CHOICEONE FINANCIAL SERVICES INC
Form 10-K
March 27, 2017

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 10-K

Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the fiscal year ended December 31, 2016

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

For the transition period from__________________ to __________________

Commission File Number: 000-19202

ChoiceOne Financial Services, Inc.

(Exact Name of Registrant as Specified in its Charter)

Michigan (State or Other Jurisdiction of Incorporation or Organization)	**38-2659066** (I.R.S. Employer Identification No.)
109 East Division Street, Sparta, Michigan (Address of Principal Executive Offices)	**49345** (Zip Code)

(616) 887-7366
(Registrant’s Telephone Number, Including Area Code)

Securities registered pursuant to Section 12(g) of the Securities Exchange Act of 1934:

Common Stock
(Title of Class)

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 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 in this form, 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 Accelerated filer

Non-accelerated filer Smaller reporting company

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

As of June 30, 2016, the aggregate market value of common stock held by non-affiliates of the Registrant was $66.5 million. This amount is based on an average bid price of $23.10 per share for the Registrant's stock as of such date.

As of February 28, 2017, the Registrant had 3,278,865 shares of common stock outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the definitive Proxy Statement of ChoiceOne Financial Services, Inc. for the Annual Meeting of Shareholders to be held on May 24, 2017 are incorporated by reference into Part III of this Form 10-K.

ChoiceOne Financial Services, Inc.

Form 10-K ANNUAL REPORT

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FORWARD-LOOKING STATEMENTS

This report and the documents incorporated into this report contain forward-looking statements that are based on management's beliefs, assumptions, current expectations, estimates and projections about the financial services industry, the economy, and ChoiceOne Financial Services, Inc. Words such as "anticipates," "believes," "expects," "forecasts," "intends," "is likely," "plans," "predicts," "projects," "may," "could," "estimates," and variations of such words and similar ex are intended to identify such forward-looking statements. Management's determination of the provision and allowance for loan losses, the carrying value of goodwill, loan servicing rights and other real estate owned, and the fair value of investment securities (including whether any impairment on any investment security is temporary or other than temporary and the amount of any impairment) and management's assumptions concerning pension and other postretirement benefit plans involve judgments that are inherently forward-looking. All of the information concerning interest rate sensitivity is forward-looking. All statements with references to future time periods are forward-looking. These statements are not guarantees of future performance and involve certain risks, uncertainties and assumptions ("risk factors") that are difficult to predict with regard to timing, extent, likelihood, and degree of occurrence. Therefore, actual results and outcomes may materially differ from what may be expressed, implied or forecasted in such forward-looking statements. Furthermore, ChoiceOne Financial Services, Inc. undertakes no obligation to update, amend, or clarify forward-looking statements, whether as a result of new information, future events, or otherwise.

Risk factors include, but are not limited to, the risk factors disclosed in Item 1A of this report. These are representative of the risk factors that could cause a difference between an ultimate actual outcome and a preceding forward-looking statement.

PART I

Item 1. Business

General

ChoiceOne Financial Services, Inc. ("ChoiceOne" or the "Company") is a financial holding company registered under the Bank Holding Company Act of 1956, as amended ("BHC Act"). The Company was incorporated on February 24, 1986, as a Michigan corporation. The Company was formed to create a bank holding company for the purpose of acquiring all of the capital stock of ChoiceOne Bank (formerly Sparta State Bank), which became a wholly owned subsidiary of the Company on April 6, 1987. The Company's only subsidiary and significant asset as of December 31, 2016, was ChoiceOne Bank (the "Bank"). Effective November 1, 2006, the Company merged with Valley Ridge Financial Corp. ("VRFC"), a one-bank holding company for Valley Ridge Bank ("VRB"). In the merger, the Company issued shares of its common stock in exchange for all outstanding shares of VRFC. In December 2006, VRB was consolidated into the Bank. The Bank owns all of the outstanding common stock of ChoiceOne Insurance Agencies, Inc., an independent insurance agency headquartered in Sparta, Michigan (the "Insurance Agency").

The Company’s business is primarily concentrated in a single industry segment - banking. The Bank is a full-service banking institution that offers a variety of deposit, payment, credit and other financial services to all types of customers. These services include time, savings, and demand deposits, safe deposit services, and automated transaction machine services. Loans, both commercial and consumer, are extended primarily on a secured basis to corporations, partnerships and individuals. Commercial lending covers such categories as business, industry, agricultural, construction, inventory and real estate. The Bank’s consumer loan department makes direct and indirect loans to consumers and purchasers of residential and real property. No material part of the business of the Company or the Bank is dependent upon a single customer or very few customers, the loss of which would have a materially adverse effect on the Company.

The Bank’s primary market area lies within Kent, Muskegon, Newaygo, and Ottawa counties in Michigan in the communities where the Bank’s offices are located. Currently the Bank serves these markets through twelve full-service offices and one loan production office. The Company and the Bank have no foreign assets or income except for foreign debt securities.

At December 31, 2016, the Company had consolidated total assets of $607.4 million, net loans of $364.7 million, total deposits of $512.4 million and total shareholders’ equity of $71.7 million. For the year ended December 31, 2016, the Company recognized consolidated net income of $6.1 million. The principal source of revenue for the Company and the Bank is interest and fees on loans. On a consolidated basis, interest and fees on loans accounted for 59%, 59%, and 61% of total revenues in 2016, 2015, and 2014, respectively. Interest on securities accounted for 13%, 12%, and 13% of total revenues in 2016, 2015, and 2014, respectively. For more information about the Company’s financial condition and results of operations, see the consolidated financial statements and related notes included in Part II, Item 8 of this report.

Competition

The Bank's competition primarily comes from other financial institutions located within Kent, Muskegon, Newaygo, and Ottawa counties in western Michigan. There are a number of larger commercial banks within the Bank's primary market area. The Bank also competes with a large number of other financial institutions, such as savings and loan associations, insurance companies, consumer finance companies, credit unions and commercial finance and leasing companies for deposits, loans and service business. Money market mutual funds, brokerage houses and nonfinancial institutions provide many of the financial services offered by the Bank. Many of these competitors have substantially greater resources than the Bank. The principal methods of competition for financial services are price (the rates of interest charged for loans, the rates of interest paid for deposits and the fees charged for services) and the convenience and quality of services rendered to customers.

Supervision and Regulation

Banks and bank holding companies are extensively regulated. The Company is subject to supervision and regulation by the Board of Governors of the Federal Reserve System (the "Federal Reserve Board"). The Company's activities are generally limited to owning or controlling banks and engaging in such other activities as the Federal Reserve Board may determine to be closely related to banking. Prior approval of the Federal Reserve Board, and in some cases various other government agencies, is required for the Company to acquire control of any additional bank holding companies, banks or other operating subsidiaries. Under Federal Reserve Board policy, the Company is expected to act as a source of financial strength to the Bank and to commit resources to support it.

The Bank is chartered under state law and is subject to regulation by the Michigan Department of Insurance and Financial Services. State banking laws place restrictions on various aspects of banking, including permitted activities, loan interest rates, branching, payment of dividends and capital and surplus requirements. The Bank is a member of the Federal Reserve System and is also subject to regulation by the Federal Reserve Board. The Bank's deposits are insured by the Federal Deposit Insurance Corporation (the "FDIC") to the maximum extent provided by law. The Bank is a member of the Federal Home Loan Bank system, which provides certain advantages to the Bank, including favorable borrowing rates for certain funds.

The Company is a legal entity separate and distinct from the Bank. The Company's primary source of funds available to pay dividends to shareholders is dividends paid to it by the Bank. There are legal limitations on the extent to which the Bank can lend or otherwise supply funds to the Company. In addition, payment of dividends to the Company by the Bank is subject to various state and federal regulatory limitations.

The FDIC formed the Deposit Insurance Fund ("DIF") in accordance with the Federal Deposit Insurance Reform Act of 2005 ("Reform Act") to create a stronger and more stable insurance system. The FDIC maintains the insurance reserves of the DIF by assessing depository institutions an insurance premium. The DIF insures deposit accounts of the Bank up to a maximum amount of $250,000 per separately insured depositor. FDIC insured depository institutions are

required to pay deposit insurance premiums based on the risk an institution poses to the DIF. In February 2011, the FDIC finalized rules, effective for assessments occurring after April 1, 2011, which redefined an institution's assessment base as average consolidated total assets minus average Tier 1 capital. The new rules also established the initial base assessment rate for Risk Category 1 institutions, such as the Bank, at 5 to 9 basis points (annualized). Effective July 1, 2016, the FDIC amended its rules to eliminate Risk Categories for small banks, replacing them with a method based on a bank's CAMELS composite rating and several financial ratios. On that date, the Bank's initial base assessment rate was reduced to 3 basis points, since the Federal Deposit Insurance Reserve Ratio reached 1.15% as of June 30, 2016.

The Deposit Insurance Funds Act of 1996 authorized the Financing Corporation ("FICO") to impose periodic assessments on all depository institutions. The purpose of these periodic assessments is to spread the cost of the interest payments on the outstanding FICO bonds issued to recapitalize the Savings Association Insurance Fund ("SAIF") over a larger number of institutions.

The federal banking agencies have adopted guidelines to promote the safety and soundness of federally-insured depository institutions. These guidelines establish standards for, among other things, internal controls, information systems, internal audit systems, loan documentation, credit underwriting, interest rate exposure, asset growth, compensation, fees and benefits, asset quality and earnings.

The Company and the Bank are subject to regulatory “risk-based” capital guidelines. Failure to meet these capital guidelines could subject the Company or the Bank to a variety of enforcement remedies, including issuance of a capital directive, the termination of deposit insurance by the FDIC, a prohibition on accepting brokered deposits, and other restrictions on its business. In addition, the Bank would generally not receive regulatory approval of any application that requires the consideration of capital adequacy, such as a branch or merger application, unless it could demonstrate a reasonable plan to meet the capital requirement within a reasonable period of time.

Under Federal Reserve Board policy, the Company is expected to act as a source of financial strength to the Bank and to commit resources to support the Bank. In addition, if DIFS deems the Bank’s capital to be impaired, DIFS may require the Bank to restore its capital by a special assessment on the Company as the Bank’s sole shareholder. If the Company fails to pay any assessment, the Company’s directors will be required, under Michigan law, to sell the shares of the Bank’s stock owned by the Company to the highest bidder at either a public or private auction and use the proceeds of the sale to restore the Bank’s capital.

The Federal Deposit Insurance Corporation Improvement Act (“FDICIA”) requires, among other things, federal banking agencies to take “prompt corrective action” in respect of depository institutions that do not meet minimum capital requirements. FDICIA sets forth the following five capital categories: “well-capitalized,” “adequately-capitalized,” “undercapitalized,” “significantly-undercapitalized” and “critically-undercapitalized.” A depository institution’s capital category will depend upon how its capital levels compare with various relevant capital measures as established by regulation, which include Tier 1 and total risk-based capital ratio measures and a leverage capital ratio measure. Under certain circumstances, the appropriate banking agency may treat a well-capitalized, adequately-capitalized, or undercapitalized institution as if the institution were in the next lower capital category.

Federal banking regulators are required to take specified mandatory supervisory actions and are authorized to take other discretionary actions with respect to institutions in the three undercapitalized categories. The severity of the action depends upon the capital category in which the institution is placed. Subject to a narrow exception, the banking regulator must generally appoint a receiver or conservator for an institution that is critically undercapitalized. An institution in any of the undercapitalized categories is required to submit an acceptable capital restoration plan to its appropriate federal banking agency. An undercapitalized institution is also generally prohibited from paying any dividends, increasing its average total assets, making acquisitions, establishing any branches, accepting or renewing any brokered deposits or engaging in any new line of business, except under an accepted capital restoration plan or with FDIC approval.

On July 3, 2013, the FDIC Board of Directors approved the Regulatory Capital Interim Final Rule, implementing Basel III. This rule redefines Tier 1 capital as two components (Common Equity Tier 1 and Additional Tier 1), creates a new capital ratio (Common Equity Tier 1 Risk-based Capital Ratio) and implements a capital conservation buffer. It also revises the prompt corrective action thresholds and makes changes to risk weights for certain assets and off-balance-sheet exposures. The Bank was required to transition into the new rule beginning on January 1, 2015.

Banks are subject to a number of federal and state laws and regulations, which have a material impact on their business. These include, among others, minimum capital requirements, state usury laws, state laws relating to fiduciaries, the Truth in Lending Act, the Truth in Savings Act, the Equal Credit Opportunity Act, the Fair Housing Act, the Fair Credit Reporting Act, the Expedited Funds Availability Act, the Community Reinvestment Act, the Real Estate Settlement Procedures Act, the Service Members Civil Relief Act, the USA PATRIOT Act, the Bank Secrecy Act, regulations of the Office of Foreign Assets Controls, the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, electronic funds transfer laws, redlining laws, predatory lending laws, antitrust laws, environmental laws, money laundering laws and privacy laws. The monetary policy of the Federal Reserve Board may influence the growth and distribution of bank loans, investments and deposits, and may also affect interest rates on loans and deposits. These policies may have a significant effect on the operating results of banks.

In general, the BHC Act limits the business of bank holding companies to banking, managing or controlling banks and other activities that the Federal Reserve Board has determined to be closely related to the business of banking. In addition, bank holding companies that qualify and elect to be financial holding companies may engage in any activities that are financial in nature or complementary to a financial activity and do not pose a substantial risk to the safety and soundness of depository institutions or the financial system without prior approval of the Federal Reserve Board. Activities that are financial in nature include securities underwriting and dealing, insurance underwriting and making merchant banking investments.

In order for the Corporation to maintain financial holding company status, both the Company and the Bank must be categorized as “well-capitalized” and “well-managed” under applicable regulatory guidelines. If the Company or the Bank ceases to meet these requirements, the Federal Reserve Board may impose corrective capital and/or managerial requirements and place limitations on the Corporation’s ability to conduct the broader financial activities permissible for financial holding companies. In addition, if the deficiencies persist, the Federal Reserve Board may require the Company to divest of the Bank. The Company and the Bank were both categorized as “well-capitalized” and “well-managed” as of December 31, 2016.

Bank holding companies may acquire banks and other bank holding companies located in any state in the United States without regard to geographic restrictions or reciprocity requirements imposed by state banking law. Banks may also establish interstate branch networks through acquisitions of and mergers with other banks. The establishment of *de novo* interstate branches or the acquisition of individual branches of a bank in another state (rather than the acquisition of an out-of-state bank in its entirety) is allowed only if specifically authorized by state law.

Michigan banking laws do not significantly restrict interstate banking. The Michigan Banking Code permits, in appropriate circumstances and with the approval of the Department of Insurance and Financial Services, (1) acquisition of Michigan banks by FDIC-insured banks, savings banks or savings and loan associations located in other states, (2) sale by a Michigan bank of branches to an FDIC-insured bank, savings bank or savings and loan association located in a state in which a Michigan bank could purchase branches of the purchasing entity, (3) consolidation of Michigan banks and FDIC-insured banks, savings banks or savings and loan associations located in other states having laws permitting such consolidation, (4) establishment of branches in Michigan by FDIC-insured banks located in other states, the District of Columbia or U.S. territories or protectorates having laws permitting a Michigan bank to establish a branch in such jurisdiction, and (5) establishment by foreign banks of branches located in Michigan.

Banks are subject to the provisions of the Community Reinvestment Act ("CRA"). Under the terms of the CRA, the appropriate federal bank regulatory agency is required, in connection with its examination of a bank, to assess the bank's record in meeting the credit needs of the community served by that bank, including low- and moderate-income neighborhoods, consistent with the safe and sound operation of the institution. Under the CRA, institutions are assigned a rating of "outstanding," "satisfactory," "needs to improve," or "substantial non-compliance." The regulatory agency's assessment of the bank's record is made available to the public. Further, a bank's federal regulatory agency is required to assess the CRA compliance record of any bank that has applied to establish a new branch office that will accept deposits, relocate an office, or merge or consolidate with, or acquire the assets or assume the liabilities of, a federally regulated financial institution. In the case of a bank holding company applying for approval to acquire a bank or another bank holding company, the Federal Reserve Board will assess the CRA compliance record of each subsidiary bank of the applicant bank holding company, and such compliance records may be the basis for denying the application. Upon receiving notice that a subsidiary bank is rated less than "satisfactory," a financial holding company will be prohibited from additional activities that are permitted to be conducted by a financial holding company and from acquiring any company engaged in such activities. The Bank's CRA rating was "Satisfactory" as of its more recent examination.

Effects of Compliance With Environmental Regulations

The nature of the business of the Bank is such that it holds title, on a temporary or permanent basis, to a number of parcels of real property. These include properties owned for branch offices and other business purposes as well as properties taken in or in lieu of foreclosure to satisfy loans in default. Under current state and federal laws, present and past owners of real property may be exposed to liability for the cost of clean up of environmental contamination on or originating from those properties, even if they are wholly innocent of the actions that caused the contamination. These liabilities can be material and can exceed the value of the contaminated property. Management is not presently aware of any instances where compliance with these provisions will have a material effect on the capital expenditures,

earnings or competitive position of the Company or the Bank, or where compliance with these provisions will adversely affect a borrower's ability to comply with the terms of loan contracts.

Employees

As of February 28, 2017, the Company, the Bank and the Insurance Agency employed 160 employees, of which 126 were full-time employees. The Company, the Bank, and the Insurance Agency believe their overall relations with their employees are good.

Statistical Information

Additional statistical information describing the business of the Company appears on the following pages and in Management's Discussion and Analysis of Financial Condition and Results of Operations and in Item 7 of this report and in the Consolidated Financial Statements and the notes thereto in Item 8 of this report. The following statistical information should be read in conjunction with Management's Discussion and Analysis of Financial Condition and Results of Operations and the Consolidated Financial Statements and notes in this report.

Securities Portfolio

The carrying value of securities categorized by type at December 31 was as follows:

(Dollars in thousands)	2016	2015	2014
U.S. Government and federal agency	$59,052	$57,207	$44,503
U.S. Treasury notes and bonds	4,072	6,100	8,058
State and municipal	88,973	77,754	69,835
Mortgage-backed securities	7,789	6,970	8,942
Corporate	7,041	8,387	7,538
Foreign debt securities	4,400	995	994
Equity securities	2,883	2,453	2,275
Asset-backed securities	178	270	376
Total	$174,388	$160,136	$142,521

The Company did not hold investment securities from any one issuer at December 31, 2016, that were greater than 10% of the Company's shareholders' equity, exclusive of U.S. Government and U.S. Government agency securities.

Presented below is the fair value of securities as of December 31, 2016 and 2015, a schedule of maturities of securities as of December 31, 2016, and the weighted average yields of securities as of December 31, 2016:

	Securities maturing within:					
(Dollars in thousands)	Less than 1 Year	1 Year - 5 Years	5 Years - 10 Years	More than 10 Years	Fair Value at Dec. 31, 2016	Fair Value at Dec. 31, 2015
U.S. Government and federal agency	$20,320	$34,822	$3,910	$—	$59,052	$57,207
U.S. Treasury notes and bonds	—	4,072	—	—	4,072	6,100
State and municipal	11,081	41,168	32,605	4,119	88,973	77,754
Corporate	1,301	5,740	—	—	7,041	8,387
Foreign debt securities	998	3,402	—	—	4,400	995
Asset-backed securities	178	—	—	—	178	270
Total debt securities	33,878	89,204	36,515	4,119	163,716	150,713
Mortgage-backed securities	82	7,584	123	—	7,789	6,970
Equity securities (2)	—	—	1,001	1,882	2,883	2,453
Total	$33,960	$96,788	$37,639	$6,001	$174,388	$160,136

	Weighted average yields:				
	Less than 1 Year	1 Year - 5 Years	5 Years - 10 Years	More than 10 Years	Total
U.S. Government and federal agency	1.72%	1.48%	1.68%	— %	1.57%
U.S. Treasury notes and bonds	—	1.54	—	—	1.54
State and municipal (1)	3.41	3.22	3.57	2.56	3.34
Corporate	1.37	1.94	—	—	1.84
Foreign debt securities	1.10	1.44	—	—	1.37
Asset-backed securities	1.25	—	—	—	1.25
Mortgage-backed securities	2.84	1.83	2.72	—	1.86
Equity securities (2)	—	—	4.62	1.06	2.30

(1) The yield is computed for tax-exempt securities on a fully tax-equivalent basis at an incremental tax rate of 34%.

(2) Equity securities are preferred and common stock that may or may not have a stated maturity.

Loan Portfolio

The Bank's loan portfolio categorized by loan type (excluding loans held for sale) as of December 31, 2016 is presented below:

(Dollars in thousands)

	2016	2015	2014	2013	2012
Agricultural	$44,614	$40,232	$41,098	$37,048	$31,790
Commercial and industrial	96,088	94,347	88,062	68,530	67,365
Consumer	21,596	20,090	20,752	19,931	19,367
Real estate - commercial	110,762	97,736	99,807	96,987	93,312
Real estate - construction	6,153	5,390	2,691	890	1,056
Real estate - residential	89,787	91,509	93,703	92,580	98,578
Total loans, gross	$369,000	$349,304	$346,113	$315,966	$311,468

Maturities and Sensitivities of Loans to Changes in Interest Rates

The following schedule presents the maturities of loans (excluding residential real estate and consumer loans) as of December 31, 2016. All loans over one year in maturity (excluding residential real estate and consumer loans) are also presented classified according to the sensitivity to changes in interest rates as of December 31, 2016.

(Dollars in thousands)	Less than 1 Year	1 Year - 5 Years	More than 5 Years	Total
Loan Type				
Agricultural	$671	$29,012	$14,931	$44,614
Commercial and industrial	131	81,569	14,388	96,088
Real estate - commercial	597	58,859	51,306	110,762
Real estate - construction	—	6,153	—	6,153
Totals	$1,399	$175,593	$80,625	$257,617

(Dollars in thousands)

Loan Sensitivity to Changes in Interest Rates	Less than 1 Year	1 Year - 5 Years	More than 5 Years	Total
Loans with fixed interest rates	$380	$115,937	$61,565	$177,882
Loans with floating or adjustable interest rates	1,019	59,656	19,060	79,735
Totals	$1,399	$175,593	$80,625	$257,617

Loan maturities are classified according to the contractual maturity date or the anticipated amortization period, whichever is appropriate. The anticipated amortization period is used in the case of loans where a balloon payment is due before the end of the loan’s normal amortization period. At the time the balloon payment is due, the loan can either be rewritten or payment in full can be requested. The decision regarding whether the loan will be rewritten or a payment in full will be requested will be based upon the loan’s payment history, the borrower’s current financial condition, and other relevant factors.

Risk Elements

The following loans were classified as nonperforming as of December 31:

(Dollars in thousands)

	2016	2015	2014	2013	2012
Loans accounted for on a nonaccrual basis	$1,983	$2,198	$3,361	$3,123	$2,331
Accruing loans which are contractually past due 90 days or more as to principal or interest payments	229	29	58	11	30
Loans defined as "troubled debt restructurings"	2,853	3,271	3,175	4,523	4,405
Totals	$5,065	$5,498	$6,594	$7,657	$6,766

A loan is placed on nonaccrual status at the point in time at which the collectability of principal or interest is considered doubtful.

