Community Bankers Trust Corp
Form 10-Q
August 08, 2017

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D. C. 20549

FORM 10-Q

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

For the quarterly period ended June 30, 2017

or

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

For the transition period from to

Commission File Number: 001-32590

COMMUNITY BANKERS TRUST CORPORATION

(Exact name of registrant as specified in its charter)

Virginia	**20-2652949**
(State or other jurisdiction of incorporation or organization)	*(I.R.S. Employer Identification No.)*
9954 Mayland Drive, Suite 2100 Richmond, Virginia	**23233**
(Address of principal executive offices)	*(Zip Code)*

(804) 934-9999
(Registrant's telephone number, including area code)

n/a
(Former name, former address and former fiscal year, if changed since last report)

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 þ 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 during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes þ No ¨

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

Large accelerated filer ¨	Accelerated filer þ
Non-accelerated filer ¨(Do not check if a smaller reporting company)	Smaller reporting company ¨
	Emerging growth company ¨

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

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

At June 30, 2017, there were 22,037,221 shares of the Company's common stock outstanding.

COMMUNITY BANKERS TRUST CORPORATION

TABLE OF CONTENTS

FORM 10-Q

June 30, 2017

PART I — FINANCIAL INFORMATION

Item 1. ***Financial Statements***

COMMUNITY BANKERS TRUST CORPORATION

UNAUDITED CONSOLIDATED BALANCE SHEETS

AS OF JUNE 30, 2017 AND DECEMBER 31, 2016

(dollars in thousands)

	June 30, 2017	December 31, 2016
ASSETS		
Cash and due from banks	$ 11,342	$ 13,828
Interest bearing bank deposits	29,908	7,244
Federal funds sold	152	—
Total cash and cash equivalents	41,402	21,072
Securities available for sale, at fair value	212,343	216,121
Securities held to maturity, at cost (fair value of $47,764 and $46,858, respectively)	46,914	46,608
Equity securities, restricted, at cost	8,048	8,290
Total securities	267,305	271,019
Loans	864,049	836,299
Purchased credit impaired (PCI) loans	48,387	51,964
Total loans	912,436	888,263
Allowance for loan losses (loans of $9,489 and $9,493, respectively; PCI loans of $200 and $200, respectively)	(9,689)	(9,693)
Net loans	902,747	878,570
Bank premises and equipment, net	29,771	28,357
Other real estate owned	2,387	4,427
Bank owned life insurance	27,723	27,339
Core deposit intangibles, net	82	898
Other assets	19,090	18,134
Total assets	$ 1,290,507	$ 1,249,816

LIABILITIES		
Deposits:		
Noninterest bearing	$ 138,471	$ 128,887
Interest bearing	944,414	908,407
Total deposits	1,082,885	1,037,294
Federal funds purchased	—	4,714
Federal Home Loan Bank advances	76,494	81,887
Long-term debt	—	1,670
Trust preferred capital notes	4,124	4,124
Other liabilities	5,247	5,591
Total liabilities	1,168,750	1,135,280
SHAREHOLDERS' EQUITY		
Common stock (200,000,000 shares authorized, $0.01 par value; 22,037,221 and 21,959,648 shares issued and outstanding, respectively)	220	220
Additional paid in capital	147,250	146,667
Retained deficit	(25,701)	(31,128)
Accumulated other comprehensive loss	(12)	(1,223)
Total shareholders' equity	121,757	114,536
Total liabilities and shareholders' equity	$ 1,290,507	$ 1,249,816

See accompanying notes to unaudited consolidated financial statements

COMMUNITY BANKERS TRUST CORPORATION

UNAUDITED CONSOLIDATED STATEMENTS OF INCOME

FOR THE THREE AND SIX MONTHS ENDED JUNE 30, 2017 AND 2016

(dollars and shares in thousands, except per share data)

	Three months ended		Six months ended	
	June 30, 2017	June 30, 2016	June 30, 2017	June 30, 2016
Interest and dividend income				
Interest and fees on loans	$ 9,952	$ 8,873	$ 19,549	$ 17,426
Interest and fees on PCI loans	1,453	1,556	2,932	3,155
Interest on deposits in other banks	52	23	78	44
Interest and dividends on securities				
Taxable	1,157	1,124	2,406	2,395
Nontaxable	606	557	1,203	1,151
Total interest and dividend income	13,220	12,133	26,168	24,171
Interest expense				
Interest on deposits	1,944	1,537	3,723	3,088
Interest on borrowed funds	302	363	604	737
Total interest expense	2,246	1,900	4,327	3,825
Net interest income	10,974	10,233	21,841	20,346
Provision for loan losses	—	200	—	200
Net interest income after provision for loan losses	10,974	10,033	21,841	20,146
Noninterest income				
Service charges on deposit accounts	690	599	1,333	1,168
Gain on securities transactions, net	37	261	132	520
Income on bank owned life insurance	235	204	469	392
Mortgage loan income	71	174	104	347
Other	155	157	303	289
Total noninterest income	1,188	1,395	2,341	2,716
Noninterest expense				
Salaries and employee benefits	4,886	4,561	9,568	9,172
Occupancy expenses	740	646	1,472	1,287
Equipment expenses	260	248	544	487
FDIC assessment	164	252	365	503
Data processing fees	477	405	965	820
Amortization of intangibles	339	476	816	953
Other real estate expense (income), net	34	(15)	61	(117)
Other operating expenses	1,636	1,656	3,196	3,155
Total noninterest expense	8,536	8,229	16,987	16,260
Income before income taxes	3,626	3,199	7,195	6,602
Income tax expense	692	881	1,768	1,864

Net income	$ 2,934	$ 2,318	$ 5,427	$ 4,738
Net income per share — basic	$ 0.13	$ 0.11	$ 0.25	$ 0.22
Net income per share — diluted	$ 0.13	$ 0.11	$ 0.24	$ 0.22
Weighted average number of shares outstanding				
Basic	21,997	21,897	21,979	21,885
Diluted	22,424	22,039	22,440	22,080

See accompanying notes to unaudited consolidated financial statements

4

COMMUNITY BANKERS TRUST CORPORATION

UNAUDITED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

FOR THE THREE AND SIX MONTHS ENDED JUNE 30, 2017 AND 2016

(dollars in thousands)

	Three months ended		Six months ended	
	June 30, 2017	June 30, 2016	June 30, 2017	June 30, 2016
Net income	$ 2,934	$ 2,318	$ 5,427	$ 4,738
Other comprehensive income:				
Unrealized gains on investment securities:				
Change in unrealized gain in investment securities	1,165	1,644	1,935	5,197
Tax related to unrealized gain in investment securities	(407)	(559)	(669)	(1,767)
Reclassification adjustment for gain in securities sold	(37)	(261)	(132)	(520)
Tax related to realized gain in securities sold	13	89	45	177
Defined benefit pension plan:				
Tax related to defined benefit pension plan	11	—	11	—
Cash flow hedge:				
Change in unrealized (loss) gain in cash flow hedge	(51)	(129)	31	(677)
Tax related to cash flow hedge	18	44	(10)	230
Total other comprehensive income	712	828	1,211	2,640
Total comprehensive income	$ 3,646	$ 3,146	$ 6,638	$ 7,378

See accompanying notes to unaudited consolidated financial statements

COMMUNITY BANKERS TRUST CORPORATION

UNAUDITED CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

FOR THE SIX MONTHS ENDED JUNE 30, 2017 AND 2016

(dollars and shares in thousands)

	Common Stock Shares	Common Stock Amount	Additional Paid in Capital	Retained Deficit	Accumulated Other Comprehensive Income (Loss)	Total
Balance January 1, 2016	21,867	$ 219	$ 145,907	$ (41,050)	$ (589)	$ 104,487
Issuance of common stock	44	—	83	—	—	83
Exercise and issuance of employee stock options	—	—	283	—	—	283
Net income	—	—	—	4,738	—	4,738
Other comprehensive income	—	—	—	—	2,640	2,640
Balance June 30, 2016	21,911	$ 219	$ 146,273	$ (36,312)	$ 2,051	$ 112,231
Balance January 1, 2017	21,960	$ 220	$ 146,667	$ (31,128)	$ (1,223)	$ 114,536
Issuance of common stock	77	—	81	—	—	81
Exercise and issuance of employee stock options	—	—	502	—	—	502
Net income	—	—	—	5,427	—	5,427
Other comprehensive income	—	—	—	—	1,211	1,211
Balance June 30, 2017	22,037	$ 220	$ 147,250	$ (25,701)	$ (12)	$ 121,757

See accompanying notes to unaudited consolidated financial statements

COMMUNITY BANKERS TRUST CORPORATION

UNAUDITED CONSOLIDATED STATEMENTS OF CASH FLOWS

FOR THE SIX MONTHS ENDED JUNE 30, 2017 AND 2016

(dollars in thousands)

	June 30, 2017			June 30, 2016		
Operating activities:						
Net income	$	5,427		$	4,738	
Adjustments to reconcile net income to net cash provided by operating activities:						
Depreciation and intangibles amortization		1,630			1,707	
Stock-based compensation expense		373			286	
Tax benefit of exercised stock options		(94	)		(20	)
Amortization of purchased loan premium		91			126	
Provision for loan losses		—			200	
Amortization of security premiums and accretion of discounts, net		833			892	
Net gain on sale of securities		(132	)		(520	)
Net loss (gain) on sale and valuation of OREO and bank premises		1			(227	)
Originations of mortgages held for sale		—			(30,940	)
Proceeds from sales of mortgages held		—			31,278	

for sale				
Increase in bank owned life insurance investment	(384	)	(321	)
Changes in assets and liabilities:				
(Increase) decrease in other assets	(1,220	)	329	
Decrease in other liabilities	(313	)	(1,124	)
Net cash provided by operating activities	6,212		6,404	
Investing activities:				
Proceeds from available for sale securities	35,173		76,311	
Proceeds from held to maturity securities	233		6,164	
Proceeds from restricted equity securities	1,035		2,253	
Purchase of available for sale securities	(30,191	)	(32,547	)
Purchase of held to maturity securities	(643	)	(18,910	)
Purchase of restricted equity securities	(793	)	(2,477	)
Proceeds from sale of other real estate owned	2,081		1,249	
Improvements of other real estate, net of insurance proceeds	—		(34	)
Net increase in loans	(24,602	)	(33,207	)
Principal recoveries of loans previously charged off	291		228	
Purchase of premises and equipment, net	(2,228	)	(1,035	)
Purchase of small business investment company fund investment	(262	)	—	
Purchase of bank owned life insurance investment	—		(5,000	)

Proceeds from sale of premises and equipment		—			146	
Net cash used in investing activities		(19,906	)		(6,859	)
Financing activities:						
Net increase in deposits		45,591			11,495	
Net decrease in federal funds purchased		(4,714	)		(6,620	)
Net decrease in Federal Home Loan Bank advances		(5,393	)		(1,382	)
Proceeds from issuance of common stock		210			56	
Payments on long-term debt		(1,670	)		(1,869	)
Net cash provided by financing activities		34,024			1,680	
Net increase in cash and cash equivalents		20,330			1,225	
Cash and cash equivalents:						
Beginning of the period		21,072			16,969	
End of the period	$	41,402		$	18,194	
Supplemental disclosures of cash flow information:						
Interest paid	$	4,315		$	3,844	
Income taxes paid		2,470			3,214	
Transfer of OREO property		42			425	

See accompanying notes to unaudited consolidated financial statements

7

COMMUNITY BANKERS TRUST CORPORATION

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

Note 1. Nature of Banking Activities and Significant Accounting Policies

Organization

Community Bankers Trust Corporation (the “Company”) is headquartered in Richmond, Virginia and is the holding company for Essex Bank (the “Bank”), a Virginia state bank with 25 full-service offices in Virginia and Maryland. The Bank also operates one loan production office in Virginia.

The Bank engages in a general commercial banking business and provides a wide range of financial services primarily to individuals and small businesses, including individual and commercial demand and time deposit accounts, commercial and industrial loans, consumer and small business loans, real estate and mortgage loans, investment services, on-line and mobile banking products, and safe deposit box facilities.

Financial Statements

The consolidated statements presented include accounts of the Company and the Bank, its wholly-owned subsidiary. All material intercompany balances and transactions have been eliminated. The statements should be read in conjunction with the Company’s consolidated financial statements and the accompanying notes to consolidated financial statements included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2016. The accounting and reporting policies of the Company conform to U.S. generally accepted accounting principles (GAAP) and to the general practices within the banking industry. The interim financial statements have not been audited; however, in the opinion of management, all adjustments, consisting of normal accruals, were made that are necessary to present fairly the balance sheet of the Company as of June 30, 2017, the statements of income and comprehensive income for the three and six months ended June 30, 2017, and the statements of changes in shareholders’ equity and cash flows for the six months ended June 30, 2017. Results for the six month period ended June 30, 2017 are not necessarily indicative of the results that may be expected for the year ending December 31, 2017.

The financial information contained within the statements is, to a significant extent, financial information that is based on measures of the financial effects of transactions and events that have already occurred. A variety of factors could affect the ultimate value that is obtained when either earning income, recognizing an expense, recovering an asset or relieving a liability. The Company uses historical loss factors as one factor in determining the inherent loss that may be present in its loan portfolio. Actual losses could differ significantly from the historical factors that the Company uses. In addition, GAAP itself may change from one previously acceptable method to another method. Although the economics of the Company's transactions would be the same, the timing of events that would impact its transactions could change.

In preparing these financial statements, the Company has evaluated subsequent events and transactions for potential recognition or disclosure through the date the financial statements were issued.

Certain reclassifications have been made to prior period balances to conform to the current year presentations.

Recent Accounting Pronouncements

In March 2017, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2017-08, *Receivables — Nonrefundable Fees and Other Costs (Subtopic 310-20), Premium Amortization on Purchased Callable Debt Securities.* The ASU shortens the amortization period for certain callable debt securities held at a premium to the earliest call date.

