agents and parties registered under the Commodity Exchange Act.

Among other requirements, Title III of the USA PATRIOT Act imposes the following requirements with respect to financial institutions:

All financial institutions must establish anti-money laundering programs that include, at a minimum: (i) internal policies, procedures, and controls; (ii) specific designation of an anti-money laundering compliance officer; (iii) ongoing employee training programs; and (iv) an independent audit function to test the anti-money laundering program.

The Secretary of the Department of the Treasury, in conjunction with other bank regulators, was authorized to issue regulations that provide for minimum standards with respect to customer identification at the time new accounts are opened.

Financial institutions that establish, maintain, administer, or manage private banking accounts or correspondent accounts in the United States for non-United States persons or their representatives (including foreign individuals visiting the United States) are required to establish appropriate, specific and, where necessary, enhanced due diligence policies, procedures, and controls designed to detect and report money laundering.

Financial institutions are prohibited from establishing, maintaining, administering or managing correspondent accounts for foreign shell banks (foreign banks that do not have a physical presence in any country), and will be subject to certain record keeping obligations with respect to correspondent accounts of foreign banks.

Bank regulators are directed to consider a holding company's effectiveness in combating money laundering when ruling on Federal Reserve Act and Bank Merger Act applications.

The United States Treasury Department has issued a number of implementing regulations which address various requirements of the USA PATRIOT Act and are applicable to financial institutions such as Lakeland. These regulations impose obligations on financial institutions to maintain appropriate policies, procedures and controls to detect, prevent and report money laundering and terrorist financing and to verify the identity of their customers. Banking agencies have strictly enforced various anti-money laundering and suspicious activity reporting requirements using formal and informal enforcement tools to cause banks to comply with these provisions.

## **Sarbanes-Oxley Act of 2002**

The Sarbanes-Oxley Act of 2002 (the SOA) added new legal requirements for public companies affecting corporate governance, accounting and corporate reporting, to increase corporate responsibility and to protect investors.

The SOA addresses, among other matters:

audit committees for all reporting companies;

certification of financial statements by the chief executive officer and the chief financial officer;

the forfeiture of bonuses or other incentive-based compensation and profits from the sale of an issuer's securities by directors and senior officers in the twelve month period following initial publication of any financial statements that later require restatement;

Edgar Filing: LAKELAND BANCORP INC - Form 10-K

a prohibition on insider trading during pension plan black out periods;

disclosure of off-balance sheet transactions;

-5-

**Table of Contents**

a prohibition on personal loans to directors and officers (other than loans made by an insured depository institution (as defined in the Federal Deposit Insurance Act), if the loan is subject to the insider lending restrictions of Section 22(h) of the Federal Reserve Act);

expedited filing requirements for Form 405;

disclosure of a code of ethics and filing a Form 8-K for a change or waiver of such code;

real time filing of periodic reports;

the formation of a public accounting oversight board;

auditor independence; and

various increased criminal penalties for violations of the securities laws.

The Securities and Exchange Commission (the SEC) has enacted various rules to implement various provisions of the SOA with respect to, among other matters, disclosure in periodic filings pursuant to the Exchange Act. Each of the national stock exchanges, including the NASDAQ Stock Market where Lakeland Bancorp's common stock is listed, have corporate governance listing standards, including rules strengthening director independence requirements for boards, and requiring the adopting of charters for the nominating, corporate governance and audit committees.

**Regulation W**

Transactions between a bank and its affiliates are quantitatively and qualitatively restricted under the Federal Reserve Act. The Federal Deposit Insurance Act applies Sections 23A and 23B to insured nonmember banks in the same manner and to the same extent as if they were members of the Federal Reserve System. The Federal Reserve Board has also issued Regulation W, which codifies prior regulations under Sections 23A and 23B of the Federal Reserve Act and interpretative guidance with respect to affiliate transactions. Regulation W incorporates the exemption from the affiliate transaction rules but expands the exemption to cover the purchase of any type of loan or extension of credit from an affiliate. Affiliates of a bank include, among other entities, the bank's holding company and companies that are under common control with the bank. The Company is considered to be an affiliate of Lakeland. In general, subject to certain specified exemptions, a bank or its subsidiaries are limited in their ability to engage in covered transactions with affiliates:

to an amount equal to 10% of the bank's capital and surplus, in the case of covered transactions with any one affiliate; and

to an amount equal to 20% of the bank's capital and surplus, in the case of covered transactions with all affiliates.

In addition, a bank and its subsidiaries may engage in covered transactions and other specified transactions only on terms and under circumstances that are substantially the same, or at least as favorable to the bank or its subsidiary, as those prevailing at the time for comparable transactions with nonaffiliated companies. A covered transaction includes:

a loan or extension of credit to an affiliate;

a purchase of, or an investment in, securities issued by an affiliate;

a purchase of assets from an affiliate, with some exceptions;

the acceptance of securities issued by an affiliate as collateral for a loan or extension of credit to any party; and

the issuance of a guarantee, acceptance or letter of credit on behalf of an affiliate.

---

## **Table of Contents**

In addition, under Regulation W:

a bank and its subsidiaries may not purchase a low-quality asset from an affiliate;

covered transactions and other specified transactions between a bank or its subsidiaries and an affiliate must be on terms and conditions that are consistent with safe and sound banking practices; and

with some exceptions, each loan or extension of credit by a bank to an affiliate must be secured by certain types of collateral with a market value ranging from 100% to 130%, depending on the type of collateral, of the amount of the loan or extension of credit.

Regulation W generally excludes all non-bank and non-savings association subsidiaries of banks from treatment as affiliates, except to the extent that the Federal Reserve Board decides to treat these subsidiaries as affiliates.

### **Community Reinvestment Act**

Under the Community Reinvestment Act ( CRA ), as implemented by FDIC regulations, a state bank has a continuing and affirmative obligation consistent with its safe and sound operation to help meet the credit needs of its entire community, including low and moderate income neighborhoods. The CRA does not establish specific lending requirements or programs for financial institutions nor does it limit an institution's discretion to develop the types of products and services that it believes are best suited to its particular community. The CRA requires the FDIC, in connection with its examination of a state non-member bank, to assess the bank's record of meeting the credit needs of its community and to take that record into account in its evaluation of certain applications by the bank. Under the FDIC's CRA evaluation system, the FDIC focuses on three tests: (i) a lending test, to evaluate the institution's record of making loans in its service areas; (ii) an investment test, to evaluate the institution's record of investing in community development projects, affordable housing and programs benefiting low or moderate income individuals and businesses; and (iii) a service test, to evaluate the institution's delivery of services through its branches, ATMs and other offices. The CRA also requires all institutions to make public disclosure of their CRA ratings. Lakeland Bank received an outstanding CRA rating in its most recent examination.

### **Securities and Exchange Commission**

The common stock of the Company is registered with the SEC under the Exchange Act. As a result, the Company and its officers, directors, and major stockholders are obligated to file certain reports with the SEC. The Company is subject to proxy and tender offer rules promulgated pursuant to the Exchange Act. You may read and copy any document the Company files with the SEC at the SEC's Public Reference Room at 100 F Street, N.E., Washington, D.C. 20549. Please call the SEC at 1-800-SEC-0330 for further information about the Public Reference Room. The SEC maintains a website at <http://www.sec.gov> that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC, such as the Company.

The Company maintains a website at <http://www.lakelandbank.com>. The Company makes available on its website the proxy statements and reports on Forms 8-K, 10-K and 10-Q that it files with the SEC as soon as reasonably practicable after such material is electronically filed with or furnished to the SEC. Additionally, the Company has adopted and posted on its website a Code of Ethics that applies to its principal executive officer, principal financial officer and principal accounting officer. The Company intends to disclose any amendments to or waivers of the Code of Ethics on its website.

### **Effect of Government Monetary Policies**

The earnings of the Company are and will be affected by domestic economic conditions and the monetary and fiscal policies of the United States government and its agencies. The monetary policies of the Federal Reserve Board have had, and will likely continue to have, an important impact on the operating results of

---

## **Table of Contents**

commercial banks through the Board's power to implement national monetary policy in order to, among other things, curb inflation or combat a recession. The Federal Reserve Board has a major effect upon the levels of bank loans, investments and deposits through its open market operations in United States government securities and through its regulation of, among other things, the discount rate of borrowings of banks and the reserve requirements against bank deposits. It is not possible to predict the nature and impact of future changes in monetary fiscal policies.

### **Dividend Restrictions**

The Company is a legal entity separate and distinct from Lakeland. Virtually all of the revenue of the Company available for payment of dividends on its capital stock will result from amounts paid to the Company by Lakeland. All such dividends are subject to various limitations imposed by federal and state laws and by regulations and policies adopted by federal and state regulatory agencies. Under state law, a bank may not pay dividends unless, following the dividend payment, the capital stock of the bank would be unimpaired and either (a) the bank will have a surplus of not less than 50% of its capital stock, or, if not, (b) the payment of the dividend will not reduce the surplus of the bank.

If, in the opinion of the FDIC, a bank under its jurisdiction is engaged in or is about to engage in an unsafe or unsound practice (which could include the payment of dividends), the FDIC may require, after notice and hearing, that such bank cease and desist from such practice or, as a result of an unrelated practice, require the bank to limit dividends in the future. The Federal Reserve Board has similar authority with respect to bank holding companies. In addition, the Federal Reserve Board and the FDIC have issued policy statements which provide that insured banks and bank holding companies should generally only pay dividends out of current operating earnings. Regulatory pressures to reclassify and charge off loans and to establish additional loan loss reserves can have the effect of reducing current operating earnings and thus impacting an institution's ability to pay dividends. Further, as described herein, the regulatory authorities have established guidelines with respect to the maintenance of appropriate levels of capital by a bank or bank holding company under their jurisdiction. Compliance with the standards set forth in these policy statements and guidelines could limit the amount of dividends which the Company and Lakeland may pay. Banking institutions that fail to maintain the minimum capital ratios, or that maintain the requisite minimum capital ratios but do so at a level below the minimum capital ratios plus the new capital conservation buffer, will face constraints on their ability to pay dividends. See [Capital Requirements](#) below.

### **Capital Requirements**

Pursuant to the Federal Deposit Insurance Corporation Improvement Act of 1991 (FDICIA), each federal banking agency has promulgated regulations, specifying the levels at which a financial institution would be considered well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized, or critically undercapitalized, and to take certain mandatory and discretionary supervisory actions based on the capital level of the institution. To qualify to engage in financial activities under the Gramm-Leach-Bliley Act, all depository institutions must be well capitalized. The financial holding company of a bank will be put under directives to raise its capital levels or divest its activities if the depository institution falls from that level.

In July 2013, the Federal Reserve Board, the FDIC and the Comptroller of the Currency adopted final rules establishing a new comprehensive capital framework for U.S. banking organizations (the [Basel Rules](#)). The Basel Rules implement the Basel Committee's December 2010 framework, commonly referred to as Basel III, for strengthening international capital standards as well as certain provisions of the Dodd-Frank Act, as discussed below. The Basel Rules substantially revise the risk-based capital requirements applicable to bank holding companies and depository institutions, including Lakeland Bancorp and Lakeland Bank, compared to prior U.S. risk-based capital rules. The Basel Rules define the components of capital and address other issues affecting the numerator in banking institutions' regulatory capital ratios. The Basel Rules also address risk weights and other issues affecting the denominator in banking institutions' regulatory capital ratios and replace the existing risk-

---

**Table of Contents**

weighting approach, which was derived from Basel I capital accords of the Basel Committee, with a more risk-sensitive approach based, in part, on the standardized approach in the Basel Committee's 2004 Basel II capital accords. The Basel Rules also implement the requirements of Section 939A of the Dodd-Frank Act to remove references to credit ratings from the federal banking agencies' rules.

The Basel Rules became effective for us on January 1, 2015 (subject to phase-in periods for certain components).

For bank holding companies and banks like Lakeland Bancorp and Lakeland Bank, January 1, 2015 was the start date for compliance with the revised minimum regulatory capital ratios and for determining risk-weighted assets under what the Basel Rules call a standardized approach. As of January 1, 2015, Lakeland Bancorp and Lakeland Bank were required to maintain the following minimum capital ratios, expressed as a percentage of risk-weighted assets:

Common Equity Tier 1 Capital Ratio of 4.5% (this is a new concept and requirement, and is referred to as the CET1);

Tier 1 Capital Ratio (CET1 capital plus Additional Tier 1 capital) of 6.0%; and

Total Capital Ratio (Tier 1 capital plus Tier 2 capital) of 8.0%.

In addition, Lakeland Bancorp and Lakeland Bank are subject to a leverage ratio of 4% (calculated as Tier 1 capital to average consolidated assets as reported on the consolidated financial statements).

The Basel Rules also require a capital conservation buffer. When fully phased in on January 1, 2019, Lakeland Bancorp and Lakeland Bank will be required to maintain a 2.5% capital conservation buffer, in addition to the minimum capital ratios described above, effectively resulting in the following minimum capital ratios on January 1, 2019:

CET1 of 7.0%;

Tier 1 Capital Ratio of 8.5%; and

Total Capital Ratio of 10.5%.

The purpose of the capital conservation buffer is to ensure that banking organizations conserve capital when it is needed most, allowing them to weather periods of economic stress. Banking institutions with a CET1, Tier 1 Capital Ratio and Total Capital Ratio above the minimum capital ratios but below the minimum capital ratios plus the capital conservation buffer will face constraints on their ability to pay dividends, repurchase equity and pay discretionary bonuses to executive officers, based on the amount of the shortfall. The implementation of the capital conservation buffer began on January 1, 2016 at the 0.625% level (thus effectively resulting in minimum capital ratios as of January 1, 2016 for CET1, Tier 1 Capital Ratio and Total Capital Ratio of 5.125%, 6.625% and 8.625%, respectively), and increases by 0.625% on each subsequent January 1 until it reaches 2.5% on January 1, 2019.

The Basel Rules also adopted a countercyclical capital buffer, which is not applicable to Lakeland Bancorp or Lakeland Bank. That buffer is applicable only to advanced approaches banking organizations, which generally are those with consolidated total assets of at least \$250 billion.

The Basel Rules provide for several deductions from and adjustments to CET1, which are being phased in between January 1, 2015 and January 1, 2018. For example, mortgage servicing rights, deferred tax assets dependent upon future taxable income and significant investments in common equity issued by nonconsolidated financial entities must be deducted from CET1 to the extent that any one of those categories exceeds 10% of CET1 or all such categories in the aggregate exceed 15% of CET1.

Under prior capital standards, the effects of accumulated other comprehensive income items included in capital were excluded for the purposes of determining regulatory capital ratios. Under the Basel Rules, the effects





---

**Table of Contents**

of certain accumulated other comprehensive income items are not excluded; however, banking organizations such as Lakeland Bancorp and Lakeland Bank may make a one-time permanent election to continue to exclude these items effective as of January 1, 2015. Lakeland Bancorp and Lakeland Bank made such an election to continue to exclude these items.

While the Basel Rules generally require the phase-out of non-qualifying capital instruments such as trust preferred securities and cumulative perpetual preferred stock, holding companies with less than \$15 billion in total consolidated assets as of December 31, 2009, such as Lakeland Bancorp, may permanently include non-qualifying instruments that were issued and included in Tier 1 or Tier 2 capital prior to May 19, 2010 in Additional Tier 1 or Tier 2 capital until they redeem such instruments or until the instruments mature.

The Basel Rules prescribe a standardized approach for calculating risk-weighted assets that expands the risk-weighting categories from the previous four categories (0%, 20%, 50% and 100%) to a much larger and more risk-sensitive number of categories, depending on the nature of the assets, generally ranging from 0% for U.S. Government and agency securities, to 600% for certain equity exposures, and resulting in higher risk weights for a variety of asset categories. In addition, the Basel Rules provide more advantageous risk weights for derivatives and repurchase-style transactions cleared through a qualifying central counterparty and increase the scope of eligible guarantors and eligible collateral for purposes of credit risk mitigation.

Consistent with the Dodd-Frank Act, the Basel Rules adopt alternatives to credit ratings for calculating the risk-weighting for certain assets.

With respect to Lakeland Bank, the Basel Rules revise the prompt corrective action regulations under Section 38 of the Federal Deposit Insurance Act by (i) introducing a CET1 ratio requirement at each capital quality level (other than critically undercapitalized), with the required CET1 ratio being 6.5% for well-capitalized status (a new standard); (ii) increasing the minimum Tier 1 capital ratio requirement for each category, with the minimum Tier 1 capital ratio for well-capitalized status being 8% (increased from 6%); and (iii) requiring a leverage ratio of 5% to be well-capitalized (increased from the previously required leverage ratio of 3% or 4%). The Basel Rules do not change the total risk-based capital requirement for any prompt corrective action category. Effective as of January 1, 2015, the FDIC's regulations implementing these provisions of FDICIA provide that an institution will be classified as well capitalized if it (i) has a total risk-based capital ratio of at least 10.0 percent, (ii) has a Tier 1 risk-based capital ratio of at least 8.0 percent, (iii) has a CET1 ratio of at least 6.5 percent, (iv) has a Tier 1 leverage ratio of at least 5.0 percent, and (v) meets certain other requirements. An institution will be classified as adequately capitalized if it (i) has a total risk-based capital ratio of at least 8.0 percent, (ii) has a Tier 1 risk-based capital ratio of at least 6.0 percent, (iii) has a CET1 ratio of at least 4.5 percent, (iv) has a Tier 1 leverage ratio of at least 4.0 percent, and (v) does not meet the definition of well capitalized. An institution will be classified as undercapitalized if it (i) has a total risk-based capital ratio of less than 8.0 percent, (ii) has a Tier 1 risk-based capital ratio of less than 6.0 percent, (iii) has a CET1 ratio of less than 4.5 percent or (iv) has a Tier 1 leverage ratio of less than 4.0 percent. An institution will be classified as significantly undercapitalized if it (i) has a total risk-based capital ratio of less than 6.0 percent, (ii) has a Tier 1 risk-based capital ratio of less than 4.0 percent, (iii) has a CET1 ratio of less than 3.0 percent or (iv) has a Tier 1 leverage ratio of less than 3.0 percent. An institution will be classified as critically undercapitalized if it has a tangible equity to total assets ratio that is equal to or less than 2.0 percent. An insured depository institution may be deemed to be in a lower capitalization category if it receives an unsatisfactory examination rating. Similar categories apply to bank holding companies. When the capital conservation buffer is fully phased in, the capital ratios applicable to depository institutions under the Basel Rules will exceed the ratios to be considered well-capitalized under the prompt corrective action regulations.

As of December 31, 2015, Lakeland Bancorp and Lakeland Bank met all capital requirements under the Basel Rules as then in effect, and the Company believes that as of such date, it would meet all capital requirements under the Basel Rules on a fully phased-in basis, if the full phase-in of such requirements were currently in effect.

---

## **Table of Contents**

### **Volcker Rule**

In December 2013, the Federal Reserve Board, the FDIC and several other governmental regulatory agencies issued final rules to implement the Volcker Rule contained in section 619 of the Dodd-Frank Act, generally to become effective on July 21, 2016. These rules generally became effective in July 2015. The Volcker Rule prohibits an insured depository institution and its affiliates from (i) engaging in proprietary trading and (ii) investing in or sponsoring certain types of funds (defined as Covered Funds) subject to certain limited exceptions. The Company does not own any interests in any hedge funds or private equity funds that are designated Covered Funds under the Volcker Rule.

### **Federal Deposit Insurance and Premiums**

Lakeland's deposits are insured up to applicable limits by the Deposit Insurance Fund (DIF) of the FDIC and are subject to deposit insurance assessments to maintain the DIF. As a result of the Dodd-Frank Act, the basic federal deposit insurance limit was permanently increased to at least \$250,000.

In November 2010, the FDIC approved a rule to change the assessment base from adjusted domestic deposits to average consolidated total assets minus average tangible equity, as required by the Dodd-Frank Act. These new assessment rates began in the second quarter of 2011 and were paid at the end of September 2011. Since the new base is larger than the current base, the FDIC's rule lowered the total base assessment rates to between 2.5 and 9 basis points for banks in the lowest risk category, and 30 to 45 basis points for banks in the highest risk category. The Company paid \$2.0 million in total FDIC assessments in both 2015 and 2014.

Pursuant to the Dodd-Frank Act, the FDIC has established 2.0% as the designated reserve ratio (DRR), that is, the ratio of the DIF to insured deposits. The FDIC has adopted a plan under which it will meet the statutory minimum DRR of 1.35% by September 30, 2020, the deadline imposed by the Dodd-Frank Act. The Dodd-Frank Act requires the FDIC to offset the effect on institutions with assets less than \$10 billion of the increase in the statutory minimum DRR to 1.35% from the former statutory minimum of 1.15%. The FDIC has not yet announced how it will implement this offset.

In addition to deposit insurance assessments, the FDIC is required to continue to collect from institutions payments for the servicing of obligations of the Financing Corporation (FICO) that were issued in connection with the resolution of savings and loan associations, so long as such obligations remain outstanding. Lakeland paid a FICO premium of approximately \$193,000 in 2015 and expects to pay a similar amount in 2016.

### **The Dodd-Frank Act**

The Dodd-Frank Act, which was signed into law on July 21, 2010, significantly changed the bank regulatory landscape and has impacted and will continue to have a broad impact on the financial services industry as a result of significant regulatory and compliance changes, including, among other things, (i) enhanced resolution authority over troubled and failing banks and their holding companies; (ii) increased capital and liquidity requirements; (iii) increased regulatory examination fees; (iv) changes to assessments to be paid to the FDIC for federal deposit insurance; and (v) numerous other provisions designed to improve supervision and oversight of, and strengthening safety and soundness for, the financial services sector. Generally, the Dodd-Frank Act became effective the day after it was signed into law, but different effective dates apply to specific sections of the law.

The following is a summary of certain provisions of the Dodd-Frank Act:

*Minimum Capital Requirements.* The Dodd-Frank Act requires new capital rules and the application of the same leverage and risk-based capital requirements that apply to insured depository institutions to most bank holding companies. In addition to making bank holding companies subject to the same capital requirements as their bank subsidiaries, these provisions (often referred to as the Collins Amendment to the Dodd-Frank Act) were also intended to eliminate or significantly reduce the use of

---

**Table of Contents**

hybrid capital instruments, especially trust preferred securities, as regulatory capital. See *Capital Requirements* for a description of new capital requirements adopted by U.S. federal banking regulators in 2013 and the treatment of trust preferred securities under such rules.

*Deposit Insurance.* The Dodd-Frank Act makes permanent the \$250,000 deposit insurance limit for insured deposits. Amendments to the Federal Deposit Insurance Act also revised the assessment base against which an insured depository institution's deposit insurance premiums paid to the Deposit Insurance Fund ( DIF ) are calculated. Under the amendments, the assessment base is no longer the institution's deposit base, but rather its average consolidated total assets less its average tangible equity during the assessment period. Additionally, the Dodd-Frank Act makes changes to the minimum designated reserve ratio of the DIF, increasing the minimum from 1.15 percent to 1.35 percent of the estimated amount of total insured deposits and eliminating the requirement that the FDIC pay dividends to depository institutions when the reserve ratio exceeds certain thresholds. In December 2010, the FDIC increased the designated reserve ratio to 2.0 percent.

*Shareholder Votes.* The Dodd-Frank Act requires publicly traded companies like Lakeland Bancorp to give shareholders a non-binding vote on executive compensation and so-called golden parachute payments in certain circumstances.

*Transactions with Affiliates.* The Dodd-Frank Act enhances the requirements for certain transactions with affiliates under Section 23A and 23B of the Federal Reserve Act, including an expansion of the definition of covered transactions and increasing the amount of time for which collateral requirements regarding covered transactions must be maintained. These requirements became effective during 2011.

*Transactions with Insiders.* Insider transaction limitations are expanded through the strengthening of loan restrictions to insiders and the expansion of the types of transactions subject to the various limits, including derivative transactions, repurchase agreements, reverse repurchase agreements and securities lending or borrowing transactions. Restrictions are also placed on certain asset sales to and from an insider to an institution, including requirements that such sales be on market terms and, in certain circumstances, approved by the institution's board of directors. These requirements became effective during 2011.

*Enhanced Lending Limits.* The Dodd-Frank Act strengthened the previous limits on a depository institution's credit exposure to one borrower which limited a depository institution's ability to extend credit to one person (or group of related persons) in an amount exceeding certain thresholds. The Dodd-Frank Act expanded the scope of these restrictions to include credit exposure arising from derivative transactions, repurchase agreements, and securities lending and borrowing transactions.

*Compensation Practices.* The Dodd-Frank Act provides that the appropriate federal regulators must establish standards prohibiting as an unsafe and unsound practice any compensation plan of a bank holding company or other covered financial institution that provides an insider or other employee with excessive compensation or compensation that gives rise to excessive risk or could lead to a material financial loss to such firm. In June 2010, prior to the Dodd-Frank Act, the bank regulatory agencies promulgated the *Interagency Guidance on Sound Incentive Compensation Policies*, which sets forth three key principles concerning incentive compensation arrangements:

such arrangements should provide employees incentives that balance risk and financial results in a manner that does not encourage employees to expose the financial institution to imprudent risks;

such arrangements should be compatible with effective controls and risk management; and

## Edgar Filing: LAKELAND BANCORP INC - Form 10-K

such arrangements should be supported by strong corporate governance with effective and active oversight by the financial institution's board of directors.

Together, the Dodd-Frank Act and guidance from the bank regulatory agencies on compensation may impact the Company's compensation practices.

-12-

---

## **Table of Contents**

*The Consumer Financial Protection Bureau ( Bureau ).* The Dodd-Frank Act created the Bureau within the Federal Reserve. The Bureau is tasked with establishing and implementing rules and regulations under certain federal consumer protection laws with respect to the conduct of providers of certain consumer financial products and services. The Bureau has rulemaking authority over many of the statutes governing products and services offered to bank consumers. In addition, the Dodd-Frank Act permits states to adopt consumer protection laws and regulations that are more stringent than those regulations promulgated by the Bureau and state attorneys general are permitted to enforce consumer protection rules adopted by the Bureau against state-chartered institutions. The Bureau has examination and enforcement authority over all banks and savings institutions with more than \$10 billion in assets. Institutions with \$10 billion or less in assets, such as the Bank, will continue to be examined for compliance with the consumer laws by their primary bank regulators.

*De Novo Banking.* The Dodd-Frank Act allows de novo interstate branching by banks. Final rules have been issued which implement the ability-to-repay and qualified mortgage (QM) provisions of the Truth in Lending Act, as amended by the Dodd-Frank Act (the QM Rule ). The QM Rule impacted our mortgage originations when it became effective in January 2014. The ability-to-repay provision requires creditors to make reasonable, good faith determinations that borrowers are able to repay their mortgages before extending the credit based on a number of factors and consideration of financial information about the borrower from reasonably reliable third-party documents. Under the Dodd-Frank Act and the QM Rule, loans meeting the definition of qualified mortgage are entitled to a presumption that the lender satisfied the ability-to-repay requirements. The presumption is a conclusive presumption/safe harbor for prime loans meeting the QM requirements, and a rebuttable presumption for higher-priced/subprime loans meeting the QM requirements. The definition of a qualified mortgage incorporates the statutory requirements, such as not allowing negative amortization or terms longer than 30 years. The QM Rule also adds an explicit maximum 43 percent debt-to-income ratio for borrowers if the loan is to meet the QM definition, though some mortgages that meet GSE, FHA and VA underwriting and eligibility guidelines may, for a period not to exceed seven years, meet the QM definition without being subject to the 43 percent debt-to-income limits. We cannot assure you that existing or future regulations will not have a material adverse impact on our residential mortgage loan business or the housing markets in which we participate.

In addition, provisions in the Dodd-Frank Act which have revised the capital requirements of the Company and the Bank could require the Company and the Bank to seek additional sources of capital in the future. See Capital Requirements.

The Dodd-Frank Act contains numerous other provisions affecting financial institutions of all types, many of which may have an impact on our operating environment in substantial and unpredictable ways. Consequently, the Dodd-Frank Act is likely to continue to increase our cost of doing business, it may limit or expand our permissible activities, and it may affect the competitive balance within our industry and market areas. The nature and extent of future legislative and regulatory changes affecting financial institutions, including as a result of the Dodd-Frank Act, remains very unpredictable at this time.

### **Proposed Legislation**

From time to time proposals are made in the United States Congress, the New Jersey Legislature, and before various bank regulatory authorities, which would alter the powers of, and place restrictions on, different types of banking organizations. It is impossible to predict the impact, if any, of potential legislative trends on the business of the Company and its subsidiaries.

In accordance with federal law providing for deregulation of interest on all deposits, banks and thrift organizations are now unrestricted by law or regulation from paying interest at any rate on most time deposits. It is not clear whether deregulation and other pending changes in certain aspects of the banking industry will result in further increases in the cost of funds in relation to prevailing lending rates.

---

**Table of Contents**

**ITEM 1A - Risk Factors.**

Our business, financial condition, operating results and cash flows can be affected by a number of factors, including, but not limited to, those set forth below, any one of which could cause our actual results to vary materially from recent results or from our anticipated future results.

**The Dodd-Frank Act could materially and adversely affect us by increasing compliance costs, heightening our risk of noncompliance with applicable regulations, and changing the competitive landscape in the banking industry.**

From time to time, the U.S. Congress and state legislatures consider changing laws and enact new laws to further regulate the financial services industry. On July 21, 2010, the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, or the Dodd-Frank Act, was signed into law. The Dodd-Frank Act has resulted in sweeping changes in the regulation of financial institutions. As discussed in the section herein entitled Business-Supervision and Regulation, the Dodd-Frank Act contains numerous provisions that affect all banks and bank holding companies. Some of the provisions in the Dodd-Frank Act remain subject to regulatory rule-making and implementation, the full effects of which are not yet known. Although we cannot predict the full and specific impact and long-term effects that the Dodd-Frank Act and the regulations promulgated thereunder will have on us and our prospects, our target markets and the financial industry more generally, we believe that the Dodd-Frank Act and the regulations promulgated thereunder are likely to continue to impose additional administrative and regulatory burdens that will obligate us to continue to incur additional expenses and will continue to adversely affect our margins and profitability. For example, the elimination of the prohibition on the payment of interest on demand deposits could materially increase our interest expense, depending on our competitors responses. Provisions in the legislation mandating modification of the capital requirements applicable to the Company and the Bank, and the resulting adoption by federal regulators in July 2013 of the new capital requirements described under Business-Supervision and Regulation-Capital Requirements, could require the Company and the Bank to seek additional sources of capital in the future. Recent or additional regulations may limit or expand our permissible activities, and may affect the competitive balance within our industry and market areas, with the nature and extent of future legislative and regulatory changes affecting financial institutions remaining very unpredictable at this time. More stringent consumer protection regulations could materially and adversely affect our profitability. We also have a heightened risk of noncompliance with all of the additional regulations. Finally, the full impact of some of these new regulations is not known and may affect our ability to compete long-term with larger competitors.

**The Company and the Bank are subject to more stringent capital and liquidity requirements.**

The Dodd-Frank Act also imposes more stringent capital requirements on bank holding companies such as Lakeland Bancorp by, among other things, imposing leverage ratios on bank holding companies and prohibiting new trust preferred issuances from counting as Tier I capital. These restrictions will limit our future capital strategies. Under the Dodd-Frank Act, our currently outstanding trust preferred securities will continue to count as Tier I capital, but we will be unable to issue replacement or additional trust preferred securities which would count as Tier I capital.

As further described above under Business-Supervision and Regulation-Capital Requirements, we were required to meet new capital requirements beginning on January 1, 2015. In addition, beginning in 2016, banks and bank holding companies are required to maintain a capital conservation buffer on top of minimum risk-weighted asset ratios. The implementation of the capital conservation buffer began on January 1, 2016 at the 0.625% level, and increases by 0.625% on each subsequent January 1 until it reaches 2.5% when fully phased in on January 1, 2019. Banking institutions which do not maintain capital in excess of the capital conservation buffer face constraints on the payment of dividends, equity repurchases and compensation based on the amount of the shortfall. Accordingly, if the Bank fails to maintain the applicable minimum capital ratios and the capital conservation buffer, distributions to Lakeland Bancorp may be prohibited or limited.

## **Table of Contents**

Future increases in minimum capital requirements could adversely affect our net income. Furthermore, our failure to comply with the minimum capital requirements could result in our regulators taking formal or informal actions against us which could restrict our future growth or operations.

**The Company's future growth may require the Company to raise additional capital in the future, but that capital may not be available when it is needed or may be available only at an excessive cost.**

The Company is required by regulatory authorities to maintain adequate levels of capital to support its operations. The Company anticipates that current capital levels will satisfy regulatory requirements for the foreseeable future. The Company, however, may at some point choose to raise additional capital to support its continued growth. The Company's ability to raise additional capital will depend, in part, on conditions in the capital markets at that time, which are outside of the Company's control. Accordingly, the Company may be unable to raise additional capital, if and when needed, on terms acceptable to the Company, or at all. If the Company cannot raise additional capital when needed, its ability to further expand operations through internal growth and acquisitions could be materially impacted. In the event of a material decrease in the Company's stock price, future issuances of equity securities could result in dilution of existing shareholder interests.

**Europe's debt crisis and volatility in China's financial markets could have a material adverse effect on our liquidity, financial condition and results of operations.**

The possibility that certain European Union (EU) member states will default on their debt obligations and concerns about Chinese financial markets have negatively impacted economic conditions and global markets. The continued uncertainty over the outcome of international and the EU's financial support programs and the possibility that other EU member states may experience similar financial troubles could further disrupt global markets. The negative impact on economic conditions and global markets could also have a material adverse effect on our liquidity, financial condition and results of operations.

**A decrease in our ability to borrow funds could adversely affect our liquidity.**

Our ability to obtain funding from the Federal Home Loan Bank or through our overnight federal funds lines with other banks could be negatively affected if we experienced a substantial deterioration in our financial condition or if such funding became restricted due to deterioration in the financial markets. While we have a contingency funds management plan to address such a situation if it were to occur (such plan includes deposit promotions, the sale of securities and the curtailment of loan growth, if necessary), a significant decrease in our ability to borrow funds could adversely affect our liquidity.

**We are subject to interest rate risk and variations in interest rates may negatively affect our financial performance.**

We are unable to predict actual fluctuations of market interest rates. Rate fluctuations are influenced by many factors, including:

inflation or deflation

excess growth or recession;

a rise or fall in unemployment;

tightening or expansion of the money supply;

domestic and international disorder;

instability in domestic and foreign financial markets; and



actions taken or statements made by the Federal Reserve Board.

-15-

## **Table of Contents**

Both increases and decreases in the interest rate environment may reduce our profits. We expect that we will continue to realize income from the difference or spread between the interest we earn on loans, securities and other interest-earning assets, and the interest we pay on deposits, borrowings and other interest-bearing liabilities. Our net interest spreads are affected by the differences between the maturities and repricing characteristics of our interest-earning assets and interest-bearing liabilities. Our interest-earning assets may not reprice as slowly or rapidly as our interest-bearing liabilities. Changes in market interest rates could materially and adversely affect our net interest spread, asset quality, levels of prepayments, cash flows, market value of our securities portfolio, loan and deposit growth, costs and yields on loans and deposits and our overall profitability. Competition for our deposits has increased significantly as a result of the recent low interest rate environment.

### **Declines in value may adversely impact our investment portfolio.**

As of December 31, 2015, the Company had approximately \$442.3 million and \$116.7 million in available for sale and held to maturity investment securities, respectively. We may be required to record impairment charges on our investment securities if they suffer a decline in value that is considered other-than-temporary. Numerous factors, including lack of liquidity for sales of certain investment securities, absence of reliable pricing information for investment securities, adverse changes in business climate, adverse actions by regulators, or unanticipated changes in the competitive environment could have a negative effect on our investment portfolio in future periods. If an impairment charge is significant enough it could affect the ability of Lakeland to upstream dividends to us, which could have a material adverse effect on our liquidity and our ability to pay dividends to shareholders and could also negatively impact our regulatory capital ratios.

### **The Company may incur impairment to goodwill.**

We review our goodwill at least annually. Our valuation methodology for assessing impairment requires management to make judgments and assumptions based on historical experience and to rely on projections of future operating performance. We operate in a competitive environment and projections of future operating results and cash flows may vary significantly from actual results. Additionally, if our analysis results in an impairment to our goodwill, we would be required to record a non-cash charge to earnings in our financial statements during the period in which such impairment is determined to exist. Any such charge could have a material adverse effect on our results of operations and our stock price.

### **The extensive regulation and supervision to which we are subject impose substantial restrictions on our business.**

The Company, Lakeland and certain non-bank subsidiaries are subject to extensive regulation and supervision. Banking regulations are primarily intended to protect depositors' funds, federal deposit insurance funds and the banking system as a whole. Such laws are not designed to protect our shareholders. These regulations affect our lending practices, capital structure, investment practices, dividend policy and growth, among other things. Lakeland is also subject to a number of laws which, among other things, govern its lending practices and require the Bank to establish and maintain comprehensive programs relating to anti-money laundering and customer identification. The United States Congress and federal regulatory agencies continually review banking laws, regulations and policies for possible changes. Changes to statutes, regulations or regulatory policies, including changes in interpretation or implementation of statutes, regulations or policies, could affect us in substantial and unpredictable ways. Such changes could subject us to additional costs, limit the types of financial services and products we may offer and/or increase the ability of non-banks to offer competing financial services and products, among other things. Failure to comply with laws, regulations or policies could result in sanctions by regulatory agencies, civil money penalties and/or reputational damage, which could have a material adverse effect on our business, financial condition and results of operations.

---

**Table of Contents**

**Lakeland's ability to pay dividends is subject to regulatory limitations which, to the extent that our holding company requires such dividends in the future, may affect our holding company's ability to pay its obligations and pay dividends to shareholders.**

As a bank holding company, the Company is a separate legal entity from Lakeland and its subsidiaries, and we do not have significant operations of our own. We currently depend on Lakeland's cash and liquidity to pay our operating expenses and dividends to shareholders. The availability of dividends from Lakeland is limited by various statutes and regulations. The inability of the Company to receive dividends from Lakeland could adversely affect our financial condition, results of operations, cash flows and prospects and the Company's ability to pay dividends.