The table below illustrates interest forgone and interest recorded on nonperforming loans for the years presented:

(Dollars in thousands)

	2016	2015	2014	2013	2012
Interest on non-performing loans which would have been earned had the loans been in an accrual or performing status	$107	$150	$204	$251	$183
Interest on non-performing loans that was actually recorded when received	$—	$—	$—	$—	$—

Potential Problem Loans

At December 31, 2016, there were $5.4 million of loans not disclosed above where some concern existed as to the borrowers' abilities to comply with original loan terms. Specific loss allocations totaling $403,000 from the allowance for loan losses had been allocated for all nonperforming and potential problem loans as of December 31, 2016. However, the entire allowance for loan losses is also available for these potential problem loans.

Loan Concentrations

As of December 31, 2016, there was no concentration of loans exceeding 10% of total loans that is not otherwise disclosed as a category of loans pursuant to Item III.A. of Industry Guide 3.

Other Interest-Bearing Assets

As of December 31, 2016, there were no other interest-bearing assets requiring disclosure under Item III.C.1. or 2. of Industry Guide 3 if such assets were loans.

Summary of Loan Loss Experience

The following schedule presents a summary of activity in the allowance for loan losses for the periods shown and the percentage of net charge-offs during each period to average gross loans outstanding during the period:

(Dollars in thousands)	2016	2015	2014	2013	2012
Allowance for loan losses at beginning of year	$4,194	$4,173	$4,735	$5,852	$5,213
Charge-offs:					
Agricultural	—	—	—	88	—
Commercial and industrial	37	30	1	122	405
Real estate - commercial	—	—	665	858	869
Real estate - construction	—	—	—	—	—
Real estate - residential	102	140	133	732	887
Consumer	218	291	273	351	338
Total	357	461	1,072	2,151	2,499
Recoveries:					
Agricultural	—	1	20	6	5
Commercial and industrial	31	64	119	337	61
Real estate - commercial	89	47	48	84	224
Real estate - construction	—	—	—	—	—
Real estate - residential	171	149	44	132	119
Consumer	149	121	179	175	214
Total	440	382	410	734	623
Net charge-offs (recoveries)	(83)	79	662	1,417	1,876
Provision for loan losses	—	100	100	300	2,515
Allowance for loan losses at end of year	$4,277	$4,194	$4,173	$4,735	$5,852
Allowance for loan losses as a percentage of:					
Total loans as of year end	1.16 %	1.20 %	1.21 %	1.50 %	1.88 %
Nonaccrual loans, accrual loans past due 90 days or more and troubled debt restructurings	84 %	76 %	63 %	62 %	86 %
Ratio of net charge-offs (recoveries) to average total loans outstanding during the year	(0.02)%	0.02 %	0.20 %	0.45 %	0.61 %
Loan recoveries as a percentage of prior year’s charge-offs	95 %	36 %	19 %	29 %	17 %

(1) Additions to the allowance for loan losses charged to operations during the periods shown were based on management’s judgment after considering factors such as loan loss experience, evaluation of the loan portfolio, and prevailing and anticipated economic conditions. The evaluation of the loan portfolio is based upon various risk factors such as the financial condition of the borrower, the value of collateral and other considerations, which, in the opinion of management, deserve current recognition in estimating loan losses.

The following schedule presents an allocation of the allowance for loan losses to the various loan categories as of the years ended December 31:

(Dollars in thousands)	2016	2015	2014	2013	2012
Agricultural	$433	$420	$186	$178	$140
Commercial and industrial	688	586	527	562	381
Consumer	305	297	184	192	250
Real estate - commercial	1,438	1,030	1,641	1,842	2,596
Real estate - construction	62	46	9	12	15
Real estate - residential	1,013	1,388	1,193	1,626	1,923
Unallocated	338	427	433	323	547
Total allowance	$4,277	$4,194	$4,173	$4,735	$5,852

The increase in the allowance allocation to commercial real estate loans was due to an increase in the concentration within this loan category. Fluctuations in allowance allocations in the other loan categories were primarily due to changes in historical charge-off levels and environmental factors affecting them.

Management periodically reviews the assumptions, loss ratios and delinquency trends in estimating the appropriate level of its allowance for loan losses and believes the unallocated portion of the total allowance was sufficient at December 31, 2016.

The following schedule presents the stratification of the loan portfolio by category, based on the amount of loans outstanding as a percentage of total loans for the respective years ended December 31:

	2016	2015	2014	2013	2012
Agricultural	12 %	12 %	12 %	12 %	10 %
Commercial and industrial	26	26	25	22	22
Consumer	6	6	6	6	6
Real estate - commercial	30	28	29	31	30
Real estate - construction	2	2	1	—	—
Real estate - residential	24	26	27	29	32
Total allowance	100 %	100 %	100 %	100 %	100 %

Deposits

The following schedule presents the average deposit balances by category and the average rates paid thereon for the respective years:

(Dollars in thousands)

	2016		2015		2014	
Noninterest-bearing demand	$123,848	— %	$115,488	— %	$109,556	— %
Interest-bearing demand and money market deposits	196,662	0.13	165,767	0.14	137,924	0.16
Savings	73,118	0.03	67,826	0.04	67,869	0.06
Certificates of deposit	86,042	0.60	94,891	0.66	107,388	0.73
Total	$479,670	0.16%	$443,972	0.20%	$422,737	0.25%

The following table illustrates the maturities of certificates of deposits issued in denominations of $100,000 or more as of December 31, 2016:

(Dollars in thousands)

Maturing in less than 3 months	$5,703
Maturing in 3 to 6 months	17,898
Maturing in 6 to 12 months	10,714
Maturing in more than 12 months	15,780
Total	$50,095

At December 31, 2016, the Bank had no material foreign deposits.

Short-Term Borrowings

Federal funds purchased by the Company are unsecured overnight borrowings from correspondent banks. Federal funds purchased are due the next business day. The table below provides additional information regarding these short-term borrowings:

(Dollars in thousands)

	2016	2015	2014
Outstanding balance at December 31	$—	$—	$—
Average interest rate at December 31	— %	— %	— %
Average balance during the year	$610	$—	$401
Average interest rate during the year	0.70 %	— %	0.36 %
Maximum month end balance during the year	$4,100	$1,857	$2,149

Repurchase agreements include advances by Bank customers that are not covered by federal deposit insurance. These agreements are direct obligations of the Company and are secured by securities held in safekeeping at a correspondent bank. The table below provides additional information regarding these short-term borrowings:

(Dollars in thousands)

	2016	2015	2014
Outstanding balance at December 31	$7,913	$9,460	$26,743
Average interest rate at December 31	0.05 %	0.04 %	0.19 %
Average balance during the year	$7,762	$17,825	$22,594
Average interest rate during the year	0.05 %	0.17 %	0.20 %
Maximum month end balance during the year	$10,539	$26,743	$28,719

Advances from the Federal Home Loan Bank ("FHLB") with original repayment terms less than one year are considered short-term borrowings for the Company. These advances are secured by residential real estate mortgage loans and U.S. government agency securities. The advances have maturities ranging from 1 month to 12 months from the date of issue.

The table below provides additional information regarding these short-term borrowings:

(Dollars in thousands)

	2016	2015	2014
Outstanding balance at December 31	$12,000	$—	$—
Average interest rate at December 31	0.86 %	0.57 %	0.41 %
Average balance during the year	$25,732	$11,332	$14,556
Average interest rate during the year	0.61 %	0.73 %	0.43 %
Maximum month end balance during the year	$45,000	$31,873	$25,868

There were no other categories of short-term borrowings whose average balance outstanding exceeded 30% of shareholders' equity in 2016, 2015 or 2014.

Return on Equity and Assets

The following schedule presents certain financial ratios of the Company for the years ended December 31:

	2016	2015	2014
Return on assets (net income divided by average total assets)	1.04 %	1.04 %	1.08 %
Return on equity (net income dividend by average equity)	8.44 %	8.39 %	8.88 %
Dividend payout ratio (dividends declared per share divided by net income per share)	36.63 %	37.79 %	34.15 %
Equity to assets ratio (average equity divided by average total assets)	12.30 %	12.40 %	12.18 %

Item 1A. Risk Factors

The Company is subject to many risks and uncertainties. Although the Company seeks ways to manage these risks and develop programs to control risks to the extent that management can control them, the Company cannot predict the future. Actual results may differ materially from management's expectations. Some of these significant risks and uncertainties are discussed below. The risks and uncertainties described below are not the only ones that the Company faces. Additional risks and uncertainties of which the Company is unaware, or that it currently does not consider to be material, also may become important factors that affect the Company and its business. If any of these risks were to occur, the Company's business, financial condition or results of operations could be materially and adversely affected.

Investments in the Company's common stock involve risk.

The market price of the Company's common stock may fluctuate significantly in response to a number of factors, including:

- Variations in quarterly or annual operating results
- Changes in dividends per share
- Changes in interest rates
- New developments, laws or regulations in the banking industry
- Acquisitions or business combinations involving the Company or its competition
- Regulatory actions, including changes to regulatory capital levels, the components of regulatory capital and how regulatory capital is calculated
- Volatility of stock market prices and volumes
- Changes in market valuations of similar companies
- New litigation or contingencies or changes in existing litigation or contingencies
- Changes in accounting policies or procedures as may be required by the Financial Accounting Standards Board or other regulatory agencies
- Rumors or erroneous information
- Credit and capital availability
- Issuance of additional shares of common stock or other debt or equity securities of the Company

Asset quality could be less favorable than expected.

A significant source of risk for the Company arises from the possibility that losses will be sustained because borrowers, guarantors and related parties may fail to perform in accordance with the terms of their loan agreements. Most loans originated by the Company are secured, but some loans are unsecured depending on the nature of the loan.

With respect to secured loans, the collateral securing the repayment of these loans includes a wide variety of real and personal property that may be insufficient to cover the obligations owed under such loans. Collateral values may be adversely affected by changes in prevailing economic, environmental and other conditions, including declines in the value of real estate, changes in interest rates, changes in monetary and fiscal policies of the federal government, terrorist activity, environmental contamination and other external events.

The Company's allowance for loan losses may not be adequate to cover actual loan losses.

The risk of nonpayment of loans is inherent in all lending activities and nonpayment of loans may have a material adverse effect on the Company's earnings and overall financial condition, and the value of its common stock. The Company makes various assumptions and judgments about the collectability of its loan portfolio and provides an allowance for potential losses based on a number of factors. If its assumptions are wrong, the allowance for loan losses may not be sufficient to cover losses, which could have an adverse effect on the Company's operating results, and may cause it to increase the allowance in the future. The actual amount of future provisions for loan losses cannot now be determined and may exceed the amounts of past provisions for loan losses. Federal and state banking regulators, as an integral part of their supervisory function, periodically review the allowance for loan losses. These regulatory agencies may require the Company to increase its provision for loan losses or to recognize further loan charge-offs based upon their judgments, which may be different from the Company's judgments. Any increase in the allowance for loan losses could have a negative effect on the Company's regulatory capital ratios, net income, financial condition and results of operations.

General economic conditions in the state of Michigan could be less favorable than expected.

The Company is affected by general economic conditions in the United States, although most directly within Michigan. An economic downturn within Michigan could negatively impact household and corporate incomes. This impact may lead to decreased demand for both loan and deposit products and increase the number of customers who fail to pay interest or principal on their loans.

The Company could be adversely affected by the soundness of other financial institutions, including defaults by larger financial institutions.

The Company's ability to engage in routine funding transactions could be adversely affected by the actions and commercial soundness of other financial institutions. Financial services institutions are interrelated as a result of credit, trading, clearing, counterparty or other relationships between financial institutions. The Company has exposure to multiple counterparties, and it routinely executes transactions with counterparties in the financial industry. As a result, defaults by, or even rumors or questions about, one or more financial services institutions, or the financial services industry generally, could lead to market-wide liquidity problems and losses or defaults by the Company or by other institutions. This is sometimes referred to as "systemic risk" and may adversely affect financial intermediaries, such as clearing agencies, clearing houses, banks, securities firms and exchanges, with which the Company interacts on a daily basis, and therefore could adversely affect the Company.

If the Company does not adjust to changes in the financial services industry, its financial performance may suffer.

The Company's ability to maintain its financial performance and return on investment to shareholders will depend in part on its ability to maintain and grow its core deposit customer base and expand its financial services to its existing customers. In addition to other banks, competitors include credit unions, securities dealers, brokers, mortgage bankers, investment advisors and finance and insurance companies. The increasingly competitive environment is, in part, a result of changes in the economic environment within the state of Michigan, regulation, changes in technology and product delivery systems and the accelerating pace of consolidation among financial service providers. New competitors may emerge to increase the degree of competition for the Company's customers and services. Financial services and products are also constantly changing. The Company's financial performance will also depend in part upon customer demand for the Company's products and services and the Company's ability to develop and offer competitive financial products and services.

Changes in interest rates could reduce the Company's income and cash flow.

The Company's income and cash flow depends, to a great extent, on the difference between the interest earned on loans and securities, and the interest paid on deposits and other borrowings. Market interest rates are beyond the Company's control, and they fluctuate in response to general economic conditions and the policies of various governmental and regulatory agencies including, in particular, the Federal Reserve Board. Changes in monetary policy, including changes in interest rates and interest rate relationships, will influence the origination of loans, the purchase of investments, the generation of deposits and the rate received on loans and securities and paid on deposits and other borrowings.

The Company is subject to liquidity risk in its operations, which could adversely affect its ability to fund various obligations.

Liquidity risk is the possibility of being unable to meet obligations as they come due or capitalize on growth opportunities as they arise because of an inability to liquidate assets or obtain adequate funding on a timely basis, at a reasonable cost and within acceptable risk tolerances. Liquidity is required to fund various obligations, including credit obligations to borrowers, loan originations, withdrawals by depositors, repayment of debt, dividends to shareholders, operating expenses and capital expenditures. Liquidity is derived primarily from retail deposit growth and earnings retention, principal and interest payments on loans and investment securities, net cash provided from operations and access to other funding. If the Company is unable to maintain adequate liquidity, then its business, financial condition and results of operations would be negatively affected.

Legislative or regulatory changes or actions could adversely impact the Company or the businesses in which it is engaged.

The financial services industry is extensively regulated. The Company and the Bank are subject to extensive state and federal regulation, supervision and legislation that govern almost all aspects of their operations. Laws and regulations may change from time to time and are primarily intended for the protection of consumers, depositors and the deposit insurance fund, and not to benefit the Company's shareholders. The impact of any changes to laws and regulations or other actions by regulatory agencies may negatively impact the Company or its ability to increase the value of its business. Regulatory authorities have extensive discretion in connection with their supervisory and enforcement activities, including the imposition of restrictions on the operation of an institution, the classification of assets by the institution and the adequacy of an institution's allowance for loan losses. Future regulatory changes or accounting pronouncements may increase the Company's regulatory capital requirements or adversely affect its regulatory capital levels. Additionally, actions by regulatory agencies against the Company or the Bank could require the Company to devote significant time and resources to defending its business and may lead to penalties that materially affect the Company.

The Company relies heavily on its management and other key personnel, and the loss of any of them may adversely affect its operations.

The Company is and will continue to be dependent upon the services of its management team and other key personnel. Losing the services of one or more key members of the Company's management team could adversely affect its operations.

The Company may be a defendant in a variety of litigation and other actions, which may have a material adverse effect on the Company's financial condition and results of operations.

The Company and the Bank are regularly involved in a variety of litigation arising out of the normal course of business. The Company's insurance may not cover all claims that may be asserted against it, and any claims asserted against it, regardless of merit or eventual outcome, may harm its reputation or cause the Company to incur unexpected expenses, which could be material in amount. Should the ultimate expenses, judgments or settlements in any litigation exceed the Company's insurance coverage, they could have a material adverse effect on the Company's financial condition and results of operations. In addition, the Company may not be able to obtain appropriate types or levels of insurance in the future, nor may it be able to obtain adequate replacement policies with acceptable terms, if at all.

If the Company cannot raise additional capital when needed, its ability to further expand its operations through organic growth or acquisitions could be materially impaired.

The Company is required by federal and state regulatory authorities to maintain specified levels of capital to support its operations. The Company may need to raise additional capital to support its current level of assets or its growth. The Company's ability to raise additional capital will depend on conditions in the capital markets at that time, which are outside its control, and on its financial performance. The Company cannot assure that it will be able to raise additional capital in the future on terms acceptable to it or at all. If the Company cannot raise additional capital when needed, its ability to maintain its current level of assets or to expand its operations through organic growth or acquisitions could be materially limited.

Unauthorized disclosure of sensitive or confidential client or customer information, whether through a breach of computer systems or otherwise, could severely harm the Company's business.

As part of its business, the Company collects, processes and retains sensitive and confidential client and customer information on behalf of itself and other third parties. Despite the security measures the Company has in place for its facilities and systems, and the security measures of its third party service providers, the Company may be vulnerable to security breaches, acts of vandalism, computer viruses, misplaced or lost data, programming and/or human errors or other similar events. Any security breach involving the misappropriation, loss or other unauthorized disclosure of confidential customer information, whether by the Company or by its vendors, could severely damage the Company's reputation, expose it to the risks of litigation and liability, disrupt the Company's operations and have a material adverse effect on the Company's business.

The Company's information systems may experience an interruption or breach in security.

The Company relies heavily on communications and information systems to conduct its business and deliver its products. Any failure, interruption or breach in security of these systems could result in failures or disruptions in the Company's customer relationship management, general ledger, deposit, loan and other systems. While the Company has policies and procedures designed to prevent or limit the effect of the failure, interruption or security breach of its information systems, there can be no assurance that any such failures, interruptions or security breaches of the Company's information systems or its customers' information or computer systems would not damage the Company's reputation, result in a loss of customer business, subject the Company to additional regulatory scrutiny, or expose the Company to civil litigation and financial liability, any of which could have a material adverse effect on the Company's financial condition and results of operations.

Environmental liability associated with commercial lending could result in losses.

In the course of its business, the Company may acquire, through foreclosure, properties securing loans it has originated or purchased that are in default. Particularly in commercial real estate lending, there is a risk that hazardous substances could be discovered on these properties. In this event, the Company might be required to remove these substances from the affected properties at the Company's sole cost and expense. The cost of this removal could substantially exceed the value of affected properties. The Company may not have adequate remedies against the prior owner or other responsible parties and could find it difficult or impossible to sell the affected properties. These events could have an adverse effect on the Company's business, results of operations and financial condition.

The Company depends upon the accuracy and completeness of information about customers.

In deciding whether to extend credit to customers, the Company relies on information provided to it by its customers, including financial statements and other financial information. The Company may also rely on representations of customers as to the accuracy and completeness of that information and on reports of independent auditors on financial statements. The Company's financial condition and results of operations could be negatively impacted to the extent that the Company extends credit in reliance on financial statements that do not comply with generally accepted accounting principles or that are misleading or other information provided by customers that is false or misleading.

The Company operates in a highly competitive industry and market area.

The Company faces substantial competition in all areas of its operations from a variety of different competitors, many of which are larger and may have more financial resources. Such competitors primarily include national and regional banks within the various markets where the Company operates, as well as internet banks. The Company also faces competition from many other types of financial institutions, including savings and loan associations, credit unions, finance companies, brokerage firms, insurance companies and other financial intermediaries. The financial services industry could become even more competitive as a result of legislative, regulatory and technological changes and continued consolidation. Banks, securities firms and insurance companies can merge under the umbrella of a financial holding company, which can offer virtually any type of financial service, including banking, securities underwriting, insurance (both agency and underwriting) and merchant banking. The Company competes with these institutions both in attracting deposits and in making new loans. Technology has lowered barriers to entry into the market and made it possible for non-banks to offer products and services traditionally provided by banks, such as automatic transfer and automatic payment systems. Many of the Company's competitors have fewer regulatory constraints and may have lower cost structures, such as credit unions that are not subject to federal income tax. Due to their size, many competitors may be able to achieve economies of scale and, as a result, may offer a broader range of products and services as well as better pricing for those products and services than the Company can.

Severe weather, natural disasters, acts of war or terrorism and other external events could significantly impact the Company's business.

Severe weather, natural disasters, acts of war or terrorism and other adverse external events could have a significant impact on the Company's ability to conduct business. Such events could affect the stability of the Company's deposit base, impair the ability of borrowers to repay outstanding loans, impair the value of collateral securing loans, cause significant property damage, result in loss of revenue and/or cause the Company to incur additional expenses.

The Company relies on dividends from the Bank for most of its revenue.

The Company is a separate and distinct legal entity from the Bank. It receives substantially all of its revenue from dividends from the Bank. These dividends are the principal source of funds to pay cash dividends on the Company's common stock. Various federal and/or state laws and regulations limit the amount of dividends that the Bank may pay to the Company. If the Bank is unable to pay dividends to the Company, the Company may not be able to pay cash dividends on its common stock. The earnings of the Bank have been the principal source of funds to pay cash dividends to shareholders. Over the long-term, cash dividends to shareholders are dependent upon earnings, as well as capital requirements, regulatory restraints and other factors affecting the Company and the Bank.

Additional risks and uncertainties could have a negative effect on financial performance.

Additional factors could have a negative effect on the financial performance of the Company and the Company's common stock. Some of these factors are financial market conditions, changes in financial accounting and reporting standards, new litigation or changes in existing litigation, regulatory actions and losses.

Item 1B. Unresolved Staff Comments

None.

Item 2. Properties

The offices of the Company as of February 28, 2017, were as follows:

Company’s main office:

109 East Division, Sparta, Michigan

Office is owned by the Bank and comprises 24,000 square feet.

Bank’s branch office:

416 West Division, Sparta, Michigan

Office is leased by the Bank and comprises 3,000 square feet.

Bank’s branch office:

4170 - 17 Mile Road, Cedar Springs, Michigan

Office is owned by the Bank and comprises 3,000 square feet.

Bank’s branch office:

6795 Courtland Drive, Rockford, Michigan

Office is owned by the Bank and comprises 2,400 square feet.

Bank’s branch office:

5050 Alpine Avenue NW, Comstock Park, Michigan

Office is owned by the Bank and comprises 2,400 square feet.

Bank's branch office:

450 West Muskegon, Kent City, Michigan

Office is owned by the Bank and comprises 27,300 square feet.

Bank's branch office:

3069 Slocum Road, Ravenna, Michigan

Office is owned by the Bank and comprises 4,800 square feet.

Bank's branch office:

5475 East Apple Avenue, Muskegon, Michigan

Office is owned by the Bank and comprises 4,800 square feet.

Bank's branch office:

661 West Randall, Coopersville, Michigan

Office is owned by the Bank and comprises 2,700 square feet.

Bank's branch office:

10 West Main Street, Grant, Michigan

Office is owned by the Bank and comprises 4,800 square feet.