Under current GAAP, entities normally amortize the premium as an adjustment of yield over the contractual life of the instrument. Stakeholders have expressed concerns with the current approach on the basis that current GAAP excludes certain callable debt securities from consideration of early repayment of principal even if the holder is certain that the call will be exercised. As a result, upon the exercise of a call on a callable debt security held at a premium, the unamortized premium is recorded as a loss in earnings. Further, there is diversity in practice (1) in the amortization period for premiums of callable debt securities, and (2) in how the potential for exercise of a call is factored into current impairment assessments.

The ASU shortens the amortization period for certain callable debt securities held at a premium and requires the premium to be amortized to the earliest call date. However, the amendments do not require an accounting change for securities held at a discount; the discount continues to be amortized to maturity.

The amendments are effective for public business entities for annual periods beginning after December 15, 2018, including interim periods within those annual periods. Early adoption is permitted. The Company is currently in compliance with this guidance; therefore, its adoption will have no impact on its financial statements.

Also in March 2017, the FASB issued ASU No. 2017-07, *Compensation — Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost***.** The amendments apply to all employers, including not-for-profit entities, that offer to their employees defined benefit pension plans, other postretirement benefit plans, or other types of benefits accounted for under Topic 715, *Compensation — Retirement Benefits*.

The amendments require that an employer report the service cost component in the same line item or items as other compensation costs arising from services rendered by the pertinent employees during the period. The other components of net benefit cost are required to be presented in the income statement separately from the service cost component. The line item or items used in the income statement to present the other components of net benefit cost must be disclosed.

The amendments are effective for public business entities for annual periods beginning after December 15, 2017, including interim periods within those annual periods. Early adoption is permitted as of the beginning of an annual period for which financial statements (interim or annual) have not been issued or made available for issuance. The Company does not expect the adoption of this guidance to have a material impact on its financial statements. The Company does not offer a post retirement benefit plan. As the Company's pension plan is frozen, no additional service cost will be incurred. The remaining components of net periodic benefit cost are not expected to be significant. See Note 10 for further details.

Note 2. Securities

Amortized costs and fair values of securities available for sale and held to maturity at June 30, 2017 and December 31, 2016 were as follows (dollars in thousands):

	June 30, 2017			
		Gross Unrealized		
	Amortized Cost	Gains	Losses	Fair Value
Securities Available for Sale				
U.S. Treasury issue and other U.S. Gov't agencies	$47,450	$20	$(641)	$46,829
U.S. Gov't sponsored agencies	2,844	—	(54)	2,790
State, county and municipal	123,625	2,877	(669)	125,833
Corporate and other bonds	16,087	119	(116)	16,090
Mortgage backed – U.S. Gov't agencies	4,372	—	(118)	4,254
Mortgage backed – U.S. Gov't sponsored agencies	16,784	17	(254)	16,547
Total Securities Available for Sale	$211,162	$3,033	$(1,852)	$212,343
Securities Held to Maturity				
U.S. Treasury issue and other U.S. Gov't agencies	$10,000	$—	$(79)	$9,921
State, county and municipal	36,392	975	(57)	37,310
Mortgage backed – U.S. Gov't agencies	522	11	—	533
Total Securities Held to Maturity	$46,914	$986	$(136)	$47,764

	December 31, 2016			
		Gross Unrealized		
	Amortized Cost	Gains	Losses	Fair Value
Securities Available for Sale				
U.S. Treasury issue and other U.S. Gov't agencies	$58,724	$15	$(763)	$57,976
U.S. Gov't sponsored agencies	3,452	—	(116)	3,336
State, county and municipal	121,686	2,247	(1,160)	122,773
Corporate and other bonds	15,936	—	(433)	15,503
Mortgage backed – U.S. Gov't agencies	3,614	—	(119)	3,495
Mortgage backed – U.S. Gov't sponsored agencies	13,330	21	(313)	13,038
Total Securities Available for Sale	$216,742	$2,283	$(2,904)	$216,121
Securities Held to Maturity				
U.S. Treasury issue and other U.S. Gov't agencies	$10,000	$—	$(154)	$9,846
State, county and municipal	35,847	568	(185)	36,230
Mortgage backed – U.S. Gov't agencies	761	21	—	782
Total Securities Held to Maturity	$46,608	$589	$(339)	$46,858

The amortized cost and fair value of securities at June 30, 2017 by final contractual maturity are shown below. Expected maturities may differ from final contractual maturities because issuers may have the right to call or prepay obligations without any penalties.

	Held to Maturity		Available for Sale	
(dollars in thousands)	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Due in one year or less	$4,126	$ 4,170	$1,560	$ 1,577
Due after one year through five years	23,226	23,416	93,522	94,729
Due after five years through ten years	13,641	14,083	99,688	99,820
Due after ten years	5,921	6,095	16,392	16,217
Total securities	$46,914	$ 47,764	$211,162	$ 212,343

Proceeds from sales of securities available for sale were $8.7 million and $20.1 million during the three months ended June 30, 2017 and 2016, respectively, and $21.0 million and $71.5 million for the six months ended June 30, 2017 and 2016, respectively. Gains and losses on the sale of securities are determined using the specific identification method. Gross realized gains and losses on sales of securities available for sale during the three and six months ended June 30, 2017 and 2016 were as follows (dollars in thousands):

	Three Months Ended		Six Months Ended	
	June 30, 2017	June 30, 2016	June 30,	June 30, 2016

			2017	
Gross realized gains	$ 134	$ 278	$ 264	$ 1,032
Gross realized losses	(97)	(17)	(132)	(512)
Net securities gains	$ 37	$ 261	$ 132	$ 520

In estimating other than temporary impairment (OTTI) losses, management considers the length of time and the extent to which the fair value has been less than cost, the financial condition and short-term prospects for the issuer, and the intent and ability of management to hold its investment for a period of time to allow a recovery in fair value. There were no investments held that had OTTI losses for the three and six months ended June 30, 2017 and 2016.

The fair value and gross unrealized losses for securities, segregated by the length of time that individual securities have been in a continuous gross unrealized loss position, at June 30, 2017 and December 31, 2016 were as follows (dollars in thousands):

	June 30, 2017					
	Less than 12 Months		12 Months or More		Total	
Securities Available for Sale	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
U.S. Treasury issue and other U.S. Gov't agencies	$16,777	$(229)	$24,266	$(412)	$41,043	$(641)
U.S. Gov't sponsored agencies	-	-	2,290	(54)	2,290	(54)
State, county and municipal	18,184	(327)	4,504	(342)	22,688	(669)
Corporate and other bonds	1,240	(9)	6,700	(107)	7,940	(116)
Mortgage backed – U.S. Gov't agencies	1,576	(23)	1,903	(95)	3,479	(118)
Mortgage backed – U.S. Gov't sponsored agencies	12,571	(253)	124	(1)	12,695	(254)
Total	$50,348	$(841)	$39,787	$(1,011)	$90,135	$(1,852)
Securities Held to Maturity						
U.S. Treasury issue and other U.S. Gov't agencies	$9,921	$(79)	$-	$-	$9,921	$(79)
State, county and municipal	3,834	(57)	-	-	3,834	(57)
Total	$13,755	$(136)	$-	$-	$13,755	$(136)

	December 31, 2016					
	Less than 12 Months		12 Months or More		Total	
Securities Available for Sale	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
U.S. Treasury issue and other U.S. Gov't agencies	$29,756	$(324)	$25,155	$(439)	$54,911	$(763)
U.S. Gov't sponsored agencies	-	-	2,523	(116)	2,523	(116)
State, county and municipal	39,713	(848)	3,885	(312)	43,598	(1,160)
Corporate and other bonds	6,864	(103)	8,639	(330)	15,503	(433)
Mortgage backed – U.S. Gov't agencies	1,598	(18)	1,897	(101)	3,495	(119)
Mortgage backed – U.S. Gov't sponsored agencies	9,247	(313)	-	-	9,247	(313)
Total	$87,178	$(1,606)	$42,099	$(1,298)	$129,277	$(2,904)
Securities Held to Maturity						
U.S. Treasury issue and other U.S. Gov't agencies	$9,846	$(154)	$-	$-	$9,846	$(154)
State, county and municipal	8,052	(185)	-	-	8,052	(185)
Total	$17,898	$(339)	$-	$-	$17,898	$(339)

The unrealized losses (impairments) in the investment portfolio at June 30, 2017 and December 31, 2016 are generally a result of market fluctuations that occur daily. The unrealized losses are from 116 securities at June 30, 2017. Of those, 102 are investment grade, have U.S. government agency guarantees, or are backed by the full faith and credit of local municipalities throughout the United States. Fourteen investment grade corporate and other bond obligations comprise the remaining securities with unrealized losses at June 30, 2017. The Company considers the reason for impairment, length of impairment, and ability and intent to hold until the full value is recovered in determining if the impairment is temporary in nature. Based on this analysis, the Company has determined these impairments to be temporary in nature. The Company does not intend to sell, and it is more likely than not that the Company will not be required to sell, these securities until they recover in value or reach maturity.

Market prices are affected by conditions beyond the control of the Company. Investment decisions are made by the management group of the Company and reflect the overall liquidity and strategic asset/liability objectives of the Company. Management analyzes the securities portfolio frequently and manages the portfolio to provide an overall positive impact to the Company’s income statement and balance sheet.

Securities with amortized costs of $67.2 million and $75.8 million at June 30, 2017 and December 31, 2016, respectively, were pledged to secure public deposits as required or permitted by law. Securities with amortized costs of $4.1 million and $4.4 million at June 30, 2017 and December 31, 2016, respectively, were pledged to secure lines of credit at the Federal Reserve discount window. At each of June 30, 2017 and December 31, 2016, there were no securities purchased from a single issuer, other than U.S. Treasury issue and other U.S. Government agencies that comprised more than 10% of the consolidated shareholders’ equity.

Note 3. Loans and Related Allowance for Loan Losses

The Company's loans, net of deferred fees and costs, at June 30, 2017 and December 31, 2016 were comprised of the following (dollars in thousands):

	June 30, 2017		December 31, 2016	
	Amount	% of Loans	Amount	% of Loans
Mortgage loans on real estate:				
Residential 1-4 family	$212,502	24.59 %	$207,863	24.86 %
Commercial	341,182	39.49	339,804	40.63
Construction and land development	100,677	11.65	98,282	11.75
Second mortgages	7,537	0.87	7,911	0.95
Multifamily	50,511	5.85	39,084	4.67
Agriculture	7,985	0.92	7,185	0.86
Total real estate loans	720,394	83.37	700,129	83.72
Commercial loans	137,261	15.89	129,300	15.46
Consumer installment loans	5,107	0.59	5,627	0.67
All other loans	1,287	0.15	1,243	0.15
Total loans	$864,049	100.00 %	$836,299	100.00 %

The Company held $15.5 million and $15.8 million in balances of loans guaranteed by the United States Department of Agriculture (USDA), which are included in various categories in the table above, at June 30, 2017 and December 31, 2016, respectively. As these loans are 100% guaranteed by the USDA, no loan loss allowance is required. These loan balances included a purchase premium of $688,000 and $749,000 at June 30, 2017 and December 31, 2016, respectively. The purchase premium is amortized as an adjustment of the related loan yield on a straight line basis, which is substantially equivalent to the results obtained using the effective interest method.

At June 30, 2017 and December 31, 2016, the Company's allowance for credit losses was comprised of the following: (i) a specific valuation component calculated in accordance with FASB ASC 310, *Receivables,* (ii) a general valuation component calculated in accordance with FASB Accounting Standards Codification (ASC) 450, *Contingencies*, based on historical loan loss experience, economic conditions and other qualitative risk factors, and (iii) an unallocated component to cover uncertainties that could affect management's estimate of probable losses. Management identified loans subject to impairment in accordance with ASC 310.