In addition, as described under Business-Supervision and Regulation-Capital Requirements, beginning in 2016, banks and bank holding companies are required to maintain a capital conservation buffer on top of minimum risk-weighted asset ratios. The implementation of the capital conservation buffer began on January 1, 2016 at the 0.625% level, and increases by 0.625% on each subsequent January 1 until it reaches 2.5% when fully phased in on January 1, 2019. Banking institutions which do not maintain capital in excess of the capital conservation buffer will face constraints on the payment of dividends, equity repurchases and compensation based on the amount of the shortfall. Accordingly, if the Bank fails to maintain the applicable minimum capital ratios and the capital conservation buffer, distributions to Lakeland Bancorp may be prohibited or limited.

**Our allowance for loan and lease losses may not be adequate to cover actual losses.**

Like all commercial banks, Lakeland maintains an allowance for loan and lease losses to provide for loan and lease defaults and non-performance. If our allowance for loan and lease losses is not adequate to cover actual loan and lease losses, we may be required to significantly increase future provisions for loan and lease losses, which could materially and adversely affect our operating results. Our allowance for loan and lease losses is determined by analyzing historical loan and lease losses, current trends in delinquencies and charge-offs, plans for problem loan and lease resolution, the opinions of our regulators, changes in the size and composition of the loan and lease portfolio and industry information. We also consider the possible effects of economic events, which are difficult to predict. The amount of future losses is affected by changes in economic, operating and other conditions, including changes in interest rates, many of which are beyond our control. These losses may exceed our current estimates. Federal regulatory agencies, as an integral part of their examination process, review our loans and the allowance for loan and lease losses. While we believe that our allowance for loan and lease losses in relation to our current loan portfolio is adequate to cover current losses, we cannot assure you that we will not need to increase our allowance for loan and lease losses or that the regulators will not require us to increase this allowance. Future increases in our allowance for loan and lease losses could materially and adversely affect our earnings and profitability.

**If we are unable to remediate the material weakness in our internal control over financial reporting that we have reported in this Annual Report, or if other material weaknesses are identified in the future, our results of operations or financial condition could be materially adversely affected.**

As disclosed elsewhere in this Annual Report on Form 10-K, during the fourth quarter of 2015, we identified a material weakness in our internal controls over financial reporting over the completeness and accuracy of the information used to determine the qualitative component of the allowance for loan and lease loss estimate. No restatement of prior period financial statements and no change in previously released financial results were required as a result of this finding. Management has taken steps to remediate this weakness by enhancing review controls, including adding an additional independent level of review over the information used to determine the qualitative factors in the allowance for loan and lease loss estimation process. If our remedial measures are insufficient to address this material weakness, or if additional material weaknesses or significant deficiencies in our internal control are discovered or occur in the future, our results of operations or financial condition could be materially adversely affected.

---

**Table of Contents**

**The concentration of our commercial real estate loan portfolio may subject us to increased regulatory analysis.**

The FDIC, the Federal Reserve and the OCC have promulgated joint guidance on sound risk management practices for financial institutions with concentrations in commercial real estate (CRE) lending. The 2006 interagency guidance did not establish specific CRE lending limits or caps; rather, the guidance set forth supervisory criteria to serve as levels of bank CRE concentration above which certain financial institutions may be identified for further supervisory analysis. According to the guidelines, institutions could be subject to further analysis if (i) their loans for construction, land, and land development (CLD) represent 100% or more of the institution's total risk-based capital, or (ii) their total non-owner-occupied CRE loans (including CLD loans), as defined, represent 300% or more of the institution's total risk-based capital, and further, that the institution's non-owner-occupied CRE loan portfolio has increased by 50% or more during the previous 36 months.

The Bank's total reported CLD loans represented 36% of total risk-based capital at December 31, 2015. The Bank's total reported CRE loans to total capital was 386% at December 31, 2015 while the Bank's CRE portfolio has increased by 54% over the preceding 36 months. Had Pascack been merged into the Company as of December 31, 2015, the combined CRE portfolio would have increased by 45% over the preceding 36 months.

The Bank's CRE portfolio is segmented and spread among various property types including retail, office, multi-family, mixed use, industrial, hospitality, healthcare, special use and residential and commercial construction. Management regularly reviews and evaluates its CRE portfolio, including concentrations within the various property types based on current market conditions and risk appetite as well as by utilizing stress testing on material exposures and believes its underwriting practices are sound.

There is no assurance that in the future we will not continue to exceed the levels set forth in the guidelines.

**Our mortgage banking operations expose us to risks that are different than the risks associated with our retail banking operations.**

The Bank's mortgage banking operations expose us to risks that are different than our retail banking operations. Our mortgage banking operations are dependent upon the level of demand for residential mortgages. During higher and rising interest rate environments, the level of refinancing activity tends to decline, which can lead to reduced volumes of business and lower revenues that may not exceed our fixed costs to run the business. In addition, mortgages sold to third-party investors are typically subject to certain repurchase provisions related to borrower refinancing, defaults, fraud or other reasons stipulated in the applicable third-party investor agreements. If the fair value of a loan when repurchased is less than the fair value when sold, a bank may be required to charge such shortfall to earnings.

In addition, the ability to repay and Qualified Mortgage rules promulgated as required by the Dodd-Frank Act, which rules became effective on January 10, 2014, may expose the Company to greater losses, reduced volume and litigation related expenses and delays in taking title to collateral real estate, if these loans do not perform and borrowers challenge whether the rules were satisfied when originating the loans.

**We are subject to various lending and other economic risks that could adversely affect our results of operations and financial condition.**

Economic, political and market conditions, trends in industry and finance, legislative and regulatory changes, changes in governmental monetary and fiscal policies and inflation affect our business. These factors are beyond our control. A deterioration in economic conditions, particularly in New Jersey, could have the following consequences, any of which could materially adversely affect our business:

loan and lease delinquencies may increase;

problem assets and foreclosures may increase;

## **Table of Contents**

demand for our products and services may decrease; and

collateral for loans made by us may decline in value, in turn reducing the borrowing ability of our customers. Deterioration in the real estate market, particularly in New Jersey, could adversely affect our business. A decline in real estate values in New Jersey would reduce our ability to recover on defaulted loans by selling the underlying real estate, which would increase the possibility that we may suffer losses on defaulted loans.

### **We may suffer losses in our loan portfolio despite our underwriting practices.**

We seek to mitigate the risks inherent in our loan portfolio by adhering to specific underwriting practices. Although we believe that our underwriting criteria are appropriate for the various kinds of loans that we make, we may incur losses on loans that meet our underwriting criteria, and these losses may exceed the amounts set aside as reserves in our allowance for loan and lease losses.

### **We face strong competition from other financial institutions, financial service companies and other organizations offering services similar to the services that we provide.**

Many competitors offer the types of loans and banking services that we offer. These competitors include other state and national banks, savings associations, regional banks and other community banks. We also face competition from many other types of financial institutions, including finance companies, brokerage firms, insurance companies, credit unions, mortgage banks and other financial intermediaries. Many of our competitors have greater financial resources than we do, which may enable them to offer a broader range of services and products, and to advertise more extensively, than we do. Our inability to compete effectively would adversely affect our business.

### **The inability to attract and retain key personnel could adversely affect our Company's business.**

The success of the Company depends partially on the ability to attract and retain a high level of experienced personnel. The inability to attract and retain key employees, as well as find suitable replacements, if necessary, could adversely affect the Company's customer relationships and internal operations.

### **The inability to stay current with technological change could adversely affect our business model.**

Financial institutions continually are required to maintain and upgrade technology in order to provide the most current products and services to their customers, as well as create operational efficiencies. This technology requires personnel resources, as well as significant costs to implement. Failure to successfully implement technological change could adversely affect the Company's business, results of operations and financial condition.

### **The occurrence of any failure, breach, or interruption in service involving our systems or those of our service providers could damage our reputation, cause losses, increase our expenses, and result in a loss of customers, an increase in regulatory scrutiny, or expose us to civil litigation and possibly financial liability, any of which could adversely impact our financial condition, results of operations and the market price of our stock.**

Communications and information systems are essential to the conduct of our business, as we use such systems to manage our customer relationships, our general ledger, our deposits and our loans. Our operations rely on the secure processing, storage and transmission of confidential and other information in our computer systems and networks. Although we take protective measures and endeavor to modify them as circumstances warrant, the security of our computer systems, software and networks may be vulnerable to breaches, unauthorized access,

## **Table of Contents**

misuse, computer viruses or other malicious code and cyber attacks that could have a security impact. In addition, breaches of security may occur through intentional or unintentional acts by those having authorized or unauthorized access to our confidential or other information or the confidential or other information of our customers, clients or counterparties. If one or more of such events were to occur, the confidential and other information processed and stored in, and transmitted through, our computer systems and networks could potentially be jeopardized, or could otherwise cause interruptions or malfunctions in our operations or the operations of our customers, clients or counterparties. This could cause us significant reputational damage or result in our experiencing significant losses.

Furthermore, we may be required to expend significant additional resources to modify our protective measures or to investigate and remediate vulnerabilities or other exposures arising from operational and security risks. We also may be subject to litigation and financial losses that are either not insured against or not fully covered through any insurance we maintain. In addition, we routinely transmit and receive personal, confidential and proprietary information by e-mail and other electronic means. We have discussed and worked with our customers, clients and counterparties to develop secure transmission capabilities, but we do not have, and may be unable to put in place, secure capabilities with all of these constituents, and we may not be able to ensure that these third parties have appropriate controls in place to protect the confidentiality of such information.

While we have established policies and procedures to prevent or limit the impact of systems failures and interruptions, there can be no assurance that such events will not occur or that they will be adequately addressed if they do. In addition, we outsource certain aspects of our data processing to certain third-party providers. If our third-party providers encounter difficulties, or if we have difficulty in communication with them, our ability to adequately process and account for customer transactions could be affected, and our business operations could be adversely impacted. Threats to information security also exist in the processing of customer information through various other vendors and their personnel.

**If we do not successfully integrate Pascack Community Bank and any banks that we may acquire in the future, including without limitation Harmony Bank, which we entered into an Agreement and Plan of Merger, dated February 17, 2016, to acquire, the combined company may be adversely affected.**

Our acquisition of Pascack Bancorp and Pascack Community Bank closed on January 7, 2016. We are in the process of integrating Pascack Community Bank and, if we make additional acquisitions in the future, including without limitation Harmony Bank, we will need to integrate the acquired entities into our existing business and systems. We may experience difficulties in accomplishing this integration or in effectively managing the combined company after the acquisition of Pascack Community Bank and after any future acquisition. Any actual cost savings or revenue enhancements that we may anticipate from a future acquisition will depend on future expense levels and operating results, the timing of certain events and general industry, regulatory and business conditions. Many of these events will be beyond our control, and we cannot assure you that if we make any acquisitions in the future, we will be successful in integrating those businesses into our own.

### **ITEM 1B - Unresolved Staff Comments.**

Not Applicable.

### **ITEM 2 - Properties.**

At December 31, 2015, Lakeland Bank conducted business through 48 branch offices located in Bergen, Essex, Morris, Passaic, Somerset, Sussex, Union and Warren counties in New Jersey. Lakeland Bank also operates five New Jersey regional commercial lending centers in Bernardville, Montville, Newton, Teaneck and Wyckoff/Waldwick; and two commercial loan production offices serving Middlesex and Monmouth counties in New Jersey and the Hudson Valley region of New York. The Company's principal office is located at 250 Oak Ridge Road, Oak Ridge, New Jersey 07438.

**Table of Contents**

The aggregate net book value of premises and equipment was \$35.9 million at December 31, 2015. As of December 31, 2015, approximately 27 of the Company’s facilities were owned and approximately 28 were leased for various terms.

On January 7, 2016, the Company closed its acquisition of Pascack Bancorp, Inc., pursuant to which Pascack Bancorp, Inc. merged with and into the Company, and Pascack Community Bank (Pascack Bancorp’s subsidiary bank) merged with and into Lakeland Bank. As a result of the mergers, the Company acquired eight branches. The Company is in the process of closing three branches in overlapping areas, which will result in a net total of 53 branches for Lakeland Bank.

**ITEM 3 - Legal Proceedings.**

Certain former shareholders of Pascack Bancorp, Inc. brought a purported class action (the Action) in the Superior Court of New Jersey, Bergen County, in connection with the merger of Pascack Bancorp with and into the Company, and the merger of Pascack Community Bank with and into Lakeland Bank. The complaint alleged that the Company had aided and abetted the individual defendants (former board members of Pascack Bancorp) in their alleged breaches of fiduciary duty. The parties reached an agreement-in-principle concerning the proposed settlement of the Action on December 1 and December 2, 2015. The mergers were consummated on January 7, 2016. The parties have agreed to a stipulation of settlement which is pending court approval.

Other than as described above, there are no pending legal proceedings involving the Company or Lakeland other than those arising in the normal course of business. Management does not anticipate that the potential liability, if any, arising out of such legal proceedings will have a material effect on the financial condition or results of operations of the Company and Lakeland on a consolidated basis.

**ITEM 3A - Executive Officers of the Registrant.**

The following table sets forth the name and age of each executive officer of the Company. Each officer is appointed by the Company’s Board of Directors. Unless otherwise indicated, the persons named below have held the position indicated for more than the past five years.

Name and Age	Officer of the Company Since	Position with the Company, its Subsidiary Banks, and Business Experience
Thomas J. Shara Age 58	2008	President and CEO, Lakeland Bancorp, Inc. and Lakeland Bank (April 2, 2008 - Present); President and Chief Credit Officer (May 2007 - April 1, 2008) and Executive Vice President and Senior Commercial Banking Officer (February 2006 - May 2007), TD Banknorth, N.A.’s Mid-Atlantic Division.
Joseph F. Hurley Age 65	1999	Executive Vice President and Chief Financial Officer of the Company (November 1999 - Present).
Robert A. Vandenberg Age 64	1999	Regional President - Lakeland Bank (May 31, 2013 - Present) and Senior Executive Vice President and Chief Operating Officer of the Company (October 2008 - Present); Senior Executive Vice President and Chief Operating Officer of Lakeland Bank (October 2008 - January 29, 2013); President of Lakeland Bank (January 29, 2013 - May 31, 2013); Senior Executive Vice President and Chief Lending Officer of the Company (December 2006 - October 2008).

**Table of Contents**

Name and Age	Officer of the Company Since	Position with the Company, its Subsidiary
		Banks, and Business Experience
Stewart E. McClure, Jr. Age 65	2013	Regional President - Lakeland Bank and Senior Executive Vice President of the Company (May 31, 2013 - Present); President, Chief Executive Officer and Chief Operating Officer, and a director, of Somerset Hills Bancorp and Somerset Hills Bank (prior years to May 31, 2013).
Jeffrey J. Buonforte Age 64	1999	Executive Vice President and Senior Government Banking/Business Services Officer of the Company (June 2009 - Present).
David S. Yanagisawa Age 64	2008	Executive Vice President and Chief Lending Officer of the Company (November 2008 - Present); Senior Vice President, TD Banknorth, N.A. (February 2006 - November 2008).
James R. Noonan Age 64	2003	Executive Vice President and Chief Credit Officer of the Company (December 2003 - Present).
Ronald E. Schwarz Age 61	2009	Senior Executive Vice President and Chief Revenue Officer of the Company (January 2016 - Present); Executive Vice President and Chief Retail Officer of the Company (June 2009 - December 2015); Executive Vice President and Market Executive of Sovereign Bank (June 2006 - June 2009).
Timothy J. Matteson, Esq. Age 46	2008	Executive Vice President, General Counsel and Corporate Secretary of the Company (March 2012 to Present); Senior Vice President and General Counsel of the Company (September 2008 - March 2012); Assistant General Counsel, Israel Discount Bank (November 2007-September 2008); Senior Attorney and Senior Vice President, TD Banknorth, N.A. (February 2006 - May 2007); General Counsel and Senior Vice President, Hudson United Bancorp and Hudson United Bank (January 2005 - February 2006).

**ITEM 4 - MINE SAFETY DISCLOSURES.**

Not applicable.



**Table of Contents****PART II****ITEM 5 - MARKET FOR THE REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES.**

Shares of the common stock of Lakeland Bancorp, Inc. have been traded under the symbol LBAI on the NASDAQ Global Select Market (or the NASDAQ National Market) since February 22, 2000 and in the over the counter market prior to that date. As of December 31, 2015, there were 2,948 shareholders of record of the common stock. The following table sets forth the range of the high and low daily closing prices of the common stock as provided by NASDAQ and dividends declared for the periods presented. All information is adjusted for the Company's 5% stock dividends distributed on June 17, 2014.

	High	Low	Dividends Declared
Year ended December 31, 2015			
First Quarter	\$ 11.66	\$ 10.66	\$ 0.075
Second Quarter	12.23	11.25	0.085
Third Quarter	12.37	10.53	0.085
Fourth Quarter	12.25	10.74	0.085

	High	Low	Dividends Declared
Year ended December 31, 2014			
First Quarter	\$ 11.53	\$ 9.87	\$ 0.071
Second Quarter	11.21	9.61	0.071
Third Quarter	11.11	9.76	0.075
Fourth Quarter	12.26	9.78	0.075

Dividends on the Company's common stock are within the discretion of the Board of Directors of the Company and are dependent upon various factors, including the future earnings and financial condition of the Company and Lakeland and bank regulatory policies.

The Bank Holding Company Act of 1956 restricts the amount of dividends the Company can pay. Accordingly, dividends should generally only be paid out of current earnings, as defined.

The New Jersey Banking Act of 1948 restricts the amount of dividends paid on the capital stock of New Jersey chartered banks. Accordingly, no dividends shall be paid by such banks on their capital stock unless, following the payment of such dividends, the capital stock of the bank will be unimpaired and the bank will have a surplus of not less than 50% of its capital stock, or, if not, the payment of such dividend will not reduce the surplus of the bank. Under this limitation, approximately \$281.5 million was available for the payment of dividends from Lakeland Bank to the Company as of December 31, 2015.

Capital guidelines and other regulatory requirements may further limit the Company's and Lakeland's ability to pay dividends. See Item 1 - Business - Supervision and Regulation - Dividend Restrictions and Capital Requirements.

**Table of Contents**

The following chart compares the Company's cumulative total shareholder return (on a dividend reinvested basis) over the past five years with the NASDAQ Market Index and the Peer Group Index. The Peer Group Index is the Zacks Regional Northeast Banks Index, which consists of 95 Regional Northeast Banks.

<b>Company/Market/Peer Group</b>	<b>12/31/2010</b>	<b>12/31/2011</b>	<b>12/31/2012</b>	<b>12/31/2013</b>	<b>12/31/2014</b>	<b>12/31/2015</b>
Lakeland Bancorp, Inc.	100.00	84.33	107.31	134.06	137.14	142.49
NASDAQ Market Index	100.00	99.17	116.48	163.21	187.27	200.31
Regional Northeast Banks	100.00	94.33	110.26	140.38	150.86	159.06

**Table of Contents****Item 6 - Selected Financial Data****SELECTED CONSOLIDATED FINANCIAL DATA**

The following should be read in conjunction with Management's Discussion and Analysis of Financial Condition and Results of Operations and the Company's consolidated financial statements included in items 7 and 8 of this report. The selective financial data set forth below has been derived from the Company's audited consolidated financial statements.

	2015	2014	2013	2012	2011
<b>Years Ended December 31</b>	(in thousands except per share data)				
Interest income	\$ 127,514	\$ 122,503	\$ 114,199	\$ 110,959	\$ 117,524
Interest expense	10,874	8,937	9,657	15,446	20,111
Net interest income	116,640	113,566	104,542	95,513	97,413
Provision for loan and lease losses	1,942	5,865	9,343	14,907	18,816
Noninterest income excluding gains on investment securities and gain on debt extinguishment	19,090	17,720	18,925	17,856	16,888
Gains on sales of investment securities	241	2	839	1,049	1,229
Gain on early debt extinguishment	1,830		1,197		
Merger related expenses	1,152		2,834		
Long-term debt prepayment fee	2,407		1,209	782	800
Noninterest expenses	83,652	79,135	74,698	66,891	67,351
Income before income taxes	48,648	46,288	37,419	31,838	28,563
Income tax provision	16,167	15,159	12,450	10,096	8,712
Net income	32,481	31,129	24,969	21,742	19,851
Dividends on preferred stock and accretion				620	2,167
Net income available to common shareholders	\$ 32,481	\$ 31,129	\$ 24,969	\$ 21,122	\$ 17,684
<b>Per-Share Data(1)</b>					
Weighted average shares outstanding:					
Basic	37,844	37,749	34,742	29,000	27,901
Diluted	37,993	37,869	34,902	29,077	28,015
Earnings per share:					
Basic	\$ 0.85	\$ 0.82	\$ 0.71	\$ 0.72	\$ 0.63
Diluted	\$ 0.85	\$ 0.82	\$ 0.71	\$ 0.72	\$ 0.63
Cash dividend per common share	\$ 0.33	\$ 0.29	\$ 0.27	\$ 0.24	\$ 0.22
Book value per common share	\$ 10.57	\$ 10.01	\$ 9.28	\$ 9.00	\$ 8.56
Tangible book value per common share(2)	\$ 7.62	\$ 7.06	\$ 6.31	\$ 6.21	\$ 5.47
<b>At December 31</b>					
Investment securities available for sale and other(5)	\$ 456,436	\$ 467,295	\$ 439,044	\$ 399,092	\$ 471,944
Investment securities held to maturity	116,740	107,976	101,744	96,925	71,700
Loans and leases, net of deferred costs	2,965,200	2,653,826	2,469,016	2,146,843	2,041,575
Goodwill and other identifiable intangible assets	111,519	111,934	112,398	87,111	87,111
Total assets	3,869,550	3,538,325	3,317,791	2,918,703	2,825,950
Total deposits	2,995,572	2,790,819	2,709,205	2,370,997	2,249,653
Total core deposits(3)	2,652,251	2,510,857	2,413,119	2,067,205	1,890,101
Term borrowings	303,143	243,736	160,238	136,548	232,322
Total stockholders' equity	400,516	379,438	351,424	280,867	259,783
<b>Performance ratios</b>					
Return on Average Assets	0.89%	0.92%	0.80%	0.77%	0.71%
Return on Average Tangible Common Equity(2)	11.58%	12.21%	11.42%	12.85%	13.65%
Return on Average Equity	8.28%	8.48%	7.78%	8.42%	7.79%
Efficiency ratio(4)	60.18%	59.35%	59.74%	58.33%	56.87%
Net Interest Margin (tax equivalent basis)	3.47%	3.64%	3.69%	3.70%	3.85%
Loans to Deposits	98.99%	95.09%	91.13%	90.55%	90.75%

Edgar Filing: LAKELAND BANCORP INC - Form 10-K

<b>Capital ratios</b>					
Common Equity to Asset ratio	<b>10.35%</b>	10.72%	10.59%	9.62%	8.54%
Tangible common equity to tangible assets(2)	<b>7.69%</b>	7.81%	7.46%	6.84%	5.63%
Tier 1 leverage ratio(6)	<b>8.70%</b>	9.08%	8.90%	8.62%	8.33%
Tier 1 risk-based capital ratio(6)	<b>10.53%</b>	11.76%	11.73%	11.52%	11.23%
Total risk-based capital ratio(6)	<b>11.61%</b>	12.98%	12.98%	12.77%	13.39%
CETI Ratio(6)	<b>9.54%</b>	NA	NA	NA	NA

-25-

**Table of Contents**

- (1) Restated for 5% stock dividends in 2014, 2012 and 2011.
- (2) A non-GAAP financial measure. See Non-GAAP Financial Measures for a reconciliation of such measures to data calculated in accordance with generally accepted accounting principles.
- (3) Core deposits represent all deposits with the exception of time deposits.
- (4) Ratio represents non-interest expense, excluding other real estate expense, other repossessed asset expense, long-term debt prepayment fee, merger related expenses, provision for unfunded lending commitments and core deposit amortization, as a percentage of total revenue (calculated on a tax equivalent basis), excluding gains (losses) on securities and gain on debt extinguishment. Total revenue represents net interest income (calculated on a tax equivalent basis) plus non-interest income.
- (5) Includes investment in Federal Home Loan Bank and other membership stock, at cost.
- (6) Beginning March 31, 2015, these ratios were calculated according to the Basel III capital rules that took effect on January 1, 2015.

---

**Table of Contents**

**ITEM 7 - MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

This section presents a review of Lakeland Bancorp, Inc.'s consolidated results of operations and financial condition. You should read this section in conjunction with the selected consolidated financial data that is presented on the preceding page as well as the accompanying consolidated financial statements and notes to financial statements. As used in the following discussion, the term "Company" refers to Lakeland Bancorp, Inc. and "Lakeland" refers to the Company's wholly owned banking subsidiary - Lakeland Bank.

***Statements Regarding Forward-Looking Information***

The information disclosed in this document includes various forward-looking statements that are made in reliance upon the safe harbor provisions of the Private Securities Litigation Reform Act of 1995 with respect to credit quality (including delinquency trends and the allowance for loan and lease losses), corporate objectives, and other financial and business matters. The words "anticipates," "projects," "intends," "estimates," "expects," "believes," "plans," "may," "will," "should," "could," and other similar expressions are intended to identify such forward-looking statements. Company cautions that these forward-looking statements are necessarily speculative and speak only as of the date made, and are subject to numerous assumptions, risks and uncertainties, all of which may change over time. Actual results could differ materially from such forward-looking statements.

In addition to the risk factors disclosed in Item 1A in this Annual Report on Form 10-K, the following factors, among others, could cause the Company's actual results to differ materially and adversely from such forward-looking statements: changes in the financial services industry and the U.S. and global capital markets, changes in economic conditions nationally, regionally and in the Company's markets, the nature and timing of actions of the Federal Reserve Board and other regulators, the nature and timing of legislation affecting the financial services industry including but not limited to the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, government intervention in the U.S. financial system, changes in levels of market interest rates, pricing pressures on loan and deposit products, credit risks of Lakeland's lending and leasing activities, customers' acceptance of Lakeland's products and services, competition, the failure to realize anticipated efficiencies and synergies from the merger of Pascack Bancorp into the Company, and Pascack Community Bank into Lakeland Bank, and failure to obtain Harmony Bank shareholder or regulatory approval for the merger of Harmony Bank into Lakeland and failure to realize anticipated efficiencies and synergies if the merger of Harmony Bank into Lakeland is consummated.

The above-listed risk factors are not necessarily exhaustive, particularly as to possible future events, and new risk factors may emerge from time to time. Certain events may occur that could cause the Company's actual results to be materially different than those described in the Company's periodic filings with the Securities and Exchange Commission. Any statements made by the Company that are not historical facts should be considered to be forward-looking statements. The Company is not obligated to update and does not undertake to update any of its forward-looking statements made herein.

***Strategy***

The Company, through its wholly owned subsidiary, Lakeland Bank, currently operates 53 banking offices located in Northern and Central New Jersey. Lakeland offers a broad range of lending, depository, and related financial services to individuals and small to medium sized businesses located in its market areas. Lakeland also offers a broad range of consumer banking services, including lending, depository, safe deposit services and other non-traditional banking services.

Lakeland's growth has come from a combination of organic growth and acquisitions. Since 1998 when Lakeland completed its first acquisition, and through 2015, Lakeland has opened 27 new branch offices (including acquired branches). In 2015, the Company opened two new Loan Production Offices (LPOs) that

---

**Table of Contents**

allowed Lakeland to expand geographically in New Jersey and to enter New York State for the first time. In addition to organic growth, through December 31, 2015, the Company has acquired five community banks with an aggregate asset total of approximately \$1.1 billion at the date of acquisition, including the acquisition of the Somerset Hills Bank and its parent, Somerset Hills Bancorp, which closed on May 31, 2013. Additionally, on January 7, 2016, the Company completed its acquisition of Pascack Community Bank and its parent company Pascack Bancorp, with eight branches and an asset total of approximately \$390.0 million. Three of the eight Pascack Community Bank Branches will be merged with Lakeland branches, resulting in 53 branches at Lakeland. All acquired banks have been merged into Lakeland and their holding companies, if applicable, have been merged into the Company. On February 18, 2016, the Company announced that it entered into a Definitive Agreement and Plan of Merger to acquire Harmony Bank. Harmony Bank will be merged into Lakeland Bank with Lakeland Bank as the surviving bank. The Company's strategy is to continue growth both organically and through acquisition should opportunities allow. The Company continues to evaluate opportunities to increase market share by expanding within existing and contiguous markets.

The Company's strategic aim is to provide an adequate return to its shareholders by focusing on profitable growth through services that meet the needs of its customers in its market areas. This will be accomplished by continuing to offer commercial and consumer loan, deposit and other financial product services in a changing economic and technological environment. The Company recognizes that there are more service delivery channels than the traditional branch office and has offered internet banking, mobile banking and cash management services to meet the needs of its business and consumer customers.

The Company's results of operations are primarily dependent upon net interest income, the difference between interest earned on interest-earning assets and the interest paid on interest-bearing liabilities. For information on how interest rate change can influence the Company's net interest income and how the Company manages its net interest income, see "Interest Rate Risk" below.

The Company generates non-interest income such as income from retail and business account fees, loan servicing fees, loan origination fees, appreciation in the cash surrender value of bank owned life insurance, income from loan or securities sales, fees from wealth management services and investment product sales, income from the origination and sale of residential mortgages and other fees. The Company's operating expenses consist primarily of compensation and benefits expense, occupancy and equipment expense, data processing expense, the amortization of intangible assets, marketing and advertising expense and other general and administrative expenses. The Company's results of operations are also affected by general economic conditions, changes in market interest rates, changes in asset quality, changes in asset values, actions of regulatory agencies and government policies.

The Company continues to control its expenses by continually reviewing its ongoing noninterest expense including evaluating its salary expense, its ongoing service contract expense, marketing expenses and other expenses. The Company also decreases its expenses by evaluating its infrastructure, which includes the consolidating and closing of branches in markets where it may have more branches than necessary. The Company closed one branch in 2014, three branches in 2015 and anticipates that trend to continue in 2016.

***Critical Accounting Policies, Judgments and Estimates***

The accounting and reporting policies of the Company and Lakeland conform with accounting principles generally accepted in the United States of America ( "U.S. GAAP" ) and predominant practices within the banking industry. The preparation of financial statements 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. These estimates and assumptions also affect reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates. Significant estimates implicit in these financial statements are as follows. For additional accounting policies and detail, refer to Note 1 to the consolidated financial statements included in item 8 of this report.

---

## Table of Contents

**Allowance for loan and lease losses.** The allowance for loan and lease losses is established through a provision for loan and lease losses charged to expense. Loan principal considered to be uncollectible by management is charged against the allowance for loan and lease losses. The allowance is an amount that management believes will be adequate to absorb losses on existing loans and leases that may become uncollectible based upon an evaluation of known and inherent risks in the loan and lease portfolio. The evaluation takes into consideration such factors as changes in the nature and size of the loan and lease portfolio, overall portfolio quality, specific problem loans and leases, and current economic conditions which may affect the borrowers' ability to pay. The evaluation also analyzes historical losses by loan and lease category, and considers the resulting loss rates when determining the reserves on current loan and lease total amounts. Additionally, management assesses the loss emergence period for each loan segment and adjusts each historical loss factor accordingly. The loss emergence period is the estimated time from the date of a loss event (such as a personal bankruptcy) to the actual recognition of the loss (typically via the first full or partial loan charge-off), and is determined based upon a study of our past loss experience by loan segment. Loss estimates for specified problem loans and leases are also detailed. All of the factors considered in the analysis of the adequacy of the allowance for loan and lease losses may be subject to change. To the extent actual outcomes differ from management estimates, additional provisions for loan and lease losses may be required that would adversely impact earnings in future periods.

The determination of the adequacy of the allowance for loan and lease losses and the periodic provisioning for estimated losses included in the consolidated financial statements is the responsibility of management and the Board of Directors. The evaluation process is undertaken on a quarterly basis.

Methodology employed for assessing the adequacy of the allowance consists of the following criteria:

The establishment of specific reserve amounts for all specifically identified classified loans and leases that have been designated as requiring attention by Lakeland.

The establishment of reserves for pools of homogeneous types of loans and leases not subject to specific review, including impaired loans under \$500,000, leases, 1-4 family residential mortgages, and consumer loans.

The establishment of reserve amounts for the non-classified loans and leases in each portfolio based upon the historical average loss experience as modified by management's assessment of the loss emergence period for these portfolios and management's evaluation of key environmental factors.

Consideration is given to the results of ongoing credit quality monitoring processes, the adequacy and expertise of Lakeland's lending staff, underwriting policies, loss histories, delinquency trends, and the cyclical nature of economic and business conditions. Since many of Lakeland's loans depend on the sufficiency of collateral as a secondary source of repayment, any adverse trend in the real estate markets could affect underlying values available to protect Lakeland from loss.

A loan that management designates as impaired is reviewed for charge-off when it is placed on non-accrual status with a resulting charge-off if the loan is not secured by collateral having sufficient liquidation value to repay the loan, and the loan is not in the process of collection. Charge-offs are recommended by the Chief Credit Officer and approved by the Board.

Loans and leases are considered impaired when, based on current information and events, it is probable that Lakeland will be unable to collect all amounts due in accordance with the original contractual terms of the loan agreement, including scheduled principal and interest payments. Impairment is measured based on the present value of expected cash flows discounted at the loan's effective interest rate, or as a practical expedient, Lakeland may measure impairment based on a loan's observable market price, or the fair value of the collateral, less estimated costs to sell, if the loan is collateral-dependent. Regardless of the measurement method, Lakeland measures impairment based on the fair value of the collateral when it is determined that foreclosure is probable.



**Table of Contents**

Most of Lakeland's impaired loans are collateral-dependent. Lakeland groups impaired commercial loans under \$500,000 into a homogeneous pool and collectively evaluates them. Interest received on impaired loans and leases may be recorded as interest income. However, if management is not reasonably certain that an impaired loan and lease will be repaid in full, or if a specific time frame to resolve full collection cannot yet be reasonably determined, all payments received are recorded as reductions of principal.

**Fair value measurements and fair value of financial instruments.** Fair values of financial instruments are volatile and may be influenced by a number of factors, including market interest rates, prepayment speeds, discount rates, credit ratings and yield curves. Fair values for investment securities are based on quoted market prices, where available. If quoted market prices are not available, fair values are based on the quoted prices of similar instruments or an estimate of fair value by using a range of fair value estimates in the market place as a result of the illiquid market specific to the type of security.

When the fair value of a security is below its amortized cost, and depending on the length of time the condition exists and the extent the fair value is below amortized cost, additional analysis is performed to determine whether an other-than-temporary impairment condition exists. Available-for-sale and held-to-maturity securities are analyzed quarterly for possible other-than-temporary impairment. The analysis considers (i) the length of time and the extent to which the fair value has been less than cost, (ii) the financial condition and near-term prospects of the issuer which may include projections of cash flows, and (iii) the intent and ability of the Company to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value. Often, the information available to conduct these assessments is limited and rapidly changing, making estimates of fair value subject to judgment. If actual information or conditions are different than estimated, the extent of the impairment of the security may be different than previously estimated, which could have a material effect on the Company's results of operations and financial condition.

**Income taxes.** The Company accounts for income taxes under the asset and liability method of accounting for income taxes. Deferred tax assets and liabilities are determined based on the difference between the financial statement and tax bases of assets and liabilities as measured by the enacted tax rates that will be in effect when these differences reverse. Deferred tax expense is the result of changes in deferred tax assets and liabilities. The principal types of differences between assets and liabilities for financial statement and tax return purposes are allowance for loan and lease losses, core deposit intangible, deferred loan costs and deferred compensation.

The Company evaluates the realizability of its deferred tax assets by examining its earnings history and projected future earnings and by assessing whether it is more likely than not that carryforwards would not be realized. Based upon the majority of the Company's deferred tax assets having no expiration date, the Company's earnings history, and the projections of future earnings, the Company's management believes that it is more likely than not that all of the Company's deferred tax assets as of December 31, 2015 will be realized.

The Company evaluates tax positions that may be uncertain using a recognition threshold of more-likely-than-not, and a measurement attribute for all tax positions taken or expected to be taken on a tax return, in order for those tax positions to be recognized in the financial statements. Additional information regarding the Company's uncertain tax positions is set forth in Note 9 to the Notes to the audited Consolidated Financial Statements contained herein.

**Goodwill and other identifiable intangible assets.** The Company reviews goodwill for impairment annually as of November 30 or when circumstances indicate a potential for impairment at the reporting unit level. U.S. GAAP requires at least an annual review of the fair value of a reporting unit that has goodwill in order to determine if it is more likely than not (that is, a likelihood of more than 50%) that the fair value of a reporting unit is less than its carrying amount, including goodwill. If this qualitative test determines it is unlikely (less than 50% probability) the carrying value of the reporting unit is less than its fair value, then the company does not have to perform a Step One impairment test. If the probability is greater than 50%, a Step One goodwill impairment test is required. The Step One test compares the fair value of each reporting unit to the carrying value of its net assets, including goodwill. The Company has determined that it has one reporting unit, Community Banking.

---

## **Table of Contents**

The Company performed a qualitative analysis to determine whether the weight of evidence, the significance of all identified events and circumstances indicated a greater than 50% likelihood existed that the carrying value of the reporting unit exceeded its fair value and if a Step One test would be required. The Company identified nine qualitative assessments that are relative to the banking industry and to the Company. These factors included macroeconomic factors, banking industry conditions, banking merger and acquisition trends, Lakeland's historical performance, the Company's stock price, the expected performance of Lakeland, the change of control premium of the Company versus its peers and other miscellaneous factors. After reviewing and weighting these factors, the Company, as well as a third party adviser, determined as of November 30, 2015 that there was a less than 50% probability that the fair value of the Company was less than its carrying amount. Therefore, no Step One test was required.

### ***Use of Non-GAAP Disclosures***

Reported amounts are presented in accordance with U.S. GAAP. The Company's management believes that the supplemental non-GAAP information, which consists of measurements and ratios based on tangible equity, tangible assets and the efficiency ratio, which excludes certain items considered to be non-recurring from earnings, is utilized by regulators and market analysts to evaluate a company's financial condition and therefore, such information is useful to investors. These disclosures should not be viewed as a substitute for financial results determined in accordance with U.S. GAAP, nor are they necessarily comparable to non-GAAP performance measures which may be presented by other companies.

### ***Financial Overview***

The year ended December 31, 2015 represented a year of continued growth for the Company. As discussed in this management's discussion and analysis:

Net income for the year ended December 31, 2015 was \$32.5 million, or \$0.85 per diluted share, a 4% increase compared to \$31.1 million, or \$0.82 per diluted share, for 2014. Excluding the impact of \$1.6 million in net non-routine transactions, described below, net income for the year ended December 31, 2015 was \$33.8 million, an 8% increase compared to 2014, or \$0.88 per diluted share.