Bank's branch office:

246 West River Valley Drive, Newaygo, Michigan

Office is owned by the Bank and comprises 2,600 square feet.

Bank's branch office:

1423 West Main Street, Fremont, Michigan

Office is owned by the Bank and comprises 1,600 square feet.

Bank's loan production office:

237 Fulton West, Grand Rapids, Michigan

Office is leased by the Bank and comprises 1,800 square feet.

The Company believes that the offices are suitable and adequate for future needs and are in good condition. The Company's management believes all offices are adequately covered by property insurance.

Item 3. Legal Proceedings
As of December 31, 2016, there are no significant pending legal proceedings to which the Company or the Bank is a party or to which any of their properties are subject, except for legal proceedings arising in the ordinary course of business. In the opinion of management, pending legal proceedings will not have a material adverse effect on the consolidated financial condition of the Company.

Item 4. Mine Safety Disclosures
Not applicable.

PART II

Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

Stock Information

Several brokers trade ChoiceOne's common shares in the OTC Pink marketplace. There is no well-established public trading market for the shares and trading activity is infrequent. ChoiceOne's trading volume and recent share price information can be viewed under the symbol '**COFS**' on certain financial websites.

The range of high and low bid prices for shares of common stock for each quarterly period during the past two years is as follows:

	2016		2015	
	Low	High	Low	High
First Quarter	$22.33	$23.80	$22.30	$24.25
Second Quarter	22.10	23.85	22.30	23.75
Third Quarter	22.02	23.74	22.25	23.79
Fourth Quarter	21.60	24.00	22.46	24.50

The prices listed above are over-the-counter market quotations reported to ChoiceOne by its market makers. The over-the-counter market quotations reflect inter-dealer prices without retail markup, markdown or commission and may not necessarily represent actual transactions. As of February 28, 2017, the average bid price for shares of

ChoiceOne common stock was $23.05.

As of February 28, 2017, there were 694 shareholders of record of ChoiceOne common stock.

The following table summarizes the quarterly cash dividends declared per share of common stock during 2016 and 2015:

	2016	2015
First Quarter	$0.17	$0.15
Second Quarter	0.17	0.17
Third Quarter	0.17	0.17
Fourth Quarter	0.17	0.17
Total	$0.68	$0.66

ChoiceOne’s principal source of funds to pay cash dividends is the earnings and dividends paid by the Bank. The Bank is restricted in its ability to pay cash dividends under current banking regulations. See Note 20 to the consolidated financial statements for a description of these restrictions. Based on information presently available, management expects ChoiceOne to declare and pay regular quarterly cash dividends in 2017, although the amount of the quarterly dividends will be dependent on market conditions and ChoiceOne’s requirements for cash and capital, among other things.

On October 26, 2016, the Company issued 896 shares of common stock to its directors pursuant to the Directors’ Stock Purchase Plan for an aggregate cash price of $20,000. The Company relied on the exemption contained in Section 4(6) of the Securities Act of 1933 in connection with these sales.

ISSUER PURCHASES OF EQUITY SECURITIES

The Company’s did not purchase any of its own common stock during the quarter ended December 31, 2016. As of December 31, 2016, there were 29,224 shares remaining that may yet be purchased under approved plans or programs. The repurchase plan was adopted and announced on July 26, 2007. There is no stated expiration date. The plan authorized the repurchase of up to 100,000 shares.

The information under Item 12 of this report regarding equity compensation plans is incorporated herein by reference.

Item 6. Selected Financial Data

ChoiceOne Financial Services, Inc.
Selected Financial Data

(Dollars in thousands, except per share data)

	2016	2015	2014	2013	2012
For the year					
Net interest income	$19,343	$18,362	$17,863	$17,596	$17,675
Provision for loan losses	—	100	100	300	2,515
Noninterest income	7,881	7,702	6,802	6,245	6,889
Noninterest expense	18,972	18,276	16,794	16,664	16,444
Income before income taxes	8,252	7,688	7,771	6,877	5,605
Income tax expense	2,162	1,945	2,076	1,783	1,343
Net income	6,090	5,743	5,695	5,094	4,262
Cash dividends declared	2,231	2,170	1,945	1,780	1,648
Per share					
Basic earnings	$1.85	$1.75	$1.73	$1.55	$1.29
Diluted earnings	1.85	1.74	1.72	1.54	1.29
Cash dividends declared	0.68	0.66	0.59	0.54	0.50
Shareholders’ equity (at year end)	21.76	21.19	20.08	18.68	18.35
Average for the year					
Securities	$173,119	$152,361	$142,361	$133,704	$129,337
Gross loans	357,880	342,382	330,355	312,798	307,639
Deposits	479,670	443,972	422,737	410,462	408,895
Federal Home Loan Bank advances	26,049	19,989	14,555	7,415	6,130
Shareholders’ equity	72,134	68,439	64,143	61,317	59,431
Assets	586,299	551,762	526,669	502,333	500,636
At year end					
Securities	$177,955	$163,323	$145,706	$139,832	$138,242
Gross loans	369,000	349,304	346,113	315,966	311,468
Deposits	512,386	474,696	434,828	418,127	424,199
Federal Home Loan Bank advances	12,301	11,332	18,363	6,392	420
Shareholders’ equity	71,698	69,842	66,190	61,558	60,506
Assets	607,371	567,746	549,640	514,575	508,913
Selected financial ratios					
Return on average assets	1.04 %	1.04 %	1.08 %	1.01 %	0.85 %
Return on average shareholders’ equity	8.44	8.39	8.88	8.31	7.17
Cash dividend payout as a percentage of net income	36.63	37.79	34.15	34.93	38.67
Shareholders’ equity to assets (at year end)	11.80	12.30	12.04	11.96	11.89

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion is designed to provide a review of the consolidated financial condition and results of operations of ChoiceOne, and its wholly-owned subsidiaries. This discussion should be read in conjunction with the consolidated financial statements and related footnotes.

RESULTS OF OPERATIONS

Summary

Net income for 2016 was $6,090,000, which represented a $347,000 or 6% increase from 2015. The growth in net income resulted primarily from an increase in interest income in 2016 compared to 2015, which was partially offset by higher noninterest expense. The effect of $34.6 million of growth in average earning assets in 2016 compared to 2015 was partially offset by an 8 basis point decrease in the rate earned on average assets. Net loan charge-offs continued to be low in 2016, which allowed for no provision expense for loan losses in 2016 compared to $100,000 in 2015. ChoiceOne had $83,000 in net loan recoveries in 2016, compared to net loan charge-offs of $79,000 in 2015. Growth in noninterest income of $179,000 in 2016 compared to 2015 was mainly caused by higher gains on sales of loans. The increase of $696,000 in noninterest expense in 2016 compared to the prior year was primarily due to higher salaries and benefits.

Net income for 2015 was $5,743,000, which represented a $48,000 or 1% increase from 2014. The growth in net income resulted primarily from lower interest expense and an increase in noninterest income in 2015 compared to 2014. Net charge-offs continued to be low in 2015, which allowed for a level provision for loan losses expense in 2015 compared to 2014. Net interest income increased $499,000 in 2015 compared to the prior year as a result of a $34,593,000 increase in average earning assets, partially offset by a 16 basis point decrease in the rate earned on earning assets, and a 6 basis point reduction in the rate paid on interest-bearing liabilities. Growth in noninterest income of $900,000 in 2015 compared to 2014 was mainly caused by higher gains on sales of loans and a death benefit received from a life insurance policy. The increase in noninterest expense was due to higher salaries and benefits and data processing partially offset by lower FDIC insurance expense and loan and collection expense in 2015 compared to the prior year.

Dividends

Cash dividends of $2,231,000 or $0.68 per common share were declared in 2016, compared to $2,170,000 or $0.66 per common share in 2015 and $1,945,000 or $0.59 per common share in 2014. Dividends declared in 2016 were $0.17 per share for all four quarters. Dividends declared in 2015 were $0.15 per share for the first quarter and $0.17 per share for the last three quarters. Dividends declared in 2014 were $0.14 per share for the first quarter and $0.15 per share for the last three quarters. The dividend yield on ChoiceOne's common stock was 2.86% in 2016, compared to 2.77% in 2015 and 2.57% in 2014. The cash dividend payout as a percentage of net income was 37% in 2016, compared to 38% in 2015 and 34% in 2014.

Table 1 – Average Balances and Tax-Equivalent Interest Rates

	Year ended December 31,								
	2016			2015			2014		
(Dollars in thousands)	Average Balance	Interest	Rate	Average Balance	Interest	Rate	Average Balance	Interest	Rate
Assets:									
Loans (1) (2)	$357,880	$16,518	4.62%	$342,382	$15,982	4.67%	$330,355	$15,775	4.78%
Taxable securities (3)	118,787	2,171	1.83	102,550	1,783	1.74	97,435	1,847	1.90
Nontaxable securities (1)	54,332	2,190	4.03	49,952	2,156	4.32	44,926	2,102	4.68
Other	4,231	21	0.49	5,753	14	0.25	4,165	9	0.22
Interest-earning assets	535,230	20,900	3.91	500,637	19,935	3.98	476,881	19,733	4.14
Noninterest-earning assets (4)	51,069			51,125			49,788		
Total assets	$586,299			$551,762			$526,669		
Liabilities and Shareholders' Equity:									
Interest-bearing demand deposits	$196,662	$253	0.13%	$165,767	$226	0.14%	$137,924	$220	0.16%
Savings deposits	73,118	20	0.03	67,826	26	0.04	67,869	41	0.06
Certificates of deposit	86,042	517	0.60	94,891	625	0.66	107,388	780	0.73
Advances from Federal Home Loan Bank	26,049	171	0.66	19,989	83	0.41	14,555	63	0.43
Other	8,372	8	0.10	18,156	30	0.17	22,995	47	0.20
Interest-bearing liabilities	390,243	969	0.25	366,629	990	0.27	350,731	1,151	0.33
Demand deposits	123,848			115,488			109,556		
Other noninterest-bearing liabilities	74			1,206			2,239		
Total liabilities	514,165			483,323			462,526		
Shareholders' equity	72,134			68,439			64,143		
Total liabilities and shareholders' equity	$586,299			$551,762			$526,669		
Net interest income (tax-equivalent basis)-interest spread		19,931	3.66%		18,944	3.71%		18,582	3.81%
Tax-equivalent adjustment (1)		(591)			(582)			(719)	
Net interest income		$19,340			$18,362			$17,863	
Net interest income as a percentage of earning assets (tax-equivalent basis)			3.72%			3.78%			3.90%

(1) Interest on nontaxable securities and loans has been adjusted to a fully tax-equivalent basis to facilitate comparison to the taxable interest-earning assets. The adjustment uses an incremental tax rate of 34% for the years presented.

(2) Interest on loans included net origination fees charged on loans of approximately $1,054,000, $957,000, and $873,000 in 2016, 2015, and 2014, respectively.

(3) Interest on taxable securities includes dividends on Federal Home Loan Bank and Federal Reserve Bank stock.

(4) Noninterest-earning assets include loans on a nonaccrual status, which averaged approximately $2,416,000, $2,145,000, and $3,613,000 in 2016, 2015, and 2014, respectively.

Table 2 – Changes in Tax-Equivalent Net Interest Income

	Year ended December 31,					
(Dollars in thousands)	2016 Over 2015			2015 Over 2014		
	Total	Volume	Rate	Total	Volume	Rate
Increase (decrease) in interest income (1)						
Loans (2)	$536	$717	$(181)	$207	$ 566	$(360)
Taxable securities	388	293	95	(64)	94	(158)
Nontaxable securities (2)	34	182	(148)	54	224	(171)
Other	8	(4)	12	4	4	2
Net change in interest income	966	1,188	(222)	201	888	(687)
Increase (decrease) in interest expense (1)						
Interest-bearing demand deposits	27	40	(13)	6	40	(34)
Savings deposits	(6)	2	(8)	(15)	—	(15)
Certificates of deposit	(108)	(56)	(52)	(155)	(86)	(69)
Advances from Federal Home Loan Bank	88	30	58	20	23	(3)
Other	(22)	(12)	(10)	(17)	(9)	(8)
Net change in interest expense	(21)	4	(25)	(161)	(32)	(129)
Net change in tax-equivalent net interest income	$987	$1,184	$(197)	$362	$ 920	$(558)

(1) The volume variance is computed as the change in volume (average balance) multiplied by the previous year's interest rate. The rate variance is computed as the change in interest rate multiplied by the previous year's volume (average balance). The change in interest due to both volume and rate has been allocated to the volume and rate changes in proportion to the relationship of the absolute dollar amounts of the change in each.

(2) Interest on tax-exempt securities and loans has been adjusted to a fully tax-equivalent basis using an incremental tax rate of 34% for the years presented.

Net Interest Income

Tax-equivalent net interest income increased $987,000 in 2016 compared to 2015. The increase was attributed to an increase of $34.6 million in interest-earning assets and a decrease of 2 basis points on interest-bearing liabilities, which were partially offset by an 8 basis point decline in the average rate on interest-earning assets. ChoiceOne's net interest spread declined 5 basis points in 2016 compared to 2015 as general market rates had more of a downward effect on assets than liabilities.

The average balance of loans increased $15.5 million in 2016 compared to 2015. Most of the increase resulted from growth of $13.6 million in commercial and industrial and commercial real estate loans. Partially offsetting the loan growth was a 5 basis point decrease in the average rate earned on loans, which caused tax-equivalent interest income on loans to increase $536,000 in 2016 compared to the prior year. The average balance of total securities increased by $20.6 million in 2016 compared to 2015 as securities were purchased to provide earning assets growth. This growth in

the average balance was partially offset by a lower average rate earned on securities; however, interest income from securities still increased $422,000 in 2016 compared to the prior year.

The average balance of interest-bearing demand deposits increased $30.9 million in 2016 compared to 2015. The effect of this increase, partially offset by a 1 basis point decline in the average rate paid, caused interest expense to be $27,000 higher in 2016 than in the prior year. The effect of the $5.3 million increase in average savings deposits was more than offset by a 1 basis point decline in average rate paid which caused a $6,000 decrease in interest expense in 2016 compared to the prior year. The average balance of certificates of deposit was $8.8 million lower in 2016 than in the prior year. The average balance decrease plus the effect of a 6 basis point decline in the average rate paid caused interest expense on certificates of deposit to fall $108,000 in 2016 compared to 2015. A $6.1 million increase in the average balance of Federal Home Loan Bank advances and a 25 basis point increase in the average rate paid caused interest expense to increase $88,000 in 2016 compared to the prior year. The growth experienced in non-interest bearing demand deposits and savings deposits was primarily due to depositors choosing the liquidity afforded by this type of deposit as compared to certificates of deposit or nonbank investments.

ChoiceOne’s net interest income spread was 3.66% for 2016 and 3.71% for 2015. The continuation of low general market interest rates in both 2015 and 2016 caused the reduction in rates for both assets and liabilities in the two years.

Tax-equivalent net interest income increased $362,000 in 2015 compared to 2014. The increase was attributed to an increase of $23.8 million in interest-earning assets and a decrease of 6 basis points on interest-bearing liabilities, partially offset by a 16 basis point decline in the average rate on interest-earning assets. ChoiceOne’s net interest spread declined 10 basis points in 2015 compared to 2014 as growth of average interest-earning assets was offset by the compression of net interest margin.

The average balance of loans increased $12.0 million in 2015 compared to 2014. $8.6 million of growth came from loans to businesses in ChoiceOne’s markets as calling efforts were emphasized in 2015. Residential mortgage loans increased $3.5 million due to a higher level of loan originations in 2015. Partially offsetting the loan growth with an 11 basis point decrease in the average rate earned on loans, interest income on loans increased $207,000 in 2015 compared to the prior year. The average balance of total securities increased by $10.1 million in 2015 compared to 2014 as securities were purchased to provide earning assets growth. This growth in the average balance was partially offset by a lower average rate earned on securities, which caused interest income from securities to decrease $10,000 in 2015 compared to the prior year.

The average balance of interest-bearing demand deposits increased $27.8 million in 2015 compared to 2014. The effect of this increase, partially offset by a 2 basis point decline in the average rate paid, caused interest expense to be $6,000 higher in 2015 than in the prior year. A $43,000 of decline in average savings deposits along with a 2 basis point decline in average rate paid caused a $15,000 decrease in interest expense in 2015 compared to the prior year. The average balance of certificates of deposit was $12.5 million lower in 2015 than in the prior year. The average balance decrease plus the effect of a 7 basis point decline in the average rate paid caused interest expense on certificates of deposit to fall $155,000 in 2015 compared to 2014. A $5.4 million increase in the average balance of Federal Home Loan Bank advances, partially offset by a 2 basis point decrease in the average rate paid, caused interest expense to increase $20,000 in 2015 compared to the prior year. The growth experienced in non-interest bearing demand deposits and savings deposits was primarily due to depositors choosing the liquidity and safety afforded by this type of deposit as compared to certificates of deposit or nonbank investments.

Provision and Allowance For Loan Losses

Table 3 – Provision and Allowance For Loan Losses

(Dollars in thousands)

	2016	2015	2014	2013	2012
Allowance for loan losses at beginning of year	$4,194	$4,173	$4,735	$5,852	$5,213
Charge-offs:					
Agricultural	—	—	—	88	—
Commercial and industrial	37	30	1	122	405
Real estate - commercial	—	—	665	858	869
Real estate - construction	—	—	—	—	—
Real estate - residential	102	140	133	732	887
Consumer	218	291	273	351	338
Total	357	461	1,072	2,151	2,499
Recoveries:					
Agricultural	—	1	20	6	5
Commercial and industrial	31	64	119	337	61
Real estate - commercial	89	47	48	84	224
Real estate - construction	—	—	—	—	—
Real estate - residential	171	149	44	132	119
Consumer	149	121	179	175	214
Total	440	382	410	734	623
Net charge-offs (recoveries)	(83)	79	662	1,417	1,876
Provision for loan losses	—	100	100	300	2,515
Allowance for loan losses at end of year	$4,277	$4,194	$4,173	$4,735	$5,852
Allowance for loan losses as a percentage of:					
Total loans as of year end	1.16 %	1.20 %	1.21 %	1.50 %	1.88 %
Nonaccrual loans, accrual loans past due 90 days or more and troubled debt restructurings	84 %	76 %	63 %	62 %	86 %
Ratio of net charge-offs (recoveries) to average total loans outstanding during the year	(0.02)%	0.02 %	0.20 %	0.45 %	0.61 %
Loan recoveries as a percentage of prior year's charge-offs	95 %	36 %	19 %	29 %	17 %

The provision for loan losses was $0 in 2016 compared to $100,000 in 2015. All loan categories experienced net recoveries during 2016 except commercial and industrial loans and consumer loans, which had net charge-offs of $6,000 and $69,000, respectively. Management believes that the lower net charge-off levels are due in part to the improving economy in the Bank's market areas. The allowance for loan losses as a percentage of total loans decreased

from 1.20% as of the end of 2015 to 1.16% as of the end of 2016. The coverage ratio of the allowance for loan losses to nonperforming loans increased from 76% as of December 31, 2015 to 84% as of December 31, 2016. The allowance balance increased slightly while the balance of nonperforming loans decreased in 2016. ChoiceOne had $403,000 of specific allowance allocations for problem loans as of the end of 2016, compared to $506,000 as of the prior year end. Special allowance amounts have been allocated where the fair values of loans were considered to be less than their carrying values. ChoiceOne obtains valuations on collateral dependent loans when the loan is considered by management to be impaired and uses the valuation amounts in the determination of fair value. Management believes the specific reserves allocated to certain problem loans at the end of 2016 and 2015 were reasonable based on the circumstances surrounding each particular borrower.

The following schedule presents an allocation of the allowance for loan losses to the various loan categories as of the years ended December 31:

(Dollars in thousands)

	2016	2015	2014	2013	2012
Agricultural	$433	$420	$186	$178	$140
Commercial and industrial	688	586	527	562	381
Real estate - commercial	1,438	1,030	1,641	1,842	2,596
Real estate - construction	62	46	9	12	15
Real estate - residential	1,013	1,388	1,193	1,626	1,923
Consumer	305	297	184	192	250
Unallocated	338	427	433	323	547
Total allowance for loan losses	$4,277	$4,194	$4,173	$4,735	$5,852

The increase in the allowance allocation to commercial real estate loans was partially due to 13% growth in this loan category during 2016. The decrease in the allowance allocation to residential real estate loans was caused by lower historical charge-off levels in 2016 than in the prior year. Fluctuations in allowance allocations in the other loan categories were primarily due to changes in historical charge-off levels and environmental factors affecting them.

Management maintains the allowance at a level that it believes adequately provides for losses inherent in the loan portfolio. Such losses are estimated by a variety of factors, including specific examination of certain borrowing relationships and consideration of historical losses incurred on certain types of credits. Current economic conditions and collateral values affect loss estimates. Management focuses on early identification of problem credits through ongoing reviews by management and the independent loan review function. Based on the current state of the economy and a recent review of the loan portfolio, management believes that the allowance for loan losses as of December 31, 2016 was adequate. As charge-offs, changes in the level of nonperforming loans, and changes within the composition of the loan portfolio occur, the provision and allowance for loan losses will be reviewed by the Bank’s management and adjusted as necessary.

Noninterest Income

Total noninterest income increased $179,000 in 2016 compared to 2015. Customer service charges decreased $27,000 in 2016 compared to the prior year due to a slight decline in service charges on checking accounts. A decrease in insurance and investment commissions of $51,000 in 2016 compared to 2015 was caused by lower commission income from sales of REIT investments during 2016 compared to 2015. Gains on sales of loans increased $332,000 in 2016 compared to 2015 as longer-term mortgage rates declined causing a positive impact on mortgage volume. Net gains on sales of securities increased $51,000 as opportunities to harvest gains on the securities portfolio increased in the low interest rate environment that existed during most of 2016. Net losses on sales of other assets were $80,000 lower in 2016 than in the prior year as write-downs of values of other real estate properties and losses on sales of

properties were lower in 2016 than in 2015. Earnings on life insurance policies were $295,000 lower in 2016 than 2015 as the result of aa death benefit received on a former employee's life insurance policy in 2015.

Total noninterest income increased $900,000 in 2015 compared to 2014. Customer service charges increased $132,000 in 2015 compared to the prior year as a result of service charges on ChoiceOne's new checking accounts and growth in debit card fee income. An increase in insurance and investment commissions of $154,000 in 2015 compared to 2014 was due to overall higher volumes including brokerage fees for investment transactions for customers. Gains on sales of loans increased $393,000 in 2015 compared to 2014 as longer-term mortgage rates declined causing a positive impact on mortgage volume. Net gains on sales of securities decreased $49,000 as opportunities to harvest gains on the securities portfolio diminished. Net losses on sales of other assets were $14,000 lower in 2015 than in the prior year as write-downs of values of other real estate properties and losses on sales of properties were significantly lower in 2015 than in 2014. Earnings on life insurance policies were $349,000 higher in 2015 than 2014 as the result of a death benefit received on a former employee's life insurance policy. Other noninterest income declined $92,000 in 2015 compared to 2014 as a result of losses experienced in the Company's investments in its data processing subsidiary and a title insurance agency.