The following table summarizes information related to impaired loans as of June 30, 2017 (dollars in thousands):

	June 30, 2017			Three months ended June 30, 2017		Six months ended June 30, 2017	
	Recorded Investment (1)	**Unpaid Principal Balance (2)**	**Related Allowance**	**Average Investment**	**Interest Recognized**	**Average Investment**	**Interest Recognized**
With no related allowance recorded:							
Mortgage loans on real estate:							
Residential 1-4 family	$ 1,941	$ 2,257	$ —	$ 2,065	$ 7	$ 1,945	$ 15
Commercial	3,699	4,282	—	3,927	38	4,808	76
Construction and land development	—	—	—	—	—	—	—
Agriculture	258	258	—	129	—	86	—
Total real estate loans	5,898	6,797	—	6,121	45	6,839	91
Commercial loans	—	—	—	—	—	400	—
Consumer installment loans	—	—	—	—	—	—	—
Subtotal impaired loans with no valuation allowance	5,898	6,797	—	6,121	45	7,239	91
With an allowance recorded:							
Mortgage loans on real estate:							
Residential 1-4 family	2,369	2,787	314	2,352	20	2,441	39
Commercial	2,796	3,194	355	1,596	2	1,270	4
Construction and land development	4,296	5,552	569	4,300	—	4,699	—
Agriculture	—	—	—	—	—	—	—
Total real estate loans	9,461	11,533	1,238	8,248	22	8,410	43
Commercial loans	1,499	1,620	189	892	1	612	2
Consumer installment loans	10	27	1	26	—	111	—
Subtotal impaired loans with a valuation allowance	10,970	13,180	1,428	9,166	23	9,133	45
Total:							
Mortgage loans on real estate:							
Residential 1-4 family	4,310	5,044	314	4,417	27	4,386	54
Commercial	6,495	7,476	355	5,523	40	6,078	80
Construction and land development	4,296	5,552	569	4,300	—	4,699	—
Agriculture	258	258	—	129	—	86	—
Total real estate loans	15,359	18,330	1,238	14,369	67	15,249	134
Commercial loans	1,499	1,620	189	892	1	1,012	2
Consumer installment loans	10	27	1	26	—	111	—
Total impaired loans	$ 16,868	$ 19,977	$ 1,428	$ 15,287	$ 68	$ 16,372	$ 136

(1) The amount of the investment in a loan, which is not net of a valuation allowance, but which does reflect any direct write-down of the investment

(2) The contractual amount due, which reflects paydowns applied in accordance with loan documents, but which does not reflect any direct write-downs or valuation allowances

13

The following table summarizes information related to impaired loans as of December 31, 2016 and the three and six months ended June 30, 2016 (dollars in thousands):

	December 31, 2016			Three months ended June 30, 2016		Six months ended June 30, 2016	
	Recorded Investment [(1)]	**Unpaid Principal Balance** [(2)]	**Related Allowance**	**Average Investment**	**Interest Recognized**	**Average Investment**	**Interest Recognized**
With no related allowance recorded:							
Mortgage loans on real estate:							
Residential 1-4 family	$ 1,704	$ 1,931	$ —	$ 2,570	$ 11	$ 2,863	$ 22
Commercial	6,570	7,078	—	4,252	39	4,282	78
Construction and land development	—	—	—	—	—	—	—
Second mortgages	—	—	—	68	—	68	—
Total real estate loans	8,274	9,009	—	6,890	50	7,213	100
Commercial loans	1,200	1,200	—	—	—	—	—
Consumer installment loans	—	—	—	246	1	122	2
Subtotal impaired loans with no valuation allowance	9,474	10,209	—	7,136	51	7,335	102
With an allowance recorded:							
Mortgage loans on real estate:							
Residential 1-4 family	2,621	3,062	283	2,984	7	2,799	14
Commercial	617	1,051	73	540	2	435	4
Construction and land development	5,495	6,746	730	5,100	—	5,107	—
Second mortgages	—	—	—	74	—	6	—
Total real estate loans	8,733	10,859	1,086	8,698	9	8,347	18
Commercial loans	53	53	7	54	—	27	—
Consumer installment loans	281	285	37	82	—	81	—
Subtotal impaired loans with a valuation allowance	9,067	11,197	1,130	8,834	9	8,455	18
Total:							
Mortgage loans on real estate:							
Residential 1-4 family	4,325	4,993	283	5,554	18	5,662	36
Commercial	7,187	8,129	73	4,792	41	4,717	82
Construction and land development	5,495	6,746	730	5,100	—	5,107	—
Second mortgages	—	—	—	142	—	74	—
Total real estate loans	17,007	19,868	1,086	15,588	59	15,560	118
Commercial loans	1,253	1,253	7	54	—	27	—
Consumer installment loans	281	285	37	328	1	203	2
Total impaired loans	$ 18,541	$ 21,406	$ 1,130	$ 15,970	$ 60	$ 15,790	$ 120

(1) The amount of the investment in a loan, which is not net of a valuation allowance, but which does reflect any direct write-down of the investment

(2)

The contractual amount due, which reflects paydowns applied in accordance with loan documents, but which does not reflect any direct write-downs or valuation allowances

Troubled debt restructures and some substandard loans still accruing interest are loans that management expects to ultimately collect all principal and interest due, but not under the terms of the original contract. A reconciliation of impaired loans to nonaccrual loans at June 30, 2017 and December 31, 2016, is set forth in the table below (dollars in thousands):

	June 30, 2017	December 31, 2016
Nonaccruals	$ 11,514	$ 10,243
Trouble debt restructure and still accruing	5,354	4,653
Substandard and still accruing	—	3,645
Total impaired	$ 16,868	$ 18,541

14

Interest income on nonaccrual loans, if recognized, is recorded using the cash basis method of accounting. There was an insignificant amount of cash basis income recognized during the three and six months ended June 30, 2017 and 2016. For the three months ended June 30, 2017 and 2016, estimated interest income of $201,000 and $219,000, respectively, would have been recorded if all such loans had been accruing interest according to their original contractual terms. For the six months ended June 30, 2017 and 2016, estimated interest income of $345,000 and $409,000, respectively, would have been recorded if all such loans had been accruing interest according to their original contractual terms.

There were no loans greater than 90 days past due and still accruing interest at June 30, 2017 and December 31, 2016. The following tables present an age analysis of past due status of loans by category as of June 30, 2017 and December 31, 2016 (dollars in thousands):

	June 30, 2017				
	30-89 Days Past Due	Nonaccrual	Total Past Due	Current	Total Loans Receivable
Mortgage loans on real estate:					
Residential 1-4 family	$1,289	$ 2,130	$ 3,419	$209,083	$ 212,502
Commercial	1,904	3,548	5,452	335,730	341,182
Construction and land development	—	4,296	4,296	96,381	100,677
Second mortgages	—	—	—	7,537	7,537
Multifamily	—	—	—	50,511	50,511
Agriculture	—	258	258	7,727	7,985
Total real estate loans	3,193	10,232	13,425	706,969	720,394
Commercial loans	1,300	1,272	2,572	134,689	137,261
Consumer installment loans	52	10	62	5,045	5,107
All other loans	—	—	—	1,287	1,287
Total loans	$4,545	$ 11,514	$ 16,059	$847,990	$ 864,049

	December 31, 2016				
	30-89 Days Past Due	Nonaccrual	Total Past Due	Current	Total Loans Receivable
Mortgage loans on real estate:					
Residential 1-4 family	$296	$ 2,893	$ 3,189	$204,674	$ 207,863
Commercial	—	1,758	1,758	338,046	339,804
Construction and land development	54	5,495	5,549	92,733	98,282
Second mortgages	—	—	—	7,911	7,911
Multifamily	—	—	—	39,084	39,084
Agriculture	—	—	—	7,185	7,185
Total real estate loans	350	10,146	10,496	689,633	700,129
Commercial loans	—	53	53	129,247	129,300

Consumer installment loans	3	44	47	5,580	5,627
All other loans	—	—	—	1,243	1,243
Total loans	$353	$ 10,243	$ 10,596	$825,703	$ 836,299

15

Activity in the allowance for loan losses on loans by segment for the three and six months ended June 30, 2017 and 2016 is presented in the following tables (dollars in thousands):

	Three Months Ended June 30, 2017				
	March 31, 2017	Provision Allocation	Charge-offs	Recoveries	June 30, 2017
Mortgage loans on real estate:					
Residential 1-4 family	$2,823	$ 927	$ (12)	$ 59	$ 3,797
Commercial	1,776	(11)	—	18	1,783
Construction and land development	1,547	(226)	—	62	1,383
Second mortgages	50	(19)	—	2	33
Multifamily	193	(26)	—	—	167
Agriculture	32	(11)	—	—	21
Total real estate loans	6,421	634	(12)	141	7,184
Commercial loans	1,316	260	(120)	1	1,457
Consumer installment loans	133	12	(78)	44	111
All other loans	15	(6)	—	—	9
Unallocated	1,628	(900)	—	—	728
Total loans	$9,513	$ —	$ (210)	$ 186	$ 9,489

	Three Months Ended June 30, 2016				
	March 31, 2016	Provision Allocation	Charge-offs	Recoveries	June 30, 2016
Mortgage loans on real estate:					
Residential 1-4 family	$2,455	$ 281	$ (305)	$ 14	$ 2,445
Commercial	3,114	516	(75)	17	3,572
Construction and land development	1,589	(13)	—	1	1,577
Second mortgages	103	(58)	—	1	46
Multifamily	300	(7)	—	—	293
Agriculture	12	13	—	—	25
Total real estate loans	7,573	732	(380)	33	7,958
Commercial loans	948	310	—	10	1,268
Consumer installment loans	86	39	(34)	11	102
All other loans	6	4	—	—	10
Unallocated	981	(885)	—	—	96
Total loans	$9,594	$ 200	$ (414)	$ 54	$ 9,434

	Six Months Ended June 30, 2017				
	December 31, 2016	Provision Allocation	Charge-offs	Recoveries	June 30, 2017
Mortgage loans on real estate:					
Residential 1-4 family	$2,769	$ 989	$ (38)	$ 77	$ 3,797
Commercial	1,952	(194)	—	25	1,783

Construction and land development	2,195	(861)	(14)	63	1,383
Second mortgages	72	(88)	—	49	33
Multifamily	260	(93)	—	—	167
Agriculture	15	6	—	—	21
Total real estate loans	7,263	(241)	(52)	214	7,184
Commercial loans	602	972	(120)	3	1,457
Consumer installment loans	135	25	(123)	74	111
All other loans	7	2	—	—	9
Unallocated	1,486	(758)	—	—	728
Total loans	$9,493	$ —	$ (295)	$ 291	$ 9,489

	Six Months Ended June 30, 2016				
	December 31, 2015	Provision Allocation	Charge-offs	Recoveries	June 30, 2016
Mortgage loans on real estate:					
Residential 1-4 family	$2,884	$ (225)	$ (325)	$ 111	$ 2,445
Commercial	3,769	(114)	(112)	29	3,572
Construction and land development	1,298	277	—	2	1,577
Second mortgages	96	(56)	—	6	46
Multifamily	141	152	—	—	293
Agriculture	24	1	—	—	25
Total real estate loans	8,212	35	(437)	148	7,958
Commercial loans	631	626	—	11	1,268
Consumer installment loans	93	56	(116)	69	102
All other loans	25	(15)	—	—	10
Unallocated	598	(502)	—	—	96
Total loans	$9,559	$ 200	$ (553)	$ 228	$ 9,434

The following tables present information on the loans evaluated for impairment in the allowance for loan losses as of June 30, 2017 and December 31, 2016 (dollars in thousands):

	June 30, 2017					
	Allowance for Loan Losses			Recorded Investment in Loans		
	Individually Evaluated for Impairment	Collectively Evaluated for Impairment	Total	Individually Evaluated for Impairment	Collectively Evaluated for Impairment	Total
Mortgage loans on real estate:						
Residential 1-4 family	$314	$ 3,483	$3,797	$4,310	$ 208,192	$212,502
Commercial	355	1,428	1,783	6,495	334,687	341,182
Construction and land development	569	814	1,383	4,296	96,381	100,677
Second mortgages	—	33	33	—	7,537	7,537
Multifamily	—	167	167	—	50,511	50,511
Agriculture	—	21	21	258	7,727	7,985
Total real estate loans	1,238	5,946	7,184	15,359	705,035	720,394
Commercial loans	189	1,268	1,457	1,499	135,762	137,261
Consumer installment loans	1	110	111	10	5,097	5,107
All other loans	—	9	9	—	1,287	1,287
Unallocated	—	728	728	—	—	—
Total loans	$1,428	$ 8,061	$9,489	$16,868	$ 847,181	$864,049

	December 31, 2016					
	Allowance for Loan Losses			Recorded Investment in Loans		
	Individually Evaluated for Impairment	Collectively Evaluated for Impairment	Total	Individually Evaluated for Impairment	Collectively Evaluated for Impairment	Total
Mortgage loans on real estate:						
Residential 1-4 family	$283	$ 2,486	$2,769	$4,325	$ 203,538	$207,863
Commercial	73	1,879	1,952	7,187	332,617	339,804
Construction and land development	730	1,465	2,195	5,495	92,787	98,282
Second mortgages	—	72	72	—	7,911	7,911
Multifamily	—	260	260	—	39,084	39,084
Agriculture	—	15	15	—	7,185	7,185
Total real estate loans	1,086	6,177	7,263	17,007	683,122	700,129
Commercial loans	7	595	602	1,253	128,047	129,300
Consumer installment loans	37	98	135	281	5,346	5,627
All other loans	—	7	7	—	1,243	1,243
Unallocated	—	1,486	1,486	—	—	—
Total loans	$1,130	$ 8,363	$9,493	$18,541	$ 817,758	$836,299

Loans are monitored for credit quality on a recurring basis. These credit quality indicators are defined as follows:

Pass - A pass loan is not adversely classified, as it does not display any of the characteristics for adverse classification. This category includes purchased loans that are 100% guaranteed by U.S. Government agencies of $15.5 million and $15.8 million at June 30, 2017 and December 31, 2016, respectively.

Special Mention - A special mention loan has potential weaknesses that deserve management's close attention. If left uncorrected, such potential weaknesses may result in deterioration of the repayment prospects or collateral position at some future date. Special mention loans are not adversely classified and do not warrant adverse classification.

Substandard - A substandard loan is inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any. Loans classified as substandard generally have a well defined weakness, or weaknesses, that jeopardize the liquidation of the debt. These loans are characterized by the distinct possibility of loss if the deficiencies are not corrected.

Doubtful - A doubtful loan has all the weaknesses inherent in a loan classified as substandard with the added characteristics that the weaknesses make collection or liquidation in full, highly questionable and improbable, on the basis of currently existing facts, conditions, and values. The possibility of loss is extremely high.

18

The following tables present the composition of loans by credit quality indicator at June 30, 2017 and December 31, 2016 (dollars in thousands):

	June 30, 2017				
	Pass	Special Mention	Substandard	Doubtful	Total
Mortgage loans on real estate:					
Residential 1-4 family	$206,324	$3,934	$ 2,244	$ —	$212,502
Commercial	333,570	2,523	5,089	—	341,182
Construction and land development	95,677	703	4,297	—	100,677
Second mortgages	7,427	110	—	—	7,537
Multifamily	47,950	—	2,561	—	50,511
Agriculture	7,327	380	278	—	7,985
Total real estate loans	698,275	7,650	14,469	—	720,394
Commercial loans	131,826	2,833	2,602	—	137,261
Consumer installment loans	5,057	40	10	—	5,107
All other loans	1,287	—	—	—	1,287
Total loans	$836,445	$10,523	$ 17,081	$ —	$864,049

	December 31, 2016				
	Pass	Special Mention	Substandard	Doubtful	Total
Mortgage loans on real estate:					
Residential 1-4 family	$199,973	$4,612	$ 3,278	$ —	$207,863
Commercial	330,851	3,168	5,785	—	339,804
Construction and land development	92,556	234	5,492	—	98,282
Second mortgages	7,474	437	—	—	7,911
Multifamily	36,474	—	2,610	—	39,084
Agriculture	7,067	118	—	—	7,185
Total real estate loans	674,395	8,569	17,165	—	700,129
Commercial loans	122,129	5,879	1,292	—	129,300
Consumer installment loans	5,563	20	44	—	5,627
All other loans	1,243	—	—	—	1,243
Total loans	$803,330	$14,468	$ 18,501	$ —	$836,299

In accordance with FASB ASU 2011-02, *Receivables (Topic 310): A Creditor's Determination of Whether a Restructuring is a Troubled Debt Restructuring,* the Company assesses all loan modifications to determine whether they are considered troubled debt restructurings (TDRs) under the guidance. The Company had 21 and 18 loans that met the definition of a TDR as of June 30, 2017 and 2016, respectively.