The \$1.6 million in net non-routine transactions in 2015 included \$1.2 million of expenses related to the Pascack Bancorp, Inc. (Pascack Bancorp) merger, \$2.4 million of prepayment fees from the repayment of \$20.0 million of 4.44% long-term debt, \$1.8 million of realized gain from the redemption of \$10.0 million of trust preferred debt, and \$173,000 in related net realized gains on the sale of securities. Merger expenses primarily include the cost of legal, accounting, and investment banking services as well as technology costs.

Total loans increased \$312.3 million, or 12%, from December 31, 2014 to December 31, 2015. Commercial real estate loans increased \$231.8 million, or 15%, from December 31, 2014 to December 31, 2015. Commercial, industrial and other loans increased \$68.8 million or 29% in the same time period.

Total deposits were \$3.00 billion at December 31, 2015, an increase of \$204.8 million, or 7%, from December 31, 2014. Noninterest-bearing demand deposits, which totaled \$693.7 million at year-end 2015, increased by \$47.7 million, or 7%, from December 31, 2014. Noninterest-bearing demand deposits represented 23% of total deposits at year-end 2015.

The Company's net interest margin at 3.47% for 2015 was 17 basis points lower than 2014.

The provision for loan and lease losses totaled \$1.9 million in 2015, which was 67% lower than the \$5.9 million reported for 2014. Net charge-offs at \$1.8 million (0.06% of average loans) for 2015 were 65% lower than the \$5.0 million (0.19% of average loans) for 2014.

Edgar Filing: LAKELAND BANCORP INC - Form 10-K

During the fourth quarter of 2015, Pascack Bancorp shareholders approved the merger of Pascack Bancorp with and into the Company. This merger, along with the merger of Pascack Community Bank

---

**Table of Contents**

with and into Lakeland Bank, was consummated on January 7, 2016, adding approximately \$390.0 million in total assets to the Company. The Company also acquired eight branches in the merger. The Company intends to close a total of three branches in overlapping areas, which will result in a net total of 53 branches for Lakeland Bank. On February 18, the Company announced that it entered into a Definitive Agreement and Plan of Merger to acquire Harmony Bank. Harmony Bank will be merged into Lakeland Bank with Lakeland Bank as the surviving bank. For more information on the Pascack and Harmony acquisitions, please see Note 2 Acquisitions.

***Net Income***

Net income for 2015 was \$32.5 million or \$0.85 per diluted share compared to net income of \$31.1 million or \$0.82 per diluted share in 2014. Net interest income at \$116.6 million for 2015 increased \$3.1 million compared to 2014 due to a \$5.0 million increase in interest income partially offset by a \$1.9 million increase in interest expense. The increase in net interest income reflects an increase in interest earning assets resulting from organic growth.

***Net Interest Income***

Net interest income is the difference between interest income on earning assets and the cost of funds supporting those assets. The Company's net interest income is determined by: (i) the volume of interest-earning assets that it holds and the yields that it earns on those assets, and (ii) the volume of interest-bearing liabilities that it has assumed and the rates that it pays on those liabilities.

Net interest income for 2015 on a tax-equivalent basis was \$117.5 million, representing an increase of \$3.0 million, or 3%, from the \$114.5 million earned in 2014. The increase in net interest income primarily resulted from growth in average interest-earning assets of \$242.8 million. The net interest margin decreased from 3.64% in 2014 to 3.47% in 2015 primarily as a result of a 13 basis point decline in the yield on interest earning assets coupled with a five basis point increase in the cost of interest bearing liabilities. The decrease in the net interest margin was somewhat mitigated by an increase in interest income earned on free funds (interest earning assets funded by non-interest bearing liabilities) resulting from an increase in average non-interest bearing deposits of \$42.9 million. The components of net interest income will be discussed in greater detail below.

**Interest income and expense volume/rate analysis.** The following table shows the impact that changes in average balances of the Company's assets and liabilities and changes in average interest rates have had on the Company's net interest income over the past three years. This information is presented on a tax equivalent basis assuming a 35% tax rate. If a change in interest income or expense is attributable to a change in volume and a change in rate, the amount of the change is allocated proportionately.

**Table of Contents****INTEREST INCOME AND EXPENSE VOLUME/RATE ANALYSIS**

(tax equivalent basis, in thousands)

	2015 vs. 2014			2014 vs. 2013		
	Increase (Decrease) Due to Change in: Volume	(Decrease) Rate	Total Change	Increase (Decrease) Due to Change in: Volume	(Decrease) Rate	Total Change
<b>Interest Income</b>						
Loans and leases	\$ 8,309	\$ (3,601)	\$ 4,708	\$ 10,473	\$ (4,215)	\$ 6,258
Taxable investment securities and other	847	(324)	523	938	1,117	2,055
Tax-exempt investment securities	(159)	(167)	(326)	(4)	24	20
Federal funds sold	(1)	(8)	(9)	(14)	(8)	(22)
<b>Total interest income</b>	<b>8,996</b>	<b>(4,100)</b>	<b>4,896</b>	<b>11,393</b>	<b>(3,082)</b>	<b>8,311</b>
<b>Interest Expense</b>						
Savings deposits	8	2	10	9	(30)	(21)
Interest-bearing transaction accounts	135	151	286	369	(750)	(381)
Time deposits	109	286	395	(164)	(459)	(623)
Borrowings	1,352	(106)	1,246	694	(389)	305
<b>Total interest expense</b>	<b>1,604</b>	<b>333</b>	<b>1,937</b>	<b>908</b>	<b>(1,628)</b>	<b>(720)</b>
<b>NET INTEREST INCOME</b>						
<b>(TAX EQUIVALENT BASIS)</b>	<b>\$ 7,392</b>	<b>\$ (4,433)</b>	<b>\$ 2,959</b>	<b>\$ 10,485</b>	<b>\$ (1,454)</b>	<b>\$ 9,031</b>

The following table reflects the components of the Company's net interest income, setting forth for the years presented, (1) average assets, liabilities and stockholders' equity, (2) interest income earned on interest-earning assets and interest expense paid on interest-bearing liabilities, (3) average yields earned on interest-earning assets and average rates paid on interest-bearing liabilities, (4) the Company's net interest spread (i.e., the average yield on interest-earning assets less the average cost of interest-bearing liabilities) and (5) the Company's net interest margin. Rates are computed on a tax equivalent basis assuming a 35% tax rate.

**Table of Contents****CONSOLIDATED STATISTICS ON A TAX EQUIVALENT BASIS**

	2015			2014			2013		
	Average Balance	Interest Income/ Expense	Average rates earned/ paid	Average Balance	Interest Income/ Expense	Average rates earned/ paid	Average Balance	Interest Income/ Expense	Average rates earned/ paid
	(dollars in thousands)								
<b>Assets</b>									
Interest-earning assets:									
Loans and leases (A)	\$ 2,773,601	\$ 115,295	4.16%	\$ 2,568,056	\$ 110,587	4.31%	\$ 2,317,158	\$ 104,329	4.50%
Taxable investment securities and other	512,145	10,563	2.06%	470,144	10,040	2.14%	423,249	7,985	1.89%
Tax-exempt securities	69,307	2,451	3.54%	73,662	2,777	3.77%	73,768	2,757	3.74%
Federal funds sold (B)	35,059	62	0.18%	35,404	71	0.20%	41,870	93	0.22%
<b>Total interest-earning assets</b>	<b>3,390,112</b>	<b>128,371</b>	<b>3.79%</b>	<b>3,147,266</b>	<b>123,475</b>	<b>3.92%</b>	<b>2,856,045</b>	<b>115,164</b>	<b>4.03%</b>
Noninterest earning assets:									
Allowance for loan and lease losses	(31,062)			(30,146)			(30,053)		
Other assets	289,786			283,341			276,868		
<b>TOTAL ASSETS</b>	<b>\$ 3,648,836</b>			<b>\$ 3,400,461</b>			<b>\$ 3,102,860</b>		
<b>Liabilities and Stockholders Equity</b>									
Interest-bearing liabilities:									
Savings accounts	\$ 399,431	\$ 212	0.05%	\$ 384,715	\$ 202	0.05%	\$ 370,980	\$ 223	0.06%
Interest-bearing transaction accounts	1,511,954	3,652	0.24%	1,454,967	3,366	0.23%	1,341,691	3,747	0.28%
Time deposits	303,682	1,891	0.62%	283,905	1,496	0.53%	309,384	2,119	0.68%
Borrowings	328,936	5,119	1.56%	241,820	3,873	1.60%	169,048	3,568	2.11%
<b>Total interest-bearing liabilities</b>	<b>2,544,003</b>	<b>10,874</b>	<b>0.43%</b>	<b>2,365,407</b>	<b>8,937</b>	<b>0.38%</b>	<b>2,191,103</b>	<b>9,657</b>	<b>0.44%</b>
Noninterest-bearing liabilities:									
Demand deposits	695,630			652,685			576,421		
Other liabilities	16,982			15,159			14,513		
Stockholders equity	392,221			367,210			320,823		
<b>TOTAL LIABILITIES AND STOCKHOLDERS EQUITY</b>	<b>\$ 3,648,836</b>			<b>\$ 3,400,461</b>			<b>\$ 3,102,860</b>		
Net interest income/spread		117,497	3.36%		114,538	3.54%		105,507	3.59%
Tax equivalent basis adjustment		857			972			965	
<b>NET INTEREST INCOME</b>		<b>\$ 116,640</b>			<b>\$ 113,566</b>			<b>\$ 104,542</b>	
<b>Net interest margin (C)</b>			<b>3.47%</b>			<b>3.64%</b>			<b>3.69%</b>

(A) Includes non-accrual loans, the effect of which is to reduce the yield earned on loans, and deferred loan fees.

(B) Includes interest-bearing cash accounts.

(C) Net interest income on a tax equivalent basis divided by interest-earning assets.

Interest income on a tax equivalent basis increased from \$123.5 million in 2014 to \$128.4 million in 2015, an increase of \$4.9 million, or 4%. The increase in interest income was primarily due to a \$205.5 million increase in average loans and leases partially offset by a decrease in the yield on interest earning assets. The yield on average loans and leases at 4.16% in 2015 was 15 basis points lower than 2014, resulting primarily from strong growth in loans and leases originated or refinanced at lower rates. The yield on average taxable and tax exempt investment securities

## Edgar Filing: LAKELAND BANCORP INC - Form 10-K

decreased by eight and 23 basis points, respectively, compared to 2014. The decrease in yield on tax exempt investment securities was primarily due to maturing securities at higher rates and new purchases at lower rates.

Interest income on a tax equivalent basis increased from \$115.2 million in 2013 to \$123.5 million in 2014, an increase of \$8.3 million, or 7%. The increase in interest income was primarily due to a \$250.9 million increase

---

**Table of Contents**

in average loans and leases partially offset by a decrease in the yield on interest earning assets. The increase in average loans and leases is due primarily to the acquisition of Somerset Hills loans and leases which totaled \$243.9 million at the time of acquisition as well as organic growth. The decline in yield on earning assets is primarily a result of loans being refinanced at lower rates and lower yields on new loans. The yield on average loans and leases at 4.31% in 2014 was 19 basis points lower than 2013. The yield on average taxable and tax exempt investment securities increased by 25 basis points and three basis points, respectively, compared to 2013.

Total interest expense increased from \$8.9 million in 2014 to \$10.9 million in 2015, an increase of \$1.9 million, or 22%. The cost of average interest-bearing liabilities increased from 0.38% in 2014 to 0.43% in 2015. The increase in the cost of funds was primarily due to increases in average time deposits and borrowings. Borrowings as a percent of interest-bearing liabilities increased from 10% in 2014, to 13% in 2015 as average borrowings increased \$87.1 million in that time period to help fund loan growth. Borrowings at a rate of 1.56% have a higher cost than interest bearing deposits which had an average cost of 0.26% 2015. Additionally, higher cost average time deposits totaling \$303.7 million increased \$19.8 million compared to 2014. Because loan growth exceeded growth in core deposits in 2015, the Company bid for higher cost time deposits and used term borrowings from the Federal Home Loan Bank of New York to fund loan growth.

Total interest expense decreased from \$9.7 million in 2013 to \$8.9 million in 2014, a decrease of \$720,000, or 7%. The cost of average interest-bearing liabilities decreased from 0.44% in 2013 to 0.38% in 2014 as a result of declining rates and a change in mix of interest earning liabilities. The decrease in the cost of funds was due primarily to the continuing low rate environment which resulted in a five basis point reduction in the cost of interest-bearing transaction accounts, a 15 basis point reduction in the cost of time deposits and a 51 basis point reduction in the cost of borrowings. The cost of borrowings declined primarily as a result of new borrowings at lower rates as well as restructurings of other long-term borrowings in 2013. From 2013 to 2014, average savings accounts and interest-bearing transaction accounts increased by \$13.7 million and \$113.3 million, respectively. Average rates paid on interest-bearing liabilities declined in all categories.

***Net Interest Margin***

Net interest margin is calculated by dividing net interest income on a fully taxable equivalent basis by average interest-earning assets. The Company's net interest margin was 3.47%, 3.64% and 3.69% for 2015, 2014 and 2013, respectively. The decreases in net interest margin was primarily a result of the decrease in yield on interest-earning assets.

***Provision for Loan and Lease Losses***

In determining the provision for loan and lease losses, management considers national and local economic conditions; trends in the portfolio including orientation to specific loan types or industries; experience, ability and depth of lending management in relation to the complexity of the portfolio; adequacy and adherence to policies, procedures and practices; levels and trends in delinquencies, impaired loans and leases and net charge-offs and the results of independent third party loan review.

The provision for loan and lease losses decreased from \$5.9 million in 2014 to \$1.9 million in 2015. The lower provision during 2015 was primarily a result of reduced net charge-offs at \$1.8 million (0.06% of average loans), which were 65% lower than the \$5.0 million (0.19% of average loans) for 2014.

The provision for loan and lease losses decreased from \$9.3 million in 2013 to \$5.9 million in 2014. The lower provision during 2014 was primarily a result of reduced net charge-offs at \$5.0 million (0.19% of average loans), which were 41% lower than the \$8.5 million (0.36% of average loans) for 2013.

***Noninterest Income***

Noninterest income at \$21.2 million in 2015 increased by \$3.4 million, or 19%, compared to 2014. Included in noninterest income during 2015 was a \$1.8 million pre-tax gain on redemption and extinguishment of \$10.0



**Table of Contents**

million of Lakeland Bancorp Capital Trust IV debentures and \$241,000 in gain on sales and calls of investment securities. Excluding these two items, noninterest income would have been \$19.1 million, a \$1.4 million increase compared to 2014. Gains on sales of loans at \$1.7 million in 2015 was \$1.1 million higher than 2014 due to increased origination and sale of residential mortgages. Income on bank owned life insurance at \$2.0 million in 2015 was \$564,000 greater than 2014 due primarily to death benefits received. Service charges on deposit accounts at \$10.0 million decreased \$499,000, or 5%, primarily due to a decline in overdraft fees. Other income totaling \$800,000 in 2015 was \$263,000 higher than 2014. Within other income, the Company recorded \$396,000 in swap income compared to no swap income in 2014. The increase in swap income was partially offset by loss on disposal of assets relating to branch closures in 2015. Noninterest income represented 15% of total revenue in 2015. (Total revenue is defined as net interest income plus noninterest income).

Noninterest income decreased \$3.2 million, or 15%, to \$17.7 million in 2014 compared to 2013. In 2013 the Company recorded a \$1.2 million pre-tax gain on the purchase and early extinguishment of \$9.0 million of Lakeland Bancorp Capital Trust I debentures. Additionally, gain on sales of investment securities was \$839,000 in 2013 compared to \$2,000 in 2014. Other income at \$537,000 in 2014 was \$796,000 lower than 2013. Within other income in 2014, the Company recorded no swap income and \$129,000 in gains on sales of other real estate owned compared to \$181,000 and \$749,000, respectively, in 2013. Noninterest income represented 13% of total revenue in 2014.

***Noninterest Expense***

Noninterest expense totaling \$87.2 million increased \$8.1 million in 2015 compared to 2014. Included in noninterest expense during 2015 was \$2.4 million in long term debt prepayment fees and \$1.2 million in merger related expenses. Excluding these two items, total noninterest expense would have been \$83.7 million, a \$4.5 million increase compared to 2014. Salary and employee benefits at \$48.6 million increased by \$3.5 million, or 8%, primarily due to the two new LPOs, as well as year-over-year incremental salary increases, pension expenses, increasing benefit costs and benefit increases. Furniture and equipment increased \$325,000 compared to 2014 due primarily to an increase in service contract and software licencing costs. Stationary, supplies and postage increased \$126,000 compared to 2014 primarily due to special mailings and expenses related to the opening of the new loan production offices. Marketing expense at \$1.6 million in 2015 decreased \$439,000 compared to 2014 primarily due to website redesign and TV commercial creation expenses during 2014 that the Company did not have in 2015. Data processing expense at \$1.5 million increased \$279,000 compared to 2014 due primarily to increases related to the Company's mobile offerings. In 2015, other real estate owned and other repossessed asset expense at \$181,000 decreased \$53,000 compared to last year as a result of fewer transfers of loans into other real estate. Other expenses at \$8.9 million increased \$669,000 compared to 2014, due primarily to a \$929,000 increase in the provision for unfunded lending commitments resulting from an increase in unfunded commercial commitments. The increase in provision for unfunded lending commitments was partially offset by a decline in professional fees.

Noninterest expense totaling \$79.1 million increased \$394,000 from 2013 to 2014. There were no long term debt prepayment fees or merger related expenses in 2014 compared to \$1.2 million and \$2.8 million, respectively, in 2013. Excluding these nonrecurring expenses, noninterest expense increased \$4.4 million. Salary and employee benefits at \$45.2 million increased by \$3.3 million, or 8%, primarily due to increased staffing resulting from the Somerset Hills merger. Also included in compensation expense in 2014 was the accrual of \$293,000 in costs associated with the termination of a pension plan. Net occupancy expense at \$8.9 million in 2014 increased \$791,000 from 2013, due primarily to expenses relating to the six new branch locations acquired in the Somerset Hills acquisition and increased snow removal expenses during the first quarter of 2014. Furniture and equipment expense at \$6.6 million increased \$424,000 due primarily to the new branches previously mentioned and increased service contract expenses. Data processing expense at \$1.2 million in 2014 decreased \$221,000 compared to 2013, while ATM and debit card expense at \$1.4 million increased \$72,000 or 5%. Other real estate owned and other repossessed assets expense at \$234,000 increased \$210,000 compared to 2013. Other expenses at \$8.3 million decreased \$179,000 compared to 2013, due primarily to decreases in consulting expense, professional fees, legal fees and loan related expenses.

**Table of Contents**

The efficiency ratio, a non-GAAP measure, expresses the relationship between noninterest expense (excluding other real estate and other repossessed asset expense, long-term debt repayment fees, merger related expenses, provision for unfunded lending commitments and core deposit amortization) to total tax-equivalent revenue (excluding gains (losses) on securities and gain on debt extinguishment). In 2015, the Company's efficiency ratio on a tax equivalent basis was 60.18% compared to 59.35% in 2014. The efficiency ratio was 59.74% in 2013.

	2015	For the year ended December 31,			2011
		2014	2013	2012	
		(dollars in thousands)			
<b>Calculation of efficiency ratio (a non-GAAP measure)</b>					
Total non-interest expense	\$ 87,211	\$ 79,135	\$ 78,741	\$ 67,673	\$ 68,151
Less:					
Amortization of core deposit intangibles	(415)	(464)	(288)		(577)
Other real estate owned and other repossessed asset expense	(181)	(234)	(24)	(99)	(780)
Merger related expenses	(1,152)		(2,834)		
Long-term debt prepayment fee	(2,407)		(1,209)	(782)	(800)
Provision for unfunded lending commitments	(864)	65	(55)	(93)	(375)
<b>Non-interest expense, as adjusted</b>	<b>\$ 82,192</b>	<b>\$ 78,502</b>	<b>\$ 74,331</b>	<b>\$ 66,699</b>	<b>\$ 65,619</b>
Net interest income	\$ 116,640	\$ 113,566	\$ 104,542	\$ 95,513	\$ 97,413
Noninterest income	21,161	17,722	20,961	18,905	18,117
Total revenue	137,801	131,288	125,503	114,418	115,530
Plus: Tax-equivalent adjustment on municipal securities	857	972	965	981	1,080
Less: Gains on sales of investment securities and debt extinguishment	(2,071)	(2)	(2,036)	(1,049)	(1,229)
<b>Total revenue, as adjusted</b>	<b>\$ 136,587</b>	<b>\$ 132,258</b>	<b>\$ 124,432</b>	<b>\$ 114,350</b>	<b>\$ 115,381</b>
Efficiency ratio (Non-GAAP)	60.18%	59.35%	59.74%	58.33%	56.87%

**Income Taxes**

The Company's effective income tax rate was 33.2%, 32.7% and 33.3%, in the years ended December 31, 2015, 2014 and 2013, respectively. The effective tax rate increase in 2015 from 2014 was primarily a result of a decrease in tax advantaged items as a percentage of pre-tax income, as well as non-tax deductible merger related expenses included in pre-tax income in 2015. The effective tax rate decrease in 2014 from 2013 was primarily a result of non-tax deductible merger related expenses included in pre-tax income in 2013, which resulted in a higher effective tax rate in 2013. Tax advantaged items include interest income on tax-exempt securities and income on bank owned life insurance.

**Financial Condition**

Total assets increased from \$3.54 billion on December 31, 2014 to \$3.87 billion on December 31, 2015, an increase of \$331.2 million, or 9%. Total loans were \$2.97 billion, an increase of \$312.3 million, or 12%, from \$2.66 billion at December 31, 2014. Total deposits were \$3.00 billion, an increase of \$204.8 million from December 31, 2014. Total assets at year-end 2014 increased \$220.5 million, or 7%, from year-end 2013.

**Loans and Leases**

Lakeland primarily serves Northern and Central New Jersey, the Hudson Valley region in New York and the surrounding areas. Its equipment finance division serves a broader market with a primary focus on the Northeast. All of its borrowers are U.S. residents or entities.



**Table of Contents**

Gross loans and leases at \$2.97 billion increased by \$312.3 million, or 12%, from December 31, 2014 primarily in the commercial loans secured by real estate category. Commercial loans secured by real estate increased \$231.8 million, or 15%, from December 31, 2014 to December 31, 2015. Commercial, industrial and other loans and real estate construction loans increased \$68.8 million, or 29%, and \$54.1 million, or 84%, respectively. Residential mortgages decreased by \$41.5 million in 2015 primarily resulting from a decision to sell most of the residential loans that the Company originates. Gross loans and leases at \$2.66 billion as of December 31, 2014 increased \$185.3 million, or 8%, compared to December 31, 2013 primarily in the commercial loans secured by real estate category.

The following table sets forth the classification of Lakeland's gross loans and leases by major category as of December 31 for each of the last five years:

	2015	2014	December 31, 2013 (in thousands)	2012	2011
Commercial, secured by real estate	\$ 1,761,589	\$ 1,529,761	\$ 1,389,861	\$ 1,125,137	\$ 1,012,982
Commercial, industrial and other	307,044	238,252	213,808	216,129	209,915
Leases	56,660	54,749	41,332	26,781	28,879
Real estate residential mortgage	389,692	431,190	432,831	423,262	406,222
Real estate construction	118,070	64,020	53,119	46,272	79,138
Home equity and consumer	334,891	337,642	339,338	309,626	304,190
	<b>2,967,946</b>	2,655,614	2,470,289	2,147,207	2,041,326
Plus deferred (fees) costs	(2,746)	(1,788)	(1,273)	(364)	249
Loans and leases net of deferred (fees) costs	<b>\$ 2,965,200</b>	\$ 2,653,826	\$ 2,469,016	\$ 2,146,843	\$ 2,041,575

At December 31, 2015, there were no concentrations of loans or leases exceeding 10% of total loans and leases outstanding other than loans that are secured by real estate. Loan concentrations are considered to exist when there are amounts loaned to a multiple number of borrowers engaged in similar activities which would cause them to be similarly impacted by economic or other related conditions.

The following table sets forth maturities and sensitivity to changes in interest rates in commercial loans in Lakeland's loan portfolio at December 31, 2015:

	Within one year	After one but within five years	After five years	Total
	(in thousands)			
Commercial, secured by real estate	\$ 77,871	\$ 303,606	\$ 1,380,112	\$ 1,761,589
Commercial, industrial and other	136,674	97,048	73,322	307,044
Real estate construction	51,975	26,222	39,873	118,070
Total	\$ 266,520	\$ 426,876	\$ 1,493,307	\$ 2,186,703
Predetermined rates	\$ 50,776	\$ 257,158	\$ 280,741	\$ 588,675
Floating or adjustable rates	215,744	169,718	1,212,566	1,598,028
Total	\$ 266,520	\$ 426,876	\$ 1,493,307	\$ 2,186,703

**Risk Elements**

Commercial loans and leases are placed on a non-accrual status with all accrued interest and unpaid interest reversed if (a) because of the deterioration in the financial position of the borrower they are maintained on a cash basis (which means payments are applied when and as received rather than on a regularly scheduled basis),



**Table of Contents**

(b) payment in full of interest or principal is not expected, or (c) principal and interest have been in default for a period of 90 days or more unless the obligation is both well-secured and in process of collection. Residential mortgage loans are placed on non-accrual status at the time principal and interest have been in default for a period of 90 days or more, except where there exists sufficient collateral to cover the defaulted principal and interest payments, and management's knowledge of the specific circumstances warrant continued accrual. Consumer loans are generally placed on non-accrual status and reviewed for charge-off when principal and interest payments are four months in arrears unless the obligations are well-secured and in the process of collection. Interest thereafter on such charged-off consumer loans is taken into income when received only after full recovery of principal. As a general rule, a non-accrual asset may be restored to accrual status when none of its principal or interest is due and unpaid, satisfactory payments have been received for a sustained period (usually six months), or when it otherwise becomes well-secured and in the process of collection.

The following schedule sets forth certain information regarding Lakeland's non-accrual (including troubled debt restructurings that are on non-accrual) and past due loans and leases and other real estate owned and other repossessed assets as of December 31, for each of the last five years:

(dollars in thousands)	At December 31,				
	2015	2014	2013	2012	2011
Commercial, secured by real estate	\$ 10,446	\$ 7,424	\$ 7,697	\$ 10,511	\$ 16,578
Commercial, industrial, and other	103	308	88	1,476	4,608
Leases, including leases held for sale	316	88		32	575
Real estate - residential mortgage	8,664	9,246	6,141	8,733	11,610
Real estate-construction		188	831	4,031	12,393
Home equity and consumer	3,167	3,415	2,175	3,197	3,252
<b>Total non-accrual loans and leases</b>	<b>22,696</b>	<b>20,669</b>	<b>16,932</b>	<b>27,980</b>	<b>49,016</b>
Other real estate and other repossessed assets	983	1,026	520	529	1,182
<b>TOTAL NON-PERFORMING ASSETS</b>	<b>\$ 23,679</b>	<b>\$ 21,695</b>	<b>\$ 17,452</b>	<b>\$ 28,509</b>	<b>\$ 50,198</b>
Non-performing assets as a percent of total assets	0.61%	0.61%	0.53%	0.98%	1.78%
Loans and leases past due 90 days or more and still accruing	\$ 331	\$ 66	\$ 1,997	\$ 1,437	\$ 1,367
Troubled debt restructurings, still accruing	\$ 10,108	\$ 10,579	\$ 10,289	\$ 7,336	\$ 8,856

Non-accrual loans and leases increased to \$22.7 million on December 31, 2015 from \$20.7 million at December 31, 2014. The increase in non-accrual loans was primarily in commercial loans secured by real estate which increased \$2.8 million or 38%.

Non-accruals include 4 loan relationships between \$500,000 and \$1.0 million totaling \$2.8 million, and 3 loan relationships exceeding \$1.0 million totaling \$5.7 million. All non-accrual loans and leases are in various stages of litigation, foreclosure, or workout. Non-accrual loans included \$2.5 million and \$1.3 million in troubled debt restructurings for the years ended December 31, 2015 and 2014, respectively.

At December 31, 2015, Lakeland had \$10.1 million in loans that were restructured and still accruing. Restructured loans are those loans where Lakeland has granted concessions to the borrower in payment terms, in rate and/or in maturity as a result of the financial condition of the borrower.

For 2015, the gross interest income that would have been recorded, had the loans and leases classified at year-end as impaired been performing in conformance with their original terms, is approximately \$1.6 million. The amount of interest income actually recorded on those loans and leases for 2015 was \$769,000. The resultant loss of \$792,000 for 2015 compares with prior year losses of \$1.1 million for 2014 and \$1.3 million for 2013.

**Table of Contents**

As of December 31, 2015, Lakeland had impaired loans and leases totaling \$26.0 million (consisting primarily of non-accrual and restructured loans and leases), compared to \$25.7 million at December 31, 2014. The valuation allowance of these loans and leases is based primarily on the fair value of the underlying collateral. Based upon such evaluation, \$608,000 has been allocated to the allowance for loan and lease losses for impairment at December 31, 2015 compared to \$1.9 million at December 31, 2014. At December 31, 2015, Lakeland also had \$46.6 million in loans and leases that were rated substandard that were not classified as non-performing or impaired compared to \$46.3 million at December 31, 2014.

There were no additional loans or leases at December 31, 2015, other than those designated non-performing, impaired or substandard, where Lakeland was aware of any credit conditions of any borrowers that would indicate a strong possibility of the borrowers not complying with the present terms and conditions of repayment and which may result in such loans or leases being included as non-accrual, past due or renegotiated at a future date.

The following table sets forth for each of the five years ended December 31, 2015, the historical relationships among the amount of loans and leases outstanding, the allowance for loan and lease losses, the provision for loan and lease losses, the amount of loans and leases charged off and the amount of loan and lease recoveries:

	2015	2014	December 31, 2013	2012	2011
	(dollars in thousands)				
Balance of the allowance at the beginning of the year	\$ 30,684	\$ 29,821	\$ 28,931	\$ 28,416	\$ 27,331
Loans and leases charged off:					
Commercial, secured by real estate	1,821	2,282	2,026	7,287	5,352
Commercial, industrial and other	205	999	1,324	949	5,249
Leases	548	597	206	999	2,858
Real estate residential mortgage	375	827	1,257	1,822	1,772
Real estate-construction	20	25	3,854	2,888	3,636
Home equity and consumer	1,511	2,697	1,624	2,074	3,010
Total loans and leases charged off	4,480	7,427	10,291	16,019	21,877
Recoveries:					
Commercial, secured by real estate	2,221	999	1,061	280	2,084
Commercial, industrial and other	183	1,039	260	428	439
Leases	26	19	121	504	1,206
Real estate residential mortgage	63	42	99	66	32
Real estate-construction	106	106	14	43	67
Home equity and consumer	129	220	283	306	318
Total Recoveries	2,728	2,425	1,838	1,627	4,146
Net charge-offs:					
Provision for loan and lease losses charged to operations	1,942	5,865	9,343	14,907	18,816
Ending balance	\$ 30,874	\$ 30,684	\$ 29,821	\$ 28,931	\$ 28,416
Ratio of net charge-offs to average loans and leases outstanding:	0.06%	0.19%	0.36%	0.69%	0.89%
Ratio of allowance at end of year as a percentage of year-end total loans and leases	1.04%	1.16%	1.21%	1.35%	1.39%

The ratio of the allowance for loan and lease losses to loans and leases outstanding reflects management's evaluation of the underlying credit risk inherent in the loan portfolio as discussed above in Critical Accounting Policies, Judgments and Estimates Allowance for Loan and Lease Losses.





**Table of Contents**

In 2015, the Company refined and enhanced its assessment of the adequacy of the allowance for loan and lease losses by extending the lookback period on its commercial loan portfolios from three years to five years and by extending the lookback period for all other portfolios from two to three years in order to capture more of the economic cycle. It also enhanced its qualitative factor framework to include a factor that captures the risk related to appraised real estate values, and how those values could change in relation to a change in capitalization rates. This enhancement is meant to increase the level of precision in the allowance for loan and lease losses. As a result, the Company will no longer have an unallocated segment in its allowance for loan losses, as the risks and uncertainties meant to be captured by the unallocated allowance have been included in the qualitative framework for the respective portfolios. As such, the unallocated allowance has in essence been reallocated to the certain portfolios based on the risks and uncertainties it was meant to capture.

While the overall balance of the allowance for loan and lease losses at \$30.9 million at December 31, 2015 only increased \$190,000, or 1%, from December 31, 2014, the distribution of the allowance changed between segments of the loan portfolio reflecting changes in the non-performing loan and charge-off statistics within each portfolio. Also reflected in the changes within categories are the enhancements in the analysis of the allowance for loan and lease losses discussed above. Loan reserves are based on a combination of historical charge-off experience, estimating the appropriate loss emergence and pre-emergence periods and assigning qualitative factors based on general economic conditions and specific bank portfolio characteristics.

Non-performing loans and leases increased from \$20.7 million on December 31, 2014 to \$22.7 million on December 31, 2015 and the allowance for loan and lease losses was 1.04% of total loans and leases on December 31, 2015 compared to 1.16% of total loans and leases on December 31, 2014. The decline in the allowance for loan and lease losses as a percent of total loans results primarily from a \$3.3 million decline in net charge-offs in 2015 compared to 2014. Management believes, based on appraisals and estimated selling costs, that the majority of its non-performing loans are well secured and that the reserves on its non-performing loans are adequate. Based upon the process employed and giving recognition to all accompanying factors related to the loan and lease portfolio, management considers the allowance for loan and lease losses to be adequate at December 31, 2015.

The following table shows how the allowance for loan and lease losses is allocated among the various types of loans and leases that Lakeland has outstanding. This allocation is based on management's specific review of the credit risk of the outstanding loans and leases in each category as well as historical trends.

	2015		2014		At December 31, 2013		2012		2011	
	Allowance	% of Loans in Each Category	Allowance	% of Loans in Each Category	Allowance	% of Loans in Each Category	Allowance	% of Loans in Each Category	Allowance	% of Loans in Each Category
Commercial, secured by real estate	\$ 20,223	59.4%	\$ 13,577	57.6%	\$ 14,463	56.2%	\$ 16,258	52.4%	\$ 16,618	49.6%
Commercial, industrial and other	2,637	10.3%	3,196	9.0%	5,331	8.7%	5,103	10.1%	3,477	10.3%
Leases	460	1.9%	582	2.1%	504	1.7%	578	1.2%	688	1.4%
Real estate residential mortgage	2,588	13.1%	4,020	16.2%	3,214	17.5%	3,568	19.7%	3,077	19.9%
Real estate construction	1,591	4.0%	553	2.4%	542	2.2%	587	2.2%	1,424	3.9%
Home equity and consumer	3,375	11.3%	6,333	12.7%	2,737	13.7%	2,837	14.4%	3,132	14.9%
Unallocated			2,423		3,030					
	<b>\$ 30,874</b>	<b>100.0%</b>	<b>\$ 30,684</b>	<b>100.0%</b>	<b>\$ 29,821</b>	<b>100.0%</b>	<b>\$ 28,931</b>	<b>100.0%</b>	<b>\$ 28,416</b>	<b>100.0%</b>

**Table of Contents****Investment Securities**

The Company has classified its investment securities into the available for sale and held to maturity categories based on its intent and ability to hold the securities to maturity. The Company has no investment securities classified as trading securities.

The following table sets forth the carrying value of the Company's investment securities, both available for sale and held to maturity, as of December 31 for each of the last three years. Investment securities available for sale are stated at fair value while securities held for maturity are stated at cost, adjusted for amortization of premiums and accretion of discounts.

	2015	December 31, 2014 (in thousands)	2013
U.S. Treasury and U.S. government agencies	<b>\$ 127,610</b>	\$ 114,397	\$ 89,897
Mortgage-backed securities, residential	<b>315,918</b>	352,264	339,098
Mortgage-backed securities, multifamily	<b>12,279</b>	7,235	2,355
Obligations of states and political subdivisions	<b>82,115</b>	71,920	80,394
Equity securities	<b>18,645</b>	17,574	16,146
Other debt securities	<b>2,522</b>	2,035	4,960
	<b>\$ 559,089</b>	\$ 565,425	\$ 532,850

The Company also does not own any interests in any hedge funds or private equity funds that are designated covered funds under the Volcker Rule issued in December 2013. All of the Company's mortgage-backed securities are issued by U.S. Government or U.S. Government sponsored entities.

The following table sets forth the maturity distribution and weighted average yields (calculated on the basis of the stated yields to maturity, considering applicable premium or discount), on a fully taxable equivalent basis, of investment securities available for sale as of December 31, 2015, at fair value:

Available for sale	Within one year	Over one but within five years	Over five but within ten years	After ten years	Total
	(dollars in thousands)				
U.S. Treasury and U.S. government agencies					
Amount	\$	\$ 60,763	\$ 36,370	\$	\$ 97,133
Yield	%	1.56%	1.98%	%	1.72%
Mortgage-backed securities, residential					
Amount	8	1,694	32,710	245,040	279,452
Yield	4.71%	3.34%	2.25%	2.15%	2.17%
Mortgage-backed securities, multifamily					
Amount		5,160	4,960		10,120
Yield	%	1.74%	2.44%	%	2.08%
Obligations of states and political subdivisions					
Amount	2,713	14,538	15,107	4,140	36,498
Yield	4.25%	3.55%	2.79%	2.93%	3.22%
Other debt securities					
Amount	501				501
Yield	2.43%	%	%	%	2.43%
Other equity securities					
Amount	18,645				18,645
Yield	1.87%	%	%	%	1.87%

Edgar Filing: LAKELAND BANCORP INC - Form 10-K

Total securities					
Amount	\$ 21,867	\$ 82,155	\$ 89,147	\$ 249,180	\$ 442,349
Yield	2.18%	1.96%	2.24%	2.16%	2.14%

-42-

**Table of Contents**

The following table sets forth the maturity distribution and weighted average yields (calculated on the basis of the stated yields to maturity, considering applicable premium or discount), on a fully taxable equivalent basis, of investment securities held to maturity as of December 31, 2015, at amortized cost:

Held to maturity	Within one year	Over one but within five years	Over five but within ten years	After ten years	Total
	(dollars in thousands)				
<b>U.S. Treasury and U.S. government agencies</b>					
Amount	\$	\$ 10,684	\$ 19,793	\$	\$ 30,477
Yield	%	1.79%	2.36%	%	2.16%
<b>Mortgage-backed securities, residential</b>					
Amount		4	348	36,114	36,466
Yield	%	2.23%	5.02%	2.54%	2.56%
<b>Mortgage-backed securities, multifamily</b>					
Amount		1,241		918	2,159
Yield	%	1.80%	%	2.36%	2.04%
<b>Obligations of states and political subdivisions</b>					
Amount	6,407	6,773	24,941	7,496	45,617
Yield	0.59%	3.50%	2.94%	3.26%	2.75%
<b>Other debt securities</b>					
Amount		1,021	1,000		2,021
Yield	%	5.74%	5.82%	%	5.78%
<b>Total securities</b>					
Amount	\$ 6,407	\$ 19,723	\$ 46,082	\$ 44,528	\$ 116,740
Yield	0.59%	2.58%	2.77%	2.61%	2.58%

**Other Assets**

Other assets increased from \$16.0 million at December 31, 2014 to \$20.4 million at December 31, 2015 primarily due to a \$1.5 million increase in swap assets, a \$1.1 million increase in deferred taxes and a \$1.2 million increase in accounts receivable.