Noninterest Expense

Total noninterest expense increased $696,000 in 2016 compared to 2015. Salaries and benefits increased $709,000 in 2016 compared to the prior year due to higher costs related to salaries, stock-based compensation, commissions, and health insurance. Occupancy and equipment expense grew $192,000 in 2016 compared to the prior year primarily as a result of costs related to the lease of the loan production office that began in early 2016 and the lease of two new ATM locations that were added during 2016. Data processing expense decreased $47,000 as expenses related to Internet banking were lower in 2016 than in the prior year. Intangible amortization expense decreased by $69,000 in 2016 compared to 2015 as intangible assets were fully amortized by the end of 2016. FDIC insurance expense decreased in the last two quarters of 2016 due to a reduced FDIC assessment rate after the Deposit Insurance Fund reached a 1.15% reserve threshold on June 30, 2016.

Total noninterest expense increased $1.5 million in 2015 compared to 2014. Salaries and benefits increased $817,000 in 2015 compared to the prior year as a result of higher costs related to salaries, health insurance, retirement contributions and higher commission expenses. Data processing expense increased $463,000 as a result of higher costs related to electronic banking and software maintenance costs and the cost to upgrade the bank’s data processing and online banking software. Professional fees increased $82,000 as an increase of $101,000 in consulting expenses was partially offset by a decline in other professional fees. The $229,000 increase in other noninterest expense was partially due to an increase in recruiting expenses and loan origination costs.

Income Taxes

Income taxes increased $217,000 in 2016 compared to 2015, primarily due to a non-taxable death benefit received in 2015. The effective tax rate was 26% in 2016, compared to 25% in 2015. Income taxes decreased $131,000 in 2015 compared to 2014. The decline in tax expense in 2015 was caused by lower income before taxes and the effect of the non-taxable death benefit received in 2015.

Financial Condition

Summary

Total assets were $607.4 million as of December 31, 2016, which represented an increase of $39.6 million or 7.0% from the end of 2015. Securities available for sale increased $14.3 million during 2016 as management purchased securities to support earning assets growth. Loans increased $19.7 million in 2016, with most of the increase occurring in commercial real estate and agricultural loans. The increase of $83,000 in the allowance for loan losses resulted from no provision expense in 2016 plus net loan recoveries equaling $83,000. Total deposits increased $37.7 million in 2016 due to growth in checking deposits, savings deposits, and brokered certificates of deposit, which were partially offset by a decrease in local certificates of deposit.

Securities

The Bank’s securities available for sale balances as of December 31 were as follows:

(Dollars in thousands)

	2016	2015
U.S. Government and federal agency	$59,052	$57,207
U.S. Treasury notes and bonds	4,072	6,100
State and municipal	88,973	77,754
Mortgage-backed	7,789	6,970
Corporate	7,041	8,387
Foreign debt	4,400	995

Equity securities	2,883	2,453
Asset-backed securities	178	270
Total	$174,388	$160,136

The securities available for sale portfolio increased $14.3 million from December 31, 2015 to December 31, 2016. ChoiceOne purchased $69.5 million of securities during 2016 to replace securities that matured or were called and to provide growth in earning assets. Approximately $34.3 million in various securities were called or matured in 2016. Principal payments for municipal and mortgage-backed securities totaling $2.4 million were received during 2016. Various securities totaling approximately $15.3 million were sold during 2016 for net gains totaling $312,000. The Bank's Investment Committee continues to monitor the portfolio and purchases securities as it considers prudent. Also, certain securities are sold under agreements to repurchase and management plans to continue this practice as a low-cost source of funding.

Equity securities included a money market preferred security (MMP) and a trust preferred security totaling $1.5 million, and common stock of $1.4 million as of December 31, 2016. As of December 31, 2015, equity securities included an MMP of $1.5 million, and common stock of $953,000.

Loans

The Bank's loan portfolio as of December 31 was as follows:

(Dollars in thousands)

	2016	2015
Agricultural	$44,614	$40,232
Commercial and industrial	96,088	94,347
Consumer	21,596	20,090
Real estate - commercial	110,762	97,736
Real estate - construction	6,153	5,390
Real estate - residential	89,787	91,509
Total loans	$369,000	$349,304

The loan portfolio (excluding loans held for sale) increased $19.7 million from December 31, 2015 to December 31, 2016. Economic factors in ChoiceOne's market areas demonstrated signs of improvement, which affected loan demand in 2016. Growth experienced in the agricultural, commercial and industrial, and commercial real estate loan categories was due in part to calling efforts by ChoiceOne's loan officers.

Information regarding impaired loans can be found in Note 3 to the consolidated financial statements included in this report. In addition to its review of the loan portfolio for impaired loans, management also monitors various nonperforming loans. Nonperforming loans are comprised of (1) loans accounted for on a nonaccrual basis; (2) loans, not included in nonaccrual loans, which are contractually past due 90 days or more as to interest or principal payments; and (3) loans, not included in nonaccrual or past due 90 days or more, which are considered troubled debt restructurings. Troubled debt restructurings consist of loans where the terms have been modified to assist the borrowers in making their payments. The modifications can include capitalization of interest onto the principal balance, reduction in interest rate, and extension of the loan term.

The balances of these nonperforming loans as of December 31 were as follows:

(Dollars in thousands)

	2016		2015	
Loans accounted for on a nonaccrual basis	$	1,983	$	2,198
Loans contractually past due 90 days or more as to principal or interest payments		229		29

Loans considered troubled debt restructurings which are not included above		2,853		3,271
Total	$	5,065	$	5,498

Nonaccrual loans included $482,000 in agricultural loans, $245,000 in commercial and industrial loans, $6,000 in consumer loans, $458,000 in commercial real estate loans, and $792,000 in residential real estate loans as of December 31, 2016. Nonaccrual loans included $50,000 in agricultural loans, $77,000 in commercial and industrial loans, $1,640,000 in commercial real estate loans, and $431,000 in residential real estate loans as of December 31, 2015. The primary reason for the decline in nonaccrual loans in 2016 was loan paydowns. Loans considered troubled debt restructurings which were not on a nonaccrual basis and were not 90 days or more past due as to principal or interest payments consisted of $26,000 in commercial and industrial loans, $615,000 in commercial real estate loans, $20,000 in consumer loans, and $2,192,000 in residential real estate loans at December 31, 2016, compared to $1,149,000 in commercial real estate loans, $24,000 in consumer loans, and $2,098,000 in residential real estate loans as of December 31, 2015.

Management also maintains a list of loans that are not classified as nonperforming loans but where some concern exists as to the borrowers' abilities to comply with the original loan terms. These loans totaled $5.3 million as of December 31, 2016, compared to $6.0 million as of December 31, 2015.

Deposits and Other Funding Sources

The Bank's deposit balances as of December 31 were as follows:

(Dollars in thousands)		
	2016	2015
Noninterest-bearing demand deposits	$127,611	$122,937
Interest-bearing demand deposits	122,465	106,882
Money market deposits	99,454	86,987
Savings deposits	75,835	70,946
Local certificates of deposit	79,108	86,944
Brokered certificates of deposit	7,913	—
Total deposits	$512,386	$474,696

Total deposits increased $37.7 million from December 31, 2015 to December 31, 2016. The demand deposit categories as well as money market deposits and savings deposits grew $37.6 million as the Bank's depositors valued more liquid funds more than the interest rates paid on certificates of deposit. A decline of $7.8 million in local certificates of deposit was virtually offset by growth of $7.9 million in brokered certificates of deposit.

Securities sold under agreements to repurchase declined $1.5 million during 2016 due to normal fluctuations in overnight balances in sweep repurchase accounts used by the Bank's local clients. Federal Home Loan Bank advances increased $969,000 from December 31, 2015 to December 31,2016. A blanket collateral agreement covering agricultural real estate loans and residential real estate loans was pledged against all outstanding advances at the end of 2016. Approximately $41.7 million of additional advances were available as of December 31, 2016 based on the collateral pledged.

In 2017, management will continue to focus its marketing efforts toward growth in local deposits. If local deposit growth is insufficient to support asset growth, management believes that advances from the FHLB, securities sold under repurchase agreements and brokered certificates of deposit can address corresponding funding needs.

Shareholders' Equity

Total shareholders' equity increased $1.9 million from December 31, 2015 to December 31, 2016. The growth in equity resulted from the retention of earnings in 2016 as net income exceeded dividends paid by $3.9 million. Accumulated other comprehensive income decreased by $1.8 million in 2016 as a result of increased interest rates in the fourth quarter of 2016 which negatively impacted the market value of available for sale securities.

Note 20 to the consolidated financial statements presents regulatory capital information for the Bank at the end of 2016 and 2015. Management will monitor these capital ratios during 2017 as they relate to asset growth and earnings retention. ChoiceOne's Board of Directors and management do not plan to allow capital to decrease below those levels necessary to be considered "well capitalized" by regulatory guidelines. At December 31, 2016, the Bank was categorized as "well-capitalized." On July 3, 2013, the FDIC Board of Directors approved the Regulatory Capital Interim Final Rule, implementing Basel III. This rule redefines Tier 1 capital as two components (Common Equity Tier 1 and Additional Tier 1), creates a new capital ratio (Common Equity Tier 1 Risk-based Capital Ratio) and implements a capital conservation buffer. It also revises the prompt corrective action thresholds and makes changes to risk weights for certain assets and off-balance-sheet exposures. Banks were required to transition into the new rule beginning on January 1, 2015. Based on ChoiceOne's capital levels and balance sheet composition at December 31, 2016, management believes implementation of the new rule will have no material impact on ChoiceOne's capital needs.

Table 4 – Contractual Obligations

The following table discloses information regarding the maturity of ChoiceOne's contractual obligations at December 31, 2016:

	Payment Due by Period				
(Dollars in thousands)	Total	Less than 1 year	1 - 3 Years	3 - 5 Years	More than 5 Years
Time deposits	$87,021	$54,111	$25,179	$7,731	$ —
Repurchase agreements	7,913	7,913	—	—	—
Advances from Federal Home Loan Bank	12,301	12,033	70	76	122
Operating leases	307	69	129	37	72
Other obligations	697	96	205	175	221
Total	$108,239	$74,222	$25,583	$8,019	$ 415

<u>Liquidity and Interest Rate Risk</u>

Net cash from operating activities was $10.9 million for 2016 compared to $4.0 million for 2015. Higher net proceeds from loan sales was the main reason for the increase. Cash used in investing activities was $41.5 million in 2016 compared to $22.7 million in 2015. The change was caused by a higher level of loan growth in 2016 than in 2015. Cash flows from financing activities were $34.2 million in 2016 compared to $13.2 million in the prior year. The increase was primarily due to a lower level of balance decline in repurchase agreements in 2016 than in the prior year.

ChoiceOne's primary market risk exposure occurs in the form of interest rate risk. Liquidity risk also can have an impact but to a lesser extent. ChoiceOne's business is transacted in U.S. dollars with no foreign exchange risk exposure. Agricultural loans comprise a relatively small portion of ChoiceOne's total assets. Management believes that ChoiceOne's exposure to changes in commodity prices is insignificant.

Management believes that the current level of liquidity is sufficient to meet the Bank's normal operating needs. This belief is based upon the availability of deposits from both the local and national markets, maturities of securities, normal loan repayments, income retention, federal funds purchased lines of credit from correspondent banks, and advances available from the FHLB. Liquidity risk deals with ChoiceOne's ability to meet its cash flow requirements. These requirements include depositors desiring to withdraw funds and borrowers seeking credit. Relatively short-term liquid funds exist in the form of lines of credit to purchase federal funds at four of the Bank's correspondent banks. As of December 31, 2016, the amount of federal funds available for purchase from the Bank's correspondent banks totaled

approximately $44.0 million. ChoiceOne had no federal funds purchased at the end of 2016 or 2015. The Bank also has a line of credit secured by ChoiceOne's commercial loans with the Federal Reserve Bank of Chicago for $65.3 million, which is designated for nonrecurring short-term liquidity needs. Longer-term liquidity needs may be met through local deposit growth, maturities of securities, normal loan repayments, advances from the FHLB, brokered certificates of deposit, and income retention. Approximately $41.7 million of borrowing capacity was available from the FHLB based on agricultural real estate loans and residential real estate loans pledged as collateral at year-end 2016. The acceptance of brokered certificates of deposit is not limited as long as the Bank is categorized as "well capitalized" under regulatory guidelines.

Critical Accounting Policies And Estimates

Management's discussion and analysis of financial condition and results of operations as well as disclosures found elsewhere in this report are based upon the Company's consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements requires the Company to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses. Material estimates that are particularly susceptible to significant change in the near-term relate to the determination of the market value of securities, the amount of the allowance for loan losses, loan servicing rights, carrying value of goodwill, and income taxes. Actual results could differ from those estimates.

Securities

Securities available for sale may be sold prior to maturity due to changes in interest rates, prepayment risks, yield, availability of alternative investments, liquidity needs, credit rating changes, or other factors. Securities classified as available for sale are reported at their fair value. Declines in the fair value of securities below their cost that are considered to be "other than temporary" are recorded as losses in the income statement. In estimating whether a fair value decline is considered to be "other than temporary," management considers the length of time and extent that the security's fair value has been less than its carrying value, the financial condition and near-term prospects of the issuer, and the Bank's ability and intent to hold the security for a period of time sufficient to allow for any anticipated recovery in fair value.

Market values for securities available for sale are obtained from outside sources and applied to individual securities within the portfolio. The difference between the amortized cost and the fair value of securities is recorded as a valuation adjustment and reported net of tax effect in other comprehensive income.

Allowance for Loan Losses

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

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

Loan Servicing Rights

Loan servicing rights represent the estimated value of servicing loans that are sold with servicing retained by ChoiceOne. Servicing rights are expensed in proportion to, and over the period of, estimated net servicing revenues. Management's accounting treatment of loan servicing rights is estimated based on current prepayment speeds that are typically market driven.

Management believes the accounting estimate related to loan servicing rights is a "critical accounting estimate" because (1) the estimate is highly susceptible to change from period to period because of significant changes within long-term interest rates affecting the prepayment speeds for current loans being serviced and (2) the impact of recognizing an impairment loss could have a material effect on ChoiceOne's net income. Management has obtained a third-party valuation of its loan servicing rights to corroborate its current carrying value at the end of each reporting period.

Goodwill

Generally accepted accounting principles require that the fair values of the assets and liabilities of an acquired entity be recorded at their fair value on the date of acquisition. The fair values are determined using both internal computations and information obtained from outside parties when deemed necessary. The net difference between the price paid for the acquired company and the net value of its balance sheet is recorded as goodwill. Accounting principles also require that goodwill be evaluated for impairment on an annual basis or more frequently whenever

events or changes in circumstances indicate that the carrying value may not be recoverable. Under recently issued accounting pronouncements, ChoiceOne is permitted to first perform a qualitative assessment to determine whether it is more likely than not (that is, a likelihood of more than 50 percent) that the fair value of equity is less than its carrying value. If the conclusion is that it is more likely than not that the fair value of equity is more than its carrying value, no further testing in the form of a quantitative assessment is necessary. If the conclusion is that it is more likely than not that the fair value of equity is less than its carrying value, then a two-step quantitative assessment test is performed to identify any potential goodwill impairment.

Management performed a qualitative assessment of goodwill as of June 30, 2015 and 2016 and December 31, 2015 and 2016. The analysis was performed including evaluation of the share price, book value, and financial results of ChoiceOne as compared to the previous year. Additionally, industry and market conditions were evaluated and compared. Average deal prices in the Midwest of closed transactions have indicated increases in deal values to tangible common equity, deal values to earnings, and core deposit premiums when compared to the observed prices used in the last quantitative assessment of goodwill in 2012. Further, macro-economic trends have been on a positive trajectory recently and there have been no adverse legal, regulatory, contractual, political or other factors that have materially impacted ChoiceOne. Upon completion of the qualitative assessment, ChoiceOne believes that it is more likely than not that the fair value of ChoiceOne's equity exceeds the carrying value at the assessment date and there is no further quantitative assessment necessary.

Taxes

Income taxes include both a current and deferred portion. Deferred tax assets and liabilities are recorded to account for differences in the timing of the recognition of revenues and expenses for financial reporting and tax purposes. Generally accepted accounting principles require that deferred tax assets be reviewed to determine whether a valuation allowance should be established using a "more likely than not" standard. Based on its review of ChoiceOne's deferred tax assets as of December 31, 2016, management determined that no valuation allowance was necessary.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk

Interest rate risk is related to liquidity because each is affected by maturing assets and sources of funds. ChoiceOne's Asset/Liability Management Committee (the "ALCO") attempts to stabilize the interest rate spread and avoid possible adverse effects when unusual or rapid changes in interest rates occur. The ALCO uses a simulation model to measure the Bank's interest rate risk. The model incorporates changes in interest rates on rate-sensitive assets and liabilities. The degree of rate sensitivity is affected by prepayment assumptions that exist in the assets and liabilities. One method the ALCO uses of measuring interest rate sensitivity is the ratio of rate-sensitive assets to rate-sensitive liabilities. An asset or liability is considered to be rate-sensitive if it matures or otherwise reprices within a given time frame.

Table 5 documents the maturity or repricing schedule for ChoiceOne’s rate-sensitive assets and liabilities for selected time periods:

Table 5 – Maturities and Repricing Schedule

	As of December 31, 2016				
(Dollars in thousands)	0 - 3 Months	3 - 12 Months	1 - 5 Years	Over 5 Years	Total
Assets					
Securities available for sale	$11,568	$23,171	$98,177	$41,472	$174,388
Federal Home Loan Bank stock	1,994	—	—	—	1,994
Federal Reserve Bank stock	—	—	—	1,573	1,573
Loans held for sale	1,974	—	—	—	1,974
Loans	151,782	61,562	139,713	15,943	369,000
Cash surrender value of life insurance policies	—	—	—	14,117	14,117
Rate-sensitive assets	$167,318	$84,733	$237,890	$73,105	$563,046
Liabilities					
Interest-bearing demand deposits	$122,465	$—	$—	$—	$122,465
Money market deposits	93,481	—	—	—	93,481
Savings deposits	75,835	—	—	—	75,835
Certificates of deposits	12,061	42,084	32,772	104	87,021
Repurchase agreements	7,913	—	—	—	7,913
Advances from FHLB	12,008	25	146	122	12,301
Rate-sensitive liabilities	$323,763	$42,109	$32,918	$226	$399,016
Rate-sensitive assets less rate-sensitive liabilities:					
Asset (liability) gap for the period	$(156,445)	$42,624	$204,972	$72,879	$164,030
Cumulative asset (liability) gap	$(156,445)	$(113,821)	$91,151	$164,030	

Under this method, the ALCO measures interest rate sensitivity by focusing on the one-year repricing gap. ChoiceOne’s ratio of rate-sensitive assets to rate-sensitive liabilities that matured or repriced within a one-year time frame was 68% at December 31, 2016, compared to 69% at December 31, 2015. Table 5 above shows the entire balance of interest-bearing demand deposits, savings deposits, money market deposits, and overnight repurchase agreements in the shortest repricing term. Although these categories have the ability to reprice immediately, management has some control over the actual timing or extent of the changes in interest rates on these liabilities. The ALCO plans to continue to monitor the ratio of rate-sensitive assets to rate-sensitive liabilities on a quarterly basis in 2017. As interest rates change during 2017, the ALCO will attempt to match its maturing assets with corresponding liabilities to maximize ChoiceOne’s net interest income.

Another method the ALCO uses to monitor its interest rate sensitivity is to subject rate-sensitive assets and liabilities to interest rate shocks. At December 31, 2016, management used a simulation model to subject its assets and liabilities up to an immediate 400 basis point increase. The maturities of loans and mortgage-backed securities were affected by certain prepayment assumptions. Maturities for interest-bearing core deposits were based on an estimate of the period over which they would be outstanding. The maturities of advances from the FHLB were based on their contractual maturity dates. In the case of variable rate assets and liabilities, repricing dates were used to determine their values. The simulation model measures the effect of immediate interest rate changes on both net interest income and shareholders' equity.

Table 6 provides an illustration of hypothetical interest rate changes as of December 31, 2016 and 2015:

Table 6 – Sensitivity to Changes in Interest Rates

(Dollars in thousands)	2016 Net Interest Income	Percent Change	Market Value of Equity	Percent Change
Change in Interest Rate				
400 basis point rise	$22,196	10 %	$154,009	9 %
300 basis point rise	21,684	7 %	151,373	8 %
200 basis point rise	21,177	5 %	148,553	6 %
100 basis point rise	20,638	2 %	145,321	3 %
Base rate scenario	20,203	— %	140,761	— %
100 basis point decline	19,097	-5 %	124,886	-11 %
200 basis point decline	18,072	-11 %	103,937	-26 %
300 basis point decline	17,476	-13 %	94,215	-33 %
400 basis point decline	17,122	-15 %	93,864	-33 %

	2015 Net Interest Income	Percent Change	Market Value of Equity	Percent Change
Change in Interest Rate				
400 basis point rise	$18,284	-14 %	$88,045	-18 %
300 basis point rise	18,571	-13 %	93,100	-13 %
200 basis point rise	18,802	-10 %	98,626	-8 %
100 basis point rise	19,015	-5 %	103,565	-4 %
Base rate scenario	19,380	— %	107,525	— %
100 basis point decline	18,444	-2 %	99,371	-8 %
200 basis point decline	17,503	-3 %	86,702	-19 %
300 basis point decline	16,956	-4 %	85,624	-20 %
400 basis point decline	16,739	-6 %	85,252	-21 %

As of December 31, 2016, the Bank was within its guidelines for immediate rate shocks up and down for net income and for immediate rate shocks up for the market value of shareholders' equity. The negative impact from immediate rate shocks upon the market value of shareholders' equity was slightly higher than the policy guidelines. Management believed that the possibility of interest rate declines was unlikely as of December 31, 2016. As of December 31, 2015, the Bank was within its guidelines for immediate rate shocks up and down for both net interest income and the market value of shareholders' equity. The ALCO plans to continue to monitor the effect of changes in interest rates on both net interest income and sharheolders' equity and will make changes in the duration of its rate-sensitive assets and rate-sensitive liabilities where necessary.

Item 8. Financial Statements and Supplementary Data

Report of Independent Registered Public Accounting Firm

To the Shareholders and Board of Directors
ChoiceOne Financial Services, Inc.

We have audited the accompanying consolidated balance sheet of ChoiceOne Financial Services, Inc. (the "Company") as of December 31, 2016 and 2015, and the related consolidated statements of income, comprehensive income, shareholders' equity, and cash flows for each year in the three-year period ended December 31, 2016. 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 audits to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated 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 provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of ChoiceOne Financial Services, Inc. as of December 31, 2016 and 2015, and the consolidated results of its operations and its cash flows for each year in the three-year period ended December 31, 2016, in conformity with accounting principles generally accepted in the United States of America.