During the three and six months ended June 30, 2017, the Company modified one 1-4 family loan and one agriculture loan that was considered to be a TDR. The Company lowered the interest rate for the 1-4 family loan, which had a pre- and post-modification balance of $894,000. The Company extended the terms for the agriculture loan, which had a pre- and post-modification balance of $258,000.

During the three months ended June 30, 2016, the Company modified one residential 1-4 family loan that was considered to be a TDR. The Company extended the terms for this loan, which had a pre- and post-modification balance of $81,000 and $97,000, respectively. During the six months ended June 30, 2016, the Company modified one residential 1-4 family loan and one consumer installment loan that was considered to be a TDR. The Company extended the terms for the residential 1-4 family loan, which had a pre- and post-modification balance of $81,000 and $97,000, respectively. The Company extended the terms and lowered the interest rate for the consumer installment loan, which had a pre- and post-modification balance of $248,000.

A loan is considered to be in default if it is 90 days or more past due. There were no TDRs that had been restructured during the previous 12 months that resulted in default during either of the three and six months ended June 30, 2017 and 2016.

In the determination of the allowance for loan losses, management considers TDRs and subsequent defaults in these restructures by reviewing for impairment in accordance with FASB ASC 310-10-35, *Receivables, Subsequent Measurement*.

At June 30, 2017, the Company had 1-4 family mortgages in the amount of $150.1 million pledged to the Federal Home Loan Bank with a lendable collateral value of $124.7 million.

Note 4. PCI Loans and Related Allowance for Loan Losses

On January 30, 2009, the Company entered into a Purchase and Assumption Agreement with the Federal Deposit Insurance Corporation (FDIC) to assume all of the deposits and certain other liabilities and acquire substantially all assets of Suburban Federal Savings Bank (SFSB). The Company is applying the provisions of FASB ASC 310-30, *Loans and Debt Securities Acquired with Deteriorated Credit Quality*, to all loans acquired in the SFSB transaction (the “PCI loans”). Of the total $198.3 million in loans acquired, $49.1 million met the criteria of FASB ASC 310-30. These loans, consisting mainly of construction loans, were deemed impaired at the acquisition date. The remaining $149.1 million of loans acquired, comprised mainly of residential 1-4 family, were analogized to meet the criteria of FASB ASC 310-30. Analysis of this portfolio revealed that SFSB utilized weak underwriting and documentation standards, which led the Company to believe that significant losses were probable given the economic environment at the time.

As of June 30, 2017 and December 31, 2016, the outstanding contractual balance of the PCI loans was $76.3 million and $81.1 million, respectively. The carrying amount, by loan type, as of these dates is as follows (dollars in thousands):

	June 30, 2017			December 31, 2016		
	Amount	% of PCI Loans		Amount	% of PCI Loans	
Mortgage loans on real estate:						
Residential 1-4 family	$43,290	89.47	%	$46,623	89.72	%
Commercial	571	1.18		649	1.25	
Construction and land development	1,915	3.96		1,969	3.79	

Second mortgages	2,348	4.85	2,453	4.72
Multifamily	263	0.54	270	0.52
Total real estate loans	48,387	100.00	51,964	100.00
Total PCI loans	$48,387	100.00 %	$51,964	100.00 %

There was no activity in the allowance for loan losses on PCI loans for the three and six months ended June 30, 2017 and 2016.

The following table presents information on the PCI loans collectively evaluated for impairment in the allowance for loan losses at June 30, 2017 and December 31, 2016 (dollars in thousands):

	June 30, 2017		December 31, 2016	
	Allowance for loan losses	Recorded investment in loans	Allowance for loan losses	Recorded investment in loans
Mortgage loans on real estate:				
Residential 1-4 family	$200	$ 43,290	$ 200	$ 46,623
Commercial	—	571	—	649
Construction and land development	—	1,915	—	1,969
Second mortgages	—	2,348	—	2,453
Multifamily	—	263	—	270
Total real estate loans	200	48,387	200	51,964
Total PCI loans	$200	$ 48,387	$ 200	$ 51,964

The change in the accretable yield balance for the six months ended June 30, 2017 and the year ended December 31, 2016, is as follows (dollars in thousands):

Balance, January 1, 2016	$49,128
Accretion	(6,206)
Reclassification from nonaccretable yield	5,433
Balance, December 31, 2016	$48,355
Accretion	(2,931)
Reclassification from nonaccretable yield	149
Balance, June 30, 2017	$45,573

The PCI loans were not classified as nonperforming assets as of June 30, 2017, as the loans are accounted for on a pooled basis, and interest income, through accretion of the difference between the carrying amount of the loans and the expected cash flows, is being recognized on all PCI loans.

Note 5. Other Real Estate Owned

The following table presents the balances of other real estate owned at June 30, 2017 and December 31, 2016 (dollars in thousands):

	June 30, 2017	December 31, 2016
Residential 1-4 family	$ 27	$ 1,276
Commercial	15	643
Construction and land development	2,345	2,508
Total other real estate owned	$ 2,387	$ 4,427

At June 30, 2017, the Company had $1.3 million in residential 1-4 family loans and PCI loans that were in the process of foreclosure.

Note 6. Deposits

The following table provides interest bearing deposit information, by type, as of June 30, 2017 and December 31, 2016 (dollars in thousands):

	June 30, 2017	December 31, 2016
NOW	$ 142,838	$ 137,332
MMDA	119,582	111,346
Savings	90,224	90,340
Time deposits less than or equal to $250,000	451,352	440,699
Time deposits over $250,000	140,418	128,690
Total interest bearing deposits	$ 944,414	$ 908,407

Note 7. Accumulated Other Comprehensive (Loss) Income

The following tables present activity net of tax in accumulated other comprehensive (loss) income (AOCI) for the three and six months ended June 30, 2017 and 2016 (dollars in thousands):

	Three months ended June 30, 2017			
	Unrealized Gain (Loss) on Securities	Defined Benefit Pension Plan	Gain (Loss) on Cash Flow Hedge	Total Other Comprehensive (Loss) Income
Beginning balance	$ 35	$ (767)	$ 8	$ (724)
Other comprehensive income (loss) before reclassifications	758	11	(33)	736
Amounts reclassified from AOCI	(24)	-	-	(24)
Net current period other comprehensive income (loss)	734	-	(33)	712
Ending balance	$ 769	$ (756)	$ (25)	$ (12)

	Three months ended June 30, 2016			
	Unrealized Gain (Loss) on Securities	Defined Benefit Pension Plan	Gain (Loss) on Cash Flow Hedge	Total Other Comprehensive (Loss) Income
Beginning balance	$ 2,617	$ (901)	$ (493)	$ 1,223
Other comprehensive income (loss) before reclassifications	1,085	-	(85)	1,000
Amounts reclassified from AOCI	(172)	-	-	(172)
Net current period other comprehensive income (loss)	913	-	(85)	828
Ending balance	$ 3,530	$ (901)	$ (578)	$ 2,051

	Six months ended June 30, 2017			
	Unrealized Gain (Loss) on Securities	Defined Benefit Pension Plan	Gain (Loss) on Cash Flow Hedge	Total Other Comprehensive (Loss) Income
Beginning balance	$ (410)	$ (767)	$ (46)	$ (1,223)
Other comprehensive income (loss) before reclassifications	1,266	11	21	1,298
Amounts reclassified from AOCI	(87)	-	-	(87)
Net current period other comprehensive income (loss)	1,179	-	21	1,211
Ending balance	$ 769	$ (756)	$ (25)	$ (12)

	Six months ended June 30, 2016			
	Unrealized Gain (Loss) on Securities	Defined Benefit Pension Plan	Gain (Loss) on Cash Flow Hedge	Total Other Comprehensive (Loss) Income
Beginning balance	$443	$ (901)	$ (131)	$ (589)
Other comprehensive income (loss) before reclassifications	3,430	-	(447)	2,983
Amounts reclassified from AOCI	(343)	-	-	(343)
Net current period other comprehensive income (loss)	3,087	-	(447)	2,640
Ending balance	$3,530	$ (901)	$ (578)	$ 2,051

22

The following table presents the effects of reclassifications out of AOCI on line items of consolidated income for the three and six months ended June 30, 2017 and 2016 (dollars in thousands):

Details about AOCI Components	Amount Reclassified from AOCI		Affected Line Item in the Unaudited Consolidated Statement of Income (Loss)
	Three months ended		
	June 30, 2017	June 30, 2016	
Securities available for sale:			
Unrealized gains on securities available for sale	$ (37)	$ (261)	Gain on securities transactions, net
Related tax expense	13	89	Income tax expense
	$ (24)	$ (172)	Net of tax

Details about AOCI Components	Amount Reclassified from AOCI		Affected Line Item in the Unaudited Consolidated Statement of Income (Loss)
	Six months ended		
	June 30, 2017	June 30, 2016	
Securities available for sale:			
Unrealized gains on securities available for sale	$ (132)	$ (520)	Gain on securities transactions, net
Related tax expense	45	177	Income tax expense
	$ (87)	$ (343)	Net of tax

Note 8. Fair Values of Assets and Liabilities

FASB ASC 820, *Fair Value Measurements and Disclosures,* defines fair value as the exchange price that would be received for an asset or paid to transfer a liability in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. FASB ASC 820 requires that valuation techniques maximize the use of observable inputs and minimize the use of unobservable inputs and also establishes a fair value hierarchy that prioritizes the valuation inputs into three broad levels. The Company groups assets and liabilities at fair value in three levels, based on the markets in which the assets and liabilities are traded and the reliability of the assumptions used to determine fair value. These levels are:

• Level 1—Valuation is based upon quoted prices for identical instruments traded in active markets.

• Level 2—Valuation is based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

• Level 3—Valuation is determined using model-based techniques with significant assumptions not observable in the market. These unobservable assumptions reflect the Company's own estimates of assumptions that market participants would use in pricing the asset or liability. Valuation techniques include the use of third party pricing services, option pricing models, discounted cash flow models and similar techniques.

FASB ASC 825, *Financial Instruments*, allows an entity the irrevocable option to elect fair value for the initial and subsequent measurement for certain financial assets and liabilities on a contract-by-contract basis. The Company has not made any material FASB ASC 825 elections as of June 30, 2017.

Assets and Liabilities Recorded at Fair Value on a Recurring Basis

The Company utilizes fair value measurements to record adjustments to certain assets to determine fair value disclosures. Securities available for sale and loans held for sale are recorded at fair value on a recurring basis. The tables below present the recorded amount of assets and liabilities measured at fair value on a recurring basis (dollars in thousands):

	June 30, 2017			
	Total	Level 1	Level 2	Level 3
Investment securities available for sale				
U.S. Treasury issue and other U.S. Gov't agencies	$46,829	$1,086	$45,743	$ -
U.S. Gov't sponsored agencies	2,790	-	2,790	-
State, county and municipal	125,833	3,552	122,281	-
Corporate and other bonds	16,090	-	16,090	-
Mortgage backed – U.S. Gov't agencies	4,254	-	4,254	-
Mortgage backed – U.S. Gov't sponsored agencies	16,547	1,809	14,738	-
Total investment securities available for sale	212,343	6,447	205,896	-
Total assets at fair value	$212,343	$6,447	$205,896	$ -
Cash flow hedge	39	-	39	-
Total liabilities at fair value	$39	$-	$39	$ -

	December 31, 2016			
	Total	Level 1	Level 2	Level 3
Investment securities available for sale				
U.S. Treasury issue and other U.S. Gov't agencies	$57,976	$11,055	$46,921	$ -
U.S. Gov't sponsored agencies	3,336	952	2,384	-
State, county and municipal	122,773	2,345	120,428	-
Corporate and other bonds	15,503	-	15,503	-
Mortgage backed – U.S. Gov't agencies	3,495	-	3,495	-
Mortgage backed – U.S. Gov't sponsored agencies	13,038	-	13,038	-
Total investment securities available for sale	216,121	14,352	201,769	-
Total assets at fair value	$216,121	$14,352	$201,769	$ -

Cash flow hedge	$(70)	$-	$(70)	$ -
Total liabilities at fair value	$(70)	$-	$(70)	$ -

Investment securities available for sale

Investment securities available for sale are recorded at fair value each reporting period. Fair value measurement is based upon quoted prices, if available (Level 1). If quoted prices are not available, fair values are measured using independent pricing models or other model-based valuation techniques such as the present value of future cash flows, adjusted for the security's credit rating, prepayment assumptions and other factors such as credit loss assumptions (Level 2).

The Company utilizes a third party vendor to provide fair value data for purposes of determining the fair value of its available for sale securities portfolio. The third party vendor uses a reputable pricing company for security market data. The third party vendor has controls and edits in place for month-to-month market checks and zero pricing, and a Statement on Standards for Attestation Engagements No. 16 report is obtained from the third party vendor on an annual basis. The Company makes no adjustments to the pricing service data received for its securities available for sale.