**Deposits**

Total deposits increased from \$2.79 billion on December 31, 2014 to \$3.00 billion on December 31 2015, an increase of \$204.8 million, or 7%. Noninterest bearing deposits increased \$47.7 million, or 7%, to \$693.7 million. Savings and interest-bearing transaction accounts and time deposits increased \$93.7 million and \$63.4 million, respectively. The 23% increase in time deposits resulted from promoting higher rates to our customer base as well as bidding on deposits from local municipalities. Lakeland also used a listing service to acquire CDs in order to fund its growing loan portfolio.

Total deposits increased from \$2.71 billion on December 31, 2013 to \$2.79 billion on December 31 2014, an increase of \$81.6 million, or 3%.

**Table of Contents**

The average amount of deposits and the average rates paid on deposits for the years indicated are summarized in the following table:

	Year Ended December 31, 2015		Year Ended December 31, 2014		Year Ended December 31, 2013	
	Average Balance	Average Rate	Average Balance	Average Rate	Average Balance	Average Rate
	(Dollars in thousands)					
Noninterest-bearing demand deposits	\$ 695,630	%	\$ 652,685	%	\$ 576,421	%
Interest-bearing transaction accounts	1,511,954	0.24%	1,454,967	0.23%	1,341,691	0.28%
Savings	399,431	0.05%	384,715	0.05%	370,980	0.06%
Time deposits	303,682	0.62%	283,905	0.53%	309,384	0.68%
<b>Total</b>	<b>\$ 2,910,697</b>	<b>0.20%</b>	<b>\$ 2,776,272</b>	<b>0.18%</b>	<b>\$ 2,598,476</b>	<b>0.23%</b>

As of December 31, 2015, the aggregate amount of outstanding time deposits issued in amounts of \$100,000 or more, broken down by time remaining to maturity, was as follows (in thousands):

Maturity	
Within 3 months	\$ 40,199
Over 3 through 6 months	25,628
Over 6 through 12 months	51,380
Over 12 months	61,228
<b>Total</b>	<b>\$ 178,435</b>

**Derivatives**

Lakeland enters into interest rate swaps ( swaps ) with loan customers to provide a facility to mitigate the fluctuations in the variable rate on the respective loans. These swaps are matched in offsetting terms to swaps that Lakeland enters into with an outside third party. The swaps are reported at fair value in other assets or other liabilities. Lakeland's swaps qualify as derivatives, but are not designated as hedging instruments; thus any net gain or loss resulting from changes in the fair value is recognized in other non-interest income. Further discussion of Lakeland's financial derivatives is set forth in Note 18 to the audited Consolidated Financial Statements.

**Liquidity**

Liquidity measures whether an entity has sufficient cash flow to meet its financial obligations and commitments on a timely basis. The Company is liquid when its subsidiary bank has the cash available to meet the borrowing and cash withdrawal requirements of customers and the Company can pay for current and planned expenditures and satisfy its debt obligations.

Lakeland funds loan demand and operation expenses from several sources:

Net income. Cash provided by operating activities was \$40.8 million in 2015 compared to \$45.6 million and \$50.7 million in 2014 and 2013, respectively.

Deposits. Lakeland can offer new products or change its rate structure in order to increase deposits. In 2015, Lakeland generated \$204.8 million in deposit growth compared to \$81.6 million in 2014.

## Edgar Filing: LAKELAND BANCORP INC - Form 10-K

Sales of securities and overnight funds. At year-end 2015, the Company had \$442.3 million in securities designated available for sale. Of these securities, \$285.8 million was pledged to secure public deposits and for other purposes required by applicable laws and regulations.

Repayments on loans and leases can also be a source of liquidity to fund further loan growth.

---

**Table of Contents**

Overnight credit lines. As a member of the Federal Home Loan Bank of New York (FHLB), Lakeland has the ability to borrow overnight based on the market value of collateral pledged. Lakeland had no overnight borrowings from the FHLB on December 31, 2015. Lakeland also has overnight federal funds lines available for it to borrow up to \$162.0 million. Lakeland had borrowings against these lines of \$115.0 million at December 31, 2015. Lakeland also has the ability to utilize an unsecured line of credit from the FHLB to secure a portion of its public deposits. Lakeland may also borrow from the discount window of the Federal Reserve Bank of New York based on the market value of collateral pledged. Lakeland had no borrowings with the Federal Reserve Bank of New York as of December 31, 2015.

Other borrowings. Lakeland can also generate funds by utilizing long-term debt or securities sold under agreements to repurchase that would be collateralized by security or mortgage collateral. At times the market values of securities collateralizing our securities sold under agreements to repurchase may decline due to changes in interest rates and may necessitate our lenders to issue a margin call which requires the Company to pledge additional collateral to meet that margin call. For more information regarding the Company's borrowings, see Note 7 to the Consolidated Financial Statements.

Management and the Board monitor the Company's liquidity through the asset/liability committee, which monitors the Company's compliance with certain regulatory ratios and other various liquidity guidelines.

The cash flow statements for the periods presented provide an indication of the Company's sources and uses of cash, as well as an indication of the ability of the Company to maintain an adequate level of liquidity. A discussion of the cash flow statement for year ended December 31, 2015 follows.

Cash and cash equivalents totaling \$118.5 million on December 31, 2015, increased \$9.2 million from December 31, 2014. Operating activities provided \$40.8 million in net cash. Investing activities used \$324.9 million in net cash, primarily reflecting an increase in loans and leases. Financing activities provided \$293.3 million in net cash primarily reflecting a net increase in deposits and other borrowings of \$204.9 million and \$67.0 million, respectively, partially offset by an early extinguishment of subordinated debentures and the payment of dividends.

The Company's management believes that its current level of liquidity is sufficient to meet its current and anticipated operational needs, including current loan commitments, deposit maturities and other obligations. This constitutes a forward-looking statement under the Private Securities Litigation Reform Act of 1995. Actual results could differ materially from anticipated results due to a variety of factors, including uncertainties relating to general economic conditions; unanticipated decreases in deposits; changes in or failure to comply with governmental regulations; and uncertainties relating to the analysis of the Company's assessment of rate sensitive assets and rate sensitive liabilities and the extent to which market factors indicate that a financial institution such as Lakeland should match such assets and liabilities.

**Table of Contents**

The following table sets forth contractual obligations and other commitments representing required and potential cash outflows as of December 31, 2015. Interest on subordinated debentures and other borrowings is calculated based on current contractual interest rates.

(dollars in thousands)	Total	Payment due period			
		Within one year	After one but within three years	After three but within five years	After five years
Minimum annual rentals or noncancellable operating leases	\$ 24,748	\$ 2,608	\$ 4,326	\$ 3,447	\$ 14,367
Benefit plan commitments	6,421	185	771	793	4,672
Remaining contractual maturities of time deposits	343,321	218,887	115,503	8,918	13
Subordinated debentures	31,238				31,238
Loan commitments	773,058	570,206	141,654	6,546	54,652
Other borrowings	271,905	77,798	184,107		10,000
Interest on other borrowings*	26,895	5,126	6,134	2,797	12,838
Standby letters of credit	11,060	9,391	1,589		80
<b>Total</b>	<b>\$ 1,488,646</b>	<b>\$ 884,201</b>	<b>\$ 454,084</b>	<b>\$ 22,501</b>	<b>\$ 127,860</b>

\* Includes interest on other borrowings and subordinated debentures at a weighted rate of 1.77%.

**Interest Rate Risk**

Closely related to the concept of liquidity is the concept of interest rate sensitivity (i.e., the extent to which assets and liabilities are sensitive to changes in interest rates). As a financial institution, the Company's potential interest rate volatility is a primary component of its market risk. Fluctuations in interest rates will ultimately impact the level of income and expense recorded on a large portion of the Company's assets and liabilities, and the market value of all interest-earning assets, other than those which possess a short term to maturity. Based upon the Company's nature of operations, the Company is not subject to foreign currency exchange or commodity price risk. The Company does not own any trading assets and does not have any off balance sheet hedging transactions in place, such as interest rate swaps and caps.

The Company's net income is largely dependent on net interest income. Net interest income is susceptible to interest rate risk to the extent that interest-bearing liabilities mature or reprice on a different basis than interest-earning assets. For example, when interest-bearing liabilities mature or reprice more quickly than interest-earning assets, an increase in market rates could adversely affect net interest income. Conversely, when interest-earning assets reprice more quickly than interest-bearing liabilities, an increase in market rates could increase net interest income.

The Company's Board of Directors has adopted an Asset/Liability Policy designed to stabilize net interest income and preserve capital over a broad range of interest rate movements. This policy outlines guidelines and ratios dealing with, among others, liquidity, volatile liability dependence, investment portfolio composition, loan portfolio composition, loan-to-deposit ratio and gap analysis ratio. Key quantitative measurements include the percentage change of net interest income in various interest rate scenarios (net interest income at risk) and changes in the market value of equity in various rate environments (net portfolio value at risk). The Company's performance as compared to the Asset/Liability Policy is monitored by its Board of Directors. In addition, to effectively administer the Asset/Liability Policy and to monitor exposure to fluctuations in interest rates, the Company maintains an Asset/Liability Committee (the ALCO), consisting of the Chief Executive Officer, the Regional Presidents, the Chief Financial Officer, Chief Lending Officer, Chief Retail Officer, Chief Credit Officer, certain other senior officers and certain directors. This committee meets quarterly to review the Company's financial results and to develop strategies to implement the Asset/Liability Policy and to respond to market conditions.



**Table of Contents**

The Company monitors and controls interest rate risk through a variety of techniques, including use of an interest rate risk management model. With the interest rate risk management model, the Company projects future net interest income, and then estimates the effect of various changes in interest rates and balance sheet growth rates on that projected net interest income. The Company also uses the interest rate risk management model to calculate the change in net portfolio value over a range of interest rate change scenarios.

Interest rate sensitivity modeling is done at a specific point in time and involves a variety of significant estimates and assumptions. Interest rate sensitivity modeling requires, among other things, estimates of how much and when yields and costs on individual categories of interest-earning assets and interest-bearing liabilities will respond to general changes in market rates, future cash flows and discount rates.

Net interest income simulation considers the relative sensitivities of the balance sheet including the effects of interest rate caps on adjustable rate mortgages and the relatively stable aspects of core deposits. As such, net interest income simulation is designed to address the probability of interest rate changes and the behavioral response of the balance sheet to those changes. Market Value of Portfolio Equity represents the fair value of the net present value of assets, liabilities and off-balance-sheet items. Changes in estimates and assumptions made for interest rate sensitivity modeling could have a significant impact on projected results and conclusions. These assumptions could include prepayment rates, sensitivity of non-maturity deposits, decay rates and other similar assumptions. Therefore, if our assumptions should change, this technique may not accurately reflect the impact of general interest rate movements on the Company's net interest income or net portfolio value.

Management tries to ensure the accuracy of its model by back testing its results (comparing predicted results in past models with current data). It periodically reviews its prepayment assumptions, decay rates and other assumptions. The assumptions regarding the sensitivity of non-maturity deposits to changes in interest rates are reviewed regularly. Towards the end of 2015, management updated its assumptions regarding how responsive its non-maturity deposits would be to changes in interest rates (referred to as betas). Management believes that in the current low interest rate environment, financial institutions such as Lakeland may not immediately increase the rates of their non-maturity deposits for changes in the federal funds rate and that when the rates of the non-maturity deposits do change, it will not be to the same extent as in prior interest rate cycles as the federal funds rate change. Therefore management lowered its beta assumptions to reflect this.

The starting point (or base case) for the following table is an estimate of the following year's net interest income assuming that both interest rates and the Company's interest-sensitive assets and liabilities remain at year-end levels. The net interest income estimated for 2016 (the base case) is \$120.3 million. The information provided for net interest income assumes that changes in interest rates change gradually in equal increments (rate ramp) over the twelve month period.

Rate Ramp	Changes in interest rates	
	+200 bp	-200 bp
Asset/Liability Policy Limit	-5.0%	-5.0%
December 31, 2015	-1.4%	-1.6%
December 31, 2014	-3.6%	-1.9%

The ALCO's policy review of interest rate risk includes policy limits for net interest income changes in various rate shock scenarios. Rate shocks assume that current interest rates change immediately. The information provided for net interest income assumes fluctuations or rate shocks for changes in interest rates as shown in the table below.

Rate Shock	+300 bp	Changes in interest rates		
		+200 bp	+100 bp	-100 bp
Asset/Liability Policy Limit	-15.0%	-10.0%	-5.0%	-5.0%
December 31, 2015	1.7%	1.3%	0.8%	-4.5%
December 31, 2014	-5.2%	-3.2%	-1.3%	-4.5%

**Table of Contents**

The base case for the following table is an estimate of the Company's net portfolio value for the periods presented using current discount rates, and assuming the Company's interest-sensitive assets and liabilities remain at year-end levels. The net portfolio value at December 31, 2015 (the base case) was \$529.0 million. The information provided for the net portfolio value assumes fluctuations or rate shocks for changes in interest rates as shown in the table below.

Rate Shock	Changes in interest rates			
	+300 bp	+200 bp	+100 bp	-100 bp
Asset/Liability Policy Limit	-35.0%	-25.0%	-15.0%	-15.0%
December 31, 2015	-10.2%	-6.5%	-2.9%	0.3%
December 31, 2014	-13.0%	-8.2%	-3.5%	0.7%

The information set forth above is based on significant estimates and assumptions, and constitutes a forward-looking statement under the Private Securities Litigation Reform Act of 1995.

The information in the above tables represent the policy scenario that the ALCO reviews on a quarterly basis. There are also other scenarios run that the ALCO examines that vary depending on the economic environment. These scenarios include a yield curve flattening scenario and scenarios that show more dramatic changes in rates. The committee uses the appropriate scenarios, depending on the economic environment, in its interest rate management decisions.

Certain shortcomings are inherent in the methodologies used in the above interest rate risk measurements. Modeling changes in net interest income requires the making of certain assumptions regarding prepayment and deposit decay rates, which may or may not reflect the manner in which actual yields and costs respond to changes in market interest rates. While management believes such assumptions are reasonable, there can be no assurance that assumed prepayment rates and decay rates will approximate actual future loan prepayment and deposit withdrawal activity. Moreover, the net interest income table presented assumes that the composition of interest sensitive assets and liabilities existing at the beginning of a period remains constant over the period being measured and also assumes that a particular change in interest rates is reflected uniformly across the yield curve regardless of the duration to maturity or repricing of specific assets and liabilities. Accordingly, although the net interest income table provides an indication of the Company's interest rate risk exposure at a particular point in time, such measurement is not intended to and does not provide a precise forecast of the effect of changes in market interest rates on net interest income and will differ from actual results.

**Capital Resources**

Stockholders' equity increased from \$379.4 million on December 31, 2014 to \$400.5 million on December 31, 2015. The increase in stockholders' equity from December 31, 2014 to December 31, 2015 was primarily due to \$32.5 million in net income, partially offset by payment of dividends on common stock of \$12.6 million.

Book value per common share (total common stockholders' equity divided by the number of shares outstanding) increased from \$10.01 on December 31, 2014 to \$10.57 on December 31, 2015 primarily as a result of net income. Book value per common share was \$9.28 on December 31, 2013. Tangible book value per share increased from \$7.06 on December 31, 2014 to \$7.62 on December 31, 2015. For more information see Non-GAAP Financial Measures.

In July, 2013, the FRB and the FDIC approved the final rules implementing the Basel Committee on Banking Supervision's (BCBS) capital guidelines for U.S. banks. The rules include a new common equity Tier 1 capital to risk-weighted assets ratio of 4.5% and a common equity Tier 1 capital conservation buffer of 2.5% of risk-weighted assets. The capital conservation buffer will be phased-in starting with 0.625% in 2016 and increasing by 0.625% annually until it reaches 2.5% in 2019. The final rules also raise the minimum ratio of Tier

**Table of Contents**

1 capital to risk-weighted assets from 4.0% to 6.0% and require a minimum leverage ratio of 4.0%. The final rules also implement strict eligibility criteria for regulatory capital instruments. The phase-in period for the final rules began for the Company on January 1, 2015, with full compliance with all of the final rule s requirements to be phased in over a multi-year schedule through January 1, 2019. As of December 31, 2015, the Company and Lakeland met all of the requirements under the new rules on a fully phased-in basis, if such requirements were in effect.

The following table reflects capital ratios of the Company and Lakeland based on the then current regulations as of December 31, 2015 and 2014:

	Tier 1 Capital to Total Average Assets Ratio		Common Equity Tier 1 to Risk-Weighted Assets Ratio		Tier 1 Capital to Risk-Weighted Assets Ratio		Total Capital to Risk-Weighted Assets Ratio	
	December 31, 2015	2014	December 31, 2015	2014	December 31, 2015	2014	December 31, 2015	2014
Capital Ratios:								
The Company	8.70%	9.08%	9.54%	N/A	10.53%	11.76%	11.61%	12.98%
Lakeland Bank	8.08%	8.39%	9.78%	N/A	9.78%	10.87%	10.87%	12.10%
Well capitalized institution under FDIC Regulations	5.00%	5.00%	6.50%	N/A	8.00%	6.00%	10.00%	10.00%

**Non-GAAP Financial Measures**

	December 31,				
	2015	2014	2013	2012	2011
	(In thousands, except per share amounts)				
<b>Calculation of tangible book value per common share</b>					
Total common stockholders equity at end of period - GAAP	\$ 400,516	\$ 379,438	\$ 351,424	\$ 280,867	\$ 241,303
Less:					
Goodwill	109,974	109,974	109,974	87,111	87,111
Other identifiable intangible assets, net	1,545	1,960	2,424		
Total tangible common stockholders equity at end of period - Non- GAAP	\$ 288,997	\$ 267,504	\$ 239,026	\$ 193,756	\$ 154,192
Shares outstanding at end of period(1)	37,906	37,911	37,874	31,212	28,178
Book value per share - GAAP(1)	\$ 10.57	\$ 10.01	\$ 9.28	\$ 9.00	\$ 8.56
Tangible book value per share - Non-GAAP(1)	\$ 7.62	\$ 7.06	\$ 6.31	\$ 6.21	\$ 5.47
<b>Calculation of tangible common equity to tangible assets</b>					
Total tangible common stockholders equity at end of period - Non- GAAP	\$ 288,997	\$ 267,504	\$ 239,026	\$ 193,756	\$ 154,192
Total assets at end of period - GAAP	\$ 3,869,550	\$ 3,538,325	\$ 3,317,791	\$ 2,918,703	\$ 2,825,950
Less:					
Goodwill	109,974	109,974	109,974	87,111	87,111
Other identifiable intangible assets, net	1,545	1,960	2,424		
Total tangible assets at end of period - Non-GAAP	\$ 3,758,031	\$ 3,426,391	\$ 3,205,393	\$ 2,831,592	\$ 2,738,839
Common equity to assets - GAAP	10.35%	10.72%	10.59%	9.62%	8.54%

Edgar Filing: LAKELAND BANCORP INC - Form 10-K

Tangible common equity to tangible assets - Non-GAAP	7.69%	7.81%	7.46%	6.84%	5.63%
--	-------	-------	-------	-------	-------

(1) Adjusted for 5% stock dividends in 2014, 2012 and 2011.



**Table of Contents****Quarterly financial data (unaudited)**

The following represents summarized quarterly financial data of the Company, which in the opinion of management reflected all adjustments, consisting only of nonrecurring adjustments, necessary for a fair presentation of the Company's results of operations.

	March 31, 2015	June 30, 2015	Quarter ended September 30, 2015	December 31, 2015
	(in thousands, except per share amounts)			
Total interest income	\$ 30,992	\$ 31,308	\$ 32,159	\$ 33,055
Total interest expense	2,474	2,639	2,825	2,936
Net interest income	28,518	28,669	29,334	30,119
Provision for loan and lease losses	870	800	332	
Noninterest income (excluding investment securities gains)	4,738	4,941	4,684	4,826
Gains on investment securities, net		17	173	51
Gain on debt extinguishment			1,830	
Long term debt prepayment fee			2,407	
Merger related expenses			330	822
Core deposit intangible amortization	111	107	98	99
Noninterest expense	19,931	21,028	20,997	21,320
Income before taxes	12,344	11,692	11,857	12,755
Income taxes	4,014	3,830	4,032	4,291
Net Income Available to Common Stockholders	\$ 8,330	\$ 7,862	\$ 7,825	\$ 8,464
<b>Earnings per share of common stock</b>				
Basic	\$ 0.22	\$ 0.21	\$ 0.20	\$ 0.22
Diluted	\$ 0.22	\$ 0.21	\$ 0.20	\$ 0.22

	March 31, 2014	June 30, 2014	Quarter ended September 30, 2014	December 31, 2014
	(in thousands, except per share amounts)			
Total interest income	\$ 29,930	\$ 30,549	\$ 30,796	\$ 31,228
Total interest expense	2,085	2,130	2,344	2,378
Net interest income	27,845	28,419	28,452	28,850
Provision for loan and lease losses	1,489	1,593	1,194	1,589
Noninterest income (excluding investment securities gains)	4,071	4,371	4,809	4,469
Gains on investment securities, net	2			
Core deposit intangible amortization	123	119	111	111
Noninterest expense	19,619	19,411	19,574	20,067
Income before taxes	10,687	11,667	12,382	11,552
Income taxes	3,524	3,886	4,136	3,613
Net Income Available to Common Stockholders	\$ 7,163	\$ 7,781	\$ 8,246	\$ 7,939
<b>Earnings per share of common stock(1)</b>				
Basic	\$ 0.19	\$ 0.20	\$ 0.22	\$ 0.21
Diluted	\$ 0.19	\$ 0.20	\$ 0.22	\$ 0.21

- (1) Adjusted for 5% stock dividend payable on June 17, 2014 to shareholders of record June 3, 2014.

---

**Table of Contents*****Recent Accounting Pronouncements***

In February 2016, the Financial Accounting Standards Board ( FASB ) issued accounting guidance that requires all lessees to recognize a lease liability and a right-of-use asset, measured at the present value of the future minimum lease payments, at the lease commencement date. Lessor accounting remains largely unchanged under the new guidance. The guidance is effective for fiscal years beginning after December 15, 2018, including interim reporting periods within that reporting period, with early adoption permitted. A modified retrospective approach must be applied for leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements. The Company is currently assessing the impact that the guidance will have on the Company's consolidated financial statements.

In January 2016, the FASB issued an accounting standards update intended to improve the recognition and measurement of financial instruments. Specifically, the accounting standards update requires all equity instruments, with the exception of those that are accounted for under the equity method of accounting, to be measured at fair value with changes in the fair value recognized through net income. Additionally, public business entities are required to use the exit price notion when measuring the fair value of financial instruments for disclosure purposes. The amendments in this update also require an entity to present separately in other comprehensive income the portion of the total change in the fair value of a liability resulting from a change in the instrument-specific credit risk when the entity has elected to measure the liability at fair value in accordance with the fair value option for financial instruments. This amendment is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2017.

In September 2015, the FASB issued an accounting standards update simplifying the accounting for adjustments made to provisional amounts recognized in a business combination, eliminating the requirement to retrospectively account for those adjustments. To simplify the accounting for adjustments made to provisional amounts, the amendments in the accounting standards update require that the acquirer recognize adjustments to provisional amounts that are identified during the measurement period in the reporting period in which the adjustment amount is determined. The acquirer is required to also record, in the same period's financial statements, the effect on earnings of changes in depreciation, amortization, or other income effects, if any, as a result of the change to the provisional amounts, calculated as if the accounting had been completed at the acquisition date. In addition, an entity is required to present separately on the face of the income statement or disclose in the notes to the financial statements the portion of the amount recorded in current-period earnings by line item that would have been recorded in previous reporting periods if the adjustment to the provisional amounts had been recognized as of the acquisition date. This amendment is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2015.

In May 2015, the FASB issued an accounting standards update clarifying how investments valued using the net asset value practical expedient within the fair value hierarchy should be classified. The accounting standards update was issued to address diversity in practice by exempting investments measured using the net asset value expedient from categorization in the fair value hierarchy. This accounting standards update is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2015. The adoption of this update is not expected to have a material impact on the Company's financial statements.

In April 2015, the FASB issued an accounting standards update requiring that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of the debt liability consistent with the presentation of debt discounts. The purpose of this update is to simplify the presentation of debt issuance costs and to align the US GAAP presentation of debt more closely with international accounting standards. In August 2015, the FASB issued a subsequent update which discussed presentation and subsequent measurement of debt issuance costs associated with line-of-credit arrangements. These amendments are effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2015. The adoption of these updates are not expected to have a material impact on the Company's financial statements.



## **Table of Contents**

In January 2015, the FASB issued an accounting standards update regarding the elimination of the concept of the extraordinary items from the statement of operations. The purpose of this update is to simplify the statement of operations presentation and to align the US GAAP income statement more closely with international accounting standards. This update is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2015. The adoption of this update is not expected to have a material impact on the Company's financial statements.

In June 2014, the FASB issued an accounting standards update that aligns the accounting for repurchase to maturity transactions and repurchase agreements executed as a repurchase financing with the accounting for other typical repurchase agreements. Going forward, these transactions would all be accounted for as secured borrowings. This update is effective for the first interim or annual period beginning after December 15, 2014. In addition, the disclosure of certain transactions accounted for as a sale is effective for the first interim or annual period beginning on or after December 15, 2014, and the disclosure for transactions accounted for as secured borrowings is required for annual periods beginning after December 15, 2014, and interim periods after March 15, 2015. The Company adopted this update in 2015. The Company does not engage in repurchase to maturity transactions, and therefore the adoption of this update did not have a material impact on the Company's financial results.

In May 2014, the FASB issued an accounting standards update that clarifies the principles for recognizing revenue. The core principle of the guidance is that an entity should recognize revenue to depict the transfer of promised goods or services to a customer in an amount that reflects the consideration to which the entity expects to be entitled in exchange for these goods or services. This guidance is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2017. The Company is still evaluating the potential impact on the Company's financial statements.

### ***Effects of Inflation***

The impact of inflation, as it affects banks, differs substantially from the impact on non-financial institutions. Banks have assets which are primarily monetary in nature and which tend to move with inflation. This is especially true for banks with a high percentage of rate sensitive interest-earning assets and interest-bearing liabilities. A bank can further reduce the impact of inflation with proper management of its rate sensitivity gap. This gap represents the difference between interest rate sensitive assets and interest rate sensitive liabilities. Lakeland attempts to structure its assets and liabilities and manages its gap to protect against substantial changes in interest rate scenarios, in order to minimize the potential effects of inflation.

### **Item 7A-Quantitative and Qualitative Disclosures About Market Risk.**

See Management's Discussion and Analysis of Financial Condition and Results of Operations.

**Table of Contents****Item 8 Financial Statements and Supplementary Data****Lakeland Bancorp, Inc. and Subsidiaries**

## CONSOLIDATED BALANCE SHEETS

ASSETS	December 31,	
	2015	2014
	(dollars in thousands)	
Cash	\$ 113,894	\$ 102,549
Interest-bearing deposits due from banks	4,599	6,767
Total cash and cash equivalents	118,493	109,316
Investment securities, available for sale, at fair value	442,349	457,449
Investment securities, held to maturity, at amortized cost with fair value of \$117,594 in 2015 and \$109,030 in 2014	116,740	107,976
Federal Home Loan Bank and other membership stock, at cost	14,087	9,846
Loans held for sale	1,233	592
Loans, net of deferred costs (fees)	2,965,200	2,653,826
Less: allowance for loan and lease losses	30,874	30,684
Net loans	2,934,326	2,623,142
Premises and equipment net	35,881	35,675
Accrued interest receivable	9,208	8,896
Goodwill	109,974	109,974
Other identifiable intangible assets	1,545	1,960
Bank owned life insurance	65,361	57,476
Other assets	20,353	16,023
<b>TOTAL ASSETS</b>	<b>\$ 3,869,550</b>	<b>\$ 3,538,325</b>
<b>LIABILITIES AND STOCKHOLDERS EQUITY</b>		
<b>LIABILITIES:</b>		
Deposits:		
Noninterest bearing	\$ 693,741	\$ 646,052
Savings and interest-bearing transaction accounts	1,958,510	1,864,805
Time deposits under \$100 thousand	164,886	165,625
Time deposits \$100 thousand and over	178,435	114,337
Total deposits	2,995,572	2,790,819
Federal funds purchased and securities sold under agreements to repurchase	151,234	108,935
Other borrowings	271,905	202,498
Subordinated debentures	31,238	41,238
Other liabilities	19,085	15,397
<b>TOTAL LIABILITIES</b>	<b>3,469,034</b>	<b>3,158,887</b>
<b>STOCKHOLDERS EQUITY</b>		
Common stock, no par value; authorized 70,000,000 shares; issued shares, 37,906,481 at December 31, 2015 and 37,910,840 at December 31, 2014	386,287	384,731
Retained Earnings (Accumulated Deficit)	13,079	(6,816)
Accumulated other comprehensive income	1,150	1,523
<b>TOTAL STOCKHOLDERS EQUITY</b>	<b>400,516</b>	<b>379,438</b>

<b>TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY</b>	<b>\$ 3,869,550</b>	\$ 3,538,325
---	---------------------	--------------

The accompanying notes are an integral part of these statements.

**Table of Contents****Lakeland Bancorp, Inc. and Subsidiaries**

## CONSOLIDATED STATEMENTS OF INCOME

	Years Ended December 31,		
	2015	2014	2013
	(dollars in thousands, except per share data)		
<b>INTEREST INCOME</b>			
Loans, leases and fees	\$ 115,295	\$ 110,587	\$ 104,329
Federal funds sold and interest-bearing deposits with banks	62	71	93
Taxable investment securities and other	10,563	10,040	7,985
Tax-exempt investment securities	1,594	1,805	1,792
<b>TOTAL INTEREST INCOME</b>	<b>127,514</b>	<b>122,503</b>	<b>114,199</b>
<b>INTEREST EXPENSE</b>			
Deposits	5,755	5,064	6,089
Federal funds purchased and securities sold under agreements to repurchase	110	78	39
Other borrowings	5,009	3,795	3,529
<b>TOTAL INTEREST EXPENSE</b>	<b>10,874</b>	<b>8,937</b>	<b>9,657</b>
<b>NET INTEREST INCOME</b>	<b>116,640</b>	<b>113,566</b>	<b>104,542</b>
Provision for loan and lease losses	1,942	5,865	9,343
<b>NET INTEREST INCOME AFTER PROVISION FOR LOAN AND LEASE LOSSES</b>	<b>114,698</b>	<b>107,701</b>	<b>95,199</b>
<b>NONINTEREST INCOME</b>			
Service charges on deposit accounts	10,024	10,523	10,837
Commissions and fees	4,568	4,634	4,585
Income on bank owned life insurance	2,017	1,453	1,410
Gain on debt extinguishment	1,830		1,197
Gains on sales of loans	1,681	573	760
Gain on sales and calls of investment securities, net	241	2	839
Other income	800	537	1,333
<b>TOTAL NONINTEREST INCOME</b>	<b>21,161</b>	<b>17,722</b>	<b>20,961</b>
<b>NONINTEREST EXPENSE</b>			
Salaries and employee benefits	48,640	45,167	41,871
Net occupancy expense	8,956	8,865	8,074
Furniture and equipment	6,930	6,605	6,181
FDIC insurance expense	2,086	2,019	2,014
Stationery, supplies and postage	1,529	1,403	1,482
Marketing expense	1,586	2,025	2,088
Data processing expense	1,524	1,245	1,466
Telecommunications expense	1,448	1,386	1,381
ATM and debit card expense	1,398	1,432	1,360
Core deposit intangible amortization	415	464	288
Other real estate and repossessed asset expense	181	234	24
Long-term debt prepayment fee	2,407		1,209
Merger related expenses	1,152		2,834
Other expenses	8,959	8,290	8,469
<b>TOTAL NONINTEREST EXPENSE</b>	<b>87,211</b>	<b>79,135</b>	<b>78,741</b>

Edgar Filing: LAKELAND BANCORP INC - Form 10-K

Income before provision for income taxes	<b>48,648</b>	46,288	37,419
Provision for income taxes	<b>16,167</b>	15,159	12,450
<b>NET INCOME</b>	<b>\$ 32,481</b>	\$ 31,129	\$ 24,969
<b>PER SHARE OF COMMON STOCK:</b>			
Basic earnings	<b>\$ 0.85</b>	\$ 0.82	\$ 0.71
Diluted earnings	<b>\$ 0.85</b>	\$ 0.82	\$ 0.71
Cash dividends	<b>\$ 0.33</b>	\$ 0.29	\$ 0.27

The accompanying notes are an integral part of these statements.

**Table of Contents****Lakeland Bancorp, Inc. and Subsidiaries****CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**

	For the Years Ended December 31,		
	2015	2014	2013
	(in thousands)		
<b>NET INCOME</b>	<b>\$ 32,481</b>	<b>\$ 31,129</b>	<b>\$ 24,969</b>
<b>OTHER COMPREHENSIVE INCOME (LOSS), NET OF TAX:</b>			
Unrealized securities (losses) gains during period	(220)	6,180	(8,690)
Less: reclassification for gains included in net income	157	2	509
Change in pension liability, net	4	20	588
Other Comprehensive Income (Loss)	(373)	6,198	(8,611)
<b>TOTAL COMPREHENSIVE INCOME</b>	<b>\$ 32,108</b>	<b>\$ 37,327</b>	<b>\$ 16,358</b>

The accompanying notes are an integral part of these statements.

**Table of Contents****Lakeland Bancorp, Inc. and Subsidiaries**

## CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS EQUITY

For the years ended December 31, 2015, 2014 and 2013

	Common stock	Retained Earnings (Accumulated Deficit)	Treasury Stock (dollars in thousands)	Accumulated Other Comprehensive Income (Loss)	Total
BALANCE December 31, 2012	\$ 303,794	(\$ 24,145)	(\$ 2,718)	\$ 3,936	\$ 280,867
Net Income		24,969			24,969
Other comprehensive loss, net of tax				(8,611)	(8,611)
Stock based compensation	895				895
Issuance of restricted stock awards	(1,301)		1,301		
Issuance of stock for acquisition	57,419				57,419
Issuance of stock options for acquisition	1,500				1,500
Issuance of stock to dividend reinvestment and stock purchase plan	458	(1,210)	938		186
Exercise of stock options, net of excess tax benefits	1,872		479		2,351
Cash dividends, common stock		(8,152)			(8,152)
BALANCE December 31, 2013	364,637	(8,538)		(4,675)	351,424
Net Income		31,129			31,129
Other comprehensive income, net of tax				6,198	6,198
Stock based compensation	1,390				1,390
Stock dividend	18,266	(18,266)			
Issuance of stock to dividend reinvestment and stock purchase plan	382	(305)			77
Retirement of restricted stock	(104)				(104)
Exercise of stock options, net of excess tax benefits	160				160
Cash dividends, common stock		(10,836)			(10,836)
BALANCE December 31, 2014	384,731	(6,816)		1,523	379,438
Net Income		32,481			32,481
Other comprehensive loss, net of tax				(373)	(373)
Stock based compensation	1,605				1,605
Issuance of stock	22				22
Retirement of restricted stock	(254)				(254)
Exercise of stock options, net of excess tax benefits	183				183
Cash dividends, common stock		(12,586)			(12,586)
BALANCE December 31, 2015	\$ 386,287	\$ 13,079	\$	\$ 1,150	\$ 400,516

The accompanying notes are an integral part of these statements.