Plante & Moran, PLLC

March 24, 2017

ChoiceOne Financial Services, Inc.
Consolidated Balance Sheets

(Dollars in thousands)	December 31, 2016	2015
Assets		
Cash and due from banks	$14,809	$11,187
Securities available for sale (Note 2)	174,388	160,136
Federal Home Loan Bank stock	1,994	1,614
Federal Reserve Bank stock	1,573	1,573
Loans held for sale	1,974	4,957
Loans (Note 3)	369,000	349,304
Allowance for loan losses (Note 3)	(4,277)	(4,194)
Loans, net	364,723	345,110
Premises and equipment, net (Note 5)	12,588	11,847
Other real estate owned, net (Note 7)	437	31
Cash value of life insurance policies	14,117	12,261
Intangible assets, net (Note 6)	—	379
Goodwill (Note 6)	13,728	13,728
Other assets	7,040	4,923
Total assets	$607,371	$567,746
Liabilities		
Deposits – noninterest-bearing (Note 8)	$127,611	$122,937
Deposits – interest-bearing (Note 8)	384,775	351,759
Total deposits	512,386	474,696
Repurchase agreements (Note 9)	7,913	9,460
Advances from Federal Home Loan Bank (Note 10)	12,301	11,332
Other liabilities (Notes 11 and 13)	3,073	2,416
Total liabilities	535,673	497,904
Shareholders' Equity (Note 20)		
Preferred stock; shares authorized: 100,000; shares outstanding: none	—	—
Common stock and paid-in capital, no par value; shares authorized: 7,000,000; shares outstanding: 3,277,944 in 2016 and 3,295,228 in 2015 (Note 14)	46,299	46,501
Retained earnings	25,997	22,138
Accumulated other comprehensive income, net	(598)	1,203
Total shareholders' equity	71,698	69,842
Total liabilities and shareholders' equity	$607,371	$567,746

See accompanying notes to consolidated financial statements.

ChoiceOne Financial Services, Inc.
Consolidated Statements of Income

(Dollars in thousands, except per share data)	Years ended December 31,		
	2016	2015	2014
Interest income			
Loans, including fees	$16,507	$15,971	$15,765
Securities:			
Taxable	2,334	1,939	1,847
Tax exempt	1,450	1,428	1,393
Other	21	14	9
Total interest income	20,312	19,352	19,014
Interest expense			
Deposits	790	877	1,042
Advances from Federal Home Loan Bank	171	83	63
Other	8	30	46
Total interest expense	969	990	1,151
Net interest income	19,343	18,362	17,863
Provision for loan losses (Note 3)	—	100	100
Net interest income after provision for loan losses	19,343	18,262	17,763
Noninterest income			
Customer service charges	4,056	4,083	3,951
Insurance and investment commissions	1,009	1,060	906
Gains on sales of loans (Note 4)	1,748	1,416	1,023
Net gains on sales of securities (Note 2)	312	261	311
Net losses on sales and write-downs of other assets (Note 7)	(41)	(121)	(135)
Earnings on life insurance policies	356	651	302
Other	441	352	444
Total noninterest income	7,881	7,702	6,802
Noninterest expense			
Salaries and benefits (Notes 13 and 14)	9,982	9,273	8,456
Occupancy and equipment (Note 5)	2,588	2,396	2,389
Data processing	2,273	2,320	1,857
Professional fees	935	971	889
Supplies and postage	385	413	440
Advertising and promotional	222	253	275
Intangible amortization (Note 6)	379	448	448
Loan and collection expense	96	104	122
FDIC insurance	238	288	337
Other	1,874	1,810	1,581
Total noninterest expense	18,972	18,276	16,794

Income before income tax	8,252	7,688	7,771
Income tax expense (Note 11)	2,162	1,945	2,076
Net income	$6,090	$5,743	$5,695
Basic earnings per share (Note 15)	$1.85	$1.75	$1.73
Diluted earnings per share (Note 15)	$1.85	$1.74	$1.72
Dividends declared per share	$0.68	$0.66	$0.59

See accompanying notes to consolidated financial statements.

ChoiceOne Financial Services, Inc.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(Dollars in thousands)	Years ended December 31,		
	2016	2015	2014
Net income	$6,090	$5,743	$5,695
Other comprehensive income:			
Changes in net unrealized gains (losses) on investment securities available for sale, net of tax expense (benefit) of $(812), $168, and $588 for the years ended December 31, 2016, 2015, and 2014 respectively	(1,573)	324	1,141
Reclassification adjustment for realized gain on sale of investment securities available for sale included in net income, net of tax expense of $104, $89, and $106 for the years ended December 31, 2016, 2015, and 2014 respectively	(206)	(172)	(205)
Change in adjustment for pension and other postretirement benefits, net of tax benefit (expense) of $12, 11, and $5 for the years ended December 31, 2016, 2015, and 2014 respectively	(22)	(22)	(11)
Other comprehensive income/(loss), net of tax	(1,801)	130	925
Comprehensive income	$4,289	$5,873	$6,620

See accompanying notes to consolidated financial statements.

ChoiceOne Financial Services, Inc.
Consolidated Statements of Changes in Shareholders' Equity

(Dollars in thousands, except per share data)	Number of Shares	Common Stock and Paid in Capital	Retained Earnings	Accumulated Other Comprehensive Income/(Loss), Net	Total
Balance, January 1, 2014	3,295,463	$ 46,595	$ 14,815	$ 148	$ 61,558
Net income			5,695		5,695
Other comprehensive income				925	925
Shares issued	8,925	132			132
Shares repurchased	(9,496)	(203)			(203)
Change in ESOP repurchase obligation		(32)			(32)
Effect of employee stock purchases		12			12
Stock compensation shares issued	942				—
Stock compensation expense		48			48
Cash dividends declared ($0.59 per share)			(1,945)		(1,945)
Balance, December 31, 2014	3,295,834	$ 46,552	$ 18,565	$ 1,073	$ 66,190
Net income			5,743		5,743
Other comprehensive income				130	130
Shares issued	13,310	206			206
Shares repurchased	(16,200)	(371)			(371)
Change in ESOP repurchase obligation		(4)			(4)
Effect of employee stock purchases		15			15
Stock compensation shares issued	2,284				—
Stock compensation expense		103			103
Cash dividends declared ($0.66 per share)			(2,170)		(2,170)
Balance, December 31, 2015	3,295,228	$ 46,501	$ 22,138	$ 1,203	$ 69,842
Net income			6,090		6,090
Other comprehensive income (loss)				(1,801)	(1,801)
Shares issued	8,460	173			173
Shares repurchased	(35,000)	(794)			(794)
Termination of ESOP repurchase obligation		127			127
Effect of employee stock purchases		13			13
Stock compensation shares issued	9,256				—
Stock compensation expense		279			279
Cash dividends declared ($0.68 per share)			(2,231)		(2,231)

Balance, December 31, 2016	3,277,944	$46,299	$25,997	$ (598)	$71,698

See accompanying notes to consolidated financial statements.

ChoiceOne Financial Services, Inc.
Consolidated Statements of Cash Flows

(Dollars in thousands)	Years ended December 31,		
	2016	2015	2014
Cash flows from operating activities:			
Net income	$6,090	$5,743	$5,695
Adjustments to reconcile net income to net cash from operating activities:			
Provision for loan losses	—	100	100
Depreciation	1,078	986	986
Amortization	1,531	1,497	1,493
Compensation expense on employee and director stock purchases, stock options, and restricted stock units	380	118	60
Net gains on sales of securities	(312)	(261)	(311)
Gains on sales of loans	(1,748)	(1,416)	(1,023)
Loans originated for sale	(53,591)	(47,498)	(29,850)
Proceeds from loan sales	57,830	46,077	29,561
Earnings on bank-owned life insurance	(356)	(347)	(302)
Earnings from death benefit	—	(304)	—
Proceeds on bank-owned life insurance	—	461	—
(Gains)/losses on sales of other real estate owned	8	30	(24)
Write-downs of other real estate owned	—	91	154
Proceeds from sales of other real estate owned	247	406	789
Deferred federal income tax (benefit)/expense	(82)	(631)	(460)
Net change in:			
Other assets	(1,952)	(503)	(380)
Other liabilities	1,804	(571)	985
Net cash from operating activities	10,927	3,978	7,473
Cash flows from investing activities:			
Sales of securities available for sale	15,317	25,876	24,766
Maturities, prepayments and calls of securities available for sale	36,705	27,084	11,427
Purchases of securities available for sale	(69,526)	(70,902)	(41,770)
Purchase of Federal Reserve Bank stock	—	(301)	—
Purchases or calls of FHLB stock	(380)	299	565
Purchase of bank-owned life insurance policies	(1,500)	—	(1,500)
Loan originations and payments, net	(20,274)	(3,678)	(31,370)
Additions to premises and equipment	(1,819)	(1,038)	(786)
Net cash from investing activities	(41,477)	(22,660)	(38,668)
Cash flows from financing activities:			
Net change in deposits	37,690	39,868	16,701
Net change in repurchase agreements	(1,547)	(17,283)	710
Proceeds from Federal Home Loan Bank advances	311,017	194,575	87,700
Payments on Federal Home Loan Bank advances	(310,048)	(201,606)	(75,729)

Cash proceeds from the issuance of common stock	85	206	132
Repurchase of common stock	(794)	(371)	(203)
Cash dividends	(2,231)	(2,170)	(1,945)
Net cash from financing activities	34,172	13,219	27,366
Net change in cash and cash equivalents	3,622	(5,463)	(3,829)
Beginning cash and cash equivalents	11,187	16,650	20,479
Ending cash and cash equivalents	$14,809	$11,187	$16,650
Supplemental disclosures of cash flow information:			
Cash paid for interest	$984	$1,005	$1,161
Cash paid for income taxes	1,760	2,395	1,760
Loans transferred to other real estate owned	661	408	561

See accompanying notes to consolidated financial statements.

Note 1 – Summary of Significant Accounting Policies

Principles of Consolidation

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

Nature of Operations

The Bank is a full-service community bank that offers commercial, consumer, and real estate loans as well as traditional demand, savings and time deposits to both commercial and consumer clients in Kent, Muskegon, Newaygo, and Ottawa counties in Michigan. Substantially all loans are secured by specific items of collateral including business assets, consumer assets, and real estate. Commercial loans are expected to be repaid from the cash flows from operations of businesses. Real estate loans are collateralized by either residential or commercial real estate.

The Insurance Agency is a wholly-owned subsidiary of the Bank. The Insurance Agency sells insurance policies such as life and health for both commercial and consumer clients. The Insurance Agency also offers alternative investment products such as annuities and mutual funds through a registered broker.

Together, the Bank and the Insurance Agency account for substantially all of ChoiceOne's assets, revenues and operating income.

Use of Estimates

To prepare financial statements in conformity with accounting principles generally accepted in the United States of America, ChoiceOne's management makes estimates and assumptions based on available information. These estimates and assumptions affect the amounts reported in the financial statements and the disclosures provided. Actual results may differ from these estimates. Estimates associated with securities available for sale, the allowance for loan losses, other real estate owned, core deposit intangible assets, loan servicing rights, goodwill, and fair values of certain financial instruments are particularly susceptible to change.

Cash and Cash Equivalents

Cash and cash equivalents are defined to include cash on hand, demand deposits with other banks, and federal funds sold. Cash flows are reported on a net basis for customer loan and deposit transactions, deposits with other financial institutions, and short-term borrowings with original terms of 90 days or less.

Securities

Securities are classified as available for sale because they might be sold before maturity. Securities classified as available for sale are carried at fair value, with unrealized holding gains and losses reported separately in the accumulated other comprehensive income or loss section of shareholders' equity, net of tax effect. Restricted investments in Federal Reserve Bank stock and Federal Home Loan Bank stock are carried at cost. Equity securities consist of investments in preferred stock, trust-preferred securities, and investments in common stock of other financial institutions.

Interest income includes amortization of purchase premium or discount. Premiums and discounts on securities are amortized using the level-yield method without anticipating prepayments. Gains or losses on sales are recorded on the trade date based on the amortized cost of the security sold.

Management evaluates securities for other-than-temporary impairment ("OTTI") on a quarterly basis, and more frequently when economic or market conditions warrant such an evaluation. The evaluation of securities includes consideration given to 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, whether the market decline was affected by macroeconomic conditions and whether ChoiceOne has the intent to sell the security or it is more likely than not it will be required to sell the security before recovery of its amortized cost basis. In analyzing an issuer's financial condition, management may consider whether the securities are issued by the federal government or its agencies, or U.S. Government sponsored enterprises, whether downgrades by bond rating agencies have occurred, and the results of reviews of the issuer's financial condition. The assessment of whether an other-than-temporary decline exists involves a high degree of subjectivity and judgment and is based on the information available to management at a point in time.

When OTTI occurs, the amount of the OTTI recognized in earnings depends on whether ChoiceOne intends to sell the security or it is more likely than not it will be required to sell the security before recovery of its amortized cost basis. If ChoiceOne intends to sell or it is more likely than not it will be required to sell the security before recovery of its amortized cost basis, the OTTI shall be recognized in earnings equal to the entire difference between the investment's amortized cost basis and its fair value at the balance sheet date. The previous amortized cost basis less the OTTI recognized in earnings becomes the new amortized cost basis of the investment. If a security is determined to be other-than-temporarily impaired, but ChoiceOne does not intend to sell the security, only the credit portion of the estimated loss is recognized in earnings, with the other portion of the loss recognized in other comprehensive income.

Loans

Loans that management has the intent and ability to hold for the foreseeable future or until maturity or payoff are reported at the principal balance outstanding, net of unearned interest, deferred loan fees and costs, and an allowance for loan losses. Loans held for sale are reported at the lower of cost or market, on an aggregate basis.

Interest income on loans is reported on the interest method and includes amortization of net deferred loan fees and costs over the estimated loan term. Interest on loans is accrued based upon the principal balance outstanding. The accrual of interest is discontinued at the time at which commercial loans are 90 days past due unless the loan is secured by sufficient collateral and is in the process of collection. Interest on consumer or real estate secured loans is discontinued at the time at which the loan is 120 days past due unless the credit is secured by sufficient collateral and is in the process of collection. Past due status is based on the contractual terms of the loan. In all cases, loans are placed into nonaccrual status or charged off at an earlier date if collection of principal or interest is considered doubtful. Interest accrued but not received is reversed against interest income when the loans are placed into nonaccrual status. Interest received on such loans is applied to principal until qualifying for return to accrual. Loans are returned to accrual basis when all the principal and interest amounts contractually due are brought current and future payment is reasonably assured.

Allowance for Loan Losses

The allowance for loan losses is a valuation allowance for probable incurred credit losses. The allowance for loan losses is increased by the provision for loan losses and decreased by loans charged off less any recoveries of charged off loans. Management estimates the allowance for loan losses balance required based on past loan loss experience, the nature and volume of the loan portfolio, information about specific borrower situations and estimated collateral values, economic conditions, and other factors. Allocations of the allowance for loan losses may be made for specific loans, but the entire allowance for loan losses is available for any loan that, in management’s judgment, should be charged off. Loan losses are charged against the allowance for loan losses when management believes that collection of a loan balance is not possible.

The allowance for loan losses consists of general and specific components. The general component covers non-classified loans and is based on historical loss experience adjusted for current factors. The specific component relates to loans that are individually classified as impaired or loans otherwise classified as substandard or doubtful.

A loan is impaired when full payment under the loan terms is not expected. Commercial loans are evaluated for impairment on an individual loan basis. If a loan is considered impaired, a portion of the allowance for loan losses is allocated to the loan so that it is reported, net, at the present value of estimated future cash flows using the loan’s existing rate or at the fair value of collateral if repayment is expected solely from the collateral. Large groups of smaller-balance homogeneous loans such as consumer and residential real estate mortgage loans are collectively evaluated for impairment and, accordingly, they are not separately identified for impairment disclosures.

Premises and Equipment

Premises and equipment are stated at cost less accumulated depreciation. Land is carried at cost. Land improvements are depreciated using the straight-line method with useful lives ranging from 7 to 15 years. Building and related components are depreciated using the straight-line method with useful lives ranging from 5 to 39 years. Leasehold improvements are depreciated over the shorter of the estimated life or the lease term. Furniture and equipment are depreciated using the straight-line method with useful lives ranging from 3 to 7 years. Fixed assets are periodically reviewed for impairment. If impaired, the assets are recorded at fair value.

Other Real Estate Owned

Real estate properties acquired in the collection of a loan are initially recorded at the lower of the Bank's basis in the loans or fair value at acquisition establishing a new cost basis. Any reduction to fair value from the carrying value of the related loan is accounted for as a loan loss. After acquisition, a valuation allowance reduces the reported amount to the lower of the initial amount or fair value less costs to sell. Expenses to repair or maintain properties are included within other noninterest expenses. Gains and losses upon disposition and changes in the valuation allowance are reported net within noninterest income.

Loan Servicing Rights

Loan servicing rights represent the allocated value of servicing rights on loans sold with servicing retained. Servicing rights are expensed in proportion to, and over the period of, estimated net servicing revenues. Impairment is evaluated based on the fair value of the rights, using groupings of the underlying loans as to interest rates and then, secondarily, as to geographic and prepayment characteristics. Fair value is determined using prices for similar assets with similar characteristics when available or based upon discounted cash flows using market-based assumptions. Any impairment of a grouping is reported as a valuation allowance.

Goodwill

Goodwill results from business acquisitions and represents the excess of the purchase price over the fair value of the acquired tangible assets and liabilities and identifiable intangible assets. Goodwill is assessed at least annually for impairment and any such impairment will be recognized in the period identified.

Loan Commitments and Related Financial Instruments

Financial instruments include off-balance sheet credit instruments, such as commitments to make loans and commercial letters of credit issued to meet financing needs of customers. The face amount for these items represents the exposure to loss, before considering customer collateral or ability to repay. Such financial instruments are recorded when they are funded.

Employee Benefit Plans

ChoiceOne's 401(k) plan allows participants to make contributions to their individual accounts under the plan in amounts up to the IRS maximum. Employer matching contributions from ChoiceOne to its 401(k) plan are discretionary. ChoiceOne also allows retired employees to participate in its health insurance plan. Employees who have attained age 55 and completed at least ten years of service to ChoiceOne are eligible to participate as a retiree until they are eligible for Medicare. These post-retirement benefits are accrued during the years in which the employee provides service.

Employee Stock Ownership Plan

Dividends on Employee Stock Ownership Plan (the "ESOP") shares are recorded as a reduction of retained earnings. Upon distribution of shares to a participant, the participant has the right to require the Company to purchase his or her shares at fair value in accordance with the terms and conditions of the ESOP. As such, these shares are not classified in shareholders' equity as permanent equity. Effective January 1, 2016, ChoiceOne terminated the ESOP and transferred shares held by the ESOP to the 401(k) plan.

Income Taxes

Income tax expense is the sum of the current year income tax due and the change in deferred tax assets and liabilities. Deferred tax assets and liabilities are the expected future tax consequences of temporary differences between the carrying amounts and tax bases of assets and liabilities, computed using enacted tax rates. A valuation allowance, if needed, reduces deferred tax assets to the amount expected to be realized.

Earnings Per Share

Basic earnings per common share ("EPS") is based on weighted-average common shares outstanding. The weighted-average number of shares used in the computation of basic and diluted EPS includes shares allocated to the ESOP. Diluted EPS further assumes issue of any dilutive potential common shares issuable under stock options or restricted stock units granted.

Comprehensive Income

Comprehensive income consists of net income and other comprehensive income or loss. Other comprehensive income or loss includes unrealized gains and losses on securities available for sale and changes in the funded status of post-retirement plans, net of tax, which are also recognized as a separate component of shareholders' equity.

Accumulated other comprehensive income was as follows:

(Dollars in thousands)	Years ended December 31, 2016	2015
Unrealized gain (loss) on available for sale securities	$(1,063)	$1,632
Unrecognized gains on post-retirement benefits	157	191
Tax effect	308	(620)
Accumulated other comprehensive income (loss)	$(598)	$1,203

Loss Contingencies

Loss contingencies, including claims and legal actions arising in the ordinary course of business, are recorded as liabilities when the likelihood of loss is probable and an amount or range of loss can be reasonably estimated. Management does not believe that there are any such matters that may have a material effect on the financial statements as of December 31, 2016.

Cash Restrictions

Cash on hand or on deposit with the Federal Reserve Bank of $621,000 and $1.1 million was required to meet regulatory reserve and clearing requirements at December 31, 2016 and 2015, respectively. The balance in excess of the amount required was interest-bearing as of December 31, 2016 and December 31, 2015.

Stock-Based Compensation

The Company values share-based stock option awards granted using the Black-Scholes option-pricing model. The Company recognizes compensation expense for its awards on a straight-line basis over the requisite service period for the entire award (straight-line attribution method), ensuring that the amount of compensation cost recognized at any

date at least equals the portion of the grant-date fair value of the award that is vested at that time. Compensation costs related to stock options granted are disclosed in Note 14.

ChoiceOne has granted restricted stock units to a select group of employees under the Stock Incentive Plan of 2012. Restricted stock units vest in three annual installments on each of the next three anniversaries of the grant date. Certain additional vesting provisions apply. Each unit, once vested, is settled by delivery of one share of ChoiceOne common stock.

Dividend Restrictions

Banking regulations require the maintenance of certain capital levels and may limit the amount of dividends that may be paid by the Bank to ChoiceOne (see Note 20).

Fair Value of Financial Instruments

Fair values of financial instruments are estimated using relevant market information and other assumptions, which are more fully documented in Note 18 to the consolidated financial statements. Fair value estimates involve uncertainties and matters of significant judgment regarding interest rates, credit risk, prepayments, and other factors, especially in the absence of broad markets for particular items. Changes in assumptions or in market conditions could significantly affect the estimates.

Operating Segments

While ChoiceOne's management monitors the revenue streams of various products and services for the Bank and Insurance Agency, operations and financial performance are evaluated on a company-wide basis. Accordingly, all of the financial service operations are considered by management to be aggregated into one reportable operating segment.

Recent Accounting Pronouncements

The Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2014-09, *Revenue from Contracts with Customers (Topic 606)*. The ASU adopts a standardized approach for revenue recognition and was a joint effort with the International Accounting Standards Board (IASB). The new revenue recognition standard is based on a core principle of recognizing revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The ASU does not apply to financial instruments. The ASU is effective for public entities for reporting periods beginning after December 15, 2017 (therefore, for the year ending December 31, 2018 for ChoiceOne). Early implementation is not allowed for public companies. Management is currently assessing the impact to the ChoiceOne's consolidated financial statements but does not expect these changes to have a significant effect on the financial statements.