Cash flow hedge

The fair values of interest rate swaps are determined using the market standard methodology of netting the discounted future fixed cash receipts (or payments) and the discounted expected variable cash payments (or receipts). The variable cash payments (or receipts) are based on an expectation of future interest rates (forward curves) derived from observable market interest rate curves.

Assets and Liabilities Measured at Fair Value on a Nonrecurring Basis

The Company is also required to measure and recognize certain other financial assets at fair value on a nonrecurring basis on the consolidated balance sheet. The following tables present assets measured at fair value on a nonrecurring basis as of June 30, 2017 and December 31, 2016 (dollars in thousands):

	June 30, 2017			
	Total	Level 1	Level 2	Level 3
Impaired loans	$11,013	$ —	$1,301	$9,712
Other real estate owned	2,387	—	1,226	1,161
Total assets at fair value	$13,400	$ —	$2,527	$10,873
Total liabilities at fair value	$—	$ —	$—	$—

	December 31, 2016			
	Total	Level 1	Level 2	Level 3
Impaired loans	$9,536	$ —	$2,168	$7,368
Other real estate owned	4,427	—	3,408	1,019
Total assets at fair value	$13,963	$ —	$5,576	$8,387
Total liabilities at fair value	$—	$ —	$—	$—

Impaired loans

Loans for which it is probable that payment of interest and principal will not be made in accordance with the contractual terms of the loan agreement are considered impaired. Once a loan is identified as individually impaired, management measures the impairment in accordance with FASB ASC 310, *Receivables*. The fair value of impaired loans is estimated using one of several methods, including collateral value and discounted cash flows. Those impaired loans not requiring an allowance represent loans for which the fair value of the expected repayments or collateral exceeds the recorded investments in such loans. At June 30, 2017 and December 31, 2016, a majority of total impaired loans were evaluated based on the fair value of the collateral. The Company frequently obtains appraisals prepared by external professional appraisers for classified loans greater than $250,000 when the most recent appraisal is greater than 18 months old and/or deemed to be invalid. The Company may also utilize internally prepared estimates that generally result from current market data and actual sales data related to the Company’s collateral. When the fair value of the collateral is based on an observable market price or a current appraised value, the Company records the impaired loan within Level 2.

The Company may also identify collateral deterioration based on current market sales data, including price and absorption, as well as input from real estate sales professionals and developers, county or city tax assessments, market data and on-site inspections by Company personnel. When management determines that the fair value of the collateral is further impaired below the appraised value and there is no observable market price, the Company records the impaired loan as nonrecurring Level 3. In instances where an appraisal received subsequent to an internally prepared estimate reflects a higher collateral value, management does not revise the carrying amount. Impaired loans can also be evaluated for impairment using the present value of expected future cash flows discounted at the loan’s effective interest rate. The measurement of impaired loans using future cash flows discounted at the loan’s effective interest rate rather than the market rate of interest rate is not a fair value measurement and is therefore excluded from fair value disclosure requirements. Reviews of classified loans are performed by management on a quarterly basis.

Other real estate owned

OREO assets are adjusted to fair value less estimated disposal costs upon transfer of the related loans to OREO property, establishing a new cost basis. Subsequent to the transfer, valuations are periodically performed by management and the assets are carried at the lower of carrying value or fair value less estimated disposal costs. Fair value is based upon independent market prices, appraised values of the collateral or management's estimation of the value of the collateral. When the fair value of the collateral is based on an observable market price or a current appraised value, the Company records the foreclosed asset within Level 2. When an appraised value is not available or management determines that the fair value of the collateral is further impaired below the appraised value due to such things as absorption rates and market conditions, the Company records the foreclosed asset within Level 3 of the fair value hierarchy.

Fair Value of Financial Instruments

FASB ASC 825, *Financial Instruments*, requires disclosure of the fair value of financial assets and financial liabilities, including those financial assets and financial liabilities that are not measured and reported at fair value on a recurring or nonrecurring basis. FASB ASC 825 excludes certain financial instruments and all nonfinancial instruments from its disclosure requirements. Accordingly, the aggregate fair value amounts presented may not necessarily represent the underlying fair value of the Company.

The following reflects the fair value of financial instruments, whether or not measured as such on the consolidated balance sheet, at fair value measures by level of valuation assumptions used for those assets. These tables exclude financial instruments for which the carrying value approximates fair value (dollars in thousands):

	June 30, 2017				
	Carrying Value	**Estimated Fair Value**	Level 1	Level 2	Level 3
Financial assets:					
Securities held to maturity	$46,914	$ 47,764	$ 643	$47,121	$—
Loans, net of allowance	854,560	855,322	—	845,610	9,712
PCI loans, net of allowance	48,187	53,879	—	—	53,879
Financial liabilities:					
Interest bearing deposits	944,414	945,069	—	945,069	—
Long-term borrowings	80,618	80,549	—	80,549	—

	December 31, 2016				
	Carrying Value	**Estimated Fair Value**	Level 1	Level 2	Level 3
Financial assets:					
Securities held to maturity	$46,608	$ 46,858	$1,093	$45,765	$—
Loans, net of allowance	826,806	829,349	—	821,981	7,368
PCI loans, net of allowance	51,764	57,100	—	—	57,100
Financial liabilities:					
Interest bearing deposits	908,407	909,627	—	909,627	—
Long-term borrowings	87,681	87,611	—	87,611	—

The following methods were used to estimate the fair value of all other financial instruments recognized in the accompanying balance sheets at amounts other than fair value as of June 30, 2017. The Company applied the provisions of FASB ASC 820 to the fair value measurements of financial instruments not recognized on the consolidated balance sheet at fair value. The provisions requiring the Company to maximize the use of observable inputs and to measure fair value using a notion of exit price were factored into the Company's selection of inputs into its established valuation techniques.

26

Financial Assets

Cash and cash equivalents

The carrying amounts of cash and due from banks, interest bearing bank deposits, and federal funds sold approximate fair value (Level 1).

Securities held to maturity

For securities held to maturity, fair values are based on quoted market prices or dealer quotes (Level 1 and 2).

Restricted securities

The carrying value of restricted securities approximates their fair value based on the redemption provisions of the respective issuer (Level 2).

Loans

The fair value of loans is estimated by discounting the future cash flows using the current rates at which similar loans would be made to borrowers with similar credit ratings and for the same remaining maturities. The fair value of impaired loans is consistent with the methodology used for the FASB ASC 820 disclosure for assets recorded at fair value on a nonrecurring basis presented above.

PCI loans

Fair values for PCI loans are based on a discounted cash flow methodology that considers various factors including the type of loan and related collateral, classification status, term of loan and whether or not the loans are amortizing.

Loans were pooled together according to similar characteristics and were treated in the aggregate when applying various valuation techniques. The discount rates used for loans are based on the rates used at acquisition (which were based on market rates for new originations of comparable loans) adjusted for any material changes in interest rates since acquisition. Increases in cash flow expectations since acquisition resulted in estimated fair value being higher than carrying value. The increase in cash flows is also reflected in a transfer from unaccretable yield to accretable yield as disclosed in Note 4.

Accrued interest receivable

The carrying amounts of accrued interest receivable approximate fair value (Level 2).

Financial Liabilities

Noninterest bearing deposits

The carrying amount of noninterest bearing deposits approximates fair value (Level 2).

Interest bearing deposits

The fair value of NOW accounts, savings accounts, and certain money market deposits is the amount payable on demand at the reporting date. The fair value of fixed-maturity certificates of deposit is estimated using the rates currently offered for deposits of similar remaining maturities.

Federal funds purchased

The carrying amount of federal funds purchased approximates fair value (Level 2).

Long-term borrowings

The fair values of the Company's long-term borrowings, such as FHLB advances and long-term debt, are estimated using discounted cash flow analyses based on the Company's current incremental borrowing rates for similar types of borrowing arrangements.

Accrued interest payable

The carrying amounts of accrued interest payable approximate fair value (Level 2).

Off-balance sheet financial instruments

The fair value of commitments to extend credit is estimated using the fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the present creditworthiness of the counterparties. For fixed-rate loan commitments, fair value also considers the difference between current levels of interest rates and the committed rates. The fair value of stand-by letters of credit is based on fees currently charged for similar agreements or on the estimated cost to terminate them or otherwise settle the obligations with the counterparties at the reporting date. The Company's off-balance sheet commitments are funded at current market rates at the date they are drawn upon. It is management's opinion that the fair value of these commitments would approximate their carrying value, if drawn upon.

The fair values of interest rate swaps are determined using the market standard methodology of netting the discounted future fixed cash receipts (or payments) and the discounted expected variable cash payments (or receipts). The variable cash payments (or receipts) are based on an expectation of future interest rates (forward curves) derived from observable market interest rate curves.

The Company assumes interest rate risk (the risk that general interest rate levels will change) as a result of its normal operations. As a result, the fair values of the Company's financial instruments will change when interest rate levels change, and that change may be either favorable or unfavorable. Management attempts to match maturities of assets and liabilities to the extent believed necessary to minimize interest rate risk. However, borrowers with fixed rate obligations are less likely to prepay in a rising rate environment and more likely to prepay in a falling rate environment. Conversely, depositors who are receiving fixed rates are more likely to withdraw funds before maturity in a rising rate environment and less likely to do so in a falling rate environment. Management monitors rates and maturities of assets and liabilities and attempts to minimize interest rate risk by adjusting terms of new loans and deposits and by investing in securities with terms that mitigate the Company’s overall interest rate risk.

Note 9. Earnings Per Common Share

Basic earnings per common share (EPS) is computed by dividing net income by the weighted average number of common shares outstanding during the period. Diluted EPS is computed using the weighted average number of common shares outstanding during the period, including the effect of all potentially dilutive common shares outstanding attributable to stock instruments. The following table presents basic and diluted EPS for the three and six months ended June 30, 2017 and 2016 (dollars and shares in thousands, except per share data):

	Net Income (Numerator)	Weighted Average Common Shares (Denominator)	Per Common Share Amount
For the three months ended June 30, 2017			
Basic EPS	$ 2,934	21,997	$ 0.13
Effect of dilutive stock awards	—	427	—
Diluted EPS	$ 2,934	22,424	$ 0.13
For the three months ended June 30, 2016			
Basic EPS	$ 2,318	21,897	$ 0.11
Effect of dilutive stock awards	—	142	—
Diluted EPS	$ 2,318	22,039	$ 0.11
For the six months ended June 30, 2017			
Basic EPS	$ 5,427	21,979	$ 0.25
Effect of dilutive stock awards	—	461	(0.01)
Diluted EPS	$ 5,427	22,440	$ 0.24
For the six months ended June 30, 2016			
Basic EPS	$ 4,738	21,885	$ 0.22
Effect of dilutive stock awards	—	195	—
Diluted EPS	$ 4,738	22,080	$ 0.22

There were no antidilutive exclusions from the computation of diluted earnings per common share for the three and six months ended June 30, 2017. Antidilutive common shares issuable under awards or options of 259,000 were excluded from the computation of diluted earnings per common share for the three and six months ended June 30, 2016.

Note 10. Employee Benefit Plan

The Company adopted the Bank of Essex noncontributory, defined benefit pension plan for all full-time pre-merger Bank of Essex employees over 21 years of age. Benefits are generally based upon years of service and the employees' compensation. The Company funds pension costs in accordance with the funding provisions of the Employee Retirement Income Security Act.

The Company has frozen the plan benefits for all the defined benefit plan participants effective December 31, 2010.

The following table provides the components of net periodic benefit cost for the plan for the three and six months ended June 30, 2017 and 2016 (dollars in thousands):

	Three months ended		Six months ended	
	June 30, 2017	June 30, 2016	June 30, 2017	June 30, 2016
Interest cost	$ 39	$ 47	$ 78	$ 95
Expected return on plan assets	(70)	(81)	(140)	(163)
Amortization of prior service cost	1	1	2	2
Recognized net loss due to settlement	—	13	—	26
Recognized net actuarial loss	12	59	24	72
Net periodic benefit (income) cost	$ (18)	$ 39	$ (36)	$ 32

In accordance with FASB ASC 715, *Compensation-Retirement Benefits*, settlement accounting is triggered when lump sum payments to plan participants exceed the sum of the plan's service cost and interest cost for the year. The impact of settlement accounting is that a percentage of any outstanding losses that the plan is currently amortizing must be recognized immediately. This percentage is calculated as the ratio of lump sums paid to the total liability for the plan. This amount changes as plan participants retire during the year.

Note 11. Cash Flow Hedge

On November 7, 2014, the Company entered into an interest rate swap with a total notional amount of $30 million. The Company designated the swap as a cash flow hedge intended to protect against the variability in the expected future cash flows on the designated variable rate borrowings. The swap hedges the interest rate risk, wherein the Company will receive an interest rate based on the three month LIBOR from the counterparty and pays an interest rate of 1.69% to the same counterparty calculated on the notional amount for a term of five years. The Company intends to sequentially issue a series of three month fixed rate debt as part of a planned roll-over of short term debt for five years. The forecasted funding will be provided through one of the following wholesale funding sources: a new FHLB advance, a new repurchase agreement, or a pool of brokered CDs, based on whichever market offers the most advantageous pricing at the time that pricing is first initially determined for the effective date of the swap and each reset period thereafter. Each quarter when the Company rolls over the three month debt, it will decide at that time which funding source to use for that quarterly period.

The swap was entered into with a counterparty that met the Company's credit standards, and the agreement contains collateral provisions protecting the at-risk party. The Company believes that the credit risk inherent in the contract is not significant. The Company had $390,000 of cash pledged as collateral for each of the periods ended June 30, 2017 and December 31, 2016.