**Table of Contents****Lakeland Bancorp, Inc. and Subsidiaries**

## CONSOLIDATED STATEMENTS OF CASH FLOWS

	Years Ended December 31,		
	2015	2014	2013
	(in thousands)		
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>			
Net income	\$ 32,481	\$ 31,129	\$ 24,969
Adjustments to reconcile net income to net cash provided by operating activities:			
Net amortization of premiums, discounts and deferred loan fees and costs	4,151	3,456	4,787
Depreciation and amortization	3,410	3,454	3,625
Amortization of intangible assets	415	464	288
Provision for loan and lease losses	1,942	5,865	9,343
Stock based compensation	1,605	1,390	895
Loans originated for sale	(71,833)	(23,386)	(34,718)
Proceeds from sales of loans	72,873	24,573	36,804
Gains on securities	(241)	(2)	(839)
Gains on sales of loans held for sale	(1,681)	(573)	(760)
Gains on proceeds from bank owned life insurance policies	(435)		
Gains on debt redemption and extinguishment	(1,830)		(1,197)
Gains on other real estate and other repossessed assets	(102)	(258)	(934)
Gain on sale of premises and equipment	(6)	(65)	(60)
Long-term debt prepayment penalty	2,407		
Deferred tax (benefit) provision	(824)	(34)	164
(Increase) decrease in other assets	(5,257)	(879)	7,366
Increase in other liabilities	3,691	495	995
<b>NET CASH PROVIDED BY OPERATING ACTIVITIES</b>	<b>40,766</b>	<b>45,629</b>	<b>50,728</b>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>			
Net cash acquired in acquisition			74,316
Proceeds from repayments on and maturity of securities:			
Available for sale	71,368	55,810	70,779
Held to maturity	24,453	22,508	22,952
Proceeds from sales of securities:			
Available for sale	33,613	15,719	64,020
Held to maturity		1,301	
Purchase of securities:			
Available for sale	(92,904)	(90,630)	(187,452)
Held to maturity	(33,811)	(30,556)	(19,603)
Net increase in Federal Home Loan Bank and other membership bank stock	(4,241)	(1,908)	(2,063)
Purchase of bank owned life insurance	(7,000)		
Proceeds from bank owned life insurance policy	1,186		
Net increase in loans and leases	(315,067)	(191,910)	(91,201)
Proceeds from sales of bank premises and equipment	696	118	463
Capital expenditures	(4,838)	(2,492)	(2,786)
Proceeds from sales of other real estate and other repossessed assets	1,608	1,484	4,509
<b>NET CASH USED IN INVESTING ACTIVITIES</b>	<b>(324,937)</b>	<b>(220,556)</b>	<b>(66,066)</b>
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>			
Net increase in deposits	204,854	81,783	26,540
Increase (decrease) in federal funds purchased and securities sold under agreements to repurchase	42,299	26,944	(35,298)
Proceeds from other borrowings	117,000	168,498	50,000
Repayments of other borrowings	(50,000)	(85,000)	(16,000)
Issuance of stock to Dividend Reinvestment and Stock Purchase Plan	22	77	186
Redemption of subordinated debentures, net	(8,170)		(9,113)
Exercise of stock options	124	90	2,209
Retirement of Restricted stock	(254)	(104)	



Edgar Filing: LAKELAND BANCORP INC - Form 10-K

Excess tax benefits	59	70	142
Dividends paid	(12,586)	(10,836)	(8,152)
<b>NET CASH PROVIDED BY FINANCING ACTIVITIES</b>	<b>293,348</b>	181,522	10,514
Net increase (decrease) in cash and cash equivalents	9,177	6,595	(4,824)
Cash and cash equivalents, beginning of year	109,316	102,721	107,545
<b>CASH AND CASH EQUIVALENTS, END OF YEAR</b>	<b>\$ 118,493</b>	\$ 109,316	\$ 102,721
Transfer of loans and leases receivable to other real estate owned and other repossessed assets	\$ 1,462	\$ 1,867	\$ 3,565
Cash paid for interest	10,770	8,882	10,804
Cash paid for income taxes	16,737	15,057	12,051
Acquisition of Somerset Hills Bancorp:			
Fair value for non-cash assets other than goodwill acquired in purchase transaction			275,287
Fair value for liabilities assumed in purchase transaction			313,546
Goodwill related to acquisition			22,862
Common stock issued and fair value of stock options converted to Lakeland Bancorp stock options			58,919

The accompanying notes are an integral part of these statements.

---

**Table of Contents**

Lakeland Bancorp, Inc. and Subsidiaries

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 - SUMMARY OF ACCOUNTING POLICIES

Lakeland Bancorp, Inc. (the Company) is a bank holding company whose principal activity is the ownership and management of its wholly owned subsidiary, Lakeland Bank (Lakeland). Lakeland operates under a state bank charter and provides full banking services and, as a state bank, is subject to regulation by the New Jersey Department of Banking and Insurance. Lakeland generates commercial, mortgage and consumer loans and receives deposits from customers located primarily in Northern and Central New Jersey. Lakeland also provides non-deposit products, such as securities brokerage services, including mutual funds and variable annuities.

Lakeland operates as a commercial bank offering a wide variety of commercial loans and leases and, to a lesser degree, consumer credits. Its primary strategic aim is to establish a reputation and market presence as the small and middle market business bank in its principal markets. Lakeland funds its loans primarily by offering time, savings and money market, and demand deposit accounts to both commercial enterprises and individuals. Additionally, it originates residential mortgage loans, and services such loans which are owned by other investors. Lakeland also has an equipment finance division which provides equipment lease financing primarily to small and medium sized business clients and an asset based lending department which specializes in utilizing particular assets to fund the working capital needs of borrowers.

The Company and Lakeland are subject to regulations of certain state and federal agencies and, accordingly, are periodically examined by those regulatory authorities. As a consequence of the extensive regulation of commercial banking activities, Lakeland's business is particularly susceptible to being affected by state and federal legislation and regulations.

*Basis of Financial Statement Presentation*

The accounting and reporting policies of the Company and its subsidiaries conform with accounting principles generally accepted in the United States of America (U.S. GAAP) and predominant practices within the banking industry. The consolidated financial statements include the accounts of the Company, Lakeland, Lakeland NJ Investment Corp., Lakeland Investment Corp., Lakeland Equity, Inc., Lakeland Preferred Equity, Inc. and Sullivan Financial Services, Inc. All intercompany balances and transactions have been eliminated.

The preparation of financial statements 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. These estimates and assumptions also affect reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates. Significant estimates implicit in these financial statements are as follows.

The principal estimates that are particularly susceptible to significant change in the near term relate to the allowance for loan and lease losses, the valuation of the Company's investment securities portfolio, the realizability of the Company's deferred tax asset and the analysis of goodwill and intangible impairment. The policies regarding these estimates are discussed below.

The Company's operating segments are components of its enterprise for which separate financial information is available and is evaluated regularly by the chief operating decision maker in deciding how to allocate resources and assess performance. The Company's chief operating decision maker is its Chief Executive Officer. All of the Company's financial services activities are interrelated, and each activity is dependent and assessed based on how each of the activities of the Company supports the others. For example, commercial lending is dependent upon the ability of Lakeland to fund itself with retail deposits and other borrowings and to manage interest rate and credit risk. The situation is also similar for consumer and residential mortgage lending. Moreover, the

## **Table of Contents**

Company primarily operates in one market area, Northern and Central New Jersey and contiguous areas. Therefore, all significant operating decisions are based upon analysis of the Company as one operating segment or unit. Accordingly, the Company has determined that it has one operating segment and thus one reporting segment.

### *Cash and Due from Banks*

Cash and cash equivalents are defined as cash on hand, cash items in the process of collection, amounts due from banks and federal funds sold with an original maturity of three months or less. A portion of Lakeland's cash on hand and on deposit with the Federal Reserve Bank was required to meet regulatory reserve and clearing requirements.

### *Investment Securities*

Investment securities are classified in one of three categories: held to maturity, trading, or available for sale. Investments in debt securities, for which management has both the ability and intent to hold to maturity, are carried at cost, adjusted for the amortization of premiums and accretion of discounts computed by the effective interest method. Investments in debt and equity securities, which management believes may be sold prior to maturity due to changes in interest rates, prepayment risk, liquidity requirements, or other factors, are classified as available for sale. Net unrealized gains and losses for such securities, net of tax effect, are reported as other comprehensive income (loss) and excluded from the determination of net income. The Company does not engage in securities trading. Gains or losses on disposition of investment securities are based on the net proceeds and the adjusted carrying amount of the securities sold using the specific identification method. Losses are recorded through the statement of income when the impairment is considered other-than-temporary, even if a decision to sell has not been made.

The Company evaluates its portfolio for impairment each quarter. In estimating other-than-temporary losses, the Company considers the length of time and the extent to which the fair value has been less than cost, the financial condition and near-term prospects of the issuer, and whether the Company is more likely than not to sell the security before recovery of its cost basis. If a security has been impaired for more than twelve months, and the impairment is deemed other-than-temporary, a write down will occur in that quarter. If a loss is deemed to be other-than-temporary, it is recognized as a realized loss in the income statement with the security assigned a new cost basis.

If the Company intends to sell an impaired security, the Company records an other-than-temporary loss in an amount equal to the entire difference between the fair value and amortized cost. If a security is determined to be other-than-temporarily impaired, but the Company does not intend to sell the security, only the credit portion of the estimated loss is recognized in earnings in gain (loss) on securities, with the other portion of the loss recognized in other comprehensive income. If a determination is made that an equity security is other-than-temporarily impaired, the unrealized loss will be recognized as an other-than-temporary impairment charge in non-interest income as a component of gain (loss) on investment securities.

### *Loans and Leases and Allowance for Loan and Lease Losses*

Loans and leases that management has the intent and ability to hold for the foreseeable future or until maturity or payoff are stated at the amount of unpaid principal and are net of unearned discount, unearned loan fees and an allowance for loan and lease losses.

Interest income is accrued as earned on a simple interest basis. All unamortized fees and costs related to the loan are amortized over the life of the loan using the interest method. Accrual of interest is discontinued on a loan or lease when management believes, after considering economic and business conditions and collection efforts, that the borrower's financial condition is such that full collection of interest and principal is doubtful. When a loan or lease is placed on such non-accrual status, all accumulated accrued interest receivable is reversed out of current period income.

---

**Table of Contents**

Commercial loans and leases are placed on a non-accrual status with all accrued interest and unpaid interest reversed if (a) because of the deterioration in the financial position of the borrower they are maintained on a cash basis (which means payments are applied when and as received rather than on a regularly scheduled basis), (b) payment in full of interest or principal is not expected, or (c) principal and interest have been in default for a period of 90 days or more unless the obligation is both well-secured and in process of collection. Residential mortgage loans are placed on non-accrual status at the time principal and interest have been in default for a period of 90 days or more, except where there exists sufficient collateral to cover the defaulted principal and interest payments, and management's knowledge of the specific circumstances warrant continued accrual. Consumer loans are generally placed on non-accrual and reviewed for charge-off when principal and interest payments are four months in arrears unless the obligations are well-secured and in the process of collection. Interest thereafter on such charged-off consumer loans is taken into income when received only after full recovery of principal. As a general rule, a non-accrual asset may be restored to accrual status when none of its principal or interest is due and unpaid, satisfactory payments have been received for a sustained period (usually six months), or when it otherwise becomes well-secured and in the process of collection.

Loans and leases are considered impaired when, based on current information and events, it is probable that Lakeland will be unable to collect all amounts due in accordance with the original contractual terms of the loan agreement, including scheduled principal and interest payments. Impairment is measured based on the present value of expected cash flows discounted at the loan's effective interest rate, or as a practical expedient, Lakeland may measure impairment based on a loan's observable market price, or the fair value of the collateral, less estimated costs to sell, if the loan is collateral-dependent. Regardless of the measurement method, Lakeland measures impairment based on the fair value of the collateral when it is determined that foreclosure is probable. Most of Lakeland's impaired loans are collateral-dependent. Lakeland groups impaired commercial loans under \$500,000 into a homogeneous pool and collectively evaluates them.

Interest received on impaired loans and leases may be recorded as interest income. However, if management is not reasonably certain that an impaired loan and lease will be repaid in full, or if a specific time frame to resolve full collection cannot yet be reasonably determined, all payments received are recorded as reductions of principal.

Loans are classified as troubled debt restructured loans in cases where borrowers experience financial difficulties and Lakeland makes certain concessionary modifications to contractual terms. Restructured loans typically involve a modification of terms such as a reduction of the stated interest rate, an extended moratorium of principal payments and/or an extension of the maturity date at a stated interest rate lower than the current market rate for a new loan with similar risk. Nonetheless, restructured loans are classified as impaired loans.

If an obligation has been restructured, it will continue to be classified as restructured until the obligation is fully repaid or until it meets all of the following criteria: 1) the borrower is no longer experiencing financial difficulties, 2) the rate is not less than the rate provided for similar credit risk, 3) other terms are no less favorable than similar new debt and 4) no concessions were granted (any prior principal forgiveness is deemed to be an ongoing concession).

The allowance for loan and lease losses is established through a provision for loan and lease losses charged to expense. Loan principal considered to be uncollectible by management is charged against the allowance for loan and lease losses. The allowance is an amount that management believes will be adequate to absorb losses on existing loans and leases that may become uncollectible based upon an evaluation of known and inherent risks in the loan and lease portfolio. The evaluation takes into consideration such factors as changes in the nature and size of the loan and lease portfolio, overall portfolio quality, specific problem loans and leases, and current economic conditions which may affect the borrowers' ability to pay. The evaluation also analyzes historical losses by loan and lease category, and considers the resulting loss rates when determining the reserves on current loan and lease total amounts. Additionally, management assesses the loss emergence period for each loan segment and adjusts each historical loss factor accordingly. The loss emergence period is the estimated time from the date of a loss event (such as a personal bankruptcy) to the actual recognition of the loss (typically via the first full or partial

## **Table of Contents**

loan charge-off), and is determined based upon a study of our past loss experience by loan segment. Loss reserves for specified problem loans and leases are also detailed. All of the factors considered in the analysis of the adequacy of the allowance for loan and lease losses may be subject to change. To the extent actual outcomes differ from management estimates, additional provisions for loan and lease losses may be required that would adversely impact earnings in future periods.

The determination of the adequacy of the allowance for loan and lease losses and the periodic provisioning for estimated losses included in the consolidated financial statements is the responsibility of management and the Board of Directors. The evaluation process is undertaken on a quarterly basis.

Methodology employed for assessing the adequacy of the allowance consists of the following criteria:

The establishment of reserve amounts for all specifically identified classified loans and leases that have been designated as requiring attention by Lakeland.

The establishment of reserves for pools of homogeneous types of loans and leases not subject to specific review, including impaired loans under \$500,000, leases, 1-4 family residential mortgages, and consumer loans.

The establishment of reserve amounts for the unimpaired loans and leases in each portfolio based upon the historical average loss experience as modified by management's assessment of the loss emergence period for these portfolios and management's evaluation of key factors.

Consideration is given to the results of ongoing credit quality monitoring processes, the adequacy and expertise of Lakeland's lending staff, underwriting policies, loss histories, delinquency trends, and the cyclical nature of economic and business conditions. Since many of Lakeland's loans depend on the sufficiency of collateral as a secondary source of repayment, any adverse trend in the real estate markets could affect underlying values available to protect Lakeland from loss.

A loan that management designates as impaired is reviewed for charge-off when it is placed on non-accrual status with a resulting charge-off if the loan is not secured by collateral having sufficient liquidation value to repay the loan, and the loan is not in the process of collection. Charge-offs are recommended by the Chief Credit Officer and approved by the Board.

Mortgage loans originated and intended for sale in the secondary market are carried at the lower of aggregate cost or estimated fair value. Gains and losses on sales of loans are specifically identified and accounted for in accordance with U.S. GAAP which requires that an entity engaged in mortgage banking activities classify the retained mortgage-backed security or other interest, which resulted from the securitization of a mortgage loan held for sale, based upon its ability and intent to sell or hold these investments.

### *Bank Premises and Equipment*

Bank premises and equipment, including leasehold improvements, are stated at cost less accumulated depreciation. Depreciation expense is computed on the straight-line method over the estimated useful lives of the assets. Leasehold improvements are depreciated over the shorter of the estimated useful lives of the improvements or the terms of the related leases.

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

Other real estate owned (OREO) and other repossessed assets, representing property acquired through foreclosure (or deed-in-lieu-of-foreclosure), are carried at fair value less estimated disposal costs of the acquired property. Costs relating to holding the assets are charged to expense. An allowance for OREO or other repossessed assets is established, through charges to expense, to maintain properties at fair value less estimated costs to sell. Operating results of OREO and other repossessed assets, including rental income and operating expenses, are included in other expenses.

---

## **Table of Contents**

### *Mortgage Servicing*

Lakeland performs various servicing functions on loans owned by others. A fee, usually based on a percentage of the outstanding principal balance of the loan, is received for these services. At December 31, 2015 and 2014, Lakeland was servicing approximately \$30.0 million and \$33.9 million, respectively, of loans for others.

Lakeland originates certain mortgages under a definitive plan to sell or securitize those loans and service the loans owned by the investor. Upon the transfer of the mortgage loans in a sale or a securitization, Lakeland records the servicing assets retained. Lakeland records mortgage servicing rights and the loans based on relative fair values at the date of origination and evaluates the mortgage servicing rights for impairment at each reporting period. Lakeland also originates loans that it sells to other banks and investors and does not retain the servicing rights.

### *Mortgage Servicing Rights*

When mortgage loans are sold with servicing retained, servicing rights are initially recorded at fair value with the income statement effect recorded in gains on sales of loans. Fair value is based on market prices for comparable mortgage servicing contracts, when available, or alternatively, is based on a valuation model that calculates the present value of estimated future net servicing income. All classes of servicing assets are subsequently measured using the amortization method which requires servicing rights to be amortized into non-interest income in proportion to, and over the period of, the estimated future net servicing income of the underlying loans. As of December 31, 2015 and 2014, Lakeland had originated mortgage servicing rights of \$167,000 and \$217,000, respectively.

Under the amortization measurement method, Lakeland subsequently measures servicing rights at fair value at each reporting date and records any impairment in value of servicing assets in earnings in the period in which the impairment occurs. The fair values of servicing rights are subject to significant fluctuations as a result of changes in estimated and actual prepayment speeds and default rates and losses. Servicing fee income, which is reported on the income statement as commissions and fees, is recorded for fees earned for servicing loans. The fees are based on a contractual percentage of the outstanding principal or a fixed amount per loan, and are recorded as income when earned.

### *Transfers of Financial Assets*

Transfers of financial assets are accounted for as sales, when control over the assets has been surrendered. Control over transferred assets is deemed to be surrendered when (1) the assets have been isolated from the Company, put presumptively beyond the reach of the transferor and its creditors even in bankruptcy or other receivership, (2) the transferee obtains the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred assets and (3) the Company does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity or the ability to unilaterally cause the holder to return specific assets.

### *Customer Derivatives*

Lakeland enters into interest rate swaps ( swaps ) with loan customers to provide a facility to mitigate the fluctuations in the variable rate on the respective loans. These swaps are matched in offsetting terms to swaps that Lakeland enters into with an outside third party. The swaps are reported at fair value in other assets or other liabilities. Lakeland's swaps qualify as derivatives, but are not designated as hedging instruments, thus any net gain or loss resulting from changes in the fair value is recognized in other non-interest income. Further discussion of Lakeland's financial derivatives is set forth in Note 18 to the Consolidated Financial Statements.

The credit risk associated with derivatives executed with customers is similar as that involved in extending loans and is subject to normal credit policies. Collateral may be obtained based on management's assessment of the customer. The positions of customer derivatives are recorded at fair value and changes in value are included in non-interest income on the consolidated statement of income.

## **Table of Contents**

### *Earnings Per Share*

Earnings per share is calculated on the basis of the weighted average number of common shares outstanding during the year. Basic earnings per share excludes dilution and is computed by dividing income available to common shareholders by the weighted average common shares outstanding during the period. Diluted earnings per share takes into account the potential dilution that could occur if securities or other contracts to issue common stock were exercised and converted into common stock. Unless otherwise indicated, all weighted average, actual shares or per share information in the financial statements have been adjusted retroactively for the effect of stock dividends.

### *Employee Benefit Plans*

The Company has certain employee benefit plans covering substantially all employees. The Company accrues such costs as incurred.

We recognize the overfunded or underfunded status of pension and postretirement benefit plans in accordance with U.S. GAAP. Actuarial gains and losses, prior service costs or credits, and any remaining transition assets or obligations are recognized as a component of Accumulated Other Comprehensive Income, net of tax effects, until they are amortized as a component of net periodic benefit cost.

### *Stock-Based Compensation*

The Company's shareholders approved the 2009 Equity Compensation Program, which authorizes the granting of incentive stock options, supplemental stock options, restricted shares and restricted stock units to employees of the Company, including those employees serving as officers and directors of the Company. The plan authorizes the issuance of up to 2.3 million shares in connection with options and awards granted under the 2009 program. The Company's stock option grants under this plan expire 10 years from the date of grant, ninety days after termination of service other than for cause, or one year after death or disability of the grantee. In 2014, the Company began issuing restricted stock units (RSUs), some of which have performance conditions attached to them. The Company generally issues shares for option exercises from its treasury stock using the cost method or issues new shares if no treasury shares are available.

The Company established the 2000 Equity Compensation Program which authorizes the granting of incentive stock options, supplemental stock options and restricted stock to employees of the Company, which includes those employees serving as officers and directors of the Company. The plan authorized 2,613,185 shares of common stock of the Company. All of the Company's stock option grants expire 10 years from the date of grant, thirty days after termination of service other than for cause, or one year after death or disability of the grantee. The Company has no option or restricted stock awards with market or performance conditions attached to them under the 2000 Equity Compensation Program. No further awards will be granted from the 2000 program.

### *Comprehensive Income (Loss)*

The Company reports comprehensive income (loss) in addition to net income (loss) from operations. Comprehensive income (loss) is a more inclusive financial reporting methodology that includes disclosure of certain financial information that historically has not been recognized in the calculation of net income.

### *Goodwill and Other Identifiable Intangible Assets*

The Company reviews goodwill for impairment annually as of November 30 or when circumstances indicate a potential for impairment at the reporting unit level. U.S. GAAP requires at least an annual review of the fair value of a Reporting Unit that has goodwill in order to determine if it is more likely than not (that is, a likelihood of more than 50%) that the fair value of a reporting unit is less than its carrying amount, including goodwill. If

---

**Table of Contents**

this qualitative test determines it is unlikely (less than 50% probability) the carrying value of the Reporting Unit is less than its fair value, then the company does not have to perform a Step One impairment test. If the probability is greater than 50%, a Step One goodwill impairment test is required. The Step One test compares the fair value of each reporting unit to the carrying value of its net assets, including goodwill. If the fair value is less than carrying value, the Step Two test is required. The Company has determined that it has one reporting unit, Community Banking.

The Company performed a qualitative analysis to determine whether the weight of evidence, the significance of all identified events and circumstances indicated a greater than 50% likelihood existed that the carrying value of the Reporting Unit exceeded its fair value and if a Step One Test would be required. The Company identified nine qualitative assessments that are relative to the banking industry and to the Company. These factors included macroeconomic factors, banking industry conditions, banking merger and acquisition trends, Lakeland's historical performance, the Company's stock price, the expected performance of Lakeland, the change of control premium of the Company versus its peers and other miscellaneous factors. After reviewing and weighting these factors, the Company, as well as a third party adviser, determined as of November 30, 2015 that there was a less than 50% probability that the fair value of the Company was less than its carrying amount. Therefore, no Step One test was required.

*Bank Owned Life Insurance*

Lakeland invests in bank owned life insurance ( BOLI ). BOLI involves the purchasing of life insurance by Lakeland on a chosen group of employees. Lakeland is owner and beneficiary of the policies. At December 31, 2015 and 2014, Lakeland had \$65.4 million and \$57.5 million, respectively, in BOLI. Income earned on BOLI was \$2.0 million, \$1.5 million and \$1.4 million for the years ended December 31, 2015, 2014 and 2013, respectively. BOLI is accounted for using the cash surrender value method and is recorded at its net realizable value.

*Income Taxes*

The Company accounts for income taxes under the asset and liability method of accounting for income taxes. Deferred tax assets and liabilities are determined based on the difference between the financial statement and tax bases of assets and liabilities as measured by the enacted tax rates that will be in effect when these differences reverse. Deferred tax expense is the result of changes in deferred tax assets and liabilities. The principal types of differences between assets and liabilities for financial statement and tax return purposes are allowance for loan and lease losses, core deposit intangibles, deferred loan fees and deferred compensation.

The Company evaluates tax positions that may be uncertain using a recognition threshold of more-likely-than-not, and a measurement attribute for all tax positions taken or expected to be taken on a tax return, in order for those tax positions to be recognized in the financial statements. Additional information regarding the Company's uncertain tax positions is set forth in Note 9 to the Consolidated Financial Statements.

*Variable Interest Entities*

Management has determined that Lakeland Bancorp Capital Trust II and Lakeland Bancorp Capital Trust IV (collectively, the Trusts ) qualify as variable interest entities. The Trusts issued mandatorily redeemable preferred stock to investors and loaned the proceeds to the Company. The Trusts hold, as their sole asset, subordinated debentures issued by the Company. The Company is not considered the primary beneficiary of the Trusts, therefore the Trusts are not consolidated in the Company's financial statements.

The Company's maximum exposure to the Trusts is \$30 million at December 31, 2015 which is the Company's liability to the Trusts and includes the Company's investment in the Trusts.



---

**Table of Contents**

The Federal Reserve has issued guidance on the regulatory capital treatment for the trust preferred securities issued by the Trusts. The rule retains the current maximum percentage of total capital permitted for trust preferred securities at 25%, but enacts other changes to the rules governing trust preferred securities that affect their use as part of the collection of entities known as restricted core capital elements. The rule allows bank holding companies to continue to count trust preferred securities as Tier 1 Capital. The Company's capital ratios continue to be categorized as well-capitalized under the regulatory framework for prompt corrective action. Under the Collins Amendment to the Dodd-Frank Wall Street Reform and Consumer Protection Act, any new issuance of trust preferred securities by the Company would not be eligible as regulatory capital.

*New Accounting Pronouncements*

In February 2016, the Financial Accounting Standards Board ( FASB ) issued accounting guidance that requires all lessees to recognize a lease liability and a right-of-use asset, measured at the present value of the future minimum lease payments, at the lease commencement date. Lessor accounting remains largely unchanged under the new guidance. The guidance is effective for fiscal years beginning after December 15, 2018, including interim reporting periods within that reporting period, with early adoption permitted. A modified retrospective approach must be applied for leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements. The Company is currently assessing the impact that the guidance will have on the Company's consolidated financial statements.

In January 2016, the FASB issued an accounting standards update intended to improve the recognition and measurement of financial instruments. Specifically, the accounting standards update requires all equity instruments, with the exception of those that are accounted for under the equity method of accounting, to be measured at fair value with changes in the fair value recognized through net income. Additionally, public business entities are required to use the exit price notion when measuring the fair value of financial instruments for disclosure purposes. The amendments in this update also require an entity to present separately in other comprehensive income the portion of the total change in the fair value of a liability resulting from a change in the instrument-specific credit risk when the entity has elected to measure the liability at fair value in accordance with the fair value option for financial instruments. This amendment is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2017.

In September 2015, the FASB issued an accounting standards update simplifying the accounting for adjustments made to provisional amounts recognized in a business combination, eliminating the requirement to retrospectively account for those adjustments. To simplify the accounting for adjustments made to provisional amounts, the amendments in the accounting standards update require that the acquirer recognize adjustments to provisional amounts that are identified during the measurement period in the reporting period in which the adjustment amount is determined. The acquirer is required to also record, in the same period's financial statements, the effect on earnings of changes in depreciation, amortization, or other income effects, if any, as a result of the change to the provisional amounts, calculated as if the accounting had been completed at the acquisition date. In addition, an entity is required to present separately on the face of the income statement or disclose in the notes to the financial statements the portion of the amount recorded in current-period earnings by line item that would have been recorded in previous reporting periods if the adjustment to the provisional amounts had been recognized as of the acquisition date. This amendment is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2015.

In May 2015, the FASB issued an accounting standards update clarifying how investments valued using the net asset value practical expedient within the fair value hierarchy should be classified. The accounting standards update was issued to address diversity in practice by exempting investments measured using the net asset value expedient from categorization in the fair value hierarchy. This accounting standards update is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2015. The adoption of this update is not expected to have a material impact on the Company's financial statements.

---

**Table of Contents**

In April 2015, the FASB issued an accounting standards update requiring that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of the debt liability consistent with the presentation of debt discounts. The purpose of this update is to simplify the presentation of debt issuance costs and to align the US GAAP presentation of debt more closely with international accounting standards. In August 2015, the FASB issued a subsequent update which discussed presentation and subsequent measurement of debt issuance costs associated with line-of-credit arrangements. These amendments are effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2015. The adoption of these updates are not expected to have a material impact on the Company's financial statements.

In January 2015, the FASB issued an accounting standards update regarding the elimination of the concept of the extraordinary items from the statement of operations. The purpose of this update is to simplify the statement of operations presentation and to align the US GAAP income statement more closely with international accounting standards. This update is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2015. The adoption of this update is not expected to have a material impact on the Company's financial statements.

In June 2014, the FASB issued an accounting standards update that aligns the accounting for repurchase to maturity transactions and repurchase agreements executed as a repurchase financing with the accounting for other typical repurchase agreements. Going forward, these transactions would all be accounted for as secured borrowings. This update is effective for the first interim or annual period beginning after December 15, 2014. In addition, the disclosure of certain transactions accounted for as a sale is effective for the first interim or annual period beginning on or after December 15, 2014, and the disclosure for transactions accounted for as secured borrowings is required for annual periods beginning after December 15, 2014, and interim periods after March 15, 2015. The Company adopted this update in 2015. The Company does not engage in repurchase to maturity transactions, and therefore the adoption of this update did not have a material impact on the Company's financial results.

In May 2014, the FASB issued an accounting standards update that clarifies the principles for recognizing revenue. The core principle of the guidance is that an entity should recognize revenue to depict the transfer of promised goods or services to a customer in an amount that reflects the consideration to which the entity expects to be entitled in exchange for these goods or services. This guidance is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2017. The Company is still evaluating the potential impact on the Company's financial statements.

**NOTE 2 - ACQUISITIONS**

*Harmony Bank*

Lakeland Bancorp, Lakeland Bank and Harmony Bank signed a merger agreement on February 17, 2016, pursuant to which Harmony Bank will be merged with and into Lakeland Bank, with Lakeland Bank as the surviving bank. The merger agreement provides that shareholders of Harmony Bank will receive 1.25 shares of Lakeland Bancorp common stock for each share of Harmony Bank common stock that they own at the effective time of the merger. Lakeland Bancorp expects to issue an aggregate of approximately 3.0 million shares of its common stock in the merger and will cash out Harmony Bank options that remain outstanding at the effective time of the merger. The closing of the merger is subject to receipt of approvals from regulators, approval of the merger by Harmony Bank's shareholders and other customary conditions. Harmony Bank, a New Jersey state-chartered commercial bank that focuses on serving consumers and small-to-medium-size businesses, is headquartered in Jackson, New Jersey, with additional branch offices in Lakewood and Toms River, New Jersey. As of December 31, 2015, Harmony Bank had total assets, total loans, total deposits and total stockholders' equity of \$295 million, \$241 million, \$257 million and \$28 million, respectively.

---

**Table of Contents**

*Pascack Bancorp*

On January 7, 2016, the Company completed its acquisition of Pascack Bancorp, Inc. ( *Pascack* ), a bank holding company headquartered in Waldwick, New Jersey. Pascack was the parent of Pascack Community Bank. This acquisition enables the Company to broaden its presence in Bergen and Essex counties. Effective as of the close of business on January 7, 2016, Pascack merged into the Company, and Pascack Community Bank merged into Lakeland Bank. The Merger Agreement provided that the shareholders of Pascack would receive, at their election, for each outstanding share of Pascack common stock that they own at the effective time of the merger, either 0.9576 shares of Lakeland Bancorp common stock or \$11.35 in cash, subject to proration as described in the Merger Agreement, so that 90% of the aggregate merger consideration was shares of Lakeland Bancorp common stock and 10% was cash. Lakeland Bancorp issued an aggregate of 3,314,452 shares of its common stock in the merger and paid approximately \$4.4 million in cash excluding the cash paid in connection with the cancellation of Pascack stock options. Outstanding Pascack stock options were paid out in cash at the difference between \$11.35 and an average strike price of \$7.37 for a total cash payment of \$122,000. As of January 7, 2016, Pascack had total assets, total loans, total deposits and total capital of \$386 million, \$320 million, \$303 million and \$23 million, respectively.

The acquisition was accounted for under the acquisition method of accounting and accordingly, assets acquired, liabilities assumed and consideration exchanged were recorded at their estimated fair values as of the acquisition date. Pascack's assets were recorded at their preliminary estimated fair values as of January 7, 2016 and Pascack's results of operations will be included in the Company's Consolidated Statements of Income from that date forward.

Direct costs related to the acquisition were expensed as incurred. During 2015, the Company incurred \$1.2 million, of merger and acquisition integration-related expenses, which have been separately reflected in the Company's Consolidated Statements of Income.

*Somerset Hills Bancorp*

On May 31, 2013, the Company completed its acquisition of Somerset Hills Bancorp ( *Somerset Hills* ), a bank holding company headquartered in Bernardsville, New Jersey. Somerset Hills was the parent company of Somerset Hills Bank, Sullivan Financial Services, and Somerset Hills Investment Holdings. This acquisition enabled the Company to expand into Somerset and Union Counties and to broaden its presence in Morris County.

The acquisition was accounted for under the acquisition method of accounting and accordingly, assets acquired, liabilities assumed and consideration exchanged were recorded at their estimated fair values as of the acquisition date. Somerset Hills' assets were recorded at their preliminary estimated fair values as of May 31, 2013 and Somerset Hills' results of operations have been included in the Company's Consolidated Statements of Income since that date.

**Table of Contents**

NOTE 3 - INVESTMENT SECURITIES

The amortized cost, gross unrealized gains and losses, and the fair value of the Company's available for sale and held to maturity securities are as follows:

AVAILABLE FOR SALE	Amortized Cost	December 31, 2015		Fair Value	Amortized Cost	December 31, 2014		Fair Value
		Gross Unrealized Gains (in thousands)	Gross Unrealized Losses (in thousands)			Gross Unrealized Gains (in thousands)	Gross Unrealized Losses (in thousands)	
U.S. treasury and U.S. government agencies	\$ 97,617	\$ 190	\$ (674)	\$ 97,133	\$ 94,466	\$ 261	\$ (807)	\$ 93,920
Mortgage-backed securities, residential	280,018	1,717	(2,283)	279,452	309,162	2,868	(2,075)	309,955
Mortgage-backed securities, multifamily	10,249		(129)	10,120	4,973	3		4,976
Obligations of states and political subdivisions	35,639	910	(51)	36,498	29,764	888	(133)	30,519
Other debt securities	498	3		501	494	11		505
Equity securities	16,550	2,393	(298)	18,645	16,196	1,589	(211)	17,574
	<b>\$ 440,571</b>	<b>\$ 5,213</b>	<b>\$ (3,435)</b>	<b>\$ 442,349</b>	<b>\$ 455,055</b>	<b>\$ 5,620</b>	<b>\$ (3,226)</b>	<b>\$ 457,449</b>

HELD TO MATURITY	Amortized Cost	December 31, 2015		Fair Value	Amortized Cost	December 31, 2014		Fair Value
		Gross Unrealized Gains (in thousands)	Gross Unrealized Losses (in thousands)			Gross Unrealized Gains (in thousands)	Gross Unrealized Losses (in thousands)	
U.S. government agencies	\$ 30,477	\$ 289	\$ (94)	\$ 30,672	\$ 20,477	\$ 232	\$ (84)	\$ 20,625
Mortgage-backed securities, residential	36,466	411	(426)	36,451	42,309	645	(385)	42,569
Mortgage-backed securities, multifamily	2,159		(60)	2,099	2,259		(60)	2,199
Obligations of states and political subdivisions	45,617	809	(156)	46,270	41,401	658	(90)	41,969
Other debt securities	2,021	81		2,102	1,530	138		1,668
	<b>\$ 116,740</b>	<b>\$ 1,590</b>	<b>\$ (736)</b>	<b>\$ 117,594</b>	<b>\$ 107,976</b>	<b>\$ 1,673</b>	<b>\$ (619)</b>	<b>\$ 109,030</b>

The following table lists contractual maturities of investment securities classified as available for sale and held to maturity. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	December 31, 2015			
	Available for Sale		Held to Maturity	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
	(in thousands)			
Due in one year or less	\$ 3,180	\$ 3,214	\$ 6,407	\$ 6,407
Due after one year through five years	75,011	75,301	18,478	18,732
Due after five years through ten years	51,464	51,477	45,734	46,296

Edgar Filing: LAKELAND BANCORP INC - Form 10-K

Due after ten years	4,099	4,140	7,496	7,609
	133,754	134,132	78,115	79,044
Mortgage-backed securities	290,267	289,572	38,625	38,550
Equity securities	16,550	18,645		
Total securities	\$ 440,571	\$ 442,349	\$ 116,740	\$ 117,594

-69-

**Table of Contents**

The following table shows proceeds from sales of securities, gross gains and gross losses on sales and calls of securities for the periods indicated:

	Years ended December 31,		
	2015	2014	2013
	(in thousands)		
Sale proceeds	\$ 33,613	\$ 17,020	\$ 64,020
Gross gains	304	346	893
Gross losses	(63)	(344)	(54)

The above sales in 2014 include sales of \$1.4 million in held to maturity mortgage-backed securities of which the Company had already collected over 90% of the principal outstanding. The Company realized \$73,000 in gains on sales of these securities.

Gains or losses on sales of securities are based on the net proceeds and the adjusted carrying amount of the securities sold using the specific identification method.

Securities with a carrying value of approximately \$347.7 million and \$356.1 million at December 31, 2015 and 2014, respectively, were pledged to secure public deposits and for other purposes required by applicable laws and regulations.

The following table indicates the length of time individual securities have been in a continuous unrealized loss position at December 31, 2015 and 2014:

December 31, 2015	Less than 12 months		12 months or longer		Number of securities	Total	
	Fair value	Unrealized Losses	Fair value	Unrealized Losses		Fair value	Unrealized Losses
<b>AVAILABLE FOR SALE</b>							
<b>U.S. treasury and</b>							
U.S. government agencies	\$ 80,192	\$ 674	\$	\$	16	\$ 80,192	\$ 674
Mortgage-backed securities, residential	103,749	1,043	50,095	1,240	50	153,844	2,283
Mortgage-backed securities, multifamily	10,120	129			2	10,120	129
<b>Obligations of states and political</b>							
subdivisions	2,051	4	1,466	47	7	3,517	51
Equity securities	247	24	4,643	274	3	4,890	298
	\$ 196,359	\$ 1,874	\$ 56,204	\$ 1,561	78	\$ 252,563	\$ 3,435
<b>HELD TO MATURITY</b>							
U.S. government agencies	\$ 15,683	\$ 94	\$	\$	3	\$ 15,683	\$ 94
Mortgage-backed securities, residential	20,283	262	6,687	164	11	26,970	426
Mortgage-backed securities, multifamily	1,223	18	876	42	2	2,099	60
<b>Obligations of states and political</b>							
subdivisions	9,181	149	2,043	7	15	11,224	156
	\$ 46,370	\$ 523	\$ 9,606	\$ 213	31	\$ 55,976	\$ 736

**Table of Contents**

December 31, 2014	Less than 12 months		12 months or longer		Number of securities	Total	
	Fair value	Unrealized Losses	Fair value	Unrealized Losses		Fair value	Unrealized Losses
(dollars in thousands)							
<b>AVAILABLE FOR SALE</b>							
U.S. treasury and U.S. government agencies	\$ 5,057	\$ 28	\$ 46,135	\$ 779	11	\$ 51,192	\$ 807
Mortgage-backed securities, residential	34,832	177	74,414	1,898	28	109,246	2,075
Obligations of states and political subdivisions	1,266	29	5,033	104	12	6,299	133
Equity securities			4,819	211	2	4,819	211
	\$ 41,155	\$ 234	\$ 130,401	\$ 2,992	53	\$ 171,556	\$ 3,226
<b>HELD TO MATURITY</b>							
U.S. government agencies	\$	\$	\$ 5,736	\$ 84	1	\$ 5,736	\$ 84
Mortgage-backed securities, residential	6,236	50	17,557	335	8	23,793	385
Mortgage-backed securities, multifamily			2,199	60	2	2,199	60
Obligations of states and political subdivisions	1,290	7	4,206	83	13	5,496	90
	\$ 7,526	\$ 57	\$ 29,698	\$ 562	24	\$ 37,224	\$ 619

Management has evaluated the securities in the above table and has concluded that none of the securities with unrealized losses has impairments that are other-than-temporary. Fair value below cost is solely due to interest rate movements and is deemed temporary.