The FASB issued ASU 2016-01, *Recognition and Measurement of Financial Assets and Financial Liabilities*. The ASU covers various changes to the accounting, measurement, and disclosure related to certain financial instruments. The most significant change included in the update is the requirement for certain equity investments (excluding investments that are consolidated or accounted for under the equity method of accounting) to be measured at fair value with changes in fair value recognized in net income. An entity may choose to measure equity investments that do not have readily determinable fair values at cost, minus impairment. When a qualitative assessment of equity investments without readily determinable fair values indicates that impairment exists, an entity is required to measure the investment at fair value. The update also eliminates the requirement for public business entities to disclose the methods and significant assumptions used to estimate the fair value that is required to be disclosed for financial instruments measured at amortized cost. The new standard is effective for ChoiceOne for the fiscal year beginning after December 15, 2017, including interim periods within this fiscal year. Management is currently assessing the impact to ChoiceOne's consolidated financial statements. Other than the impact in the accounting for the change in fair value of equity securities discussed in Note 2, ChoiceOne does not expect any significant changes as a result of adopting this update.

The FASB issued ASU 2016-02, *Leases*. The new standard establishes a right-of-use (ROU) model that requires a lessee to record a ROU asset and a lease liability on the balance sheet for all leases with terms longer than 12 months. Leases will be classified as either finance or operating, with classification affecting the pattern of expense recognition in the income statement. The new standard is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. A modified retrospective transition approach is required for lessees for capital and operating leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements, with certain practical expedients available. As ChoiceOne owns most of its branch locations, the impact of this ASU is not expected to be material.

The FASB issued ASU No. 2016-13*, Financial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments*. This ASU provides financial statement users with more decision-useful information about the expected credit losses on financial instruments and other commitments to extend credit held by a reporting entity at each reporting date by replacing the incurred loss impairment methodology in current generally accepted

accounting principles (GAAP) with a methodology that reflects expected credit losses and requires consideration of a broader range of reasonable and supportable information to inform credit loss estimates. The new guidance attempts to reflect an entity's current estimate of all expected credit losses and broadens the information that an entity must consider in developing its expected credit loss estimate for assets measured either collectively or individually to include forecasted information, as well as past events and current conditions. There is no specified method for measuring expected credit losses, and an entity may apply methods that reasonably reflect its expectations of the credit loss estimate. Although an entity may still use its current systems and methods for recording the allowance for credit losses, under the new rules, the inputs used to record the allowance for credit losses generally will need to change to appropriately reflect an estimate of all expected credit losses and the use of reasonable and supportable forecasts. Additionally, credit losses on available-for-sale debt securities will have to be presented as an allowance rather than as a write-down. This ASU is effective for fiscal years beginning after December 15, 2019, and for interim periods within those years. Management is currently evaluating the impact of this new ASU on its consolidated financial statements.

Reclassifications

Certain amounts presented in prior year consolidated financial statements have been reclassified to conform to the current year's presentation.

Note 2 – Securities

The fair value of securities available for sale and the related gross unrealized gains and losses recognized in accumulated other comprehensive income (loss) at December 31 were as follows:

	2016			
(Dollars in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. Government and federal agency	$59,864	$ 34	$ (846)	$59,052
U.S. Treasury notes and bonds	4,111	—	(39)	4,072
State and municipal	89,169	748	(944)	88,973
Mortgage-backed	7,925	19	(155)	7,789
Corporate	7,069	12	(40)	7,041
Foreign debt	4,514	—	(114)	4,400
Equity securities	2,617	266	—	2,883
Asset-backed securities	182	—	(4)	178
Total	$175,451	$ 1,079	$ (2,142)	$174,388

	2015			
(Dollars in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. Government and federal agency	$57,406	$ 30	$ (229)	$57,207
U.S. Treasury notes and bonds	6,133	—	(33)	6,100
State and municipal	76,005	1,858	(109)	77,754
Mortgage-backed	6,989	26	(45)	6,970
Corporate	8,418	8	(39)	8,387
Foreign debt	1,000	—	(5)	995
Equity securities	2,279	174	—	2,453
Asset-backed securities	274	—	(4)	270
Total	$158,504	$ 2,096	$ (464)	$160,136

Information regarding sales of securities available for sale for the year ended December 31 follows:

(Dollars in thousands)

	2016	2015	2014
Proceeds from sales of securities	$15,317	$25,876	$24,766
Gross realized gains	312	261	341
Gross realized losses	0	0	30

Contractual maturities of securities available for sale at December 31, 2016 were as follows:

(Dollars in thousands)	Amortized Cost	Fair Value
Due within one year	$ 34,174	$ 33,879
Due after one year through five years	89,413	89,204
Due after five years through ten years	37,153	36,514
Due after ten years	4,168	4,119
Total debt securities	164,908	163,716
Mortgage-backed securities	7,925	7,789
Equity securities	2,883	2,883
Total	$ 175,716	$ 174,388

Various securities were pledged as collateral for securities sold under agreements to repurchase, advances from the Federal Home Loan Bank, and participation in a program that provided Community Reinvestment Act credits. The carrying amount of securities pledged as collateral at December 31 was as follows:

(Dollars in thousands)	2016	2015
Securities pledged for securities sold under agreements to repurchase	$ 13,186	$ 7,011
Securities pledged for advances from the Federal Home Loan Bank	—	24,199
Security pledged for Community Reinvestment Act credits	250	276
Total	$ 13,436	$ 31,486

The fair value of securities pledged to secure repurchase agreements may decline, and the Company may be required to provide additional collateral. The Company manages this risk by pledging securities with fair values in excess of the repurchase liability.

Securities with unrealized losses at year-end 2016 and 2015, aggregated by investment category and length of time the individual securities have been in an unrealized loss position, were as follows:

	2016					
	Less than 12 months		More than 12 months		Total	
(Dollars in thousands)	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses

U.S. Government and federal agency	$46,283	$ (846)	$—	$ —	$46,283	$ (846)
U.S. Treasury notes and bonds	4,072	(39)	—	—	4,072	(39)
State and municipal	47,832	(944)	—	—	47,832	(944)
Mortgage-backed	5,980	(150)	251	(5)	6,231	(155)
Corporate	2,838	(40)	—	—	2,838	(40)
Foreign debt	4,400	(114)	—	—	4,400	(114)
Asset-backed securities	—	—	178	(4)	178	(4)
Total temporarily impaired	$111,405	$ (2,133)	$429	$ (9)	$111,834	$ (2,142)

	2015					
	Less than 12 months		More than 12 months		Total	
(Dollars in thousands)	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
U.S. Government and federal agency	$38,567	$ (216)	$986	$ (13)	$39,553	$ (229)
U.S. Treasury notes and bonds	6,101	(33)	—	—	6,101	(33)
State and municipal	10,382	(69)	2,906	(40)	13,288	(109)
Mortgage-backed	4,459	(41)	382	(4)	4,841	(45)
Corporate	4,284	(33)	896	(6)	5,180	(39)
Foreign debt	995	(5)	—	—	995	(5)
Asset-backed securities	—	—	270	(4)	270	(4)
Total temporarily impaired	$64,788	$ (397)	$5,440	$ (67)	$70,228	$ (464)

ChoiceOne evaluates all securities on a quarterly basis to determine whether unrealized losses are temporary or other than temporary. Consideration is given to 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 the intent and ability of ChoiceOne to retain its investment in the issue for a period of time sufficient to allow for any anticipated recovery in fair value of amortized cost basis. Management believed that unrealized losses as of December 31, 2016 were temporary in nature and were caused primarily by changes in interest rates, increased credit spreads, and reduced market liquidity and were not caused by the credit status of the issuer. No other than temporary impairments were recorded in 2016 or 2015.

At December 31, 2016, there were 196 securities with an unrealized loss, compared to 82 securities with an unrealized loss as of December 31, 2015. The increase in the number of securities in an unrealized loss position was caused by higher interest rates at the end of 2016 compared to the end of 2015.

Note 3 – Loans and Allowance for Loan Losses

The Bank's loan portfolio as of December 31 was as follows:

(Dollars in thousands)

	2016	2015
Agricultural	$44,614	$40,232
Commercial and industrial	96,088	94,347
Consumer	21,596	20,090
Real estate - commercial	110,762	97,736
Real estate - construction	6,153	5,390
Real estate - residential	89,787	91,509
Loans, gross	369,000	349,304
Allowance for loan losses	(4,277)	(4,194)
Loans, net	$364,723	$345,110

ChoiceOne manages its credit risk through the use of its loan policy and its loan approval process and by monitoring of loan credit performance. The loan approval process for commercial loans involves individual and group approval authorities. Individual authority levels are based on the experience of the lender. Group authority approval levels can consist of an internal loan committee that includes the Bank's President or Senior Lender and other loan officers for loans that exceed individual approval levels, or a loan committee of the Board of Directors for larger commercial loans. Most consumer loans are approved by individual loan officers based on standardized underwriting criteria, with larger consumer loans subject to approval by the internal loan committee.

Ongoing credit review of commercial loans is the responsibility of the loan officers. ChoiceOne's internal credit committee meets at least monthly and reviews loans with payment issues and loans with a risk rating of 5, 6, or 7. Risk ratings of commercial loans are reviewed periodically and adjusted if needed. ChoiceOne's consumer loan portfolio is primarily monitored on an exception basis. Loans where payments are past due are turned over to the Bank's collection department, which works with the borrower to bring payments current or take other actions when necessary. In addition to internal reviews of credit performance, ChoiceOne contracts with a third party for independent loan review that monitors the loan approval process and the credit quality of the loan portfolio.

Activity in the allowance for loan losses and balances in the loan portfolio were as follows:

(Dollars in thousands)

	Agricultural	Commercial and Industrial	Consumer	Commercial Real Estate	Construction Real Estate	Residential Real Estate	Unallocated	Total
2016								
Allowance for Loan Losses								
Beginning balance	$ 420	$ 586	$ 297	$ 1,030	$ 46	$ 1,388	$ 427	$ 4,194
Charge-offs	—	(37)	(218)	—	—	(102)	—	(357)
Recoveries	—	31	149	89	—	171	—	440
Provision	13	108	77	319	16	(444)	(89)	—
Ending balance	$ 433	$ 688	$ 305	$ 1,438	$ 62	$ 1,013	$ 338	$ 4,277
Individually evaluated for impairment	$ 3	$ 11	$ 2	$ 91	$ —	$ 296	$ —	$ 403
Collectively evaluated for impairment	$ 430	$ 677	$ 303	$ 1,347	$ 62	$ 717	$ 338	$ 3,874
Loans								
Individually evaluated for impairment	$ 526	$ 301	$ 28	$ 1,073	$ —	$ 2,983		$ 4,911
Collectively evaluated for impairment	44,088	95,787	21,568	109,689	6,153	86,804		364,089
Ending balance	$ 44,614	$ 96,088	$ 21,596	$ 110,762	$ 6,153	$ 89,787		$ 369,000

(Dollars in thousands)

	Agricultural	Commercial and Industrial	Consumer	Commercial Real Estate	Construction Real Estate	Residential Real Estate	Unallocated	Total
2015								
Allowance for Loan Losses								
Beginning balance	$ 186	$ 527	$ 184	$ 1,641	$ 9	$ 1,193	$ 433	$ 4,173
Charge-offs	—	(30)	(291)	—	—	(140)	—	(461)
Recoveries	1	64	121	47	—	149	—	382
Provision	233	25	283	(658)	37	186	(6)	100
Ending balance	$ 420	$ 586	$ 297	$ 1,030	$ 46	$ 1,388	$ 427	$ 4,194
Individually evaluated for impairment	$ 3	$ 15	$ 1	$ 191	$ —	$ 296	$ —	$ 506

Collectively evaluated for impairment	$ 417	$ 571	$ 296	$ 839	$ 46	$ 1,092	$ 427	$ 3,688
Loans								
Individually evaluated for impairment	$ 50	$ 192	$ 24	$ 2,790	$ —	$ 2,529		$ 5,585
Collectively evaluated for impairment	40,182	94,155	20,066	94,946	5,390	88,980		343,719
Ending balance	$ 40,232	$ 94,347	$ 20,090	$ 97,736	$ 5,390	$ 91,509		$ 349,304

(Dollars in thousands)

	Agricultural	Commercial and Industrial	Consumer	Commercial Real Estate	Construction Real Estate	Residential Real Estate	Unallocated	Total
2014								
Allowance for Loan Losses								
Beginning balance	$ 178	$ 562	$ 192	$ 1,842	$ 12	$ 1,626	$ 323	$ 4,735
Charge-offs	—	(1)	(273)	(665)	—	(133)	—	(1,072)
Recoveries	20	119	179	48	—	44	—	410
Provision	(12)	(153)	86	416	(3)	(344)	110	100
Ending balance	$ 186	$ 527	$ 184	$ 1,641	$ 9	$ 1,193	$ 433	$ 4,173
Individually evaluated for impairment	$ —	$ —	$ 4	$ 745	$ —	$ 365	$ —	$ 1,114
Collectively evaluated for impairment	$ 186	$ 527	$ 180	$ 896	$ 9	$ 828	$ 433	$ 3,059
Loans								
Individually evaluated for impairment	$ —	$ 38	$ 36	$ 3,853	$ —	$ 2,958		$ 6,885
Collectively evaluated for impairment	41,098	88,024	20,716	95,954	2,691	90,745		339,228
Ending balance	$ 41,098	$ 88,062	$ 20,752	$ 99,807	$ 2,691	$ 93,703		$ 346,113

The process to monitor the credit quality of ChoiceOne's loan portfolio includes tracking (1) the risk ratings of business loans, (2) the level of classified business loans, and (3) delinquent and nonperforming consumer loans. Business loans are risk rated on a scale of 1 to 8. A description of the characteristics of the ratings follows:

Risk ratings 1 and 2: These loans are considered pass credits. They exhibit good to exceptional credit risk and demonstrate the ability to repay the loan from normal business operations.

Risk rating 3: These loans are considered pass credits. They exhibit acceptable credit risk and demonstrate the ability to repay the loan from normal business operations.

Risk rating 4: These loans are considered watch credits. They have potential developing weaknesses that, if not corrected, may cause deterioration in the ability of the borrower to repay the loan. While a loss is possible for a loan with this rating, it is not anticipated.

Risk rating 5: These loans are considered special mention credits. Loans in this risk rating are considered to be inadequately protected by the net worth and debt service coverage of the borrower or of any pledged collateral. These loans have well defined weaknesses that may jeopardize the borrower's ability to repay the loan. If the weaknesses are not corrected, loss of principal and interest could be probable.

Risk rating 6: These loans are considered substandard credits. These loans have well defined weaknesses, the severity of which makes collection of principal and interest in full questionable. Loans in this category may be placed on nonaccrual status.

Risk rating 7: These loans are considered doubtful credits. Some loss of principal and interest has been determined to be probable. The estimate of the amount of loss could be affected by factors such as the borrower's ability to provide additional capital or collateral. Loans in this category are on nonaccrual status.

Risk rating 8: These loans are considered loss credits. They are considered uncollectible and will be charged off against the allowance for loan losses.

Information regarding the Bank's credit exposure as of December 31 was as follows:

Corporate Credit Exposure - Credit Risk Profile By Creditworthiness Category

(Dollars in thousands)	Agricultural		Commercial and Industrial		Commercial Real Estate	
	2016	2015	2016	2015	2016	2015
Risk ratings 1 and 2	$12,005	$10,416	$12,135	$10,480	$8,013	$3,875
Risk rating 3	23,852	25,189	56,714	66,921	59,343	57,540
Risk rating 4	7,505	3,086	25,895	16,169	39,641	29,826
Risk rating 5	726	1,491	1,267	574	1,867	3,776
Risk rating 6	526	50	77	129	1,898	2,719
Risk rating 7	—	—	—	74	—	—
	$44,614	$40,232	$96,088	$94,347	$110,762	$97,736

Consumer Credit Exposure - Credit Risk Profile Based On Payment Activity

(Dollars in thousands)	Consumer		Construction Real Estate		Residential Real Estate	
	2016	2015	2016	2015	2016	2015
Performing	$21,590	$20,090	$6,153	$5,390	$88,767	$90,796
Nonperforming	—	—	—	—	229	282
Nonaccrual	6	—	—	—	791	431
	$21,596	$20,090	$6,153	$5,390	$89,787	$91,509

Included within the loan categories above were loans in the process of foreclosure. As of December 31, 2016, and 2015 loans in the process of foreclosure totaled $282,000 and $13,000, respectively.

The following schedule provides information on loans that were considered troubled debt restructurings ("TDRs") that were modified during the twelve months ended December 31, 2016 and December 31, 2015:

(Dollars in thousands)	December 31, 2016			December 31, 2015		
	Number of Loans	Pre-Modification Outstanding Recorded	Post-Modification Outstanding Recorded	Number of Loans	Pre-Modification Outstanding Recorded	Post-Modification Outstanding Recorded

		Investment	Investment		Investment	Investment
Agricultural	1	$ 105	$ 105	—	$ —	$ —
Commercial and industrial	—	—	—	—	—	—
Consumer	—	—	—	—	—	—
Commercial real estate	—	—	—	4	439	439
Residential real estate	2	155	155	2	195	195
	3	$ 260	$ 260	6	$ 634	$ 634

The pre-modification and post-modification outstanding recorded investment represents amounts as of the date of loan modification. If a difference exists between the pre-modification and post-modification outstanding recorded investment, it represents impairment recognized through the provision for loan losses computed based on a loan's post-modification present value of expected future cash flows discounted at the loan's original effective interest rate. If no difference exists, a loss is not expected to be incurred based on an assessment of the borrower's expected cash flows.

The following schedule provides information on TDRs as of December 31, 2016 and December 31, 2015 where the borrower was past due with respect to principal and/or interest for 30 days or more during the twelve months ended December 31, 2016 and December 31, 2015 that had been modified during the 12-month period prior to the default:

	With Payment Defaults During the Following Periods			
	December 31, 2016		December 31, 2015	
(Dollars in thousands)	Number of Loans	Recorded Investment	Number of Loans	Recorded Investment
Agricultural	—	$ —	—	$ —
Commercial and industrial	—	—	—	—
Consumer	—	—	—	—
Commercial real estate	1	105	3	400
Residential real estate	—	—	—	—
	1	$ 105	3	$ 400

Loans are classified as performing when they are current as to principal and interest payments or are past due on payments less than 90 days. Loans are classified as nonperforming when they are past due 90 days or more as to principal and interest payments or are considered a troubled debt restructuring.

Impaired loans by loan category as of December 31 were as follows:

(Dollars in thousands)	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
2016					
With no related allowance recorded					
Agricultural	$ 482	$ 485	$ —	$ 220	$ 13
Commercial and industrial	206	207	—	91	3
Consumer	—	—	—	1	—
Commercial real estate	342	939	—	925	2
Residential real estate	301	292	—	167	5
Subtotal	1,331	1,923	—	1,404	23
With an allowance recorded					
Agricultural	44	44	3	72	3
Commercial and industrial	95	95	11	218	—
Consumer	28	28	2	24	2
Commercial real estate	731	804	91	1,281	33
Residential real estate	2,682	2,711	296	2,672	108
Subtotal	3,580	3,682	403	4,267	146
Total					
Agricultural	526	529	3	292	16
Commercial and industrial	301	302	11	309	3
Consumer	28	28	2	25	2
Commercial real estate	1,073	1,743	91	2,206	35
Residential real estate	2,983	3,003	296	2,839	113
Total	$ 4,911	$ 5,605	$ 403	$ 5,671	$ 169

(Dollars in thousands)	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
2015					
With no related allowance recorded					
Agricultural	$ —	$ —	$ —	$ —	$ —
Commercial and industrial	74	103	—	25	—
Consumer	—	—	—	2	—
Commercial real estate	1,540	1,540	—	1,061	11
Residential real estate	13	13	—	191	—
Subtotal	1,627	1,656	—	1,279	11
With an allowance recorded					
Agricultural	50	50	3	62	(6)
Commercial and industrial	118	118	15	44	1
Consumer	24	24	1	34	3
Commercial real estate	1,250	1,755	191	2,002	64

Residential real estate	2,516	2,516	296	2,425	86
Subtotal	3,958	4,463	506	4,567	148
Total					
Agricultural	50	50	3	62	(6)
Commercial and industrial	192	221	15	69	1
Consumer	24	24	1	36	3
Commercial real estate	2,790	3,295	191	3,063	75
Residential real estate	2,529	2,529	296	2,616	86
Total	$ 5,585	$ 6,119	$ 506	$ 5,846	$ 159

(Dollars in thousands)	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
2014					
With no related allowance recorded					
Agricultural	$ —	$ —	$ —	$ 90	$ —
Commercial and industrial	38	43	—	81	—
Consumer	8	8	—	3	—
Commercial real estate	413	419	—	352	6
Residential real estate	502	502	—	492	9
Subtotal	961	972	—	1,018	15
With an allowance recorded					
Agricultural	—	—	—	130	—
Commercial and industrial	—	—	—	292	4
Consumer	28	28	4	31	3
Commercial real estate	3,440	4,498	745	3,932	81
Residential real estate	2,456	2,474	365	2,323	91
Subtotal	5,924	7,000	1,114	6,708	179
Total					
Agricultural	—	—	—	220	—
Commercial and industrial	38	43	—	373	4
Consumer	36	36	4	34	3
Commercial real estate	3,853	4,917	745	4,284	87
Residential real estate	2,958	2,976	365	2,815	100
Total	$ 6,885	$ 7,972	$ 1,114	$ 7,726	$ 194

An aging analysis of loans by loan category as of December 31 follows:

(Dollars in thousands)	Loans Past Due 30 to 59 Days (1)	Loans Past Due 60 to 89 Days (1)	Loans Past Due Greater Than 90 Days (1)	Total (1)	Loans Not Past Due	Total Loans	Loans 90 Days Past Due and Accruing
2016							
Agricultural	$—	$ —	$—	$—	$44,614	$44,614	$ —
Commercial and industrial	—	30	245	275	95,813	96,088	—
Consumer	99	2	6	107	21,489	21,596	—
Commercial real estate	—	—	260	260	110,502	110,762	—
Construction real estate	—	—	—	—	6,153	6,153	—

Residential real estate	1,027	109	646	1,782	88,005	89,787	229
	$1,126	$141	$1,157	$2,424	$366,576	$369,000	$ 229
2015							
Agricultural	$3	$—	$—	$3	$40,229	$40,232	$ —
Commercial and industrial	90	322	77	489	93,858	94,347	—
Consumer	115	—	—	115	19,975	20,090	—
Commercial real estate	505	297	1,233	2,035	95,701	97,736	—
Construction real estate	299	—	—	299	5,091	5,390	—
Residential real estate	1,012	364	200	1,576	89,933	91,509	29
	$2,024	$983	$1,510	$4,517	$344,787	$349,304	$ 29

(1) Includes nonaccrual loans.