Amounts receivable or payable are recognized as accrued under the terms of the agreements. In accordance with FASB ASC 815, *Derivatives and Hedging*, the Company has designated the swap as a cash flow hedge, with the effective portions of the derivatives' unrealized gains or losses recorded as a component of other comprehensive income. The ineffective portions of the unrealized gains or losses, if any, would be recorded in other operating expense. The Company has assessed the effectiveness of each hedging relationship by comparing the changes in cash flows on the designated hedged item. The Company's cash flow hedge was deemed to be effective for the three and six months ended June 30, 2017 and 2016. The fair value of the Company's cash flow hedge was an unrealized loss of $39,000 and $70,000 at June 30, 2017 and December 31, 2016, respectively, and was recorded in other liabilities. The loss was recorded as a component of other comprehensive income net of associated tax effects.

Item 2. ***Management's Discussion and Analysis of Financial Condition and Results of Operations***

The following discussion and analysis of the financial condition at June 30, 2017 and results of operations of Community Bankers Trust Corporation (the "Company") for the three and six months ended June 30, 2017 should be read in conjunction with the Company's consolidated financial statements and the accompanying notes to consolidated financial statements included in this report and in the Company's Annual Report on Form 10-K for the year ended December 31, 2016.

OVERVIEW

Community Bankers Trust Corporation (the "Company") is headquartered in Richmond, Virginia and is the holding company for Essex Bank (the "Bank"), a Virginia state bank with 25 full-service offices in Virginia and Maryland. The Bank also operates one loan production office in Virginia.

The Bank engages in a general commercial banking business and provides a wide range of financial services primarily to individuals and small businesses, including individual and commercial demand and time deposit accounts, commercial and industrial loans, consumer and small business loans, real estate and mortgage loans, investment services, on-line and mobile banking products, and safe deposit box facilities.

The Company generates a significant amount of its income from the net interest income earned by the Bank. Net interest income is the difference between interest income and interest expense. Interest income depends on the amount of interest earning assets outstanding during the period and the interest rates earned thereon. The Company's cost of funds is a function of the average amount of interest bearing deposits and borrowed money outstanding during the period and the interest rates paid thereon. The quality of the assets further influences the amount of interest income lost on nonaccrual loans and the amount of additions to the allowance for loan losses. Additionally, the Bank earns noninterest income from service charges on deposit accounts and other fee or commission-based services and products. Other sources of noninterest income can include gains or losses on securities transactions, mortgage loan income and income from Bank Owned Life Insurance (BOLI) policies. The Company's income is offset by noninterest expense, which consists of salaries and employee benefits, occupancy and equipment costs, professional fees, transactions involving bank-owned property, the amortization of intangible assets and other operational expenses. The provision for loan losses and income taxes may materially affect net income.

CAUTION ABOUT FORWARD-LOOKING STATEMENTS

The Company makes certain forward-looking statements in this report that are subject to risks and uncertainties. These forward-looking statements include statements regarding our profitability, liquidity, allowance for loan losses, interest rate sensitivity, market risk, future strategy, and financial and other goals. These forward-looking statements are generally identified by phrases such as “the Company expects,” “the Company believes” or words of similar import.

These forward-looking statements are subject to significant uncertainties because they are based upon or are affected by factors, including, without limitation, the effects of and changes in the following:

- the quality or composition of the Company’s loan or investment portfolios, including collateral values and the repayment abilities of borrowers and issuers;
- assumptions that underlie the Company’s allowance for loan losses;
- general economic and market conditions, either nationally or in the Company’s market areas;
- the interest rate environment;
- competitive pressures among banks and financial institutions or from companies outside the banking industry;
- real estate values;
- the demand for deposit, loan, and investment products and other financial services;

- the demand, development and acceptance of new products and services;
- the performance of vendors or other parties with which the Company does business;
- time and costs associated with de novo branching, acquisitions, dispositions and similar transactions;
- the realization of gains and expense savings from acquisitions, dispositions and similar transactions;
- assumptions and estimates that underlie the accounting for purchased credit impaired loans;
- consumer profiles and spending and savings habits;
- levels of fraud in the banking industry;
- the level of attempted cyber attacks in the banking industry;
- the securities and credit markets;
- costs associated with the integration of banking and other internal operations;
- the soundness of other financial institutions with which the Company does business;
- inflation;
- technology; and
- legislative and regulatory requirements.

These factors and additional risks and uncertainties are described in the Company’s Annual Report on Form 10-K for the year ended December 31, 2016 and other reports filed from time to time by the Company with the Securities and Exchange Commission.

Although the Company believes that its expectations with respect to the forward-looking statements are based upon reliable assumptions within the bounds of its knowledge of its business and operations, there can be no assurance that actual results, performance or achievements of the Company will not differ materially from any future results, performance or achievements expressed or implied by such forward-looking statements.

CRITICAL ACCOUNTING POLICIES

The Company’s financial statements are prepared in accordance with accounting principles generally accepted in the United States (GAAP). The financial information contained within the statements is, to a significant extent, financial information that is based on measures of the financial effects of transactions and events that have already occurred. A variety of factors could affect the ultimate value that is obtained when either earning income, recognizing an expense, recovering an asset or relieving a liability. For example, the Company uses historical loss factors as one factor in determining the inherent loss that may be present in its loan portfolio. Actual losses could differ significantly from the historical factors that the Company uses. In addition, GAAP itself may change from one previously acceptable method to another method. Although the economics of the Company’s transactions would be the same, the timing of events that would impact its transactions could change.

The following is a summary of the Company’s critical accounting policies that are highly dependent on estimates, assumptions and judgments.

Allowance for Loan Losses on Loans

The allowance for loan losses is established as losses are estimated to have occurred through a provision for loan losses charged to earnings. Loan losses are charged against the allowance when management believes the uncollectability of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance.

The allowance is an amount that management believes is appropriate to absorb estimated losses relating to specifically identified loans, as well as probable credit losses inherent in the balance of the loan portfolio, based on an evaluation of the collectability of existing loans and prior loss experience. This evaluation also takes into consideration such factors as changes in the nature and volume of the loan portfolio, overall portfolio quality, review of specific problem loans, and current economic conditions that may affect the borrower's ability to pay. This evaluation does not include the effects of expected losses on specific loans or groups of loans that are related to future events or expected changes in economic conditions. The evaluation also considers the following risk characteristics of each loan portfolio:

- Residential 1-4 family mortgage loans include HELOCs and single family investment properties secured by first liens. The carry risks associated with owner-occupied and investment properties are the continued credit-worthiness of the borrower, changes in the value of the collateral, successful property maintenance and collection of rents due from tenants. The Company manages these risks by using specific underwriting policies and procedures and by avoiding concentrations in geographic regions.

- Commercial real estate loans, including owner occupied and non-owner occupied mortgages, carry risks associated with the successful operations of the principal business operated on the property securing the loan or the successful operation of the real estate project securing the loan. General market conditions and economic activity may impact the performance of these loans. In addition to using specific underwriting policies and procedures for these types of loans, the Company manages risk by avoiding concentrations to any one business or industry, and by diversifying the lending to various lines of businesses, such as retail, office, office warehouse, industrial and hotel.

- Construction and land development loans are generally made to commercial and residential builders/developers for specific construction projects, as well as to consumer borrowers. These carry more risk than real estate term loans due to the dynamics of construction projects, changes in interest rates, the long-term financing market and state and local government regulations. The Company manages risk by using specific underwriting policies and procedures for these types of loans and by avoiding concentrations to any one business or industry and by diversifying lending to various lines of businesses, in various geographic regions and in various sales or rental price points.

- Second mortgages on residential 1-4 family loans carry risk associated with the continued credit-worthiness of the borrower, changes in value of the collateral and a higher risk of loss in the event the collateral is liquidated due to the inferior lien position. The Company manages risk by using specific underwriting policies and procedures.

- Multifamily loans carry risks associated with the successful operation of the property, general real estate market conditions and economic activity. In addition to using specific underwriting policies and procedures, the Company manages risk by avoiding concentrations to geographic regions and by diversifying the lending to various unit mixes, tenant profiles and rental rates.

- Agriculture loans carry risks associated with the successful operation of the business, changes in value of non-real estate collateral that may depreciate over time and inventory that may be affected by weather, biological, price, labor, regulatory and economic factors. The Company manages risks by using specific underwriting policies and procedures, as well as avoiding concentrations to individual borrowers and by diversifying lending to various agricultural lines of business (i.e., crops, cattle, dairy, etc.).

- Commercial loans carry risks associated with the successful operation of the business, changes in value of non-real estate collateral that may depreciate over time, accounts receivable whose collectability may change and inventory values that may be subject to various risks including obsolescence. General market conditions and economic activity may also impact the performance of these loans. In addition to using specific underwriting policies and procedures for these types of loans, the Company manages risk by diversifying the lending to various industries and avoids geographic concentrations.

- Consumer installment loans carry risks associated with the continued credit-worthiness of the borrower and the value of rapidly depreciating assets or lack thereof. These types of loans are more likely than real estate loans to be quickly and adversely affected by job loss, divorce, illness or personal bankruptcy. The Company manages risk by using specific underwriting policies and procedures for these types of loans.

- All other loans generally support the obligations of state and political subdivisions in the U.S. and are not a material source of business for the Company. The loans carry risks associated with the continued credit-worthiness of the obligations and economic activity. The Company manages risk by using specific underwriting policies and procedures for these types of loans.

While management uses the best information available to make its evaluation, future adjustments to the allowance may be necessary if there are significant changes in economic conditions. In addition, regulatory agencies, as an integral part of their examination process, periodically review the Company's allowance for loan losses, and may require the Company to make additions to the allowance based on their judgment about information available to them at the time of their examinations.

The allowance consists of specific, general and unallocated components. For loans that are also classified as impaired, an allowance is established when the discounted cash flows (or collateral value or observable market price) of the impaired loan is lower than the carrying value of that loan. The general component covers non-classified loans and is based on historical loss experience adjusted for qualitative factors. The unallocated component covers uncertainties that could affect management's estimate of probable losses.

A loan is considered impaired when, based on current information and events, it is probable that the Company will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed. Impairment is measured by either the present value of the expected future cash flows discounted at the loan's effective interest rate, the loan's obtainable market price, or the fair value of the collateral if the loan is collateral dependent.

Large groups of smaller balance homogeneous loans are collectively evaluated for impairment.

Accounting for Certain Loans Acquired in a Transfer

FASB ASC 310, *Receivables,* requires acquired loans to be recorded at fair value and prohibits carrying over valuation allowances in the initial accounting for acquired impaired loans. Loans carried at fair value, mortgage loans held for sale, and loans to borrowers in good standing under revolving credit arrangements are excluded from the scope of FASB ASC 310, which limits the yield that may be accreted to the excess of the undiscounted expected cash flows over the investor's initial investment in the loan. The excess of the contractual cash flows over expected cash flows may not be recognized as an adjustment of yield. Subsequent increases in cash flows to be collected are recognized prospectively through an adjustment of the loan's yield over its remaining life. Decreases in expected cash flows are recognized as impairments through the allowance for loan losses.

The Company's acquired loans from the Suburban Federal Savings Bank (SFSB) transaction (the "PCI loans"), subject to FASB ASC Topic 805, *Business Combinations*, were recorded at fair value and no separate valuation allowance was recorded at the date of acquisition. FASB ASC 310-30, *Loans and Debt Securities Acquired with Deteriorated Credit Quality,* applies to loans acquired in a transfer with evidence of deterioration of credit quality for which it is probable, at acquisition, that the investor will be unable to collect all contractually required payments receivable. The Company is applying the provisions of FASB ASC 310-30 to all loans acquired in the SFSB transaction. The Company has grouped loans together based on common risk characteristics including product type, delinquency status and loan documentation requirements among others.

The PCI loans are subject to the credit review standards described above for loans. If and when credit deterioration occurs subsequent to the date that the loans were acquired, a provision for loan loss for PCI loans will be charged to earnings for the full amount.

The Company has made an estimate of the total cash flows it expects to collect from each pool of loans, which includes undiscounted expected principal and interest. The excess of that amount over the fair value of the pool is referred to as accretable yield. Accretable yield is recognized as interest income on a constant yield basis over the life of the pool. The Company also determines each pool’s contractual principal and contractual interest payments. The excess of that amount over the total cash flows that it expects to collect from the pool is referred to as nonaccretable difference, which is not accreted into income. Judgmental prepayment assumptions are applied to both contractually required payments and cash flows expected to be collected at acquisition. Over the life of the loan or pool, the Company continues to estimate cash flows expected to be collected. Subsequent decreases in cash flows expected to be collected over the life of the pool are recognized as an impairment in the current period through the allowance for loan losses. Subsequent increases in expected or actual cash flows are first used to reverse any existing valuation allowance for that loan or pool. Any remaining increase in cash flows expected to be collected is recognized as an adjustment to the accretable yield with the amount of periodic accretion adjusted over the remaining life of the pool.

Other Real Estate Owned

Real estate acquired through, or in lieu of, loan foreclosure is held for sale and is initially recorded at the fair value at the date of foreclosure net of estimated disposal costs, establishing a new cost basis. Subsequent to foreclosure, valuations are periodically performed by management and the assets are carried at the lower of the carrying amount or the fair value less costs to sell. Revenues and expenses from operations and changes in the valuation allowance are included in other operating expenses. Costs to bring a property to salable condition are capitalized up to the fair value of the property while costs to maintain a property in salable condition are expensed as incurred.

Other Intangible Assets

The Company is accounting for other intangible assets in accordance with FASB ASC 350, *Intangibles - Goodwill and Others*. Under FASB ASC 350, acquired intangible assets (such as core deposit intangibles) are separately recognized if the benefit of the assets can be sold, transferred, licensed, rented, or exchanged, and amortized over their useful lives. The costs of purchased deposit relationships and other intangible assets, based on independent valuation by a qualified third party, are being amortized over their estimated lives. The core deposit intangible is evaluated for impairment in accordance with FASB ASC 350.