Investment securities, including the mortgage-backed securities and corporate securities, are evaluated on a periodic basis to determine if factors are identified that would require further analysis. In evaluating the Company's securities, management considers the following items:

The Company's ability and intent to hold the securities, including an evaluation of the need to sell the security to meet certain liquidity measures, or whether the Company has sufficient levels of cash to hold the identified security in order to recover the entire amortized cost of the security;

The financial condition of the underlying issuer;

The credit ratings of the underlying issuer and if any changes in the credit rating have occurred;

The length of time the security's fair value has been less than amortized cost; and

Adverse conditions related to the security or its issuer if the issuer has failed to make scheduled payments or other factors. If the above factors indicate an additional analysis is required, management will perform a discounted cash flow analysis evaluating the security.

As of December 31, 2015, the equity securities include investments in other financial institutions for market appreciation purposes. These equities had a purchase price of \$2.7 million and market value of \$5.1 million as of December 31, 2015.

As of December 31, 2015, equity securities also included \$13.6 million in investment funds that do not have a quoted market price but use net asset value per share or its equivalent to measure fair value.





**Table of Contents**

The investment funds include \$2.9 million in funds that are primarily invested in community development loans that are guaranteed by the Small Business Administration (SBA). Because the funds are primarily guaranteed by the federal government there are minimal changes in market value between accounting periods. These funds can be redeemed within 60 days notice at the net asset value less unpaid management fees with the approval of the fund manager. As of December 31, 2015, the net amortized cost equaled the market value of the investment. There are no unfunded commitments related to this investment.

The investment funds also include \$10.7 million in funds that are invested in government guaranteed loans, mortgage-backed securities, small business loans and other instruments supporting affordable housing and economic development. The Company may redeem these funds at the net asset value calculated at the end of the current business day less any unpaid management fees. As of December 31, 2015, the amortized cost of these securities was \$11.0 million and the fair value was \$10.7 million. There are no restrictions on redemptions for the holdings in these investments other than the notice required by the fund manager. There are no unfunded commitments related to this investment.

**NOTE 4 LOANS AND LEASES AND OTHER REAL ESTATE**

The following sets forth the composition of Lakeland's loan and lease portfolio for the years ended December 31, 2015 and 2014:

	December 31,	
	2015	2014
	(in thousands)	
Commercial, secured by real estate	<b>\$ 1,761,589</b>	\$ 1,529,761
Commercial, industrial and other	<b>307,044</b>	238,252
Leases	<b>56,660</b>	54,749
Real estate-residential mortgage	<b>389,692</b>	431,190
Real estate-construction	<b>118,070</b>	64,020
Home equity and consumer	<b>334,891</b>	337,642
<b>Total loans and leases</b>	<b>2,967,946</b>	2,655,614
Less deferred fees	<b>(2,746)</b>	(1,788)
<b>Loans and leases, net of deferred fees</b>	<b>\$ 2,965,200</b>	\$ 2,653,826

As of December 31, 2015 and 2014, Home Equity and Consumer loans included overdraft deposit balances of \$705,000 and \$791,000, respectively. At December 31, 2015 and December 31, 2014, Lakeland had \$738.7 million and \$338.5 million in residential loans pledged for potential borrowings at the Federal Home Loan Bank of New York (FHLB).

Purchased Credit-Impaired (PCI) loans, are loans acquired at a discount that is due, in part, to credit quality. In conjunction with the Somerset Hills acquisition, three loan relationships totaling \$1.6 million were deemed to be PCI loans at May 31, 2013 (the acquisition date). PCI loans are accounted for in accordance with ASC Subtopic 310-30 and are initially recorded at fair value (as determined by the present value of expected future cash flows) with no valuation allowance (i.e., allowance for loan losses).

Subsequent to the acquisition date, one PCI loan for \$149,000 was paid in full in the first quarter of 2014. There was credit deterioration in the remaining two loans. One loan totaling \$250,000 was charged off in the third quarter of 2014. The remaining loan relationship at a balance of \$1.3 million was charged off in 2015. Lakeland recognized \$109,000 and \$46,000 of interest income on credit impaired loans for the years ended December 31, 2014 and 2013, respectively.

*Portfolio Segments*

Lakeland currently manages its credit products and the respective exposure to credit losses (credit risk) by the following specific portfolio segments which are levels at which Lakeland develops and documents its systematic methodology to determine the allowance for loan and lease losses attributable to each respective portfolio segment. These segments are:

Edgar Filing: LAKELAND BANCORP INC - Form 10-K

Commercial, secured by real estate - consists of commercial mortgage loans secured by owner occupied properties and non-owner occupied properties. The loans secured by owner occupied

-72-

**Table of Contents**

properties involve a variety of property types to conduct the borrower's operations. The primary source of repayment for this type of loan is the cash flow from the business and is based upon the borrower's financial health and the ability of the borrower and the business to repay. The loans secured by non-owner occupied properties involve investment properties for warehouse, retail, office space, etc., with a history of occupancy and cash flow. This commercial real estate category contains mortgage loans to the developers and owners of commercial real estate where the borrower intends to operate or sell the property at a profit and use the income stream or proceeds from the sale(s) to repay the loan.

Commercial, industrial and other - are loans made to provide funds for equipment and general corporate needs. Repayment of a loan primarily uses the funds obtained from the operation of the borrower's business. Commercial loans also include lines of credit that are utilized to finance a borrower's short-term credit needs and/or to finance a percentage of eligible receivables and inventory.

Leases - includes a small portfolio of equipment leases, which consists of leases primarily for essential equipment used by small to medium sized businesses.

Real estate - residential mortgage - contains permanent mortgage loans principally to consumers secured by residential real estate. Residential real estate loans are evaluated for the adequacy of repayment sources at the time of approval, based upon measures including credit scores, debt-to-income ratios, and collateral values. Loans may be either conforming or non-conforming.

Real estate-construction - construction loans, as defined, are intended to finance the construction of commercial properties and include loans for the acquisition and development of land. Construction loans represent a higher degree of risk than permanent real estate loans and may be affected by a variety of factors such as the borrower's ability to control costs and adhere to time schedules and the risk that constructed units may not be absorbed by the market within the anticipated time frame or at the anticipated price. The loan commitment on these loans often includes an interest reserve that allows the lender to periodically advance loan funds to pay interest charges on the outstanding balance of the loan.

Home Equity and consumer - includes primarily home equity loans and lines, installment loans, personal lines of credit and automobile loans. The home equity category consists mainly of loans and revolving lines of credit to consumers which are secured by residential real estate. These loans are typically secured with second mortgages on the homes, although many are secured with first mortgages. Other consumer loans include installment loans used by customers to purchase automobiles, boats and recreational vehicles.

*Non-accrual and Past Due Loans*

The following schedule sets forth certain information regarding Lakeland's non-accrual loans and leases, its other real estate owned and other repossessed assets, and accruing troubled debt restructurings (TDRs):

(in thousands)	At December 31,	
	2015	2014
Commercial, secured by real estate	\$ 10,446	\$ 7,424
Commercial, industrial and other	103	308
Leases	316	88
Real estate - residential mortgage	8,664	9,246
Real estate - construction		188
Home equity and consumer	3,167	3,415
<b>Total non-accrual loans and leases</b>	<b>22,696</b>	<b>20,669</b>
Other real estate and other repossessed assets	983	1,026
<b>TOTAL NON-PERFORMING ASSETS</b>	<b>\$ 23,679</b>	<b>\$ 21,695</b>

Edgar Filing: LAKELAND BANCORP INC - Form 10-K

Troubled debt restructurings, still accruing	<b>\$ 10,108</b>	\$ 10,579
--	------------------	-----------

-73-

**Table of Contents**

Non-accrual loans included \$2.5 million and \$1.3 million of troubled debt restructurings for the years ended December 31, 2015 and 2014, respectively. As of December 31, 2015, the Company had \$7.9 million in residential mortgages and consumer home equity loans included in the table above that were in the process of foreclosure.

An age analysis of past due loans, segregated by class of loans as of December 31, 2015 and 2014 is as follows:

December 31, 2015	30-59 Days Past Due	60-89 Days Past Due	Greater Than 89 Days	Total Past Due (in thousands)	Current	Total Loans and Leases	Recorded Investment greater than 89 Days and still accruing
Commercial, secured by real estate	\$ 1,465	\$ 693	\$ 7,853	\$ 10,011	\$ 1,751,578	\$ 1,761,589	\$
Commercial, industrial and other	205		103	308	306,736	307,044	
Leases	62	26	316	404	56,256	56,660	
Real estate - residential mortgage	1,361	725	7,472	9,558	380,134	389,692	
Real estate - construction					118,070	118,070	
Home equity and consumer	876	141	3,498	4,515	330,376	334,891	331
	\$ 3,969	\$ 1,585	\$ 19,242	\$ 24,796	\$ 2,943,150	\$ 2,967,946	\$ 331

December 31, 2014	30-59 Days Past Due	60-89 Days Past Due	Greater Than 89 Days	Total Past Due (in thousands)	Current	Total Loans and Leases	Recorded Investment greater than 89 Days and still accruing
Commercial, secured by real estate	\$ 2,714	\$ 2,999	\$ 5,972	\$ 11,685	\$ 1,518,076	\$ 1,529,761	\$
Commercial, industrial and other	944	2	308	1,254	236,998	238,252	
Leases	108	24	88	220	54,529	54,749	
Real estate - residential mortgage	3,325	354	6,710	10,389	420,801	431,190	
Real estate - construction	224		188	412	63,608	64,020	
Home equity and consumer	1,583	598	2,951	5,132	332,510	337,642	66
	\$ 8,898	\$ 3,977	\$ 16,217	\$ 29,092	\$ 2,626,522	\$ 2,655,614	\$ 66

**Table of Contents***Impaired Loans*

Lakeland's policy regarding impaired loans is discussed in Note 1 – Summary of Accounting Policies – Loans and Leases and Allowance for Loan and Lease Losses. The Company defines impaired loans as all non-accrual loans with recorded investments of \$500,000 or greater. Impaired loans also includes all loans modified in troubled debt restructurings.

December 31, 2015	Recorded Investment in Impaired loans	Contractual Unpaid Principal Balance	Related Allowance (in thousands)	Interest Income Recognized	Average Investment in Impaired loans
Loans without related allowance:					
Commercial, secured by real estate	\$ 14,065	\$ 14,712	\$	\$ 344	\$ 12,928
Commercial, industrial and other	209	887		14	749
Leases					
Real estate - residential mortgage	2,195	2,242			2,096
Real estate - construction					94
Home equity and consumer	574	575		5	762
Loans with related allowance:					
Commercial, secured by real estate	5,721	5,918	598	271	6,249
Commercial, industrial and other	1,023	1,023	77	32	717
Leases	6	6	1		
Real estate-residential mortgage	832	865	73	37	840
Real estate-construction	380	380	21	13	308
Home equity and consumer	1,001	1,013	73	54	1,006
Total:					
Commercial, secured by real estate	\$ 19,786	\$ 20,630	\$ 598	\$ 615	\$ 19,177
Commercial, industrial and other	1,232	1,910	77	46	1,466
Leases	6	6	1		
Real estate - residential mortgage	3,027	3,107	73	37	2,936
Real estate - construction	380	380	21	13	402
Home equity and consumer	1,575	1,588	73	59	1,768
	\$ 26,006	\$ 27,621	\$ 843	\$ 770	\$ 25,749

**Table of Contents**

December 31, 2014	Recorded Investment in Impaired loans	Contractual Unpaid Principal Balance	Related Allowance (in thousands)	Interest Income Recognized	Average Investment in Impaired loans
<b>Loans without related allowance:</b>					
Commercial, secured by real estate	\$ 14,172	\$ 15,520	\$	\$ 436	\$ 16,092
Commercial, industrial and other	327	1,697		43	1,513
Real estate-residential mortgage	1,681	1,681			308
Real estate-construction	188	552			464
Home equity and consumer	741	741		7	153
<b>Loans with related allowance:</b>					
Commercial, secured by real estate	5,666	5,818	634	156	3,858
Commercial, industrial and other	425	425	10	9	342
Real estate - residential mortgage	1,238	1,238	217	19	438
Real estate - construction					
Home equity and consumer	1,255	1,255	1,031	41	975
<b>Total:</b>					
Commercial, secured by real estate	\$ 19,838	\$ 21,338	\$ 634	\$ 592	\$ 19,950
Commercial, industrial and other	752	2,122	10	52	1,855
Real estate - residential mortgage	2,919	2,919	217	19	746
Real estate - construction	188	552			464
Home equity and consumer	1,996	1,996	1,031	48	1,128
	\$ 25,693	\$ 28,927	\$ 1,892	\$ 711	\$ 24,143

December 31, 2013	Recorded Investment in Impaired loans	Contractual Unpaid Principal Balance	Related Allowance (in thousands)	Interest Income Recognized	Average Investment in Impaired loans
<b>Loans without related allowance:</b>					
Commercial, secured by real estate	\$ 8,223	\$ 9,656	\$	\$ 198	\$ 8,853
Commercial, industrial and other	4,020	4,118		189	4,333
Real estate - residential mortgage	617	672			622
Real estate - construction	501	2,411			2,111
Home equity and consumer	17	17		1	17
<b>Loans with related allowance:</b>					
Commercial, secured by real estate	10,152	10,217	739	442	9,727
Commercial, industrial and other	155	155	31	5	396
Home equity and consumer	934	936	140	42	907
<b>Total:</b>					
Commercial, secured by real estate	\$ 18,375	\$ 19,873	\$ 739	\$ 640	\$ 18,580
Commercial, industrial and other	4,175	4,273	31	194	4,729
Real estate - residential mortgage	617	672			622
Real estate - construction	501	2,411			2,111
Home equity and consumer	951	953	140	43	924
	\$ 24,619	\$ 28,182	\$ 910	\$ 877	\$ 26,966

Interest which would have been accrued on impaired loans and leases during 2015, 2014 and 2013 was \$1.6 million, \$1.8 million and \$2.2 million, respectively.





**Table of Contents***Credit Quality Indicators*

The class of loans are determined by internal risk rating. Management closely and continually monitors the quality of its loans and leases and assesses the quantitative and qualitative risks arising from the credit quality of its loans and leases. It is the policy of Lakeland to require that a Credit Risk Rating be assigned to all commercial loans and loan commitments. The Credit Risk Rating System has been developed by management to provide a methodology to be used by Loan Officers, Department Heads and Senior Management in identifying various levels of credit risk that exist within Lakeland's loan portfolios. The risk rating system assists Senior Management in evaluating Lakeland's loan portfolio, analyzing trends, and determining the proper level of required reserves to be recommended to the Board. In assigning risk ratings, management considers, among other things, a borrower's debt service coverage, earnings strength, loan to value ratios, industry conditions and economic conditions. Management categorizes loans and commitments into a one (1) to nine (9) numerical structure with rating 1 being the strongest rating and rating 9 being the weakest. Ratings 1 through 5W are considered Pass ratings. Pass ratings on loans are given to loans that management considers to be of acceptable or better quality. A rating of 5W, or Watch is a loan that requires more than the usual amount of monitoring due to declining earnings, strained cash flow, increasing leverage and/or weakening market. These borrowers generally have limited additional debt capacity and modest coverage and average or below average asset quality, margins and market share. Rating 6, Other Assets Especially Mentioned is used for loans exhibiting identifiable credit weakness which if not checked or corrected could weaken the loan quality or inadequately protect the bank's credit position at some future date. Rating 7, Substandard, is used on loans that are inadequately protected by the current sound worth and paying capacity of the obligors or of the collateral pledged, if any. A substandard loan has a well-defined weakness or weaknesses that may jeopardize the liquidation of the debt. Rating 8, Doubtful, are loans that exhibit all of the weaknesses inherent in substandard loans, but have the added characteristics that the weaknesses make collection or liquidation in full improbable on the basis of existing facts. Rating 9, Loss, is a rating for loans or portions of loans that are considered uncollectible and of such little value that their continuance as bankable loans is not warranted.

The following table shows Lakeland's commercial loan portfolio as of December 31, 2015 and 2014, by the risk ratings discussed above (in thousands):

December 31, 2015	Commercial, secured by real estate	Commercial, Industrial and other	Real estate- construction
Risk Rating			
1	\$	\$ 3,517	\$
2		9,662	
3	65,199	56,895	
4	526,909	111,702	19,125
5	1,044,888	105,301	94,535
5W - Watch	43,342	4,259	146
6 - Other Assets Especially Mentioned	34,570	4,105	1,851
7 - Substandard	46,681	11,603	2,413
8 - Doubtful			
9 - Loss			
<b>Total</b>	<b>\$ 1,761,589</b>	<b>\$ 307,044</b>	<b>\$ 118,070</b>

**Table of Contents**

December 31, 2014

Risk Rating	Commercial, secured by real estate	Commercial, Industrial and other	Real estate- construction
1	\$	\$ 1,040	\$
2		8,755	
3	69,243	30,386	
4	479,667	91,836	7,527
5	867,023	69,723	51,833
5W - Watch	40,991	15,572	225
6 - Other Assets Especially Mentioned	27,764	8,057	2,710
7 - Substandard	45,073	12,883	1,725
8 - Doubtful			
9 - Loss			
<b>Total</b>	<b>\$ 1,529,761</b>	<b>\$ 238,252</b>	<b>\$ 64,020</b>

This table does not include consumer or residential loans or leases because they are evaluated on their payment status.

*Allowance for Loan and Lease Losses*

In 2015, The Company refined and enhanced its assessment of the adequacy of the allowance for loan and lease losses by extending the lookback period on its commercial loan portfolios from three years to five years and by extending the lookback period for all other portfolios from two to three years in order to capture more of the economic cycle. It also enhanced its qualitative factor framework to include a factor that captures the risk related to appraised real estate values, and how those values could change in relation to a change in capitalization rates. This enhancement is meant to increase the level of precision in the allowance for loan and lease losses. As a result, the Company will no longer have an unallocated segment in its allowance for loan losses, as the risks and uncertainties meant to be captured by the unallocated allowance have been included in the qualitative framework for the respective portfolios. As such, the unallocated allowance has in essence been reallocated to the certain portfolios based on the risks and uncertainties it was meant to capture.

**Table of Contents**

The following table details activity in the allowance for loan and lease losses by portfolio segment and the related recorded investment in loans and leases for the years ended December 31, 2015, 2014 and 2013:

12/31/2015	Commercial, secured by real estate	Commercial, industrial and other	Leases	Real estate- residential mortgage (in thousands)	Real estate- Construction	Home equity and consumer	Unallocated	Total
<b>Allowance for Loan and Lease Losses:</b>								
Beginning Balance	\$ 13,577	\$ 3,196	\$ 582	\$ 4,020	\$ 553	\$ 6,333	\$ 2,423	\$ 30,684
Charge-offs	(1,821)	(205)	(548)	(375)	(20)	(1,511)		(4,480)
Recoveries	2,221	183	26	63	106	129		2,728
Provision	6,246	(537)	400	(1,120)	952	(1,576)	(2,423)	1,942
Ending Balance	\$ 20,223	\$ 2,637	\$ 460	\$ 2,588	\$ 1,591	\$ 3,375	\$	\$ 30,874
Ending Balance: Individually evaluated for impairment	\$ 598	\$ 77	\$ 1	\$ 73	\$ 21	\$ 73	\$	\$ 843
Ending Balance: Collectively evaluated for impairment	19,625	2,560	459	2,515	1,570	3,302		\$ 30,031
Ending Balance	\$ 20,223	\$ 2,637	\$ 460	\$ 2,588	\$ 1,591	\$ 3,375	\$	\$ 30,874
<b>Loans and Leases:</b>								
Ending Balance: Individually evaluated for impairment	\$ 19,786	\$ 1,232	\$ 6	\$ 3,027	\$ 380	\$ 1,575	\$	\$ 26,006
Ending Balance: Collectively evaluated for impairment	1,741,803	305,812	56,654	386,665	117,690	333,316		\$ 2,941,940
Ending Balance(1)	\$ 1,761,589	\$ 307,044	\$ 56,660	\$ 389,692	\$ 118,070	\$ 334,891	\$	\$ 2,967,946

(1) Excludes deferred fees

12/31/2014	Commercial, secured by real estate	Commercial, industrial and other	Leases	Real estate- residential mortgage (in thousands)	Real estate- Construction	Home equity and consumer	Unallocated	Total
<b>Allowance for Loan and Lease Losses:</b>								
Beginning Balance	\$ 14,463	\$ 5,331	\$ 504	\$ 3,214	\$ 542	\$ 2,737	\$ 3,030	\$ 29,821
Charge-offs	(2,282)	(999)	(597)	(827)	(25)	(2,697)		(7,427)
Recoveries	999	1,039	19	42	106	220		2,425
Provision	397	(2,175)	656	1,591	(70)	6,073	(607)	5,865
Ending Balance	\$ 13,577	\$ 3,196	\$ 582	\$ 4,020	\$ 553	\$ 6,333	\$ 2,423	\$ 30,684
Ending Balance: Individually evaluated for impairment	\$ 634	\$ 10	\$	217		\$ 1,031	\$	\$ 1,892
	12,943	3,186	582	3,803	553	5,302	2,423	\$ 28,792

Edgar Filing: LAKELAND BANCORP INC - Form 10-K

Ending Balance: Collectively  
evaluated for impairment

Ending Balance	\$ 13,577	\$ 3,196	\$ 582	\$ 4,020	\$ 553	\$ 6,333	\$ 2,423	\$ 30,684
----------------	-----------	----------	--------	----------	--------	----------	----------	-----------

**Loans and Leases:**

Ending Balance: Individually evaluated for impairment	\$ 19,838	\$ 752	\$	\$ 2,919	\$ 188	\$ 1,996	\$	\$ 25,693
--	-----------	--------	----	----------	--------	----------	----	-----------

Ending Balance: Collectively evaluated for impairment	1,509,923	237,500	54,749	428,271	63,832	335,646		\$ 2,629,921
--	-----------	---------	--------	---------	--------	---------	--	--------------

Ending Balance(1)	\$ 1,529,761	\$ 238,252	\$ 54,749	\$ 431,190	\$ 64,020	\$ 337,642	\$	\$ 2,655,614
-------------------	--------------	------------	-----------	------------	-----------	------------	----	--------------

(1) Excludes deferred costs

**Table of Contents**

12/31/2013	Commercial, secured by real estate	Commercial, industrial and other	Leases	Real estate- residential mortgage (in thousands)	Real estate- Construction	Home equity and consumer	Unallocated	Total
<b>Allowance for Loan and Lease Losses:</b>								
Beginning Balance	\$ 16,258	\$ 5,103	\$ 578	\$ 3,568	\$ 587	\$ 2,837	\$	\$ 28,931
Charge-offs	(2,026)	(1,324)	(206)	(1,257)	(3,854)	(1,624)		(10,291)
Recoveries	1,061	260	121	99	14	283		1,838
Provision	(830)	1,292	11	804	3,795	1,241	3,030	9,343
Ending Balance	\$ 14,463	\$ 5,331	\$ 504	\$ 3,214	\$ 542	\$ 2,737	\$ 3,030	\$ 29,821
Ending Balance: Individually evaluated for impairment	\$ 739	\$ 31	\$	\$	\$	\$ 140	\$	\$ 910
Ending Balance: Collectively evaluated for impairment	13,724	5,300	504	3,214	542	2,597	\$ 3,030	\$ 28,911
Ending Balance: Loans acquired with deteriorated credit quality								
Ending Balance	\$ 14,463	\$ 5,331	\$ 504	\$ 3,214	\$ 542	\$ 2,737	\$ 3,030	\$ 29,821
<b>Loans and Leases:</b>								
Ending Balance: Individually evaluated for impairment	\$ 18,375	\$ 4,175	\$	\$ 617	\$ 501	\$ 951	\$	\$ 24,619
Ending Balance: Collectively evaluated for impairment	1,371,486	209,633	41,332	432,214	52,618	337,976		\$ 2,445,259
Ending Balance: Loans acquired with deteriorated credit quality						411		\$ 411
Ending Balance(1)	\$ 1,389,861	\$ 213,808	\$ 41,332	\$ 432,831	\$ 53,119	\$ 339,338	\$	\$ 2,470,289

(1) Excludes deferred costs

Lakeland also maintains a reserve for unfunded lending commitments which are included in other liabilities. This reserve was \$2.0 million and \$1.1 million at December 31, 2015 and December 31, 2014, respectively. Lakeland analyzes the adequacy of the reserve for unfunded lending commitments in conjunction with its analysis of the adequacy of the allowance for loan and lease losses. For more information on this analysis, see *Risk Elements* in Management's Discussion and Analysis.

*Troubled Debt Restructurings*

Troubled debt restructurings (TDRs) are those loans where significant concessions have been made due to borrowers' financial difficulties. Restructured loans typically involve a modification of terms such as a reduction of the stated interest rate, an extended moratorium of principal payments and/or an extension of the maturity date at a stated interest rate lower than the current market rate of a new loan with similar risk. Lakeland considers the potential losses on these loans as well as the remainder of its impaired loans when considering the adequacy of the allowance for loan losses.

**Table of Contents**

The following table summarizes loans that have been restructured during the periods presented:

	Number of Contracts	For the year ended December 31, 2015		Number of Contracts	For the year ended December 31, 2014	
		Pre- Modification Outstanding Recorded Investment (Dollars in thousands)	Post- Modification Outstanding Recorded Investment (Dollars in thousands)		Pre- Modification Outstanding Recorded Investment (Dollars in thousands)	Post- Modification Outstanding Recorded Investment (Dollars in thousands)
<b>Troubled Debt Restructurings:</b>						
Commercial, secured by real estate	2	\$ 1,458	\$ 1,458	5	\$ 4,146	\$ 4,146
Commercial, industrial and other	3	1,934	1,934	2	285	285
Leases	1	14	14			
Real estate - residential mortgage				5	1,238	1,238
Real estate - construction	1	396	396			
Home equity and consumer	1	9	9	9	840	840
	8	\$ 3,811	\$ 3,811	21	\$ 6,509	\$ 6,509

The following table presents loans modified as TDRs within the previous 12 months from December 31, 2015 and 2014 that have defaulted during the subsequent twelve months:

	For the year ended December 31, 2015		For the year ended December 31, 2014	
	Number of Contracts (Dollars in thousands)	Recorded Investment (Dollars in thousands)	Number of Contracts (Dollars in thousands)	Recorded Investment (Dollars in thousands)
<b>Defaulted Troubled Debt Restructurings:</b>				
Commercial, secured by real estate		\$	1	\$ 32
Real estate - residential mortgage			1	354
Home equity and consumer			2	238
		\$	4	\$ 624

*Related Party Loans*

Lakeland has entered into lending transactions in the ordinary course of business with directors, executive officers, principal stockholders and affiliates of such persons on similar terms, including interest rates and collateral, as those prevailing for comparable transactions with other borrowers not related to Lakeland. At December 31, 2015, loans to these related parties amounted to \$28.4 million. There were new loans of \$12.4 million to related parties and repayments of \$11.6 million from related parties in 2015.

*Mortgages Held for Sale*

Residential mortgages originated by the bank and held for sale in the secondary market are carried at the lower of cost or fair market value. Fair value is generally determined by the value of purchase commitments on individual loans. Losses are recorded as a valuation allowance and charged to earnings. As of December 31, 2015, Lakeland had \$1.2 million in mortgages held for sale compared to \$592,000 as of December 31, 2014.

*Leases*

Edgar Filing: LAKELAND BANCORP INC - Form 10-K

Gains (losses) on held for sale leasing assets are included in other income along with other miscellaneous leasing income typically recorded in Lakeland's leasing business.

-81-

**Table of Contents**

Future minimum lease payments of lease receivables are as follows (in thousands):

2015	\$ 20,520
2016	16,554
2017	11,419
2018	5,977
2019	1,956
Thereafter	234
	<b>\$ 56,660</b>

*Other Real Estate and Other Repossessed Assets*

At December 31, 2015, Lakeland had other repossessed assets and other real estate owned of \$49,000 and \$934,000, respectively. The other real estate owned that the Company held at December 31, 2015 included \$805,000 in residential property acquired as a result of foreclosure proceedings or through a deed in lieu of foreclosure. At December 31, 2014, Lakeland had other repossessed assets and other real estate owned of \$49,000 and \$977,000, respectively. For the years ended December 31, 2015, 2014 and 2013, Lakeland had writedowns of \$119,000, \$135,000 and \$0, respectively, on other real estate and other repossessed assets which are included in other real estate and repossessed asset expense in the Statement of Income.

## NOTE 5 - PREMISES AND EQUIPMENT

	Estimated useful lives	December 31, 2015      2014 (in thousands)	
Land	Indefinite	\$ 6,039	\$ 6,319
Buildings and building improvements	10 to 50 years	35,469	34,951
Leasehold improvements	10 to 25 years	10,361	9,845
Furniture, fixtures and equipment	2 to 30 years	35,900	38,773
		<b>87,769</b>	89,888
Less accumulated depreciation and amortization		<b>51,888</b>	54,213
		<b>\$ 35,881</b>	\$ 35,675

Depreciation expense was \$4.0 million, \$3.9 million and \$3.7 million for the years ended December 31, 2015, 2014 and 2013, respectively.

## NOTE 6 TIME DEPOSITS

At December 31, 2015, the schedule of maturities of certificates of deposit is as follows (in thousands):

Year	
2016	\$ 218,887
2017	76,465
2018	39,038
2019	8,720
2020	198
Thereafter	13





**Table of Contents**

## NOTE 7 - DEBT

Lines of Credit

As a member of the Federal Home Loan Bank of New York (FHLB), Lakeland has the ability to borrow overnight based on the market value of collateral pledged. As of December 31, 2015 and 2014, there were no overnight borrowings from the FHLB. As of December 31, 2015, Lakeland also had overnight federal funds lines available for it to borrow up to \$162.0 million. Lakeland had borrowed \$115.0 million and \$81.0 million against these lines as of December 31, 2015 and 2014, respectively. Lakeland may also borrow from the discount window of the Federal Reserve Bank of New York based on the market value of collateral pledged. Lakeland had no borrowings with the Federal Reserve Bank of New York as of December 31, 2015 or 2014.

Federal Funds Purchased and Securities Sold Under Agreements to Repurchase

Short-term borrowings at December 31, 2015 and 2014 consisted of short-term securities sold under agreements to repurchase and federal funds purchased. Securities underlying the agreements were under Lakeland's control. The following tables summarize information relating to securities sold under agreements to repurchase and federal funds purchased for the years presented. For purposes of the tables, the average amount outstanding was calculated based on a daily average.

Federal funds purchased:	2015	2014	2013
		(dollars in thousands)	
Balance at December 31	\$ 115,000	\$ 81,000	\$ 50,000
Interest rate at December 31	0.65%	0.35%	0.37%
Maximum amount outstanding at any month-end during the year	\$ 130,000	\$ 117,000	\$ 81,000
Average amount outstanding during the year	\$ 22,734	\$ 17,605	\$ 8,424
Weighted average interest rate during the year	0.45%	0.39%	0.34%
Securities sold under agreements to repurchase:	2015	2014	2013
		(dollars in thousands)	
Balance at December 31	\$ 36,234	\$ 27,935	\$ 31,991
Interest rate at December 31	0.02%	0.02%	0.02%
Maximum amount outstanding at any month-end during the year	\$ 40,140	\$ 54,550	\$ 48,315
Average amount outstanding during the year	\$ 31,293	\$ 38,192	\$ 37,277
Weighted average interest rate during the year	0.03%	0.03%	0.03%

Other BorrowingsFHLB Debt

At December 31, 2015, advances from the FHLB totaling \$221.9 million will mature within one to three years and are reported as other borrowings. These advances are collateralized by certain securities and first mortgage loans. The advances had a weighted average interest rate of 1.38%.

At December 31, 2014, Lakeland had advances from the FHLB totaling \$132.5 million maturing within one to four years and reported as other borrowings. These advances were collateralized by certain securities and first mortgage loans. The advances had a weighted average interest rate of 1.52%.

FHLB debt matures as follows (in thousands):

2016	\$ 67,798
2017	87,355
2018	66,752



**Table of Contents****Long-term Securities Sold Under Agreements to Repurchase**

At December 31, 2015, Lakeland had \$50.0 million in long-term securities sold under agreements to repurchase compared to \$70.0 million at December 31, 2014. These borrowings were able to be called at various dates starting in 2009. These borrowings are collateralized by certain securities. The borrowings had a weighted average interest rate of 2.80% and 2.14% on December 31, 2015 and December 31, 2014, respectively. During the third quarter of 2015, Lakeland prepaid \$20.0 million of its long-term securities sold under agreements to repurchase that had a rate of 4.44% and incurred a prepayment penalty of \$2.4 million. These long-term securities sold under agreements to repurchase mature as follows (in thousands):

2016	\$ 10,000
2017	
2018	30,000
Thereafter	10,000
	\$ 50,000

The above FHLB debt and long-term securities sold under agreements to repurchase are collateralized by certain securities. At times the market value of securities collateralizing our borrowings may decline due to changes in interest rates and may necessitate our lenders to issue a margin call which requires Lakeland to pledge additional securities to meet that margin call. As of December 31, 2015, the Company had \$109.1 million in securities pledged for its short-term and long-term securities sold under agreements to repurchase, including \$61.5 million in mortgage backed securities and \$47.6 million in U.S. government agency securities.

**Subordinated Debentures**

In May 2007, the Company issued \$20.6 million of junior subordinated debentures due August 31, 2037 to Lakeland Bancorp Capital Trust IV, a Delaware business trust. The distribution rate on these securities was 6.61% for 5 years and floats at LIBOR plus 152 basis points thereafter. The debentures are the sole asset of the Trust. The Trust issued 20,000 shares of trust preferred securities, \$1,000 face value, for total proceeds of \$20.0 million. The Company's obligations under the debentures and related documents, taken together, constitute a full, irrevocable and unconditional guarantee on a subordinated basis by the Company of the Trust's obligations under the preferred securities. The preferred securities are callable by the Company on or after August 1, 2012, or earlier if the deduction of related interest for federal income taxes is prohibited, treatment as Tier I capital is no longer permitted, or certain other contingencies arise. The preferred securities must be redeemed upon maturity of the debentures in 2037. On August 3, 2015, the Company acquired and extinguished \$10.0 million of Lakeland Bancorp Capital Trust IV debentures and recorded a \$1.8 million gain on the extinguishment of debt. The interest rate on this debenture floated at LIBOR plus 152 basis points and had a rate of 1.80% at the time of extinguishment.

In June 2003, the Company issued \$10.3 million of junior subordinated debentures due July 7, 2033 to Lakeland Bancorp Capital Trust I, a Delaware business trust. The distribution rate on these securities was 6.20% for 7 years and floats at LIBOR plus 310 basis points thereafter. The debentures are the sole asset of the Trust. The Trust issued 10,000 shares of trust preferred securities, \$1,000 face value, for total proceeds of \$10.0 million. The Company's obligations under the debentures and related documents, taken together, constitute a full, irrevocable and unconditional guarantee on a subordinated basis by the Company of the Trust's obligations under the preferred securities. The preferred securities are callable by the Company on or after July 7, 2010, or earlier if the deduction of related interest for federal income taxes is prohibited, treatment as Tier I capital is no longer permitted, or certain other contingencies arise. On June 18, 2013, the Company acquired and extinguished \$9.0 million of Lakeland Bancorp Capital Trust I debentures and recorded a \$1.2 million gain on extinguishment of debt. The interest rate on this debenture floated at LIBOR plus 310 basis points and had a rate of 3.38% at the time of extinguishment. The Company redeemed the remaining \$1.0 million in the fourth quarter of 2013 at par value.

**Table of Contents**

In June 2003, the Company also issued \$20.6 million of junior subordinated debentures due June 30, 2033 to Lakeland Bancorp Capital Trust II, a Delaware business trust. The distribution rate on these securities was 5.71% for 5 years and floats at LIBOR plus 310 basis points thereafter. The debentures are the sole asset of the Trust. The Trust issued 20,000 shares of trust preferred securities, \$1,000 face value, for total proceeds of \$20.0 million. The Company's obligations under the debentures and related documents, taken together, constitute a full, irrevocable and unconditional guarantee on a subordinated basis by the Company of the Trust's obligations under the preferred securities. The preferred securities are callable by the Company on or after June 30, 2008, or earlier if the deduction of related interest for federal income taxes is prohibited, treatment as Tier I capital is no longer permitted, or certain other contingencies arise. The preferred securities must be redeemed upon maturity of the debentures in 2033.

**NOTE 8 - STOCKHOLDERS' EQUITY**

On May 21, 2014, the Company's Board of Directors authorized a 5% stock dividend which was distributed on June 17, 2014, to holders of record as of June 3, 2014.

On May 31, 2013, the Company completed its acquisition of Somerset Hills Bancorp, a bank holding company headquartered in Bernardville, New Jersey. Lakeland Bancorp issued an aggregate of 6,083,783 shares of its common stock in the merger, and also assumed outstanding Somerset Hills Bancorp stock options (which were converted into options to purchase Lakeland Bancorp common stock). Lakeland Bancorp paid \$6.5 million in cash in the transaction.