Nonaccrual loans by loan category as of December 31 follow:

(Dollars in thousands)

	2016	2015
Agricultural	$482	$50
Commercial and industrial	245	77
Consumer	6	—
Commercial real estate	458	1,640
Construction real estate	—	—
Residential real estate	792	431
	$1,983	$2,198

Note 4 – Mortgage Banking

Activity in secondary market loans during the year was as follows:

(Dollars in thousands)

	2016	2015	2014
Loans originated for resale, net of principal payments	$53,591	$47,498	$29,850
Proceeds from loan sales	57,830	46,077	29,561
Net gains on sales of loans held for sale	1,748	1,416	1,023
Loan servicing fees, net of amortization	159	113	166

Net gains on sales of loans held for sale include capitalization of loan servicing rights. Loans serviced for others are not reported as assets in the accompanying consolidated balance sheets. The unpaid principal balances of these loans were $103.6 million and $79.4 million at December 31, 2016 and 2015, respectively. The Bank maintains custodial escrow balances in connection with these serviced loans; however, such escrows were immaterial at December 31, 2016 and 2015.

Activity for loan servicing rights (included in other assets) was as follows:

(Dollars in thousands)

	2016	2015	2014
Balance, beginning of year	$378	$489	$544
Capitalized	491	49	73
Amortization	(172)	(160)	(128)

Balance, end of year	$698	$378	$489

The fair value of loan servicing rights was $1,029,000 and $739,000 as of December 31, 2016 and 2015, respectively. Consequently, a valuation allowance was not necessary at year-end 2016 or 2015. The fair value of servicing rights at December 31, 2016 was determined using a discount rate of 5.82% and prepayment speeds ranging from 10% to 19%. The fair value of servicing rights at December 31, 2015 was determined using a discount rate of 6.37% and prepayment speeds ranging from 9% to 13%.

Note 5 – Premises and Equipment

As of December 31, premises and equipment consisted of the following:

(Dollars in thousands)

	2016	2015
Land and land improvements	$5,869	$4,529
Leasehold improvements	38	38
Buildings	12,052	12,076
Furniture and equipment	5,394	5,322
Total cost	23,353	21,965
Accumulated depreciation	(10,765)	(10,118)
Premises and equipment, net	$12,588	$11,847

Depreciation expense was $1,078,000, $986,000, and $986,000 for 2016, 2015 and 2014, respectively.

The Bank leases certain branch properties, a loan production office, and automated-teller machine locations in its normal course of business. Rent expense totaled $99,000, $53,000, and $52,000 for 2016, 2015 and 2014, respectively. Rent commitments under non-cancelable operating leases were as follows, before considering renewal options that generally are present:

(Dollars in thousands)

2017	$69
2018	71
2019	59
2020	18
2021	19
Thereafter	72
Total	$308

Note 6 - Goodwill and Intangible Assets

Goodwill

There were no changes in the goodwill balance in 2016 or 2015. ChoiceOne evaluates goodwill annually for impairment. Recently issued accounting pronouncements allow a company to first perform a qualitative assessment for goodwill prior to a quantitative assessment (Step 1 assessment). If the results of the qualitative assessment indicate that it is more likely than not that goodwill is impaired, then a quantitative assessment must be performed. If not, there is no further assessment required.

ChoiceOne engaged an outside consulting firm to assist management in performing its annual evaluation of goodwill for impairment as of June 30, 2016. The following steps were used in the valuation: determination of the reporting unit, determination of the appropriate standard of value, determination of the appropriate level of value, calculation of fair value, and comparison of the fair value computed to the equity carrying value. It was determined that the relevant reporting unit to be valued was ChoiceOne Bank. The standard of value used in the valuation was fair value as determined by generally accepted accounting principles. The appropriate level of value was determined to be the controlling interest level. The appraisal methodology used to calculate the fair value included the income approach, which was a discounted cash flow value based on projected earnings capacity. The income approach used a discount rate of 11.50%, a growth assumption of 5.0% for assets, and an assumption of cost savings of 20% of noninterest expense as a result of synergies and cost reductions from a change in control. The appraisal methodology also included the market approach, which was based on price-to-earnings multiples, price-to-tangible book value ratios, and core deposit premiums for selected bank sale transactions. The asset approach was also an approach that was reviewed, but it was not used in determining the fair value since it did not render a control level indication of value. The results from the valuation approaches were used to calculate an estimate of the fair value of ChoiceOne's equity,

which was compared to the carrying value of equity to determine whether the Step 1 test under generally accepted accounting principles that govern the valuation of goodwill was passed. The goodwill analysis determined that the fair value of ChoiceOne's equity exceeded the carrying value by 31%. Based on this assessment, management believed that there was no indication of goodwill impairment at June 30, 2016. Based on the testing performed and a review of factors that might impact ChoiceOne's stock value subsequent to this evaluation, no impairment of goodwill was deemed to exist as of December 31, 2016.

Management performed a qualitative assessment of goodwill as of June 30, 2015 and December 31, 2015. The analysis was performed including evaluation of the share price, book value, and financial results of ChoiceOne as compared to the previous year. Additionally, industry and market conditions were evaluated. Average deal prices during 2015 in the Midwest of closed transactions indicated increases in deal values to tangible common equity, deal values to earnings, and core deposit premiums when compared to the observed prices used in the prior quantitative assessment of goodwill in 2012. Further, macro-economic trends were on a positive trajectory during 2015 and there had been no adverse legal, regulatory, contractual, political or other factors that materially impacted ChoiceOne. Upon completion of the qualitative assessment, ChoiceOne believed that it is more likely than not that the fair value of ChoiceOne's equity exceeded the carrying value at the assessment date and there was no further quantitative assessment necessary for 2015.

Acquired Intangible Assets

Information for acquired intangible assets at December 31 follows:

	2016		2015	
(Dollars in thousands)	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
Core deposit intangible	$4,134	$ 4,134	$4,134	$ 3,790
Other intangible assets	348	348	348	313
Totals	$4,482	$ 4,482	$4,482	$ 4,103

The core deposit intangible and other intangible assets were being amortized on a straight-line basis over ten years. Intangible assets are reviewed for impairment on a quarterly basis. No impairment was indicated as of December 31, 2015. These intangible assets were fully amortized as of the end of 2016 and will have no carrying value on the balance sheet going forward. Aggregate amortization expense was $379,000 in 2016 and $448,000 in 2015 and 2014.

Note 7 – Other Real Estate Owned

Other real estate owned represents residential and commercial properties primarily owned as a result of loan collection activities and is reported net of a valuation allowance. Activity within other real estate owned was as follows:

(Dollars in thousands)	2016	2015	2014
Balance, beginning of year	$31	$150	$508
Transfers from loans	661	408	561
Proceeds from sales	(247)	(406)	(789)
Gains/(losses) on sales	(8)	(30)	24
Write-downs	—	(91)	(154)
Balance, end of year	$437	$31	$150

Included in the balances above were residential real estate mortgage loans of $291,000, $31,000, and $54,000 as of December 31, 2016, 2015, and 2014, respectively.

Note 8 – Deposits

Deposit balances as of December 31 consisted of the following:

(Dollars in thousands)	2016	2015
Noninterest-bearing demand deposits	$127,611	$122,937
Interest-bearing demand deposits	122,465	106,882
Money market deposits	99,454	86,987
Savings deposits	75,835	70,946
Local certificates of deposit	79,108	86,944
Brokered certificates of deposit	7,913	—
Total deposits	$512,386	$474,696

Scheduled maturities of certificates of deposit at December 31, 2016 were as follows:

(Dollars in thousands)

2017	$54,111
2018	17,778
2019	7,401
2020	7,627
2021	104
Total	$87,021

The Bank had certificates of deposit issued in denominations of $250,000 or greater totaling $22.2 million and $21.4 million at December 31, 2016 and 2015, respectively. The Bank held $7.9 million in brokered certificates of deposit at December 31, 2016 as brokered rates became competitive with other wholesale funding channels. In addition, the Bank had $2.0 million of certificates of deposit as of December 31, 2016 and $2.1 million as of December 31, 2015 that had been issued through the Certificate of Deposit Account Registry Service (CDARS). Although certificates of deposit issued through CDARS are issued to local customers, this type of deposit is classified as brokered deposits for regulatory purposes.

Note 9 – Repurchase Agreements

Securities sold under agreements to repurchase are advances to the Bank by customers or another bank. These agreements are direct obligations of the Bank and are secured by securities held in safekeeping at a correspondent bank. Repurchase agreements with Bank customers mature daily. Information regarding repurchase agreements follows:

(Dollars in thousands)	2016	2015
Outstanding balance at December 31	$7,913	$9,460
Average interest rate at December 31	0.05 %	0.04 %
Average balance during the year	$7,762	$17,825
Average interest rate during the year	0.05 %	0.17 %
Maximum month end balance during the year	$10,539	$26,743

Repurchase agreements accounted for as secured borrowings as of December 31, 2016 were as follows:

(Dollars in thousands)	Remaining Contractual Maturity of the Agreements Overnight and Continuous
U.S. Government agencies	$ 13,186
Total securities	13,186
Unsecured borrowings	—
Total borrowings	$ 13,186

Note 10 – Federal Home Loan Bank Advances

At December 31, advances from the FHLB were as follows:

(Dollars in thousands)	2016	2015

Maturity of November 2024 with fixed interest rate of 3.98%	$301	$332
Maturities ranging from January 2017 to March 2017, fixed interest rates ranging from 0.81% to 0.88%, with an average of 0.86%	12,000	—
Maturity of February 2016 with fixed interest rate of 0.47%		11,000
Total advances outstanding at year-end	$12,301	$11,332

Fees are charged on fixed rate advances that are paid prior to maturity. No fixed rate advances were paid prior to maturity in 2016 or 2015. Advances were secured by agricultural loans and residential real estate loans with a carrying value of approximately $92.3 million and $107.6 million at December 31, 2016 and December 31, 2015, respectively. Advances were also secured by $24.2 million of U.S. Government agency securities and U.S. Treasury securities at December 31, 2015. Based on this collateral, the Bank was eligible to borrow an additional $41.7 million at year-end 2016.

The scheduled maturities of advances from the FHLB at December 31, 2016 were as follows:

(Dollars in thousands)	
2017	$12,033
2018	34
2019	36
2020	37
2021	39
Thereafter	122
Total	$12,301

Note 11 – Income Taxes

Information as of December 31 and for the year follows:

(Dollars in thousands)

	2016	2015	2014
Provision for Income Taxes			
Current federal income tax expense	$2,244	$2,576	$2,536
Deferred federal income tax expense/(benefit)	(82)	(631)	(460)
Income tax expense	$2,162	$1,945	$2,076
Reconciliation of Income Tax Provision to Statutory Rate			
Income tax computed at statutory federal rate of 34%	$2,806	$2,614	$2,642
Tax exempt interest income	(496)	(488)	(475)
Tax exempt earnings on bank-owned life insurance	(121)	(221)	(103)
Other items	(27)	40	12
Income tax expense	$2,162	$1,945	$2,076
Effective income tax rate	26 %	25 %	27 %

(Dollars in thousands)

Components of Deferred Tax Assets and Liabilities	2016	2015
Deferred tax assets:		
Allowance for loan losses	$1,454	$1,426
Unrealized losses on securities available for sale	361	—
Deferred compensation	232	269
Loan costs/fees deferred	84	86
Other	339	181
Total deferred tax assets	2,470	1,962
Deferred tax liabilities:		
Depreciation	1,181	1,182
Loan servicing rights	238	129
Post-retirement benefits obligation	53	65
Unrealized gains on securities available for sale	—	555
Purchase accounting adjustments from merger	—	117
Other	190	117
Total deferred tax liabilities	1,662	2,165
Net deferred tax asset/(liability)	$808	$(203)

Note 12 – Related Party Transactions

Loans to executive officers, directors and their affiliates were as follows at December 31:

(Dollars in thousands)	2016	2015
Balance, beginning of year	$10,234	$10,339
New loans	6,797	4,054
Repayments	(4,125)	(4,159)
Effect of changes in related parties	—	—
Balance, end of year	$12,906	$10,234

Deposits from executive officers, directors and their affiliates were $14.7 million and $16.1 million at December 31, 2016 and 2015, respectively.

Note 13 – Employee Benefit Plans

401(k) Plan:

The 401(k) plan allows employees to contribute to their individual accounts under the plan amounts up to the IRS maximum. Matching company contributions to the plan are discretionary. Expense for matching company contributions under the plan was $180,000, $168,000, and $140,000 in 2016, 2015, and 2014, respectively.

Employee Stock Ownership Plan:

Through December 31, 2015, employees participated in an Employee Stock Ownership Plan (“ESOP”). ChoiceOne could make discretionary contributions to the ESOP. Shares of ChoiceOne common stock were allocated to participants based on relative compensation earned and compensation expense was recorded when allocated. Dividends on allocated shares increased the participant accounts. Participants became fully vested upon completing six years of qualifying service. Participants received the shares at the end of employment. A participant could require stock received to be repurchased by ChoiceOne at any time. ChoiceOne did not contribute to the ESOP nor was any expense recorded in 2016, 2015, or 2014. Effective January 1, 2016, ChoiceOne terminated the ESOP and transferred shares held by the ESOP to the 401(k) plan and ChoiceOne no longer has a mandatory obligation to repurchase shares from the 401(k) plan.

Shares held by the ESOP as of December 31 were as follows:

(Dollars in thousands)	2016	2015	2014
Shares allocated to participants	—	5,355	5,355
Shares unallocated	—	—	—
Total shares of ChoiceOne stock held by ESOP	—	5,355	5,355
Fair value of allocated shares, subject to repurchase obligation, recorded in other liabilities	$ —	$127	$123

Post-retirement Benefits Plan:

ChoiceOne maintains an unfunded post-retirement health care plan, which permits employees (and their dependents) the ability to participate upon retirement from ChoiceOne. ChoiceOne does not pay any portion of the health care premiums charged to its retired participants. A liability has been accrued for the obligation under this plan. ChoiceOne incurred a negative post-retirement benefit expense of $18,000 in 2016, a benefit expense of $2,000 in 2015, and a negative expense of $20,000 in 2014. The post-retirement obligation liability was $148,000 as of December 31, 2016 and $127,000 as of December 31, 2015.

Deferred Compensation Plans:

A deferred director compensation plan covers certain former directors. Under the plan, ChoiceOne pays each former director the amount of director fees deferred plus interest at rates ranging from 5.50% to 5.84% over various periods as elected by each director. The payout periods range from one month to ten years beginning with the individual's termination of service. A liability has been accrued for the obligation under this plan. ChoiceOne incurred deferred compensation plan expense of $7,000, $12,000, and $12,000 in 2016, 2015, and 2014, respectively. The deferred compensation liability was $138,000 as of December 31, 2016 and $173,000 as of December 31, 2015.

A supplemental executive retirement plan covers four former executive officers. Under the plan, ChoiceOne pays these individuals a specific amount of compensation plus interest at 7.50% over a 15-year period commencing upon early retirement age (as defined in the plan) or normal retirement age (as defined in the plan). A liability has been accrued for the obligation under this plan. The effective interest rate used for the accrual for the retirement liability is based on long-term interest rates. Slightly higher long-term interest rates during 2016 caused a slight decrease in plan expense in 2016 and in 2015. ChoiceOne incurred deferred compensation plan expense of $19,000 in 2016 and $32,000 in 2015 and a negative expense of $42,000 in 2014. Liabilities related to the supplemental executive retirement plan of $558,000 and $618,000 were outstanding as of December 31, 2016 and December 31, 2015, respectively.

Note 14 - Stock Based Compensation

Options to buy stock have been granted to key employees under an incentive stock option plan to provide them with additional equity interests in ChoiceOne. Compensation expense in connection with stock options granted during 2016, 2015, or 2014 was $71,000 in 2016 and $0 in 2015 and 2014. The Amended and Restated Executive Stock Incentive Plan under which the stock options were granted expired in 2012. The Stock Incentive Plan of 2012 was approved by the Company's shareholders at the Annual Meeting held on April 25, 2012. The new plan provides for the issuance of up to 100,000 shares of common stock. At December 31, 2016, there were 40,750 shares available for future grants.

	2016		2015		2014	
	Shares	Weighted average exercise price	Shares	Weighted average exercise price	Shares	Weighted average exercise price
Options outstanding, beginning of year	40,750	$ 21.69	20,250	$ 16.65	38,625	$ 17.29
Options granted	—	—	30,000	23.30	—	—
Options exercised	8,000	17.95	9,500	16.03	14,550	18.87
Options forfeited or expired	750	18.85	—	—	3,825	18.51
Options outstanding, end of year	32,000	$ 22.69	40,750	$ 21.69	20,250	$ 16.65
Options exercisable at December 31	22,000	$ 22.69	18,250	$ 19.70	20,250	$ 16.65

The exercise prices for options outstanding and exercisable at the end of 2016 ranged from $13.50 to $23.30 per share. The weighted average remaining contractual life of options outstanding and exercisable at the end of 2016 was approximately 8.4 years.

The intrinsic value of all outstanding in-the-money stock options and exercisable in-the-money stock options was $34,000 and $29,000 respectively, at December 31, 2016. The aggregate intrinsic values of outstanding and exercisable options at December 31, 2016 were calculated based on the closing market price of the Company's common stock on December 31, 2016 of $23.75 per share less the exercise price.

Information pertaining to options outstanding at December 31, 2016 is as follows:

Exercise price of stock options:	Number of options outstanding at year-end	Number of options exercisable at year-end	Average remaining contractual life (in years)
$ 13.50	2,000	2,000	1.08
$ 23.30	30,000	20,000	9.09

The fair value of each option award is estimated on the date of grant using a Black-Scholes option valuation model. ChoiceOne uses historical data to estimate the volatility of the market price of ChoiceOne stock and employee terminations within the valuation model. The risk-free rate for periods within the contractual life of the option is based on the U.S. Treasury yield curve in effect at the time of grant. No options were granted in 2016 or 2014. As of December 31, 2016 there was $35,000 in unrecognized compensation expense related to stock options issued in 2015.

The fair value of stock options granted during 2015 was $106,000; determined using the following weighted-average assumptions as of the grant date.

	2015	
Risk-free interest rate	2.28	%
Expected option life	5.75 years	
Expected stock price volatility	22.95	%
Dividend yield	3.64	%
Fair value of options granted	$3.54	

ChoiceOne has granted restricted stock units to a select group of employees under the Stock Incentive Plan of 2012. Restricted stock units vest in three annual installments on each of the next three anniversaries of the grant date. Certain additional vesting provisions apply. Each restricted stock unit, once vested, is settled by delivery of one share of ChoiceOne common stock. ChoiceOne recognized compensation expense of $207,000 and $103,000 in 2016 and 2015, respectively, in connection with restricted stock units for current participants during these years. At December 31, 2016, there were 14,933 restricted stock units outstanding with an approximate stock value of $355,000 based on ChoiceOne's December 31, 2016 stock price. At December 31, 2015, there were 17,850 restricted stock units outstanding with an approximate stock value of $425,000. Unrecognized compensation expense as of December 31, 2016, and based on the stock price at time of award was approximately $241,000 and will be allocated $139,000 to 2017, $79,000 to 2018 and $23,000 in 2019.

Note 15 - Earnings Per Share

(Dollars in thousands, except per share data)	2016	2015	2014
Basic			
Net income	$6,090	$5,743	$5,695
Weighted average common shares outstanding	3,287,109	3,289,296	3,298,177
Basic earnings per common shares	$1.85	$1.75	$1.73
Diluted			
Net income	$6,090	$5,743	$5,695
Weighted average common shares outstanding	3,287,109	3,289,296	3,298,177
Plus dilutive stock options and restricted stock units	4,972	7,925	12,116
Weighted average common shares outstanding and potentially dilutive shares	3,292,081	3,297,221	3,310,293

Diluted earnings per common share	$1.85	$1.74	$1.72

There were 30,000 stock options that were considered anti-dilutive to earnings per share as of December 31, 2016 and thus have been excluded from the calculations above. There were 30,000 stock options that were considered anti-dilutive to earnings per share as of December 31, 2015, and there were no stock options as of December 31, 2014 considered to be anti-dilutive to earnings per share.

Note 16 – Condensed Financial Statements of Parent Company

Condensed Balance Sheets

(Dollars in thousands)	December 31,	
	2016	2015
Assets		
Cash	$516	$1,145
Securities available for sale	3,406	2,263
Other assets	151	83
Investment in ChoiceOne Bank	67,698	66,539
Total assets	$71,771	$70,030
Liabilities		
Mandatory redeemable shares under ESOP, at fair value	$—	$127
Other liabilities	73	61
Total liabilities	73	188
Shareholders' equity	71,698	69,842
Total liabilities and shareholders' equity	$71,771	$70,030

Condensed Statements of Income

(Dollars in thousands)	Years Ended December 31,		
	2016	2015	2014
Interest and dividends from ChoiceOne Bank	$3,161	$3,579	$2,731
Interest and dividends from other securities	52	26	16
Other income	—	—	27
Total income	3,213	3,605	2,774
Other expenses	133	137	92
Income before income tax and equity in undistributed net income of subsidiary	3,080	3,468	2,682
Income tax benefit	39	44	21
Income before equity in undistributed net income of subsidiary	3,119	3,512	2,703
Equity in undistributed net income of subsidiary	2,971	2,231	2,992
Net income	$6,090	$5,743	$5,695

Condensed Statements of Cash Flows
(Dollars in thousands)

	Years Ended December 31,		
	2016	2015	2014
Cash flows from operating activities:			
Net income	$6,090	$5,743	$5,695
Adjustments to reconcile net income to net cash from operating activities:			
Equity in undistributed net income of subsidiary	(2,971)	(2,231)	(2,992)
Amortization	20	11	3
Net expense of restricted stock units	367	103	48
Net gain on sale of securities	—	—	(26)
Changes in other assets	(68)	71	(125)
Changes in other liabilities	(1)	4	(35)
Net cash from operating activities	3,437	3,701	2,568
Cash flows from investing activities:			
Sales of securities	—	—	1,184
Purchases of securities	(1,126)	(1,029)	(1,565)
Net cash from investing activities	(1,126)	(1,029)	(381)
Cash flows from financing activities:			
Cash proceeds from the issuance of common stock	85	206	132
Repurchase of common stock	(794)	(371)	(203)
Cash dividends paid	(2,231)	(2,170)	(1,945)
Net cash from financing activities	(2,940)	(2,335)	(2,016)
Net change in cash	(629)	337	171
Beginning cash	1,145	808	637
Ending cash	$516	$1,145	$808

Note 17 – Financial Instruments

Financial instruments as of the dates indicated were as follows:

(Dollars in thousands)	Carrying Amount	Estimated Fair Value	Quoted Prices In Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
December 31, 2016					
Assets					
Cash and due from banks	$ 14,809	$ 14,809	$ 14,809	$ —	$ —
Securities available for sale	174,388	174,388	1,383	157,902	15,103
Federal Home Loan Bank and Federal Reserve Bank stock	3,567	3,567	—	3,567	—
Loans held for sale	1,974	2,044	—	2,044	—
Loans, net	364,723	365,780	—	—	365,780
Liabilities					
Noninterest-bearing deposits	127,611	127,611	—	127,611	—
Interest-bearing deposits	384,775	383,879	—	383,879	—
Repurchase agreements	7,913	7,913	—	7,913	—
Federal Home Loan Bank advances	12,301	12,323	—	12,323	—
December 31, 2015					
Assets					
Cash and due from banks	$ 11,187	$ 11,187	$ 11,187	$ —	$ —
Securities available for sale	160,136	160,136	953	147,384	11,799
Federal Home Loan Bank and Federal Reserve Bank stock	3,187	3,187	—	3,187	—
Loans held for sale	4,957	5,109	—	5,109	—
Loans, net	345,110	349,875	—	—	349,875
Liabilities					
Noninterest-bearing deposits	122,937	122,937	—	122,937	—
Interest-bearing deposits	351,759	353,113	—	353,113	—
Repurchase agreements	9,460	9,460	—	9,460	—
Federal Home Loan Bank advances	11,332	12,028	—	12,028	—

The estimated fair values approximate the carrying amounts for all financial instruments except those described later in this paragraph. The methodology for determining the estimated fair value for securities available for sale is described in Note 18. The estimated fair value for loans is based on the rates charged at December 31 for new loans with similar maturities, applied until the loan is assumed to reprice or be paid. The allowance for loan losses is considered to be a reasonable estimate of discount for credit quality concerns. The estimated fair value of deposits is based on comparing the average rate paid on deposits compared to the three month Libor rate which is assumed to be the replacement value of these deposits. At December 31, 2016, all average rates were lower than the three month Libor rate causing fair values to be higher than carrying amounts. The estimated fair values for time deposits and FHLB advances are based on the rates paid at December 31 for new deposits or FHLB advances, applied until maturity. The estimated fair values for other financial instruments and off-balance sheet loan commitments are considered nominal.