Income Taxes

Deferred income tax assets and liabilities are determined using the liability (or balance sheet) method. Under this method, the net deferred tax asset or liability is determined based on the tax effects of the temporary differences between the book and tax bases of the various balance sheet assets and liabilities and gives current recognition to changes in tax rates and laws.

Positions taken in the Company's tax returns may be subject to challenge by the taxing authorities upon examination. Uncertain tax positions are initially recognized in the consolidated financial statements when it is more likely than not that the position will be sustained upon examination by the tax authorities. Such tax positions are both initially and subsequently measured as the largest amount of tax benefit that is greater than 50 percent likely of being realized upon settlement with the tax authority, assuming full knowledge of the position and all relevant facts. The Company provides for interest and, in some cases, penalties on tax positions that may be challenged by the taxing authorities. Interest expense is recognized beginning in the first period that such interest would begin accruing. Penalties are recognized in the period that the Company claims the position in the tax return. Interest and penalties on income tax uncertainties are classified within income tax expense in the consolidated statement of income. The Company had no interest or penalties during the three and six months ended June 30, 2017 and 2016. Under FASB ASC 740, *Income Taxes,* a valuation allowance is provided when it is more likely than not that some portion of the deferred tax asset will not be realized. In management's opinion, based on a three year taxable income projection, tax strategies that would result in potential securities gains and the effects of off-setting deferred tax liabilities, it is more likely than not that the deferred tax assets are realizable.

The Company and its subsidiaries are subject to U. S. federal income tax as well as Virginia and Maryland state income tax. All years from 2013 through 2016 are open to examination by the respective tax authorities.

RESULTS OF OPERATIONS

Overview

Net income was $2.9 million for the second quarter of 2017, compared with $2.3 million in the second quarter of 2016. Earnings per common share, basic and fully diluted, were $0.13 per share and $0.11 per share for the three months ended June 30, 2017 and 2016, respectively.

The increase of $616,000 in net income in the second quarter of 2017 over the same period in 2016 was principally driven by a $1.1 million increase in interest and fees on loans, which resulted in an increase in net interest income of $741,000, or 7.2%. Also improving in the second quarter of 2017 versus the same period in 2016 was a reduction of $189,000, or 21.5%, in income tax expense. Offsetting these improvements was an increase of $307,000, or 3.7%, in noninterest expenses and a decrease of $207,000 in noninterest income, as gains on securities transactions declined $224,000 year-over-year.

Net income was $5.4 million for the six months ended June 30, 2017 compared with $4.7 million for the first half of 2016. The increase in net income was the result of an increase of $2.0 million in interest and dividend income, driving an improvement in net interest income of $1.5 million. Another improvement was a decline of $96,000 in income tax expense. Offsetting the increases in net income was an increase of $727,000, or 4.5%, in noninterest expenses and a decline of $375,000 in noninterest income. Basic and fully diluted earnings per common share for the six months ended June 30, 2017 were $0.25 and $0.24, respectively, compared with basic and fully diluted earnings per common share of $0.22 for the same period in 2016. The change in basic earnings per common share represents an increase of 13.6%.

Net Interest Income

The Company’s operating results depend primarily on its net interest income, which is the difference between interest income on interest-earning assets, including securities and loans, and interest expense incurred on interest bearing liabilities, including deposits and other borrowed funds. Net interest income is affected by changes in the amount and mix of interest earning assets and interest bearing liabilities, referred to as a “volume change.” It is also affected by changes in yields earned on interest earning assets and rates paid on interest bearing deposits and other borrowed funds, referred to as a “rate change.”

Net interest income for the second quarter of 2017 was $11.0 million, an increase of $741,000, or 7.2%, from the second quarter of 2016. The yield on earning assets of 4.53% in the second quarter of 2017 is an increase of two basis points from 4.51% for the second quarter of 2016. The yield for the second quarter of 2017 was positively influenced by an increase in the yield on loans, from 4.59% in the second quarter of 2016 to 4.64% for the same period in 2017. Additionally, the tax-equivalent yield on securities increased from 3.03% in the second quarter of 2016 to 3.09% in the second quarter of 2017. Interest and dividend income increased $1.1 million, or 9.0%, over this time period. The average balance of loans increased $85.8 million, or 11.1%, from $774.6 million in the second quarter of 2016 to $860.4 million in the second quarter of 2017. Interest income on securities on a tax equivalent basis increased by $107,000, year-over-year, from $2.0 million in the second quarter of 2016 to $2.1 million in the second quarter of 2017. Interest and fees on PCI loans decreased by $103,000 year-over-year and was $1.5 million for the second quarter of 2017. The yield on the PCI portfolio was 11.8% in the second quarter of 2017 compared with 11.2% in the second quarter of 2016. The average balance of the PCI portfolio declined $6.5 million for the year-over-year comparison period.

Interest expense increased $346,000, or 18.2%, when comparing the second quarter of 2016 and the second quarter of 2017. Interest expense on deposits increased $407,000, or 26.5%, as the average balance of interest bearing deposits increased $93.3 million, or 11.1%. The Bank's cost of interest bearing liabilities increased from 0.80% in the second quarter of 2016 to 0.89% in the second quarter of 2017.

The tax equivalent net interest margin declined four basis points from 3.82% in the second quarter of 2016 to 3.78% in the second quarter of 2017. Likewise, the interest spread decreased from 3.71% to 3.64% over the same time period. The decline in the margin was precipitated by an increase of two basis points in yield on earning assets, offset by an increase of nine basis points in the cost of total interest bearing liabilities.

For the first half of 2017, net interest income increased $1.5 million, or 7.3%, over the prior year and was $21.8 million. The yield on earning assets of 4.57% for the same period compared with 4.52% for the first six months of 2016. Interest and fees on loans of $19.5 million in the first two quarters of 2017 was an increase of $2.1 million compared with $17.4 million for the same period in 2016. Interest and fees on PCI loans declined $223,000 over this same time frame. Securities income increased $63,000 for the first six months of 2017 compared with the same period in 2016. On a tax-equivalent basis, income on securities increased $89,000 and the tax-equivalent yield on the portfolio was 3.15% for the first two quarters of 2017 and 3.12% for the same period in 2016.

Interest expense of $4.3 million represents an increase of $502,000 in the first six months of 2017 compared with the same period in 2016. Total average interest bearing liabilities increased 5.9%, or $56.5 million, as loan growth has been fueled by an average balance increase of 12.1%, or $63.4 million, in time deposits and by a $23.8 million, or 22.4%, increase in noninterest bearing deposits.

The tax equivalent net interest margin was 3.83% for the first six months of 2017 versus 3.82% for the first six months of 2016. The net interest spread was 3.70% for the first six months of 2017 versus 3.71% for the first six months of 2016.

The following tables set forth, for each category of interest-earning assets and interest bearing liabilities, the average amounts outstanding, the interest earned or paid on such amounts, and the average rate earned or paid for the three and six months ended June 30, 2017 and 2016. The table also sets forth the average rate paid on total interest bearing liabilities, and the net interest margin on average total interest earning assets for the same periods. Except as indicated in the footnotes, no tax equivalent adjustments were made and all average balances are daily average balances. Any nonaccruing loans have been included in the tables, as loans carrying a zero yield.

NET INTEREST MARGIN ANALYSIS

AVERAGE BALANCE SHEETS

(Dollars in thousands)

	Three months ended June 30, 2017			Three months ended June 30, 2016		
	Average Balance Sheet	Interest Income/ Expense	Average Rates Earned/ Paid	Average Balance Sheet	Interest Income/ Expense	Average Rates Earned/ Paid
ASSETS:						
Loans	$ 860,393	$ 9,952	4.64 %	$ 774,553	$ 8,873	4.59 %
Purchased credit impaired (PCI) loans	49,253	1,453	11.80	55,780	1,556	11.19
Total loans	909,646	11,405	5.03	830,333	10,429	5.04
Interest bearing bank balances	19,225	52	1.10	13,338	23	0.71
Federal funds sold	137	-	1.04	-	-	-
Securities (taxable)	182,227	1,157	2.54	178,915	1,124	2.51
Securities (tax exempt)(1)	85,972	918	4.27	81,205	844	4.16
Total earning assets	1,197,207	13,532	4.53	1,103,791	12,420	4.51
Allowance for loan losses	(9,697)			(10,014)		
Non-earning assets	89,222			84,859		
Total assets	$ 1,276,732			$ 1,178,636		

LIABILITIES AND SHAREHOLDERS' EQUITY								
Demand - interest bearing	$ 241,376	154	0.26		$ 234,051	152	0.26	
Savings	91,723	60	0.26		84,508	55	0.26	
Time deposits	598,965	1,730	1.16		520,207	1,330	1.02	
Total deposits	932,064	1,944	0.84		838,766	1,537	0.73	
Short-term borrowings	517	2	1.37		1,405	3	0.92	
FHLB and other borrowings	84,761	300	1.42		103,883	302	1.17	
Long-term debt	-	-	-		4,862	58	4.75	
Total interest bearing liabilities	1,017,342	2,246	0.89		948,916	1,900	0.80	
Noninterest bearing deposits	133,320				113,777			
Other liabilities	5,654				5,076			
Total liabilities	1,156,316				1,067,769			
Shareholders' equity	120,416				110,867			
Total liabilities and shareholders' equity	$ 1,276,732				$ 1,178,636			
Net interest earnings		$ 11,286				$ 10,520		
Interest spread			3.64	%			3.71	%
Net interest margin			3.78	%			3.82	%
Tax equivalent adjustment:								
Securities		$ 312				$ 287		

(1) Income and yields are reported on a tax equivalent basis assuming a federal tax rate of 34%.

37

NET INTEREST MARGIN ANALYSIS

AVERAGE BALANCE SHEETS

(Dollars in thousands)

	Six months ended June 30, 2017			Six months ended June 30, 2016		
	Average Balance Sheet	Interest Income/ Expense	Average Rates Earned/ Paid	Average Balance Sheet	Interest Income/ Expense	Average Rates Earned/ Paid
ASSETS:						
Loans	$ 849,839	$ 19,549	4.64 %	$ 764,093	$ 17,426	4.57 %
Purchased credit impaired (PCI) loans	50,011	2,932	11.66	56,820	3,155	11.14
Total loans	899,850	22,481	5.04	820,913	20,581	5.03
Interest bearing bank balances	14,207	78	1.11	11,665	44	0.77
Federal funds sold	93	-	1.00	-	-	-
Securities (taxable)	182,734	2,406	2.63	181,788	2,395	2.63
Securities (tax exempt)[1]	85,353	1,822	4.27	83,631	1,744	4.17
Total earning assets	1,182,237	26,787	4.57	1,097,997	24,764	4.52
Allowance for loan losses	(9,709)			(10,046)		
Non-earning assets	88,919			83,344		
Total assets	$ 1,261,447			$ 1,171,295		
LIABILITIES AND SHAREHOLDERS' EQUITY						
Demand - interest bearing	$ 240,110	295	0.25	$ 232,356	325	0.28
Savings	91,829	121	0.27	83,818	118	0.28
Time deposits	586,722	3,307	1.14	523,337	2,645	1.01
Total deposits	918,661	3,723	0.82	839,511	3,088	0.74
Short-term borrowings	1,306	7	1.14	2,102	8	0.80
FHLB and other borrowings	87,354	597	1.38	103,949	608	1.17
Long-term debt	-	-	-	5,264	121	4.54
Total interest bearing liabilities	1,007,321	4,327	0.87	950,826	3,825	0.81
Noninterest bearing deposits	130,091			106,282		
Other liabilities	5,534			5,067		
Total liabilities	1,142,946			1,062,175		
Shareholders' equity	118,500			109,120		
Total liabilities and shareholders' equity	$ 1,261,446			$ 1,171,295		
Net interest earnings		$ 22,460			$ 20,939	
Interest spread			3.70 %			3.71 %
Net interest margin			3.83 %			3.82 %

Tax equivalent adjustment:		
Securities	$ 619	$ 593

(1) Income and yields are reported on a tax equivalent basis assuming a federal tax rate of 34%.

38

Provision for Loan Losses

Management actively monitors the Company’s asset quality and provides specific loss provisions when necessary. Provisions for loan losses are charged to income to bring the total allowance for loan losses to a level deemed appropriate by management of the Company based on such factors as historical credit loss experience, industry diversification of the commercial loan portfolio, the amount of nonperforming loans and related collateral, the volume growth and composition of the loan portfolio, current economic conditions that may affect the borrower’s ability to pay and the value of collateral, the evaluation of the loan portfolio through the internal loan review function and other relevant factors. See *Allowance for Loan Losses on Loans* in the Critical Accounting Policies section above for further discussion.

Loans are charged-off against the allowance for loan losses when appropriate. Although management believes it uses the best information available to make determinations with respect to the provision for loan losses, future adjustments may be necessary if economic conditions differ from the assumptions used in making the initial determinations.

Management also actively monitors its PCI loan portfolio for impairment and necessary loan loss provisions. Provisions for these loans may be necessary due to a change in expected cash flows or an increase in expected losses within a pool of loans.

The Company did not record a provision for loan losses during the three and six months ended June 30, 2017. Likewise, there was no provision for loan losses on the PCI loan portfolio during the three and six months ended June 30, 2017 and 2016, respectively. The Company recorded a $200,000 provision for loan losses for the three and six months ended June 30, 2016. The provision for loan losses booked in the second quarter of 2016 supported general reserves following loan growth of $19.5 million during the quarter. During the other periods, the absence of a provision was the direct result of minimal charge-offs and the ongoing stabilization of asset quality. Additional discussion of loan quality is presented below.

There were net charge-offs of $24,000 in the second quarter of 2017, compared with net charge-offs of $360,000 in the second quarter of 2016. Total charge-offs for the second quarter of 2017 were $210,000 compared with $414,000 in the second quarter of 2016. Recoveries of previously charged-off loans were $186,000 for the second quarter of 2017 compared with $54,000 in the second quarter of 2016.