**NOTE 9 - INCOME TAXES**

The components of income taxes are as follows:

	Years Ended December 31,		
	2015	2014	2013
		(in thousands)	
Current tax provision	\$ 16,991	\$ 15,193	\$ 12,286
Deferred tax (benefit) provision	(824)	(34)	164
<b>Total provision for income taxes</b>	<b>\$ 16,167</b>	<b>\$ 15,159</b>	<b>\$ 12,450</b>

The income tax provision reconciled to the income taxes that would have been computed at the statutory federal rate of 35% is as follows:

	Years Ended December 31,		
	2015	2014	2013
		(in thousands)	
Federal income tax, at statutory rates	\$ 17,028	\$ 16,201	\$ 13,097
Increase (deduction) in taxes resulting from:			
Tax-exempt income	(1,467)	(1,387)	(1,370)
State income tax, net of federal income tax effect	132	337	339
Other, net	474	8	384
<b>Provision for income taxes</b>	<b>\$ 16,167</b>	<b>\$ 15,159</b>	<b>\$ 12,450</b>

**Table of Contents**

The net deferred tax asset consisted of the following:

	December 31,	
	2015	2014
Deferred tax assets:	(in thousands)	
Allowance for loan and lease losses	<b>\$ 13,445</b>	\$ 13,014
Share based compensation plans	<b>857</b>	686
Purchase accounting fair market value adjustments	<b>431</b>	694
Non-accrued interest	<b>632</b>	554
Deferred compensation	<b>2,207</b>	1,814
Other than temporary impairment loss on investment securities	<b>255</b>	255
Unfunded pension benefits	<b>9</b>	9
Other, net	<b>579</b>	537
<b>Deferred tax assets</b>	<b>18,415</b>	17,563
Deferred tax liabilities:		
Core deposit intangible from acquired companies	<b>631</b>	800
Undistributed income from subsidiary not consolidated for tax return purposes (REIT).	<b>845</b>	724
Deferred loan costs	<b>1,433</b>	1,407
Prepaid expenses	<b>549</b>	460
Depreciation and amortization	<b>1,440</b>	1,438
Deferred gain on securities	<b>194</b>	194
Unrealized gains on securities available for sale	<b>622</b>	862
Other	<b>591</b>	633
<b>Deferred tax liabilities</b>	<b>6,305</b>	6,518
<b>Net deferred tax assets, included in other assets</b>	<b>\$ 12,110</b>	\$ 11,045

The Company evaluates the realizability of its deferred tax assets by examining its earnings history and projected future earnings and by assessing whether it is more likely than not that carryforwards would not be realized. Based upon the majority of the Company's deferred tax assets having no expiration date, the Company's earnings history, and the projections of future earnings, the Company's management believes that it is more likely than not that all of the Company's deferred tax assets as of December 31, 2015 will be realized.

The Company evaluates tax positions that may be uncertain using a recognition threshold of more-likely-than-not, and a measurement attribute for all tax positions taken or expected to be taken on a tax return, in order for those tax positions to be recognized in the financial statements. The Company had an unrecognized tax benefit of \$111,000 as of December 31, 2013. In 2014, the Company reevaluated this unrecognized tax benefit and concluded that based on current information the tax position that it has taken is more-likely-than-not to be upheld. Therefore, the Company recognized the tax benefit in the fourth quarter of 2014.

The Company is subject to U.S. federal income tax law as well as income tax of various state jurisdictions. Tax regulations within each jurisdiction are subject to the interpretation of the related tax laws and regulations and require significant judgment to apply. With few significant exceptions, the Company is no longer subject to U.S. federal examinations by tax authorities for the years before 2012 or to state and local examinations by tax authorities for the years before 2011.

**Table of Contents**

## NOTE 10 - EARNINGS PER SHARE

The Company uses the two class method to compute earnings per common share. Participating securities include non-vested restricted stock. The following tables present the computation of basic and diluted earnings per share for the periods presented.

Year ended December 31, 2015			
	Income (numerator) (in thousands, except per share amounts)	Shares (denominator)	Per share amount
<b>Basic earnings per share</b>			
Net income available to common shareholders	\$ 32,481	37,844	\$ 0.86
Less: earnings allocated to participating securities	(263)		(0.01)
Net income available to common shareholders	\$ 32,218	37,844	\$ 0.85
<b>Effect of dilutive securities</b>			
Stock options and restricted stock		149	
<b>Diluted earnings per share</b>			
Net income available to common shareholders plus assumed conversions	\$ 32,218	37,993	\$ 0.85

There were no antidilutive options to purchase common stock to be excluded from the above computation.

Year ended December 31, 2014			
	Income (numerator) (in thousands, except per share amounts)	Shares (denominator)	Per share amount
<b>Basic earnings per share</b>			
Net income available to common shareholders	\$ 31,129	37,749	\$ 0.82
Less: earnings allocated to participating securities	(222)		0.00
Net income available to common shareholders	\$ 30,907	37,749	\$ 0.82
<b>Effect of dilutive securities</b>			
Stock options and restricted stock		120	
<b>Diluted earnings per share</b>			
Net income available to common shareholders plus assumed conversions	\$ 30,907	37,869	\$ 0.82

Options to purchase 115,831 shares of common stock at a weighted average of \$12.06 per share were not included in the computation of diluted earnings per share because the option price and the grant date price were greater than the average market price during the period.

Year ended December 31, 2013			
	Income (numerator) (in thousands, except per share amounts)	Shares (denominator)	Per share amount
<b>Basic earnings per share</b>			
Net income available to common shareholders	\$ 24,969	34,742	\$ 0.72
Less: earnings allocated to participating securities	(178)		(0.01)
Net income available to common shareholders	\$ 24,791	34,742	\$ 0.71
<b>Effect of dilutive securities</b>			

Stock options and restricted stock

160

Diluted earnings per share

Net income available to common shareholders plus assumed conversions	\$ 24,791	34,902	\$ 0.71
--	-----------	--------	---------

Options to purchase 358,340 shares of common stock at a weighted average of \$11.91 per share were not included in the computation of diluted earnings per share because the option price and the grant date price were greater than the average market price during the period.



**Table of Contents**

## NOTE 11 - EMPLOYEE BENEFIT PLANS

*Profit Sharing Plan*

The Company has a profit sharing plan for all its eligible employees. The Company's annual contribution to the plan is determined by its Board of Directors. Annual contributions are allocated to participants on a point basis with accumulated benefits payable at retirement, or, at the discretion of the plan committee, upon termination of employment. Contributions made by the Company were approximately \$600,000 a year for each of the years ended 2015, 2014, and 2013.

*Benefit Obligations from Somerset Hills Acquisition*

Somerset Hills, acquired by the Company in 2013, entered into a non-qualified Supplemental Executive Retirement Plan ( SERP ) with its former Chief Executive Officer and its Chief Financial Officer which entitles them to a benefit of \$48,000 and \$24,000, respectively, per year for 15 years after the earlier of retirement or death. The beneficiary of the Chief Financial Officer is currently being paid out under the plan. As of December 31, 2015 and 2014, the Company has a liability of \$745,000 and \$675,000, respectively, for these SERPs and has recognized an expense of \$95,000, \$109,000 and \$50,000 in 2015, 2014 and 2013, respectively.

*Retirement Savings Plans (401(k) plans)*

Beginning in January 2002, the Company began contributing to its 401(k) plan. All eligible employees can contribute a portion of their annual salary with the Company matching up to 50% of the employee's contributions. The Company's contributions in 2015, 2014 and 2013 totaled \$760,000, \$740,000 and \$715,000, respectively.

*Pension Plan*

Newton Trust Company, acquired by the Company in 2004, had a defined benefit pension plan (the Plan) that was frozen prior to the acquisition by the Company. All participants of the Plan ceased accruing benefits as of that date.

In 2014, the Company filed appropriate forms with the Internal Revenue Service and the Pension Benefit Guaranty Corporation to terminate the Plan and awaited approval from both entities. As a result of the Company's intent to terminate the plan, the Company changed the portfolio allocation of the plan to minimize the fluctuation of the market value of the Plan's assets. The Company also recorded a realized loss for the difference between the plan assets and the estimated payout of the plan of approximately \$293,000 in 2014 and \$238,000 in 2015.

In 2015, the Company received the requisite approvals and terminated the plan. The Company made lump sum payments totaling \$2.6 million as a result of this termination.

The following table shows the fair value and the portfolio allocations of the assets in the Plan by type of investment as of December 31, 2014 (dollars in thousands):

	December 31, 2014	
	Market Value	Percent of Assets
Cash and cash equivalents	\$ 519	26%
Fixed Income Mutual funds	976	48%
U.S. Large-Cap funds	525	26%
	\$ 2,020	100%

**Table of Contents**

The accumulated benefit obligation as of December 31 is as follows:

(in thousands)	2015	2014
Accumulated postretirement benefit obligation	\$ 2,334	\$ 2,027
Interest Cost	14	94
Actuarial loss	213	401
Divestiture Curtailments or settlements	(2,508)	
Estimated benefit payments	(53)	(188)
Total accumulated postretirement benefit obligation		2,334
Fair value of plan assets beginning of period	2,020	1,987
Return on plan assets	9	61
Benefits paid	(2,561)	(188)
Contribution	532	160
Fair value of plan assets at end of year		2,020
Funded status		(314)
Unrecognized net actuarial loss		
Liability	\$	\$ (314)
Accumulated benefit obligation	\$	\$ 2,334

The components of net periodic pension cost are as follows:

(in thousands)	2015	2014	2013
Amortization of actuarial loss	\$ 84	\$ 39	\$ 82
Interest cost on APBO	14	94	90
Expected return on plan assets	(74)	(95)	(72)
Net periodic postretirement cost	\$ 24	\$ 38	\$ 100

In 2014, as a result of the pending termination of the Plan, the benefit obligation was determined by calculating the lump sum amounts payable under the terms of the plan assuming a December 1, 2015 distribution date and discounted to December 31, 2014 using the one year Citigroup Pension Liability Index of 0.65%. Annuity liabilities were calculated using an interest rate of 2.40%. The expected return on plan assets was not relevant due to the pending termination of the Plan.

*Deferred Compensation Arrangements*

High Point Financial Corp., a bank holding company acquired in 1999, had established deferred compensation arrangements for certain directors and executives of High Point Financial Corp. and its subsidiary, the National Bank of Sussex County. The deferred compensation plans differ, but generally provide for annual payments for ten to fifteen years following retirement. The Company's liabilities under these arrangements are being accrued from the commencement of the plans over the participants' remaining periods of service. The Company intends to fund its obligations under the deferred compensation arrangements with the increase in cash surrender value of life insurance policies that it has purchased on the respective participants. The deferred compensation plans do not hold any assets. For the years ended December 31, 2015, 2014 and 2013, there were expenses related to this plan of \$4,000, \$16,000 and \$3,000, respectively. As of December 31, 2015 and 2014, the accrued liability for these plans was \$241,000 and \$267,000, respectively.

*Supplemental Executive Retirement Plans*

Edgar Filing: LAKELAND BANCORP INC - Form 10-K

In 2003, the Company entered into a supplemental executive retirement plan (SERP) agreement with its former CEO that provides annual retirement benefits of \$150,000 a year for a 15 year period when the former CEO reached

**Table of Contents**

the age of 65. Our former CEO retired and is receiving annual retirement benefits pursuant to the plan. In 2008, the Company entered into a SERP agreement with its current CEO that provides annual retirement benefits of \$150,000 for a 15 year period when the CEO reaches the age of 65. In November 2008, the Company entered into a SERP with its Regional President and Chief Operating Officer that provides annual retirement benefits of \$90,000 a year for a 10 year period upon his reaching the age of 65. In December 2014, the Company entered into a SERP with a Regional President that provides \$84,500 a year for a 15 year period upon his reaching the age of 66 in November 2016. The Company intends to fund its obligations under the deferred compensation arrangements with the increase in cash surrender value of bank owned life insurance policies. In 2015, 2014 and 2013, the Company recorded compensation expense of \$814,000, \$359,000 and \$247,000, respectively, for these plans.

*Deferred Compensation Agreement*

In February 2015, the Company entered into a Deferred Compensation Agreement with its CEO where it would contribute \$16,500 monthly into a deferral account which would earn interest at an annual rate of the Company's prior year Return On Equity, provided that the Company's return on equity remained in a range of 0% to 15%. The Company has agreed to make such contributions each month that the CEO is actively employed from February 2015 through December 31, 2022. The expense incurred in 2015 and the accrued liability at December 31, 2015 was \$188,000. Following the CEO's normal retirement date, he shall be paid out in 180 consecutive monthly installments.

*Elective Deferral Plan*

In March 2015, the Company established an Elective Deferral Plan for eligible executives in which the executive may elect to contribute a portion of his base salary and bonus to a deferral account which will earn an interest rate of 75% of the Company's prior year return on equity provided that the return on equity remains in the range of 0% to 15%. The Company recorded an expense of \$3,000 in 2015, and had a liability recorded of \$190,000 at December 31, 2015.

**NOTE 12 - DIRECTORS RETIREMENT PLAN**

The Company provides a plan that any director who became a member of the Board of Directors prior to 2009 who completes five years of service may retire and continue to be paid for a period of ten years at a rate ranging from \$5,000 through \$17,500 per annum, depending upon years of credited service. This plan is unfunded. The following tables present the status of the plan and the components of net periodic plan cost for the years then ended. The measurement date for the accumulated benefit obligation is December 31 of the years presented.

	December 31,	
	2015	2014
	(in thousands)	
Accrued plan cost included in other liabilities	<b>\$ 702</b>	<b>\$ 743</b>
Amount not recognized as component of net postretirement benefit cost		
Recognized in accumulated other comprehensive income		
Net actuarial gain	<b>(\$ 41)</b>	(\$ 141)
Unrecognized prior service cost		
Amounts not recognized as a component of net postretirement benefit (benefit)	<b>(\$ 41)</b>	(\$ 141)

**Table of Contents**

	Years ended December 31,		
	2015	2014	2013
	(in thousands)		
Net periodic plan cost included the following components:			
Service cost	\$ 19	\$ 26	\$ 29
Interest cost	46	39	36
Amortization of prior service cost	13	14	21
	<b>\$ 78</b>	<b>\$ 79</b>	<b>\$ 86</b>

A discount rate of 3.87% and 3.52% was assumed in the plan valuation for 2015 and 2014, respectively. As the benefit amount is not dependent upon compensation levels, a rate of increase in compensation assumption was not utilized in the plan valuation.

The director's retirement plan holds no plan assets. The benefits expected to be paid in each of the next five years and in aggregate for the five years thereafter are as follows (in thousands):

2016	\$ 75
2017	70
2018	75
2019	63
2020	62
2021 - 2025	188

The Company expects its contribution to the director's retirement plan to be \$75,000 in 2016.

The amount in accumulated other comprehensive loss expected to be recognized as a component of net periodic benefit cost in 2016 is \$13,000.

**NOTE 13- STOCK-BASED COMPENSATION***Employee Stock Option Plans*

On May 21, 2009, the Company's shareholders approved the 2009 Equity Compensation Program, which authorizes the granting of incentive stock options, supplemental stock options, restricted shares and restricted stock units to employees of the Company, including those employees serving as officers and directors of the Company. The plan authorizes the issuance of 2.3 million shares in connection with options and awards granted under the 2009 program.

The Company established the 2000 Equity Compensation Program which authorizes the granting of incentive stock options, supplemental stock options and restricted stock to employees of the Company which includes those employees serving as officers and directors of the Company. The plan authorized 2,613,185 shares of common stock of the Company. No further awards will be granted from the 2000 program.

On May 31, 2013, the Company granted options to purchase 52,500 shares (26,250 shares each) to two new non-employee directors of the Company at an exercise price of \$9.44 per share under the 2009 program. The directors' options are exercisable in five equal installments beginning on the date of grant and continuing on the next four anniversaries of the date of grant.

The estimated fair values were determined on the dates of grant using the Black-Scholes Option pricing model. The fair value of the Company stock option awards are expensed on a straight-line basis over the vesting period of the stock option. The risk-free rate is based on the implied yield on a U.S. Treasury bond with a term approximating the expected term of the option. The expected volatility computation is based on historical

**Table of Contents**

volatility over a period approximating the expected term of the option. The dividend yield is based on the annual dividend payment per share, divided by the grant date stock price. The expected option term is estimated examining historical terms on similar option grants and is a function of the option life and the vesting period.

The fair value of these options were estimated using the Black-Scholes pricing model with the following weighted average assumptions:

Risk-free interest rates	1.55%
Expected dividend yield	2.82%
Expected volatility	45.45%
Expected lives (years)	7.00
Weighted average fair value of options granted	\$ 3.31

As of December 31, 2015 and 2014, 111,829 and 140,772 options granted to directors were outstanding, respectively.

The Company also assumed the outstanding options granted under Somerset Hills stock option plans at the time of merger. Based on the conversion ratio in the merger, the Company assumed options to purchase 395,191 shares of Lakeland stock in these plans at a weighted average exercise price of \$6.33. The fair value of these options were estimated using the Black Scholes pricing model with the following range of assumptions:

Risk-free interest rates	0.04% - 1.55%
Expected dividend yield	2.82%
Expected volatility	13% - 47%
Expected lives (years)	3 months - 7 years
Weighted average fair value of options granted	\$3.79

As of December 31, 2015 and 2014, there were 64,057 and 84,043 options outstanding, respectively, under these plans.

As of December 31, 2015 and 2014, outstanding options to purchase common stock granted to key employees were 0 and 86,890, respectively.

Excess tax benefits of stock based compensation were \$59,000, \$70,000 and \$142,000 for the years 2015, 2014 and 2013, respectively.

A summary of the status of the Company's option plans as of December 31, 2015 and the changes during the year ending on that date is represented below.

	Number of shares	Weighted average exercise price	Weighted average remaining contractual term (in years)	Aggregate Intrinsic Value
Outstanding, beginning of year	311,705	\$ 9.69		\$ 681,861
Granted				
Exercised	(16,918)	7.34		
Expired	(86,110)	12.13		
Forfeited	(32,785)	11.48		
Outstanding, end of year	175,892	\$ 8.38	5.03	\$ 602,236
Options exercisable at year-end	154,891	\$ 8.22	4.70	\$ 552,308



**Table of Contents**

A summary of the Company's non-vested options under the Company's option plans as of December 31, 2015 and changes for the year then ended is presented below.

Non-vested Options	Shares	Weighted-Average Grant-date Fair Value
Non-vested, January 1, 2015	<b>31,501</b>	<b>\$ 3.31</b>
Granted		
Vested	<b>(10,500)</b>	<b>3.31</b>
Non-vested, December 31, 2015	<b>21,001</b>	<b>\$ 3.31</b>

As of December 31, 2015, there was \$49,000 of unrecognized compensation expense related to unvested stock options under the 2009 Equity Compensation Program. Compensation expense recognized for stock options was \$35,000, \$42,000 and \$72,000 for 2015, 2014 and 2013, respectively.

The aggregate intrinsic values of options exercised in 2015 and 2014 were \$68,000 and \$44,000, respectively. Exercise of stock options during 2015 and 2014 resulted in cash receipts of \$124,000 and \$89,000, respectively. The total fair value of options that vested in 2015 and 2014 were \$35,000 and \$52,000, respectively.

In 2013, the Company granted 109,391 shares of restricted stock at a grant date fair value of \$9.41 per share under the Company's 2009 equity compensation program. These shares vest over a five year period. Compensation expense on these shares is expected to average approximately \$206,000 per year for the next five years. In 2014, the Company granted 1,942 shares of restricted stock at a grant date fair value of \$11.21 per share under the Company's 2009 equity compensation program. These shares vest over a five year period. Compensation expense on these shares is expected to average approximately \$4,000 per year for the next five years. No restricted stock was granted in 2015.

Information regarding the Company's restricted stock for the year ended December 31, 2015 is as follows:

	Number of shares	Weighted average price
Outstanding, January 1, 2015	<b>160,284</b>	<b>\$ 9.21</b>
Granted		
Vested	<b>(86,696)</b>	<b>9.11</b>
Forfeited	<b>(88)</b>	<b>9.39</b>
Outstanding, December 31, 2015	<b>73,500</b>	<b>\$ 9.33</b>

The total fair value of the restricted stock vested during the year ended December 31, 2015 was approximately \$1.0 million. Compensation expense recognized for restricted stock was \$497,000, \$707,000 and \$823,000 in 2015, 2014 and 2013, respectively. There was approximately \$188,000 in unrecognized compensation expense related to restricted stock grants as of December 31, 2015, which is expected to be recognized over a period of 1.4 years.

In 2015, the Company granted 137,009 RSUs at a weighted average grant date fair value of \$11.08 per share under the Company's 2009 Equity Compensation Program. These units vest within a range of two to three years. A portion of these RSUs will vest subject to certain performance conditions in the restricted stock unit agreement. There are also certain provisions in the compensation program which state that if a holder of the RSUs reaches a certain age and years of service, the person has effectively earned a portion of the RSUs at that time. Compensation expense on these restricted stock units is expected to average approximately \$506,000 per year over a three year period. Compensation expense for restricted stock units was \$1.1 million in 2015. In 2014, the Company granted 127,791 RSUs at a weighted average grant date fair value of \$10.65 per share under the





**Table of Contents**

Company's 2009 equity compensation program. Compensation expense on these restricted stock units is expected to average approximately \$453,000 per year over a three year period. Compensation expense for restricted stock units was \$1.1 million and \$641,000 in 2015 and 2014, respectively. There was approximately \$1.1 million in unrecognized compensation expense related to restricted stock units as of December 31, 2015, which is expected to be recognized over a period of 1.5 years.

Information regarding the Company's RSUs and changes during the year ended December 31, 2015 is as follows:

	Number of shares	Weighted average price
Outstanding, January 1, 2015	98,535	\$ 10.64
Granted	137,009	11.08
Vested	(33,919)	11.03
Forfeited	(715)	10.78
Outstanding, December 31, 2015	200,910	\$ 10.87

**NOTE 14 - COMMITMENTS AND CONTINGENCIES*****Lease Obligations***

Lakeland is obligated under various non-cancelable operating leases on building and land used for office space and banking purposes. These leases contain renewal options and escalation clauses. Rent expense under long-term operating leases amounted to approximately \$2.7 million, \$2.7 million and \$2.5 million for the years ended December 31, 2015, 2014 and 2013, respectively, including rent expense to related parties of \$143,000 in 2015, \$139,000 in 2014, and \$180,000, in 2013. At December 31, 2015, the minimum commitments under all noncancellable leases with remaining terms of more than one year and expiring through 2033 are as follows (in thousands):

Year	
2016	\$ 2,608
2017	2,283
2018	2,043
2019	1,835
2020	1,612
Thereafter	14,367
	\$ 24,748

***Litigation***

Certain former shareholders of Pascack Bancorp, Inc. brought a purported class action (the "Action") in the Superior Court of New Jersey, Bergen County, in connection with the merger of Pascack Bancorp with and into the Company, and the merger of Pascack Community Bank with and into Lakeland Bank. The complaint alleged that the Company had aided and abetted the individual defendants (former board members of Pascack Bancorp) in their alleged breaches of fiduciary duty. The parties reached an agreement-in-principle concerning the proposed settlement of the Action on December 1 and December 2, 2015. The mergers were consummated on January 7, 2016. The parties have agreed to a stipulation of settlement which is pending court approval.

Other than as described above, there are no pending legal proceedings involving the Company or Lakeland other than those arising in the normal course of business. Management does not anticipate that the potential liability, if any, arising out of such legal proceedings will have a material effect on the financial condition or results of operations of the Company and Lakeland on a consolidated basis.



**Table of Contents**

## NOTE 15 - FINANCIAL INSTRUMENTS WITH OFF-BALANCE-SHEET RISK AND CONCENTRATIONS OF CREDIT RISK

Lakeland is party to financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit and standby letters of credit. Such financial instruments are recorded in the consolidated financial statements when they become payable. Those instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the consolidated balance sheets. The contract or notional amounts of those instruments reflect the extent of involvement Lakeland has in particular classes of financial instruments.

Lakeland's exposure to credit loss in the event of non-performance by the other party to the financial instrument for commitments to extend credit and standby letters of credit is represented by the contractual or notional amount of those instruments. Lakeland uses the same credit policies in making commitments and conditional obligations as it does for on-balance-sheet instruments.

Lakeland generally requires collateral or other security to support financial instruments with credit risk. The approximate contract amounts are as follows:

	December 31,	
	2015	2014
	(in thousands)	
<b>Financial instruments whose contract amounts represent credit risk</b>		
Commitments to extend credit	<b>\$ 773,058</b>	\$ 621,305
Standby letters of credit and financial guarantees written	<b>11,060</b>	10,449

At December 31, 2015 and 2014 there were \$8,000 and \$19,000, respectively, in commitments to lend additional funds to borrowers whose terms have been modified in troubled debt restructurings.

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. Lakeland evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by Lakeland upon extension of credit, is based on management's credit evaluation.

Standby letters of credit are conditional commitments issued by Lakeland to guarantee the payment by or performance of a customer to a third party. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. Lakeland holds deposit accounts, residential or commercial real estate, accounts receivable, inventory and equipment as collateral to support those commitments for which collateral is deemed necessary. The extent of collateral held for those commitments at December 31, 2015 and 2014 varies based on management's credit evaluation.

Lakeland issues financial and performance letters of credit. Financial letters of credit require Lakeland to make payment if the customer fails to make payment, as defined in the agreements. Performance letters of credit require Lakeland to make payments if the customer fails to perform certain non-financial contractual obligations. Lakeland defines the initial fair value of these letters of credit as the fees received from the customer. Lakeland records these fees as a liability when issuing the letters of credit and amortizes the fee over the life of the letter of credit.

The maximum potential undiscounted amount of future payments of these letters of credit as of December 31, 2015 is \$11.1 million and they expire through 2024. Lakeland's exposure under these letters of credit would be reduced by actual performance, subsequent termination by the beneficiaries and by any proceeds that Lakeland obtained in liquidating the collateral for the loans, which varies depending on the customer.

**Table of Contents**

As of December 31, 2015, Lakeland had \$773.1 million in loan and lease commitments, with \$570.2 million maturing within one year, \$141.7 million maturing after one year but within three years, \$6.5 million maturing after three years but within five years, and \$54.7 million maturing after five years. As of December 31, 2015, Lakeland had \$11.1 million in standby letters of credit, with \$9.4 million maturing within one year, \$1.6 million maturing after one year but within three years, and \$80,000 maturing after five years.

Lakeland grants loans primarily to customers in its immediately adjacent suburban counties which include Bergen, Morris, Passaic, Sussex, Warren, Somerset, Union and Essex counties in Northern and Central New Jersey, the Hudson Valley region in New York State, and surrounding areas. Certain of Lakeland's consumer loans and lease customers are more diversified nationally. Although Lakeland has a diversified loan portfolio, a large portion of its loans are secured by commercial or residential real property. Although Lakeland has a diversified loan portfolio, a substantial portion of its debtors' ability to honor their contracts is dependent upon the economy. Commercial and standby letters of credit were granted primarily to commercial borrowers.

**NOTE 16 - COMPREHENSIVE INCOME**

The Company reports comprehensive income in addition to net income (loss) from operations. Comprehensive income is a more inclusive financial reporting methodology that includes disclosure of certain financial information that historically has not been recognized in the calculation of net income.

The following table shows the changes in the balances of each of the components of other comprehensive income for the periods presented:

	Year ended December 31, 2015		
	Before tax amount	Tax Benefit (Expense)	Net of tax amount
	(dollars in thousands)		
Unrealized losses on available for sale securities			
Unrealized holding losses arising during period	\$ (375)	\$ 155	\$ (220)
Less reclassification adjustment for net gains realized in net income	241	(84)	157
Net unrealized losses on available for sale securities	(616)	239	(377)
Change in pension liabilities	3	1	4
Other comprehensive loss, net	\$ (613)	\$ 240	\$ (373)
	Year ended December 31, 2014		
	Before tax amount	Tax Benefit (Expense)	Net of tax amount
	(dollars in thousands)		
Unrealized gains on available for sale securities			
Unrealized holding gains arising during period	\$ 9,663	\$ (3,483)	\$ 6,180
Less reclassification adjustment for net gains realized in net income	3	(1)	2
Net unrealized gains on available for sale securities	9,660	(3,482)	6,178
Change in pension liabilities	31	(11)	20
Other comprehensive income, net	\$ 9,691	\$ (3,493)	\$ 6,198

**Table of Contents**

	Year ended December 31, 2013		
	Before tax amount	Tax Benefit (Expense)	Net of tax amount
	(dollars in thousands)		
Unrealized losses on available for sale securities			
Unrealized holding losses arising during period	\$ (13,675)	\$ 4,985	\$ (8,690)
Less reclassification adjustment for net gains realized in net income	839	(330)	509
Net unrealized losses on available for sale securities	(14,514)	5,315	(9,199)
Change in pension liabilities	866	(278)	588
Other comprehensive loss, net	\$ (13,648)	\$ 5,037	\$ (8,611)

	For the Year Ended December 31, 2015			For the Year Ended December 31, 2014			For the Year Ended December 31, 2013		
	Unrealized Gains and Losses on Available-for-sale Securities	Pension Items	Total	Unrealized Gains and Losses on Available-for-sale Securities	Pension Items	Total	Unrealized Gains and Losses on Available-for-sale Securities	Pension Items	Total
Beginning Balance	\$ 1,531	(\$ 8)	\$ 1,523	(\$ 4,647)	(\$ 28)	(\$ 4,675)	\$ 4,552	(\$ 616)	\$ 3,936
Other comprehensive income (loss) before classifications	(220)	4	(216)	6,180	20	6,200	(8,690)	588	(8,102)
Amounts reclassified from accumulated other comprehensive income	(157)		(157)	(2)		(2)	(509)		(509)
Net current period other comprehensive income (loss)	(377)	4	(373)	6,178	20	6,198	(9,199)	588	(8,611)
Ending balance	\$ 1,154	(\$ 4)	\$ 1,150	\$ 1,531	(\$ 8)	\$ 1,523	(\$ 4,647)	(\$ 28)	(\$ 4,675)

\* All amounts are net of tax.

**NOTE 17 - FAIR VALUE MEASUREMENT AND FAIR VALUE OF FINANCIAL INSTRUMENTS**

**Fair Value Measurement**

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in the principal or most advantageous market for an asset or liability in an orderly transaction between market participants at the measurement date. U.S. GAAP establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value into three broad levels giving the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (level 1 measurements) and the lowest level priority to unobservable inputs (level 3 measurements). The following describes the three levels of fair value hierarchy:

Level 1 - unadjusted quoted prices in active markets for identical assets or liabilities; includes U.S. Treasury Notes, and other U.S. Government Agency securities that actively trade in over-the-counter markets; equity securities and mutual funds that actively trade in over-the-counter markets.

Level 2 - quoted prices for similar assets or liabilities in active markets; or quoted prices for identical or similar assets or liabilities in markets that are not active; or inputs other than quoted prices that are observable for the asset or liability including yield curves, volatilities, and prepayment speeds.

Edgar Filing: LAKELAND BANCORP INC - Form 10-K

Level 3 - unobservable inputs for the asset or liability that reflect the Company's own assumptions about assumptions that market participants would use in the pricing of the asset or liability and that are consequently not based on market activity but on particular valuation techniques.

**Table of Contents**

The Company's assets that are measured at fair value on a recurring basis are its available for sale investment securities and its interest rate swaps. The Company obtains fair values on its securities using information from a third party servicer. If quoted prices for securities are available in an active market, those securities are classified as Level 1 securities. The Company has U.S. Treasury Notes and certain equity securities that are classified as Level 1 securities. Level 2 securities were primarily comprised of U.S. Agency bonds, residential mortgage-backed securities, obligations of state and political subdivisions and corporate securities. Fair values were estimated primarily by obtaining quoted prices for similar assets in active markets or through the use of pricing models supported with market data information. Standard inputs include benchmark yields, reported trades, broker-dealer quotes, issuer spreads, bids and offers. On a quarterly basis, the Company reviews the pricing information received from the Company's third party pricing service. This review includes a comparison to non-binding third-party quotes.

The fair values of derivatives are based on valuation models using current market terms (including interest rates and fees), the remaining terms of the agreements and the credit worthiness of the counter-party as of the measurement date (Level 2).

The following table sets forth the Company's financial assets that were accounted for at fair value on a recurring basis as of the periods presented by level within the fair value hierarchy. During the year ended December 31, 2015 and 2014, the Company did not make any transfers between recurring Level 1 fair value measurements and recurring Level 2 fair value measurements. Financial assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement:

December 31, 2015	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total Fair Value
<b>Assets:</b>	(in thousands)			
Investment securities, available for sale				
U.S. treasury and government agencies	\$ 4,888	\$ 92,245	\$	\$ 97,133
Mortgage-backed securities		289,572		289,572
Obligations of states and political subdivisions		36,498		36,498
Corporate debt securities		501		501
Equity securities	5,052	13,593		18,645
Total securities available for sale	9,940	432,409		442,349
Other Assets(a)		1,518		1,518
Total Assets	\$ 9,940	\$ 433,927	\$	\$ 443,867
Other Liabilities(a)	\$	\$ 1,518	\$	\$ 1,518
Total Liabilities	\$	\$ 1,518	\$	\$ 1,518

(a) Non-hedging interest rate derivatives



**Table of Contents**

December 31, 2014	Quoted Prices in			Total Fair Value
	Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
<b>Assets:</b>				
Investment securities, available for sale				
U.S. treasury and government agencies	\$ 8,321	\$ 85,599	\$	\$ 93,920
Mortgage backed securities		314,931		314,931
Obligations of states and political subdivisions		30,519		30,519
Corporate debt securities		505		505
Equity securities	4,154	13,420		17,574
Total securities available for sale	12,475	444,974		457,449
Other Assets(a)		37		37
Total Assets	\$ 12,475	\$ 445,011	\$	\$ 457,486
Other Liabilities(a)	\$	\$ 37	\$	\$ 37
Total Liabilities	\$	\$ 37	\$	\$ 37

## (a) Non-hedging interest rate derivatives

The following table sets forth the Company's financial assets subject to fair value adjustments (impairment) on a nonrecurring basis. Assets are classified in their entirety based on the lowest level of input that is significant to the fair value measurement:

December 31, 2015	(Level 1)	(Level 2)	(Level 3)	Total Fair Value
<b>Assets:</b>				
Impaired Loans and Leases	\$	\$	\$ 26,006	\$ 26,006
Loans held for sale		1,233		1,233
Other real estate owned and other repossessed assets			983	983

December 31, 2014	(Level 1)	(Level 2)	(Level 3)	Total Fair Value
<b>Assets:</b>				
Impaired Loans and Leases	\$	\$	\$ 25,693	\$ 25,693
Loans held for sale		592		592
Other real estate owned and other repossessed assets			1,026	1,026

Impaired loans and leases are evaluated and valued at the time the loan is identified as impaired at the lower of cost or market value. Because most of Lakeland's impaired loans are collateral dependent, fair value is generally measured based on the value of the collateral, less estimated costs to sell, securing these loans and leases and is classified at a level 3 in the fair value hierarchy. Collateral may be real estate, accounts receivable, inventory, equipment and/or other business assets. The value of the real estate is assessed based on appraisals by qualified third party licensed appraisers. The appraisers may use the income approach to value the collateral using discount rates (with ranges of 5-11%) or capitalization rates (with ranges of 5-9%) to evaluate the property. The value of the equipment may be determined by an appraiser, if significant, inquiry through a recognized valuation resource, or by the value on the borrower's financial statements. Field examiner reviews on business assets may be conducted based on the loan exposure and reliance on this type of collateral. Appraised and reported values may be discounted

## Edgar Filing: LAKELAND BANCORP INC - Form 10-K

based on management's historical knowledge, changes in market conditions from the time of valuation, and/or management's expertise and knowledge of the client and client's business. Impaired loans and

-99-

## **Table of Contents**

leases are reviewed and evaluated on at least a quarterly basis for additional impairment and adjusted accordingly, based on the same factors identified above.

The Company has a held for sale loan portfolio that consists of residential mortgages that are being sold in the secondary market. The Company records these mortgages at the lower of cost or fair market value. Fair value is generally determined by the value of purchase commitments.

Other real estate owned (OREO) and other repossessed assets, representing property acquired through foreclosure, are carried at fair value less estimated disposal costs of the acquired property. Fair value on other real estate owned is based on the appraised value of the collateral using discount rates or capitalization rates similar to those used in impaired loan valuation. The fair value of other repossessed assets is estimated by inquiry through a recognized valuation resource.

Changes in the assumptions or methodologies used to estimate fair values may materially affect the estimated amounts. Changes in economic conditions, locally or nationally, could impact the value of the estimated amounts of impaired loans, OREO and other repossessed assets.

### **Fair Value of Certain Financial Instruments**

Estimated fair values have been determined by the Company using the best available data and an estimation methodology suitable for each category of financial instruments. Management is concerned that there may not be reasonable comparability between institutions due to the wide range of permitted assumptions and methodologies in the absence of active markets. This lack of uniformity gives rise to a high degree of subjectivity in estimating financial instrument fair values.

The estimation methodologies used, the estimated fair values, and recorded book balances at December 31, 2015 and December 31, 2014 are outlined below.

This summary, as well as the table below, excludes financial assets and liabilities for which carrying value approximates fair value. For financial assets, these include cash and cash equivalents. For financial liabilities, these include noninterest bearing demand deposits, savings and interest-bearing transaction accounts and federal funds sold and securities sold under agreements to repurchase. The estimated fair value of demand, savings and interest-bearing transaction accounts is the amount payable on demand at the reporting date. Carrying value is used because there is no stated maturity on these accounts, and the customer has the ability to withdraw the funds immediately. Also excluded from this summary and the following table are those financial instruments recorded at fair value on a recurring basis, as previously described.

The fair value of Investment Securities Held to Maturity was measured using information from the same third-party servicer used for Investment Securities Available for Sale using the same methodologies discussed above. Investment Securities Held to Maturity includes \$6.3 million in short-term municipal bond anticipation notes and \$1.0 million in subordinated debt that are non-rated and do not have an active secondary market or information readily available on standard financial systems. As a result, the securities are classified as Level 3 securities. These are investments that management performs a credit analysis on before investing in these securities.

Federal Home Loan Bank of New York (FHLB) stock is an equity interest that can be sold to the issuing FHLB, to other FHLBs, or to other member banks at its par value. Because ownership of these securities is restricted, they do not have a readily determinable fair value. As such, the Company's FHLB Stock is recorded at cost or par value and is evaluated for impairment each reporting period by considering the ultimate recoverability of the investment rather than temporary declines in value. The Company's evaluation primarily includes an evaluation of liquidity, capitalization, operating performance, commitments, and regulatory or legislative events.