Note 18 – Fair Value Measurements

The following tables present information about the Bank's assets and liabilities measured at fair value on a recurring basis at December 31, 2016 and December 31, 2015, and the valuation techniques used by the Bank to determine those fair values.

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

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

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

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

There were no liabilities measured at fair value as of December 31, 2015 or December 31, 2016. Disclosures concerning assets measured at fair value are as follows:

Assets Measured at Fair Value on a Recurring Basis

	Quoted Prices In Active	Significant Other	Significant

(Dollars in thousands)	Markets for Identical Assets (Level 1)	Observable Inputs (Level 2)	Unobservable Inputs (Level 3)	Balance at Date Indicated
Investment Securities, Available for Sale - December 31, 2016				
U. S. Government and federal agency	$—	$59,052	$ —	$59,052
U. S. Treasury notes and bonds	—	4,072	—	4,072
State and municipal	—	75,370	13,603	88,973
Mortgage-backed	—	7,789	—	7,789
Corporate	—	7,041	—	7,041
Foreign debt	—	4,400	—	4,400
Equity securities	1,383	—	1,500	2,883
Asset backed securities	—	178	—	178
Total	$1,383	$157,902	$ 15,103	$174,388
Investment Securities, Available for Sale - December 31, 2015				
U. S. Government and federal agency	$—	$57,207	$ —	$57,207
U. S. Treasury notes and bonds	—	6,100	—	6,100
State and municipal	—	67,852	9,902	77,754
Mortgage-backed	—	6,970	—	6,970
Corporate	—	7,990	397	8,387
Foreign debt	—	995	—	995
Equity securities	953	—	1,500	2,453
Asset backed securities	—	270	—	270
Total	$953	$147,384	$ 11,799	$160,136

Securities classified as available for sale are generally reported at fair value utilizing Level 2 inputs. ChoiceOne's external investment advisor obtained fair value measurements from an independent pricing service that uses matrix pricing, which is a mathematical technique widely used in the industry to value debt securities without relying exclusively on quoted prices for the specific securities but rather by relying on the securities' relationship to other benchmark quoted securities (Level 2 inputs). The fair value measurements considered observable data that may include dealer quotes, market spreads, cash flows and the bonds' terms and conditions, among other things. Securities classified in Level 2 included U.S. Government and federal agency securities, U.S. Treasury notes and bonds, state and municipal securities, mortgage-backed securities, corporate bonds, foreign debt, and asset backed securities. The Company classified certain state and municipal securities and corporate bonds, and equity securities as Level 3. Based on the lack of observable market data, estimated fair values were based on the observable data available and reasonable unobservable market data.

Changes in Level 3 Assets Measured at Fair Value on a Recurring Basis

(Dollars in thousands)

	2016	2015
Investment Securities, Available for Sale		
Balance, January 1	$11,799	$11,642
Total realized and unrealized gains included in income	—	—
Total unrealized gains/(losses) included in other comprehensive income	(307)	806
Net purchases, sales, calls, and maturities	3,611	(649)
Net transfers into Level 3	—	—
Balance, December 31	$15,103	$11,799

Of the Level 3 assets that were still held by the Bank at December 31, 2016, the net unrealized loss for the twelve months ended December 31, 2016 was $307,000 compared to a $806,000 unrealized gain as of December 31, 2015, which is recognized in other comprehensive income in the consolidated balance sheets. A total of $6.7 million and $3.2 million of Level 3 securities were purchased in 2016 and 2015, respectively.

Both observable and unobservable inputs may be used to determine the fair value of positions classified as Level 3 assets and liabilities. As a result, the unrealized gains and losses for these assets and liabilities presented in the tables above may include changes in fair value that were attributable to both observable and unobservable inputs.

Available for sale investment securities categorized as Level 3 assets consist of bonds issued by local municipalities and a trust-preferred security. The Bank estimates the fair value of these assets based on the present value of expected future cash flows using management's best estimate of key assumptions, including forecasted interest yield and payment rates, credit quality and a discount rate commensurate with the current market and other risks involved.

The Bank also has assets that under certain conditions are subject to measurement at fair value on a non-recurring basis. These assets are not normally measured at fair value, but can be subject to fair value adjustments in certain circumstances, such as impairment. Disclosures concerning assets measured at fair value on a non-recurring basis are as follows:

Assets Measured at Fair Value on a Non-recurring Basis

(Dollars in thousands)	Balances at Dates Indicated	Quoted Prices In Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Impaired Loans				
December 31, 2016	$ 4,911	$ —	$ —	$ 4,911
December 31, 2015	$ 5,585	$ —	$ —	$ 5,585
Other Real Estate				
December 31, 2016	$ 437	$ —	$ —	$ 437
December 31, 2015	$ 31	$ —	$ —	$ 31

Impaired loans categorized as Level 3 assets consist of non-homogeneous loans that are considered impaired. The Bank estimates the fair value of the loans based on the present value of expected future cash flows using management's best estimate of key assumptions. These assumptions include future payment ability, timing of payment streams, and estimated realizable values of available collateral (typically based on outside appraisals). The changes in fair value consisted of charge-downs of impaired loans that were posted to the allowance for loan losses and write-downs of other real estate owned that were posted to a valuation account. The fair value of other real estate owned was based on appraisals or other reviews of property values, adjusted for estimated costs to sell.

Note 19 – Off-Balance Sheet Activities

Some financial instruments, such as loan commitments, credit lines, letters of credit, and overdraft protection, are issued to meet customers' financing needs. These are agreements to provide credit or to support the credit of others, as long as conditions established in the contract are met, and usually have expiration dates. Commitments may expire without being used. Off-balance sheet risk to credit loss exists up to the face amount of these instruments, although material losses are not anticipated. The same credit policies are used to make such commitments as are used for loans, including obtaining collateral at exercise of the commitment.

The contractual amount of financial instruments with off-balance sheet risk was as follows at December 31:

	2016		2015	
	Fixed	Variable	Fixed	Variable
(Dollars in thousands)	Rate	Rate	Rate	Rate
Unused lines of credit and letters of credit	$9,219	$38,422	$14,445	$77,089
Commitments to fund loans (at market rates)	16,788	3,005	18,654	1,740

Commitments to fund loans are generally made for periods of 180 days or less. The fixed rate loan commitments have interest rates ranging from 3.00% to 6.75% and maturities ranging from 3 years to 30 years.

Note 20 – Regulatory Capital

ChoiceOne and the Bank are subject to regulatory capital requirements administered by federal banking agencies. Capital adequacy guidelines and prompt corrective action regulations involve quantitative measures of assets, liabilities, and certain off-balance sheet items calculated under regulatory accounting practices. The prompt corrective action regulations provide five classifications, including well capitalized, adequately capitalized, undercapitalized,

significantly undercapitalized, and critically undercapitalized, although these terms are not used to represent overall financial condition. Depending upon the capital category to which an institution is assigned, the regulators' corrective powers include: prohibiting the acceptance of brokered deposits; requiring the submission of a capital restoration plan; placing limits on asset growth and restrictions on activities; requiring the institution to issue additional capital stock (including additional voting stock) or to be acquired; restricting transactions with affiliates; restricting the interest rate the institution may pay on deposits; ordering a new election of directors of the institution; requiring that senior executive officers or directors be dismissed; prohibiting the institution from accepting deposits from correspondent banks; requiring the institution to divest certain subsidiaries; prohibiting the payment of principal or interest on subordinated debt; and ultimately, appointing a receiver for the institution. At year-end 2016 and 2015, the Bank was categorized as well capitalized under the regulatory framework for prompt corrective action.

Actual capital levels and minimum required levels for ChoiceOne and the Bank were as follows:

(Dollars in thousands)	Actual		Minimum Required for Capital Adequacy Purposes		Minimum Required to be Well Capitalized Under Prompt Corrective Action Regulations	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
December 31, 2016						
ChoiceOne Financial Services Inc.						
Total capital (to risk weighted assets)	$62,822	14.2 %	$35,289	8.0 %	N/A	N/A
Common equity Tier 1 capital (to risk weighted assets)	58,568	13.3	19,850	4.5	N/A	N/A
Tier 1 capital (to risk weighted assets)	58,568	13.3	26,467	6.0	N/A	N/A
Tier 1 capital (to average assets)	58,568	9.9	23,641	4.0	N/A	N/A
ChoiceOne Bank						
Total capital (to risk weighted assets)	$58,963	13.4 %	$35,119	8.0 %	$43,899	10.0 %
Common equity Tier 1 capital (to risk weighted assets)	54,709	12.5	19,754	4.5	28,534	6.5
Tier 1 capital (to risk weighted assets)	54,709	12.5	26,339	6.0	35,119	8.0
Tier 1 capital (to average assets)	54,709	9.3	23,504	4.0	29,380	5.0
December 31, 2015						
ChoiceOne Financial Services Inc.						
Total capital (to risk weighted assets)	$59,737	14.2 %	$33,600	8.0 %	N/A	N/A
Common equity Tier 1 capital (to risk weighted assets)	54,532	13.0	18,900	4.5	N/A	N/A
Tier 1 capital (to risk weighted assets)	54,532	13.0	16,800	4.0	N/A	N/A
Tier 1 capital (to average assets)	54,532	9.7	22,434	4.0	N/A	N/A
ChoiceOne Bank						
Total capital (to risk weighted assets)	$55,723	13.3 %	$33,470	8.0 %	$41,837	10.0 %
Common equity Tier 1 capital (to risk weighted assets)	51,574	12.3	18,827	4.5	27,194	6.5
Tier 1 capital (to risk weighted assets)	51,574	12.3	16,735	4.0	25,102	6.0
Tier 1 capital (to average assets)	51,574	9.2	22,350	4.0	27,937	5.0

Banking regulations limit capital distributions by state-chartered banks. Generally, capital distributions are limited to undistributed net income for the current and prior two years. At December 31, 2016, approximately $10.9 million was available for ChoiceOne Bank to pay dividends to ChoiceOne. ChoiceOne's ability to pay dividends to shareholders is dependent on the payment of dividends from the Bank, which is restricted by state law and regulations.

On July 3, 2013, the FDIC Board of Directors approved the Regulatory Capital Interim Final Rule, implementing Basel III. This rule redefines Tier 1 capital as two components (Common Equity Tier 1 and Additional Tier 1), creates a new capital ratio (Common Equity Tier 1 Risk-based Capital Ratio) and implements a capital conservation buffer. It also revises the prompt corrective action thresholds and makes changes to risk weights for certain assets and off-balance-sheet exposures. Banks were required to transition into the new rule beginning on January 1, 2015.

Note 21 – Quarterly Financial Data (Unaudited)

(Dollars in thousands)	Interest Income	Net Interest Income	Net Income	Earnings Per Share Basic	Earnings Per Share Fully Diluted
2016					
First Quarter	$4,921	$4,680	$1,274	$0.39	$ 0.39
Second Quarter	5,037	4,789	1,445	0.43	0.43
Third Quarter	5,168	4,931	1,683	0.52	0.52
Fourth Quarter	5,186	4,943	1,688	0.51	0.51
2015					
First Quarter	$4,746	$4,490	$1,642	$0.50	$ 0.50
Second Quarter	4,832	4,578	1,430	0.44	0.43
Third Quarter	4,870	4,624	1,449	0.44	0.44
Fourth Quarter	4,904	4,670	1,222	0.37	0.37

There were no significant fluctuations in the quarterly financial data in 2015 or 2016. The growth in net income that occurred in 2016 was due to an increase in interest and non-interest income offset by an increase in interest expense.

Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure

None.

Item 9A. Controls and Procedures

An evaluation was performed under the supervision and with the participation of the Company's management, including the Chief Executive Officer and principal financial officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures. Based on and as of the time of that evaluation, the Company's management, including the Chief Executive Officer and principal financial officer, concluded that the Company's disclosure controls and procedures were effective as of the end of the period covered by this report to ensure that information required to be disclosed by the Company in the reports that it files or submits under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the required time periods.

Management of ChoiceOne Financial Services, Inc. is responsible for establishing and maintaining adequate internal control over financial reporting that is designed to produce reliable financial statements in conformity with United States generally accepted accounting principles. The system of internal control over financial reporting as it relates to the financial statements is evaluated for effectiveness by management and tested for reliability through a program of internal audits. Actions are taken to correct potential deficiencies as they are identified. Any system of internal control, no matter how well designed, has inherent limitations, including the possibility that a control can be circumvented or overridden and misstatements due to error or fraud may occur and not be detected. Also, because of changes in conditions, internal control effectiveness may vary over time. Accordingly, even an effective system of internal control will provide only reasonable assurance with respect to financial statement preparation.

Management assessed the effectiveness of the Company's system of internal control over financial reporting as of December 31, 2016, as required by Section 404 of the Sarbanes-Oxley Act of 2002. Management's assessment is based on the criteria for effective internal control over financial reporting as described in "Internal Control – Integrated Framework (2013)," issued by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO"). Based on this assessment, management has concluded that, as of December 31, 2016, its system of internal control over financial reporting was effective and meets the criteria of the "Internal Control – Integrated Framework." This annual report is not required to include an attestation report of the Company's independent registered public accounting firm regarding internal control over financial reporting.

There was no change in the Company's internal control over financial reporting that occurred during the three months ended December 31, 2016 that has materially affected, or that is reasonably likely to materially affect, the Company's internal control over financial reporting.

Item 9B. Other Information

None.

PART III

Item 10. Directors, Executive Officers and Corporate Governance

The information under the captions "ChoiceOne's Board of Directors and Executive Officers," "Related Matters – Section 16(a) Beneficial Ownership Reporting Compliance" and "Corporate Governance" in the Company's Definitive Proxy Statement for the Annual Meeting of Shareholders to be held May 24, 2017, is incorporated herein by reference.

The Company has adopted a Code of Ethics for Executive Officers and Senior Financial Officers, which applies to the Chief Executive Officer and the Chief Financial Officer, as well as all other senior financial and accounting officers. The Code of Ethics is posted on the Company's website at "www.choiceone.com." The Company intends to satisfy the disclosure requirements under Item 5.05 of Form 8-K regarding an amendment to, or a waiver from, a provision of the Code of Ethics by posting such information on its website at "www.choiceone.com."

Item 11. Executive Compensation

The information under the captions “Executive Compensation” in the Company’s Definitive Proxy Statement for the Annual Meeting of Shareholders to be held May 24, 2017, is incorporated herein by reference.

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

The information under the caption “Ownership of ChoiceOne Common Stock” in the Company’s Definitive Proxy Statement for the Annual Meeting of Shareholders to be held May 24, 2017, is incorporated herein by reference.

The following table presents information regarding the equity compensation plans both approved and not approved by shareholders at December 31, 2016:

	Number of securities to be issued upon exercise of outstanding options, warrants and rights	Weighted-average exercise price of outstanding options, warrants and rights	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a))
	(a)	(b)	(c)
Equity compensation plans approved by security holders	47,033	$ 15.44	73,875
Equity compensation plans not approved by security holders	—	—	13,744
Total	47,033	$ 15.44	87,619

Equity compensation plans approved by security holders include the Stock Incentive Plan of 2012, the Amended and Restated Executive Stock Incentive Plan and the Employee Stock Purchase Plan. 40,750 shares remain available for future issuance under the Stock Incentive Plan of 2012 and 33,125 shares remain available for future issuance under the Employee Stock Purchase Plan, in each case other than upon the exercise of outstanding stock options. No further future issuances of shares are permitted under the Amended and Restated Executive Stock Incentive Plan other than upon the exercise of outstanding stock options.

The Directors' Stock Purchase Plan is the only equity compensation plan not approved by security holders. The plan is designed to provide directors of the Company the option of receiving their fees in the Company's common stock. Directors who elect to participate in the plan may elect to contribute to the plan twenty-five, fifty, seventy-five or one hundred percent of their board of director fees and one hundred percent of their director committee fees earned as directors of the Company. Contributions to the plan are made by the Company on behalf of each electing participant. Plan participants may terminate their participation in the plan at any time by written notice of withdrawal to the Company. Participants will cease to be eligible to participate in the plan when they cease to serve as directors of the Company. Shares are distributed to participants on a quarterly basis. The plan provides for issuance of a maximum of 100,000 shares of the Company's common stock, subject to adjustments for certain changes in the capital structure of the Company. New issuances of up to 13,744 shares may be made under this plan.

Item 13. Certain Relationships and Related Transactions, and Director Independence

The information under the captions "Related Matters - Transactions with Related Persons" and "Corporate Governance" in the Company's Definitive Proxy Statement for the Annual Meeting of Shareholders to be held May 24, 2017, is incorporated herein by reference.

Item 14. Principal Accountant Fees and Services

The information under the caption "Related Matters - Independent Certified Public Accountants" in the Company's Definitive Proxy Statement for the Annual Meeting of Shareholders to be held May 24, 2017, is incorporated herein by reference.

PART IV

Item 15. Exhibits and Financial Statement Schedules

(a)(1) Financial Statements. The following financial statements and independent auditors' reports are filed as part of this report:

Consolidated Balance Sheets at December 31, 2016 and 2015.

Consolidated Statements of Income for the years ended December 31, 2016, 2015, and 2014.

Consolidated Statement of Comprehensive Income for the years ended December 31, 2016, 2015, and 2014.

Consolidated Statements of Changes in Shareholders' Equity for the years ended December 31, 2016, 2015, and 2014.

Consolidated Statements of Cash Flows for the years ended December 31, 2016, 2015, and 2014.

Notes to Consolidated Financial Statements.

Report of Independent Registered Public Accounting Firm dated March 24, 2017.

(2) Financial Statement Schedules. None.

Exhibit	Document
3.1	Amended and Restated Articles of Incorporation. Previously filed as an exhibit to ChoiceOne Financial Services, Inc.'s Form 10-K Annual Report for the year ended December 31, 2013. Here incorporated by reference.
3.2	Bylaws of the Registrant as currently in effect and any amendments thereto. Previously filed as an exhibit to ChoiceOne Financial Services, Inc.'s Form 10-K Annual Report for the year ended December 31, 2013. Here incorporated by reference.
4	Advances, Pledge and Security Agreement between ChoiceOne Bank and the Federal Home Loan Bank of Indianapolis. Previously filed as an exhibit to ChoiceOne Financial Services, Inc.'s Form 10-K Annual Report for the year ended December 31, 2013. Here incorporated by reference.
10.1	Change in Control Agreement with Kelly J. Potes. (1) Previously filed as an exhibit to ChoiceOne Financial Services, Inc.'s Form 10-Q Quarterly Report for the period ended March 31, 2016. Here incorporated by reference.

10.2 Stock Incentive Plan of 2012. (1) Previously filed as an appendix to ChoiceOne Financial Services, Inc.'s definitive proxy statement filed with the commission on March 30, 2012. Here incorporated by reference.

10.3 Amended and Restated Executive Stock Incentive Plan. (1)

10.4 Directors' Stock Purchase Plan. (1)

10.5 Former Valley Ridge Executive Employee Salary Continuation Agreements, as amended. (1) Previously filed as an exhibit to ChoiceOne Financial Services, Inc.'s Form 10-K Annual Report for the year ended December 31, 2013. Here incorporated by reference.

10.6 Former Valley Ridge Directors' Deferred Compensation Plan and Agreement. (1) Previously filed as an exhibit to the ChoiceOne Financial Services, Inc.'s Form 10-K Annual Report for the year ended December 31, 2013. Here incorporated by reference.

10.7 Amended and Restated Employee Stock Purchase Plan. (1)

21	Subsidiaries of ChoiceOne Financial Services, Inc.
23	Consent of Independent Registered Public Accounting Firm.
24.1	Powers of Attorney.
31.1	Certification of Chief Executive Officer.
31.2	Certification of Treasurer.
32	Certification pursuant to 18 U.S.C. § 1350.
101.1	Interactive Data File.

(1) This agreement is a management contract or compensation plan or arrangement to be filed as an exhibit to this Form 10-K.

Copies of any exhibits will be furnished to shareholders upon written request. Requests should be directed to: Thomas L. Lampen, Treasurer, ChoiceOne Financial Services, Inc., 109 East Division, Sparta, Michigan, 49345.

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.

ChoiceOne Financial Services, Inc.

By: /s/ Kelly J. Potes Kelly J. Potes Chief Executive Officer	March 27, 2017

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

/s/ Kelly J. Potes Kelly J. Potes	Chief Executive Officer and Director (Principal Executive Officer)	March 27, 2017
/s/ Thomas L. Lampen Thomas L. Lampen	Treasurer (Principal Financial and Accounting Officer)	March 27, 2017
*/s/ Paul L. Johnson Paul L. Johnson	Chairman of the Board and Director	March 27, 2017
*/s/ Frank G. Berris Frank G. Berris	Director	March 27, 2017
*/s/ Keith D. Brophy Keith D. Brophy	Director	March 27, 2017

*/s/ K. Timothy Bull K. Timothy Bull	Director	March 27, 2017
*/s/ William F. Cutler, Jr. William F. Cutler, Jr.	Director	March 27, 2017
*/s/ Jack G. Hendon Jack G. Hendon	Director	March 27, 2017
*/s/ Raymond A. Lanning Raymond A. Lanning	Director	March 27, 2017
*/s/ Dennis C. Nelson Dennis C. Nelson	Director	March 27, 2017
*/s/ Nels W. Nyblad Nels W. Nyblad	Director	March 27, 2017
*/s/ Roxanne M. Page Roxanne M. Page	Director	March 27, 2017
*/s/ James A. Bosserd James A. Bosserd	Director	March 27, 2017

* By /s/ Thomas L. Lampen
Attorney-in-Fact