**Table of Contents**

The net loan portfolio at December 31, 2015 and December 31, 2014 has been valued using a present value discounted cash flow where market prices were not available. The discount rate used in these calculations is the estimated current market rate for new loans with similar credit risk. The valuation of our loan portfolio is consistent with accounting guidance but does not fully incorporate the exit price approach.

For fixed maturity certificates of deposit, fair value was estimated based on the present value of discounted cash flows using the rates currently offered for deposits of similar remaining maturities. The carrying amount of accrued interest payable approximates its fair value.

The fair value of long-term debt is based upon the discounted value of contractual cash flows. The Company estimates the discount rate using the rates currently offered for similar borrowing arrangements. The fair value of subordinated debentures is based on bid/ask prices from brokers for similar types of instruments.

The fair values of commitments to extend credit and standby letters of credit are estimated using the fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the present creditworthiness of the counterparties. For fixed-rate loan commitments, fair value also considers the difference between current levels of interest rates and the committed rates. The fair value of guarantees and letters of credit is based on fees currently charged for similar agreements or on the estimated cost to terminate them or otherwise settle the obligations with the counterparties at the reporting date. The fair values of commitments to extend credit and standby letters of credit are deemed immaterial.

The following table presents the carrying values, fair values and placement in the fair value hierarchy of the Company's financial instruments as of December 31, 2015 and December 31, 2014:

	Carrying Value	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1) (in thousands)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
<b>December 31, 2015</b>					
<b>Financial Assets:</b>					
Investment securities held to maturity	\$ 116,740	\$ 117,594	\$	\$ 110,293	\$ 7,301
Federal Home Loan and other membership bank stock	14,087	14,087		14,087	
Loans and leases, net	2,934,326	2,930,188			2,930,188
<b>Financial Liabilities:</b>					
Certificates of Deposit	343,321	341,998		341,998	
Other borrowings	271,905	275,409		275,409	
Subordinated debentures	31,238	24,366			24,366
<b>December 31, 2014</b>					
<b>Financial Assets:</b>					
Investment securities held to maturity	\$ 107,976	\$ 109,030	\$	\$ 103,916	\$ 5,114
Federal Home Loan and other membership bank stock	9,846	9,846		9,846	
Loans and leases, net	2,623,142	2,624,581			2,624,581
<b>Financial Liabilities:</b>					
Certificates of Deposit	279,962	279,439		279,439	
Other borrowings	202,498	205,343		205,343	
Subordinated debentures	41,238	30,929			30,929

**Table of Contents**

## NOTE 18 - DERIVATIVES

Lakeland is a party to interest rate derivatives that are not designated as hedging instruments. Under a program, Lakeland executes interest rate swaps with commercial lending customers to facilitate their respective risk management strategies. These interest rate swaps with customers are simultaneously offset by interest rate swaps that Lakeland executes with a third party, such that Lakeland minimizes its net risk exposure resulting from such transactions. Because the interest rate swaps associated with this program do not meet the strict hedge accounting requirements, changes in the fair value of both the customer swaps and the offsetting swaps are recognized directly in earnings. The changes in the fair value of the swaps offset each other, except for the credit risk of the counterparties, which is determined by taking into consideration the risk rating, probability of default and loss given default for all counterparties. As of December 31, 2015 and 2014, Lakeland had \$2.5 million and \$505,000, respectively, in securities pledged for collateral on its interest rate swaps with the financial institution.

The following table presents summary information regarding these derivatives for the periods presented (dollars in thousands):

December 31, 2015	Notional Amount	Average Maturity (Years)	Weighted Average Rate Fixed	Weighted Average Variable Rate	Fair Value
3rd party interest rate swaps	\$ 35,664	14.6	4.540%	1 Mo Libor + 2.00	(\$ 1,518)
Customer interest rate swaps	(35,664)	14.6	4.540%	1 Mo Libor + 2.00	1,518

December 31, 2014	Notional Amount	Average Maturity (Years)	Weighted Average Rate Fixed	Weighted Average Variable Rate	Fair Value
3rd party interest rate swaps	\$ 17,279	5.7	3.840%	1 Mo Libor + 2.21	(\$ 37)
Customer interest rate swaps	(17,279)	5.7	3.840%	1 Mo Libor + 2.21	\$ 37

## NOTE 19 - REGULATORY MATTERS

The Bank Holding Company Act of 1956 restricts the amount of dividends the Company can pay. Accordingly, dividends should generally only be paid out of current earnings, as defined.

The New Jersey Banking Act of 1948 restricts the amount of dividends paid on the capital stock of New Jersey chartered banks. Accordingly, no dividends shall be paid by such banks on their capital stock unless, following the payment of such dividends, the capital stock of Lakeland will be unimpaired, and: (1) Lakeland will have a surplus, as defined, of not less than 50% of its capital stock, or, if not, (2) the payment of such dividend will not reduce the surplus, as defined, of Lakeland. Under these limitations, approximately \$281.5 million was available for payment of dividends from Lakeland to the Company as of December 31, 2015.

The Company and Lakeland are subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory and possible additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the Company's and Lakeland's consolidated financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Company must meet specific capital guidelines that involve quantitative measures of the Company's and Lakeland's assets, liabilities and certain off-balance-sheet items as calculated under regulatory accounting practices. The Company's and Lakeland's capital amounts and classifications are also subject to qualitative judgments by the regulators about components, risk weightings and other factors.

Quantitative measures established by regulations to ensure capital adequacy require the Company and Lakeland to maintain minimum amounts and ratios (set forth in the table below) of total and Tier 1 capital (as defined in the regulations) to risk-weighted assets, and of Tier 1 capital to average assets. Management believes, as of December 31, 2015, that the Company and Lakeland met all capital adequacy requirements to which they are subject.

**Table of Contents**

As of December 31, 2015, the most recent notification from the FDIC categorized Lakeland as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized, Lakeland must maintain minimum total risk-based, Tier 1 risk-based, common equity Tier 1 capital and Tier 1 leverage ratios as set forth in the table below. There are no conditions or events since that notification that management believes have changed the institution's category.

In July 2013, the FRB and the FDIC approved the final rules implementing the Basel Committee on Banking Supervision's (BCBS) capital guidelines for U.S. banks. The rules include a new common equity Tier 1 capital to risk-weighted assets ratio of 4.5% and a common equity Tier 1 capital conservation buffer of 2.5% of risk-weighted assets. The capital conservation buffer will be phased-in starting with 0.625% in 2016 and increasing by 0.625% annually until it reaches 2.5% in 2019. The final rules also raise the minimum ratio of Tier 1 capital to risk-weighted assets from 4.0% to 6.0% and require a minimum leverage ratio of 4.0%. The final rules implement strict eligibility criteria for regulatory capital instruments. The phase-in period for the final rules began for the Company on January 1, 2015, with full compliance with all of the final rules requirements to be phased in over a multi-year schedule through January 1, 2019. As of December 31, 2015, the Company and Lakeland met all of the requirements under the new rules on a fully phased-in basis, if such requirements were in effect.

As of December 31, 2015 and 2014, the Company and Lakeland have the following capital ratios based on the then current regulations:

	Actual		For capital adequacy purposes		To be well capitalized under prompt corrective action provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
<b>As of December 31, 2015</b>						
Total capital (to risk-weighted assets)						
Company	\$ 351,779	11.61%	<sup>3</sup> \$242,299	<sup>3</sup> 8.00%	N/A	N/A
Lakeland	328,574	10.87	241,880	8.00	<sup>3</sup> \$302,350	<sup>3</sup> 10.00%
Tier 1 capital (to risk-weighted assets)						
Company	\$ 318,867	10.53%	<sup>3</sup> \$181,724	<sup>3</sup> 6.00%	N/A	N/A
Lakeland	295,662	9.78	181,410	6.00	<sup>3</sup> \$241,880	<sup>3</sup> 8.00%
Common equity Tier 1 capital (to risk-weighted assets)						
Company	\$ 288,867	9.54%	<sup>3</sup> \$136,293	<sup>3</sup> 4.50%	N/A	N/A
Lakeland	295,662	9.78	136,057	4.50	<sup>3</sup> \$196,527	<sup>3</sup> 6.50%
Tier 1 capital (to average assets)						
Company	\$ 318,867	8.70%	<sup>3</sup> \$146,594	<sup>3</sup> 4.00%	N/A	N/A
Lakeland	295,662	8.08	146,453	4.00	<sup>3</sup> \$183,066	<sup>3</sup> 5.00%

**Table of Contents**

	Actual		For capital adequacy purposes		To be well capitalized under prompt corrective action provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of December 31, 2014						
Total capital (to risk-weighted assets)						
Company	\$ 337,597	12.98%	<sup>3</sup> \$208,024	<sup>3</sup> 8.00%	N/A	N/A
Lakeland	314,047	12.10	207,714	8.00	<sup>3</sup> \$259,642	<sup>3</sup> 10.00%
Tier 1 capital (to risk-weighted assets)						
Company	\$ 305,814	11.76%	<sup>3</sup> \$104,012	<sup>3</sup> 4.00%	N/A	N/A
Lakeland	282,267	10.87	103,857	4.00	<sup>3</sup> \$155,785	<sup>3</sup> 6.00%
Common equity Tier 1 capital (to risk-weighted assets)						
Company	N/A	N/A	N/A	N/A	N/A	N/A
Lakeland	N/A	N/A	N/A	N/A	N/A	N/A
Tier 1 capital (to average assets)						
Company	\$ 305,814	9.08%	<sup>3</sup> \$134,760	<sup>3</sup> 4.00%	N/A	N/A
Lakeland	282,267	8.39	134,614	4.00	<sup>3</sup> \$168,268	<sup>3</sup> 5.00%

NOTE 20 - GOODWILL AND OTHER INTANGIBLE ASSETS

The Company has goodwill of \$110.0 million at December 31, 2015 and December 31, 2014, which includes \$22.9 million from the Somerset Hills acquisition and \$87.1 million from prior acquisitions. The Company recorded \$2.7 million in Core Deposit Intangible from the Somerset Hills Acquisition in 2013. Core Deposit Intangible was \$1.5 million on December 31, 2015 compared to \$2.0 million on December 31, 2014. The Company recorded \$415,000 in core deposit amortization in 2015 compared to \$464,000 and \$288,000 in 2014 and 2013, respectively.

The estimated future amortization expense for each of the succeeding five years ended December 31 is as follows (dollars in thousands):

For the year ended:	
2016	\$ 366
2017	316
2018	267
2019	218
2020	168

**Table of Contents**

NOTE 21 - CONDENSED FINANCIAL INFORMATION PARENT COMPANY ONLY:

**CONDENSED BALANCE SHEETS**

	December 31,	
	2015	2014
	(in thousands)	
<b>ASSETS</b>		
Cash and due from banks	\$ 15,921	\$ 11,893
Investment securities, available for sale	5,060	4,162
Investment securities, held to maturity	1,000	
Investment in subsidiaries	406,538	395,664
Other assets	3,265	9,344
<b>TOTAL ASSETS</b>	<b>\$ 431,784</b>	<b>\$ 421,063</b>
<b>LIABILITIES AND STOCKHOLDERS EQUITY</b>		
Other liabilities	\$ 30	\$ 387
Subordinated debentures	31,238	41,238
Total stockholders equity	400,516	379,438
<b>TOTAL LIABILITIES AND STOCKHOLDERS EQUITY</b>	<b>\$ 431,784</b>	<b>\$ 421,063</b>

**CONDENSED STATEMENTS OF OPERATIONS**

	Years Ended December 31,		
	2015	2014	2013
	(in thousands)		
<b>INCOME</b>			
Dividends from subsidiaries	\$ 23,376	\$ 16,581	\$ 20,916
Other income	1,987	102	1,640
<b>TOTAL INCOME</b>	<b>25,363</b>	<b>16,683</b>	<b>22,556</b>
<b>EXPENSE</b>			
Interest on subordinated debentures	1,009	1,068	1,286
Noninterest expenses	605	313	2,551
<b>TOTAL EXPENSE</b>	<b>1,614</b>	<b>1,381</b>	<b>3,837</b>
Income before benefit for income taxes	23,749	15,302	18,719
Income taxes provision (benefit)	67	(447)	(722)
Income before equity in undistributed income of subsidiaries	23,682	15,749	19,441
Equity in undistributed income of subsidiaries	8,799	15,380	5,528
<b>Net Income Available to Common Shareholders</b>	<b>\$ 32,481</b>	<b>\$ 31,129</b>	<b>\$ 24,969</b>



**Table of Contents****CONDENSED STATEMENTS OF CASH FLOWS**

	Years Ended December 31,		
	2015	2014	2013
	(in thousands)		
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>			
Net income	\$ 32,481	\$ 31,129	\$ 24,969
Adjustments to reconcile net income to net cash provided by (used in) operating activities:			
Share based compensation			895
Gain on securities	(29)		(359)
Gain on early extinguishment	(1,830)		(1,197)
Decrease (increase) in other assets	3,861	(174)	(954)
Increase (decrease) in other liabilities	176	(46)	25
Equity in undistributed income of subsidiaries	(8,799)	(15,380)	(5,528)
<b>NET CASH PROVIDED BY OPERATING ACTIVITIES</b>	<b>25,860</b>	<b>15,529</b>	<b>17,851</b>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>			
Net cash used in acquisition			(6,233)
Purchases of available for sale securities	(56)	(471)	(415)
Purchases of held to maturity securities	(1,000)		
Sale of land held for sale		60	
Proceeds from sale of securities, available for sale	29		654
<b>NET CASH USED IN INVESTING ACTIVITIES</b>	<b>(1,027)</b>	<b>(411)</b>	<b>(5,994)</b>
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>			
Cash dividends paid on common and preferred stock	(12,586)	(10,836)	(8,152)
Issuance of stock to the dividend reinvestment and stock purchase plan		77	186
Proceeds on issuance of stock, net	22		
Redemption of subordinated debentures, net	(8,170)		(9,113)
Retirement of Restricted stock	(254)	(104)	
Excess tax benefits	59	70	142
Exercise of stock options	124	90	2,209
<b>NET CASH USED IN FINANCING ACTIVITIES</b>	<b>(20,805)</b>	<b>(10,703)</b>	<b>(14,728)</b>
Net increase (decrease) in cash and cash equivalents	4,028	4,415	(2,871)
Cash and cash equivalents, beginning of year	11,893	7,478	10,349
<b>CASH AND CASH EQUIVALENTS, END OF YEAR</b>	<b>\$ 15,921</b>	<b>\$ 11,893</b>	<b>\$ 7,478</b>

**Table of Contents**

**Report of Independent Registered Public Accounting Firm**

The Board of Directors and Stockholders

Lakeland Bancorp, Inc.:

We have audited the accompanying consolidated balance sheets of Lakeland Bancorp, Inc. and Subsidiaries (the Company) as of December 31, 2015 and 2014, and the related consolidated statements of income, comprehensive income, changes in stockholders' equity, and cash flows for each of the years in the three-year period ended December 31, 2015. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Lakeland Bancorp, Inc. and Subsidiaries as of December 31, 2015 and 2014, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2015, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the Company's internal control over financial reporting as of December 31, 2015, based on criteria established in *Internal Control - Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) and our report dated March 15, 2016 expressed an adverse opinion on the effectiveness of the Company's internal control over financial reporting.

/s/ KPMG LLP

Short Hills, New Jersey

March 15, 2016

---

**Table of Contents**

**ITEM 9 - Changes in and Disagreements with Accountants on Accounting and Financial Disclosure.**

Not Applicable

**ITEM 9A - Controls and Procedures.**

**Disclosure Controls**

As of the end of the period covered by this Annual Report on Form 10-K, the Company's management, including the Chief Executive Officer and Chief Financial Officer, carried out an evaluation of the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934) pursuant to Securities Exchange Act Rule 15d-15(b).

Based on their evaluation as of December 31, 2015, the Company's Chief Executive Officer and Chief Financial Officer have concluded that because of the material weakness described below, the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934) were not effective as of such date in ensuring that the information required to be disclosed by the Company in the reports that the Company files or submits under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms and were not operating in an effective manner to ensure that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

**Management's Report on Internal Control over Financial Reporting.**

The management of Lakeland Bancorp, Inc. and its subsidiaries (the "Company") is responsible for establishing and maintaining adequate internal control over financial reporting as defined in Rule 13a-15(f) and 15d-15(f) under the Securities Exchange Act of 1934.

The Company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles and includes those policies and procedures that:

Pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the Company;

Provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the Company are being made only in accordance with authorizations of management and the board of directors of the Company; and

Provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the Company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to risk that controls may become inadequate because of changes in conditions or because of declines in the degree of compliance with policies or procedures.

The Company's management assessed the effectiveness of the Company's internal control over financial reporting as of December 31, 2015. In making this assessment, the Company's management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission ( "COSO" ) in *Internal Control-Integrated Framework (2013)*.

## **Table of Contents**

A material weakness is a deficiency, or a combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the company's annual

or interim financial statements will not be prevented or detected on a timely basis. During the fourth quarter management identified a material weakness in internal controls over the completeness and accuracy of the information used to determine the qualitative component of the allowance for loan and lease losses estimate. This material weakness in internal controls occurred due to the control operator not executing the review control, as designed, of the completeness and accuracy of the information used in the qualitative component of the allowance for loan and lease losses estimate as of December 31, 2015. No restatement of prior period financial statements and no change in previously issued financial results were required as a result of this weakness in internal control. Management has taken steps to remediate this weakness by enhancing review controls, including adding an additional independent level of review over the information used to determine the qualitative component in the allowance for loan and lease losses estimation process. As of December 31, 2015, based on management's assessment, the Company's internal control over financial reporting was ineffective.

Our independent registered public accounting firm, KPMG LLP, audited our internal control over financial reporting as of December 31, 2015. Their report, dated March 15, 2016, expressed an adverse opinion on our internal control over financial reporting.

## **Changes in Internal Controls over Financial Reporting**

Except for the foregoing, there was no change in the Company's internal control over financial reporting in the quarter ended December 31, 2015 that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

---

**Table of Contents**

**Report of Independent Registered Public Accounting Firm**

The Board of Directors and Shareholders

Lakeland Bancorp, Inc.:

We have audited the internal control over financial reporting of Lakeland Bancorp, Inc. (a New Jersey Corporation) and its subsidiaries (the Company) as of December 31, 2015, based on criteria established in *Internal Control Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

A material weakness is a deficiency, or a combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the company's annual or interim financial statements will not be prevented or detected on a timely basis. A material weakness related to internal controls over the completeness and accuracy of the information used to determine the qualitative component of the allowance for loan and lease losses estimate has been identified during the fourth quarter and included in management's assessment. We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of Lakeland Bancorp, Inc. and Subsidiaries (the Company) as of December 31, 2015 and 2014, and the related consolidated statements of income, comprehensive income, changes in stockholders' equity, and cash flows for each of the years in the three-year period ended December 31, 2015. This material weakness was considered in determining the nature, timing, and extent of audit tests applied in our audit of the 2015 consolidated financial statements, and this report does not affect our report dated March 15, 2016, which expressed an unqualified opinion on those consolidated financial statements.

In our opinion, because of the effect of the aforementioned material weakness on the achievement of the objectives of the control criteria, the Company has not maintained effective internal control over financial reporting as of December 31, 2015, based on criteria established in *Internal Control Integrated Framework (2013)* issued by COSO.

We do not express an opinion or any other form of assurance on management's statements referring to remedial actions taken after December 31, 2015, relative to the aforementioned material weakness in internal control over financial reporting.

/s/ KPMG LLP

Short Hills, New Jersey

March 15, 2016



**Table of Contents****ITEM 9B - Other Information.**

None.

**PART III****ITEM 10 - Directors, Executive Officers and Corporate Governance.**

The Company responds to this Item by incorporating by reference the material responsive to this Item in the Company's definitive proxy statement for its 2016 Annual Meeting of Shareholders.

**ITEM 11 - Executive Compensation.**

The Company responds to this Item by incorporating by reference the material responsive to this Item in the Company's definitive proxy statement for its 2016 Annual Meeting of Shareholders.

**ITEM 12 - Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters.**

The Company responds to this Item by incorporating by reference the material responsive to this Item in the Company's definitive proxy statement for its 2016 Annual Meeting of Shareholders.

**Equity Compensation Plan Information**

The following table gives information about the Company's common stock that may be issued upon the exercise of options under the Company's Amended and Restated 2000 Equity Compensation Program and the Company's 2009 Equity Compensation Program as of December 31, 2015. These plans were the Company's only equity compensation plans in existence as of December 31, 2015. The 2009 Equity Compensation Program is the successor to the 2000 Equity Compensation Program, and no additional awards will be granted under the 2000 Equity Compensation Program. No warrants or rights may be granted, or are outstanding, under the 2000 or the 2009 Equity Compensation Programs.

Plan Category	(a) Number Of Securities To Be Issued Upon Exercise Of Outstanding Options, Warrants and Rights	(b) Weighted-Average Exercise Price Of Outstanding Options, Warrants and Rights	(c) Number Of Securities Remaining Available For Future Issuance Under Equity Compensation Plans (Excluding Securities Reflected In Column(a))
Equity Compensation Plans Approved by Shareholders	386,245	\$ 9.16	1,616,644
Equity Compensation Plans Not Approved by Shareholders			
<b>TOTAL</b>	<b>386,245</b>	<b>\$ 9.16</b>	<b>1,616,644</b>

The number in column (a) does not include a total of 64,057 shares of Lakeland common stock that are issuable upon the exercise of options assumed in the Somerset Hills merger with a weighted average exercise price of \$7.01.

**ITEM 13 - Certain Relationships and Related Transactions, and Director Independence.**

Edgar Filing: LAKELAND BANCORP INC - Form 10-K

The Company responds to this Item by incorporating by reference the material responsive to this Item in the Company's definitive proxy statement for its 2016 Annual Meeting of Shareholders.

-111-



---

**Table of Contents**

**ITEM 14 - Principal Accounting Fees and Services.**

The Company responds to this Item by incorporating by reference the material responsive to this Item in the Company's definitive proxy statement for its 2016 Annual Meeting of Shareholders.

**PART IV**

**ITEM 15 - Exhibits and Financial Statement Schedules**

(a) 1. The following portions of the Company's consolidated financial statements are set forth in Item 8 of this Annual Report:

- (i) Consolidated Balance Sheets as of December 31, 2015 and 2014.
- (ii) Consolidated Statements of Operations for each of the three years in the period ended December 31, 2015.
- (iii) Consolidated Statements of Changes in Stockholders' Equity for each of the three years in the period ended December 31, 2015.
- (iv) Consolidated Statements of Cash Flows for each of the three years in the period ended December 31, 2015.
- (v) Notes to Consolidated Financial Statements.
- (vi) Report of Independent Registered Public Accounting Firm.
- (vii) Report of Former Independent Registered Public Accounting Firm.

(a) 2. Financial Statement Schedules

All financial statement schedules are omitted as the information, if applicable, is presented in the consolidated financial statements or notes thereto.

(a) 3. Exhibits

- 2.1 Agreement and Plan of Merger, dated as of January 28, 2013, by and between the Registrant and Somerset Hills Bancorp, is incorporated by reference to Exhibit 2.1 to the Registrant's Current Report on Form 8-K filed with the SEC on January 29, 2013.
- 2.2 Agreement and Plan of Merger, dated as of August 3, 2015, by and between the Registrant and Pascack Bancorp, Inc., is incorporated by reference to Exhibit 2.1 to the Registrant's Current Report on Form 8-K filed with the SEC on August 4, 2015.
- 2.3 Agreement and Plan of Merger, dated as of February 17, 2016, by and among the Registrant, Lakeland Bank and Harmony Bank, is incorporated by reference to Exhibit 2.1 to the Registrant's Current Report on Form 8-K filed with the SEC on February 18, 2016.
- 3.1 Registrant's Restated Certificate of Incorporation, dated May 19, 2005, including Certificate of Amendment dated February 4, 2009 to the Registrant's Restated Certificate of Incorporation, is incorporated by reference to Exhibit 3.1 to the Registrant's

## Edgar Filing: LAKELAND BANCORP INC - Form 10-K

Current Report on Form 8-K filed with the SEC on February 9, 2009.

- 3.2 Certificate of Amendment, dated January 29, 2009, to the Registrant's Restated Certificate of Incorporation is incorporated by reference to Exhibit 3.1 to the Registrant's Current Report on Form 8-K filed with the SEC on February 3, 2009.
- 3.3 Certificate of Amendment, dated May 8, 2013, to the Registrant's Restated Certificate of Incorporation is incorporated by reference to Exhibit 3.1 to the Registrant's Current Report on Form 8-K filed with the SEC on May 14, 2013.

-112-

**Table of Contents**

- 3.4 Registrant's Amended and Restated Bylaws are incorporated by reference to Exhibit 3.3 to the Registrant's Annual Report on Form 10-K for the year ended December 31, 2012.
- 10.1 Lakeland Bancorp, Inc. Amended and Restated 2000 Equity Compensation Program is incorporated by reference to Appendix A to the Registrant's definitive proxy materials for its 2005 Annual Meeting of Shareholders.
- 10.2 Lakeland Bancorp, Inc. 2009 Equity Compensation Program, as amended and restated effective February 27, 2014, is incorporated by reference to Exhibit 10.1 to the Registrant's Current Report on Form 8-K filed with the SEC on February 28, 2014.
- 10.3 Employment Agreement, dated as of April 2, 2008 and executed on May 22, 2008, among Lakeland Bancorp, Inc., Lakeland Bank and Thomas J. Shara, is incorporated by reference to Exhibit 10.1 to the Registrant's Current Report on Form 8-K filed with the SEC on May 28, 2008.
- 10.4 Supplemental Executive Retirement Plan Agreement for Thomas J. Shara, effective as of April 2, 2008, among Lakeland Bancorp, Inc., Lakeland Bank and Thomas J. Shara is incorporated by reference to Exhibit 10.2 to the Registrant's Current Report on Form 8-K filed with the SEC on May 28, 2008.
- 10.5 Change of Control Agreement dated March 1, 2001, among Lakeland Bancorp, Inc., Lakeland Bank and Joseph F. Hurley is incorporated by reference to Exhibit 10.8 to the Registrant's Annual Report on Form 10-K for the year ended December 31, 2000.
- 10.6 Change of Control Agreement dated March 1, 2001, among Lakeland Bancorp, Inc., Lakeland Bank and Robert A. Vandenberg is incorporated by reference to Exhibit 10.9 to the Registrant's Annual Report on Form 10-K for the year ended December 31, 2000.
- 10.7 Change of Control Agreement dated March 7, 2001, among Lakeland Bancorp, Inc. Lakeland Bank and Jeffrey J. Buonforte is incorporated by reference to Exhibit 10.11 to the Registrant's Annual Report on Form 10-K for the year ended December 31, 2000.
- 10.8 Amendments to Change of Control Agreements, dated March 10, 2003, among Lakeland Bancorp, Inc., Lakeland Bank and each of Joseph F. Hurley, Robert A. Vandenberg and Jeffrey J. Buonforte are incorporated by reference to Exhibit 10.13 to the Registrant's Annual Report on Form 10-K for the year ended December 31, 2002.
- 10.9 Change of Control Agreement dated April 7, 2004, among Lakeland Bancorp, Inc. Lakeland Bank and James R. Noonan is incorporated by reference to Exhibit 10.11 to the Registrant's Annual Report on Form 10-K for the year ended December 31, 2004.
- 10.10 Lakeland Bancorp, Inc. Directors' Deferred Compensation Plan, as amended and restated, is incorporated by reference to Exhibit 10.6 to the Registrant's Current Report on Form 8-K filed with the SEC on December 30, 2008.
- 10.11 Change in Control, Severance and Employment Agreement, dated as of November 24, 2008, among Lakeland Bancorp, Inc., Lakeland Bank and David S. Yanagisawa, is incorporated by reference to Exhibit 10.9 of the Registrant's Current Report on Form 8-K filed with the SEC on December 30, 2008.
- 10.12 Second Amending Agreement to Change in Control Agreement, dated as of December 31, 2008, among Lakeland Bancorp, Inc., Lakeland Bank and Jeffrey J. Buonforte, is incorporated by reference to Exhibit 10.1 to the Registrant's Current Report on Form 8-K filed with the SEC on December 30, 2008.
- 10.13 Second Amending Agreement to Change in Control Agreement, dated as of December 31, 2008, among Lakeland Bancorp, Inc., Lakeland Bank and Joseph F. Hurley, is incorporated by reference to Exhibit 10.2 to the Registrant's Current Report on Form 8-K filed with the SEC on December 30, 2008.

**Table of Contents**

- 10.14 First Amendatory Agreement to Change in Control Agreement, dated as of December 31, 2008, among Lakeland Bancorp, Inc., Lakeland Bank and James R. Noonan, is incorporated by reference to Exhibit 10.4 to the Registrant's Current Report on Form 8-K filed with the SEC on December 30, 2008.
- 10.15 Second Amendatory Agreement to Change in Control Agreement, dated as of December 31, 2008, among Lakeland Bancorp, Inc., Lakeland Bank and Robert A. Vandenberg, is incorporated by reference to Exhibit 10.5 to the Registrant's Current Report on Form 8-K filed with the SEC on December 30, 2008.
- 10.16 Supplemental Executive Retirement Plan Agreement, effective as of December 23, 2008, among Lakeland Bancorp, Inc., Lakeland Bank and Robert A. Vandenberg, is incorporated by reference to Exhibit 10.7 to the Registrant's Current Report on Form 8-K filed with the SEC on December 30, 2008.
- 10.17 Amendment No. 3 to Salary Continuation Agreement, dated as of December 31, 2008, among Lakeland Bancorp, Inc., Lakeland Bank and Robert A. Vandenberg, is incorporated by reference to Exhibit 10.8 to the Registrant's Current Report on Form 8-K filed with the SEC on December 30, 2008.
- 10.18 Change in Control Agreement, dated as of June 12, 2009, among Lakeland Bancorp, Inc., Lakeland Bank and Ronald E. Schwarz, is incorporated by reference to Exhibit 10.25 to the Registrant's Annual Report on Form 10-K for the year ended December 31, 2010.
- 10.19 Employment Agreement, dated as of January 28, 2013, by and among the Registrant, Lakeland Bank and Stewart E. McClure, Jr., is incorporated by reference to Exhibit 10.1 to the Registrant's Current Report on Form 8-K filed with the SEC on January 29, 2013.
- 10.20 Amendatory Agreement, dated as of January 28, 2013 to the Amended and Restated Supplemental Executive Retirement Plan, among Somerset Hills Bancorp, Somerset Hills Bank and Stewart E. McClure, Jr., is incorporated by reference to Exhibit 10.2 to the Registrant's Current Report on Form 8-K filed with the SEC on January 29, 2013.
- 10.21 Somerset Hills Bancorp 1998 Combined Stock Option Plan is incorporated by reference to Exhibit 4.5 to the Registrant's Registration Statement on Form S-8 filed with the SEC on June 3, 2013.
- 10.22 Somerset Hills Bancorp 2001 Combined Stock Option Plan is incorporated by reference to Exhibit 4.6 to the Registrant's Registration Statement on Form S-8 filed with the SEC on June 3, 2013.
- 10.23 Somerset Hills Bancorp 2007 Equity Incentive Plan is incorporated by reference to Exhibit 4.7 to the Registrant's Registration Statement on Form S-8 filed with the SEC on June 3, 2013.
- 10.24 Somerset Hills Bancorp 2012 Equity Incentive Plan is incorporated by reference to Exhibit 4.8 to the Registrant's Registration Statement on Form S-8 filed with the SEC on June 3, 2013.
- 10.25 Third Amendatory Agreement to Change of Control Agreement, dated October 31, 2013, among Lakeland Bancorp, Inc., Lakeland Bank and Jeffrey J. Buonforte, is incorporated by reference to Exhibit 10.1 to the Registrant's Quarterly Report on Form 10-Q for the quarter ended September 30, 2013.
- 10.26 Change of Control Agreement, dated October 31, 2013, among Lakeland Bancorp, Inc., Lakeland Bank and Timothy J. Matteson, is incorporated by reference to Exhibit 10.2 to the Registrant's Quarterly Report on Form 10-Q for the quarter ended September 30, 2013.
- 10.27 Supplemental Executive Retirement Plan Agreement, dated as of December 26, 2014, among Lakeland Bancorp, Inc., Lakeland Bank and Stewart E. McClure, Jr., is incorporated by reference to Exhibit 10.28 to the Registrant's Annual Report on Form 10-K for the year ended December 31, 2014.

**Table of Contents**

10.28	Deferred Compensation Agreement, dated February 27, 2015, among Lakeland Bancorp, Inc., Lakeland Bank and Thomas J. Shara, is incorporated by reference to Exhibit 10.1 to the Registrant's Current Report on Form 8-K filed with the SEC on March 2, 2015.
10.29	Lakeland Bancorp, Inc. Elective Deferral Plan is incorporated by reference to Exhibit 10.1 to the Registrant's Current Report on Form 8-K filed with the SEC on March 20, 2015.
10.30	Amendment, dated August 7, 2015, to Employment Agreement, dated April 2, 2008 and executed May 22, 2008, among Lakeland Bancorp, Inc., Lakeland Bank and Thomas J. Shara, is incorporated by reference to Exhibit 10.1 to the Registrant's Current Report on Form 8-K filed with the SEC on August 7, 2015.
10.31	Amendment, dated August 7, 2015, to Change in Control Agreement, dated March 1, 2001, as amended by agreements dated March 10, 2003 and December 31, 2008, among Lakeland Bancorp, Inc., Lakeland Bank and Joseph F. Hurley, is incorporated by reference to Exhibit 10.2 to the Registrant's Current Report on Form 8-K filed with the SEC on August 7, 2015.
10.32	Amendment, dated August 7, 2015, to Change in Control Agreement, dated March 1, 2001, as amended by agreements dated March 10, 2003 and December 31, 2008, among Lakeland Bancorp, Inc., Lakeland Bank and Robert A. Vandenberg, is incorporated by reference to Exhibit 10.3 to the Registrant's Current Report on Form 8-K filed with the SEC on August 7, 2015.
10.33	Amendment, dated August 7, 2015, to Change in Control Agreement, dated June 12, 2009, among Lakeland Bancorp, Inc., Lakeland Bank and Ronald E. Schwarz, is incorporated by reference to Exhibit 10.4 to the Registrant's Current Report on Form 8-K filed with the SEC on August 7, 2015.
10.34	Amendment, dated August 7, 2015, to Change in Control Agreement, dated November 24, 2008, as amended, among Lakeland Bancorp, Inc., Lakeland Bank and David S. Yanagisawa, is incorporated by reference to Exhibit 10.5 to the Registrant's Quarterly Report on Form 10-Q for the period ended June 30, 2015.
10.35	Amendment, dated August 7, 2015, to Change in Control Agreement, dated March 7, 2001, as amended, among Lakeland Bancorp, Inc., Lakeland Bank and Jeffrey J. Buonforte, is incorporated by reference to Exhibit 10.6 to the Registrant's Quarterly Report on Form 10-Q for the period ended June 30, 2015.
10.36	Amendment, dated August 7, 2015, to Change in Control Agreement, dated April 7, 2004, as amended, among Lakeland Bancorp, Inc., Lakeland Bank and James R. Noonan, is incorporated by reference to Exhibit 10.7 to the Registrant's Quarterly Report on Form 10-Q for the period ended June 30, 2015.
10.37	Amendment, dated August 7, 2015, to Change in Control Agreement, dated October 31, 2013, as amended, among Lakeland Bancorp, Inc., Lakeland Bank and Timothy J. Matteson, is incorporated by reference to Exhibit 10.8 to the Registrant's Quarterly Report on Form 10-Q for the period ended June 30, 2015.
10.38	Amendatory Agreement, dated as of December 26, 2014, to the Employment Agreement, dated as of January 28, 2013, amended on May 31, 2013, among Lakeland Bancorp, Inc., Lakeland Bank and Steward E. McClure, Jr.
12.1	Statement of Ratios of Earnings to Fixed Charges.
21.1	Subsidiaries of Registrant.
23.1	Consent of KPMG LLP.
24.1	Power of Attorney.
31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

**Table of Contents**

32.1	Certification of Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema Document
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	XBRL Taxonomy Extension Label Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document

**Table of Contents****SIGNATURES**

Pursuant to the requirements of Section 13 or 15(d) 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.

LAKELAND BANCORP, INC.

Dated: March 15, 2016

By: /s/ Thomas J. Shara  
Thomas J. Shara  
President and Chief Executive Officer

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

<b>Signature</b>	<b>Capacity</b>	<b>Date</b>
/s/ Bruce D. Bohuny*	Director	March 15, 2016
Bruce D. Bohuny		
/s/ Mary Ann Deacon*	Director	March 15, 2016
Mary Ann Deacon		
/s/ Edward B. Deutsch*	Director	March 15, 2016
Edward B. Deutsch		
/s/ Brian Flynn*	Director	March 15, 2016
Brian Flynn		
/s/ Mark J. Fredericks*	Director	March 15, 2016
Mark J. Fredericks		
/s/ Janeth C. Hendershot*	Director	March 15, 2016
Janeth C. Hendershot		
/s/ Lawrence R. Inserra, Jr.*	Director	March 15, 2016
Lawrence R. Inserra, Jr.		
/s/ Thomas J. Marino*	Director	March 15, 2016
Thomas J. Marino		
/s/ Robert E. McCracken*	Director	March 15, 2016
Robert E. McCracken		

Edgar Filing: LAKELAND BANCORP INC - Form 10-K

/s/ Robert B. Nicholson, III*	Director	March 15, 2016
Robert B. Nicholson, III		
/s/ Joseph P. O Dowd*	Director	March 15, 2016
Joseph P. O Dowd		
/s/ Thomas J. Shara	Director, President and Chief Executive Officer (Principal Executive Officer)	March 15, 2016
Thomas J. Shara		

-117-



**Table of Contents**

<b>Signature</b>	<b>Capacity</b>	<b>Date</b>
/s/ Stephen R. Tilton, Sr.* Stephen R. Tilton, Sr.	Director	March 15, 2016
/s/ Joseph F. Hurley Joseph F. Hurley	Executive Vice President and Chief Financial Officer (Principal Financial Officer and Principal Accounting Officer)	March 15, 2016
*By: /s/ Thomas J. Shara Thomas J. Shara  Attorney-in-Fact		March 15, 2016