There were net charge-offs of $4,000 for the six months ended June 30, 2017, compared with net charge-offs of $325,000 for the six months ended June 30, 2016. Total charge-offs for the six months ended June 30, 2017 were $295,000 compared with $553,000 for the six months ended June 30, 2016. Recoveries of previously charged-off loans were $291,000 for the six months ended June 30, 2017 compared with $228,000 for the six months ended June 30, 2016.

Noninterest Income

Noninterest income decreased $207,000, or 14.8%, from the second quarter of 2016 to the second quarter of 2017. Gains on securities transactions were $37,000 in the second quarter of 2017 compared with $261,000 in the second quarter of 2016, decreasing $224,000. Also decreasing year-over-year was mortgage loan income, which decreased $103,000. Offsetting these decreases were increases in service charges on deposit accounts, which increased by $91,000, or 15.2%, on a higher level of demand deposit accounts. Income on bank owned life insurance increased by $31,000 over the comparison period.

Noninterest income was $2.3 million for the first six months of 2017, a decrease of $375,000, or 13.8%, compared with $2.7 million for the first six months of 2016. Securities gains of $132,000 in the first two quarters of 2017 compared with $520,000 for the same period in 2016, a decrease of $388,000. Mortgage loan income of $104,000 for the first six months of 2017 is a decline of $243,000 from mortgage loan income of $347,000 for the same period in 2016. The Company discontinued a wholesale mortgage operation at the end of the third quarter of 2016 and has shifted to a platform that requires lower overhead but has equivalent or better net revenue potential. Offsetting these declines were a $165,000 increase in service charges on deposit accounts, which were $1.3 million for the first six months of 2017, and a $77,000 increase in income on bank owned life insurance. The increase in service charges is the result of an increased volume of DDA accounts in 2017 versus the same period in 2016.

Noninterest Expense

Noninterest expenses increased $307,000, or 3.7%, when comparing the second quarter of 2017 to the same period in 2016. Salaries and employee benefits increased $325,000 over this time frame while occupancy expenses increased $94,000, data processing expenses increased $72,000, other real estate expense increased $49,000 and equipment expenses increased $12,000. Offsetting these increases was a decrease of $137,000 in amortization of intangibles and a decrease of $88,000 in FDIC assessment.

Noninterest expenses were $17.0 million for the first six months of 2017, as compared with $16.3 million for the same period in 2016. This is an increase of $727,000, or 4.5%. This increase is primarily the result from staffing, occupancy, equipment, data processing, advertising and supply costs associated with the six full months in 2017 of operating new offices opened in Fairfax during the first quarter of 2016, in Cumberland in August 2016 and in western Henrico and Lynchburg during 2017. The largest increase in noninterest expenses over this time frame was in salaries and employee benefits, which increased $396,000, or 4.3%. Occupancy expenses increased by $185,000. Other real estate (ORE) expenses increased by $178,000 for the first six months of 2017 compared with the same period in 2016. The increase in other real estate expenses was the direct result of $197,000 in net gain on sale of ORE and $30,000 in gain on disposal of the Catonsville branch during the first six months of 2016. Offsetting those gains were ORE legal and direct expenses of $158,000 in 2016 versus $103,000 in 2017 and rental income on ORE properties of $47,000 during the first six months of 2016, compared to $41,000 during the first six months of 2017. Data processing fees increased by $145,000, equipment expenses by $57,000 and other operating expenses by $41,000 in the first six month of 2017 compared with the same period in 2016. Offsetting these increases to noninterest expenses were decreases to amortization of intangibles, which declined $137,000, and to FDIC assessment, which declined $138,000.

Income Taxes

Income tax expense was $692,000 for the three months ended June 30, 2017 compared with income tax expense of $881,000 for the second quarter of 2016. The effective tax rate was 19.1% for the second quarter of 2017 compared with 27.5% for the second quarter of 2016. The effective tax rate was 24.6% for the six month period ended June 30, 2017 compared with 28.2% for the same period in 2016.

FINANCIAL CONDITION

General

Total assets increased $40.7 million, or 3.3%, to $1.291 billion at June 30, 2017 as compared with $1.250 billion at December 31, 2016. Total loans were $864.0 million at June 30, 2017, increasing $27.8 million, or 3.3%, from year end 2016. Total PCI loans were $48.4 million at June 30, 2017 versus $52.0 million at year end 2016.

During the first six months of 2017, multifamily loans exhibited the largest dollar volume increase, $11.4 million, or 29.2%, and were $50.5 million, representing less than 6% of the total portfolio. Commercial loans grew $8.0 million, or 6.2%, and had total balances of $137.3 million at June 30, 2017. Residential 1-4 family loans grew $4.6 million, or 2.2%, and had total balances of $212.5 million at June 30, 2017. Construction and land development loan balances of

$100.7 million at June 30, 2017 grew $2.4 million during 2017.

The Company’s securities portfolio, excluding equity securities, declined $3.5 million, or 1.3%, from $262.7 million at December 31, 2016 to $259.3 million at June 30, 2017. Net realized gains of $132,000 were recognized during the first six months of 2017 through sales and call activity, as compared with $520,000 recognized during the first six months of 2016.

The Company is required to account for the effect of market changes in the value of securities available-for-sale (AFS) under FASB ASC 320, *Investments – Debt and Equity Securities*. The market value of the AFS portfolio was $212.3 million at June 30, 2017 and $216.1 million at December 31, 2016. At June 30, 2017, the Company had a net unrealized gain on the AFS portfolio of $1.2 million compared with a net unrealized loss of $621,000 at December 31, 2016. Municipal securities comprised 59.3% of the total AFS portfolio at June 30, 2017. These securities exhibit more price volatility in a changing interest rate environment because of their longer weighted average life, as compared to other categories contained within the rest of the portfolio.

The Company had cash and cash equivalents of $41.4 million and $21.1 million at June 30, 2017 and December 31, 2016, respectively. There were federal funds sold of $152,000 at June 30, 2017 and federal funds purchased of $4.7 million at December 31, 2016.

Interest bearing deposits at June 30, 2017 were $944.4 million, an increase of $36.0 million, or 4.0%, from $908.4 million at December 31, 2016. During this period, time deposits $250,000 and over increased $11.7 million, or 9.1%, time deposits less than or equal to $250,000 increased $10.7 million, or 2.4%, MMDA balances increased $8.2 million, or 7.4%, and NOW accounts increased $5.5 million, or 4.0%. Total deposits grew 4.4%, or $45.6 million, during 2017. That increase included a decline in brokered funding of $17.4 million, meaning retail deposits actually grew $63.0 million, or 6.4%, during 2017.

FHLB advances were $76.5 million at June 30, 2017, compared with $81.9 million at December 31, 2016. Long term debt was $0 at June 30, 2017 compared with $1.7 million at December 31, 2016. The Company has fully paid a borrowing, initially in the amount of $10.7 million and obtained in April 2014, the proceeds of which were used to redeem the Company's remaining outstanding TARP preferred stock.

Shareholders' equity was $121.8 million at June 30, 2017 and $114.5 million at December 31, 2016.

Asset Quality – excluding PCI loans

The allowance for loan losses represents management's estimate of the amount appropriate to provide for probable losses inherent in the loan portfolio.

Loan quality is continually monitored, and the Company's management has established an allowance for loan losses that it believes is appropriate for the risks inherent in the loan portfolio. Among other factors, management considers the Company's historical loss experience, the size and composition of the loan portfolio, the value and appropriateness of collateral and guarantors, nonperforming loans and current and anticipated economic conditions. There are additional risks of future loan losses, which cannot be precisely quantified nor attributed to particular loans or classes of loans. Because those risks include general economic trends, as well as conditions affecting individual borrowers, the allowance for loan losses is an estimate. The allowance is also subject to regulatory examinations and determination as to appropriateness, which may take into account such factors as the methodology used to calculate the allowance and size of the allowance in comparison to peer companies identified by regulatory agencies. See *Allowance for Loan Losses on Loans* in the Critical Accounting Policies section above for further discussion.

The Company maintains a list of loans that have potential weaknesses and thus may need special attention. This loan list is used to monitor such loans and is used in the determination of the appropriateness of the allowance for loan losses. Nonperforming assets totaled $13.9 million at June 30, 2017 and net charge-offs were $4,000 for the six months ended June 30, 2017. This compares with nonperforming assets of $14.7 million and net charge-offs of $516,000 at and for the year ended December 31, 2016.

Nonperforming loans were $11.5 million at June 30, 2017, a $1.3 million increase from $10.2 million at December 31, 2016. The $1.3 million increase in nonperforming loans since December 31, 2016 was the net result of $4.4 million in additions to nonperforming loans and $3.1 million in reductions. With respect to the reductions in nonperforming loans, $841,000 were payments to existing credits, $172,000 were charge-offs, $926,000 were loans returned to accruing status, and $1.2 million paid off.

The allowance for loan losses, excluding PCI, equaled 82.41% of nonaccrual loans at June 30, 2017 compared with 92.68% at December 31, 2016. The ratio of the allowance for loan losses to total nonperforming assets was 69.70% at June 30, 2017, compared with 66.07% at December 31, 2016. The ratio of nonperforming assets to loans and OREO continued to decline. The ratio was 1.60% at June 30, 2017 versus 1.74% at December 31, 2016.

In accordance with GAAP, an individual loan is impaired when, based on current information and events, it is probable that a creditor will be unable to collect all amounts due in accordance with contractual terms of the loan agreement. The Company considers all troubled debt restructures and nonaccrual loans to be impaired loans. In addition, the Company reviews all substandard and doubtful loans that are not on nonaccrual status, as well as loans with other risk characteristics, pursuant to and specifically for compliance with the accounting definition of impairment as described above. These impaired loans have been determined through analysis, appraisals, or other methods used by management.

See Note 3 to the Company's financial statements for information related to the allowance for loan losses. At June 30, 2017 and December 31, 2016, total impaired loans, excluding PCI loans, equaled $16.9 million and $18.5 million, respectively.

The following table sets forth selected asset quality data, excluding PCI loans, and ratios for the dates indicated (dollars in thousands):

	June 30, 2017		December 31, 2016	
Nonaccrual loans	$ 11,514		$ 10,243	
Loans past due 90 days and accruing interest	—		—	
Total nonperforming loans	11,514		10,243	
OREO	2,387		4,427	
Total nonperforming assets	$ 13,901		$ 14,670	
Accruing troubled debt restructure loans	$ 5,354		$ 4,653	
Balances				
Specific reserve on impaired loans	1,428		1,130	
General reserve related to unimpaired loans	8,061		8,363	
Total allowance for loan losses	9,489		9,493	
Average loans during the year, net of unearned income	849,839		787,245	
Impaired loans	16,868		18,541	
Non-impaired loans	847,181		817,758	
Total loans, net of unearned income	864,049		836,299	
Ratios				
Allowance for loan losses to loans, excluding PCI loans, to loans	1.10	%	1.14	%
Allowance for loan losses to nonperforming assets	69.70		66.07	
Allowance for loan losses, excluding PCI loans, to nonaccrual loans	82.41		92.68	
General reserve to non-impaired loans	0.95		1.02	
Nonaccrual loans to loans	1.33		1.22	
Nonperforming assets to loans and OREO	1.60		1.74	
Net charge-offs to average loans	0.00		0.07	

The Company grants troubled debt restructures (TDR) and other various loan workouts whereby an existing loan may be restructured into multiple new loans. At June 30, 2017, the Company had 21 loans that met the definition of a TDR, which are loans that for reasons related to the debtor's financial difficulties have been restructured on terms and conditions that would otherwise not be offered or granted. Six of these loans were restructured using multiple new loans. The aggregated outstanding principal of all TDR loans at June 30, 2017 was $6.9 million, of which $1.5 million were classified as nonaccrual.

The primary benefit of the restructured multiple loan workout strategy is to maximize the potential return by restructuring the loan into a “good loan” (the A loan) and a “bad loan” (the B loan). The impact on interest is positive because the Bank is collecting interest on the A loan rather than potentially not collecting interest on the entire original loan structure. The A loan is underwritten pursuant to the Bank’s standard requirements and graded accordingly. The B loan is classified as either “doubtful” or “loss”. An impairment analysis is performed on the B loan and, based on its results, all or a portion of the B loan is charged-off or a specific loan loss reserve is established.

The Company does not modify its nonaccrual policies in this arrangement, and the A loan and the B loan stand on their own terms. At inception, this structure meets the definition of a TDR. If the loan is on nonaccrual at the time of restructure, the A loan is held on nonaccrual until six consecutive payments have been received, at which time it may be put back on an accrual status. The B loan is placed on nonaccrual. Under the terms of each loan, the borrower’s payment is contractually due.

A further breakout of nonaccrual loans, excluding PCI loans, at June 30, 2017 and December 31, 2016 is below (dollars in thousands):

	June 30, 2017	December 31, 2016
Mortgage loans on real estate:		
Residential 1-4 family	$ 2,130	$ 2,893
Commercial	3,548	1,758
Construction and land development	4,296	5,495
Agriculture	258	—
Total real estate loans	10,232	10,146
Commercial loans	1,272	53
Consumer installment loans	10	44
Total loans	$ 11,514	$ 10,243

At June 30, 2017, the Company had six construction and land development credit relationships in nonaccrual status. The borrowers for all of these relationships are residential land developers. All of the relationships are secured by the real estate to be developed and are in the Company’s central Virginia market. The total amount of the credit exposure outstanding at June 30, 2017 was $4.3 million. These loans have either been charged-down or sufficiently reserved against to equal the current expected realizable value.

The total amount of the allowance for loan losses attributed to all six relationships was $569,000 at June 30, 2017, or 13.25% of the total credit exposure outstanding. The Company establishes its reserves as described above in *Allowance for Loan Losses on Loans* in the Critical Accounting Policies section. In conjunction with the impairment analysis the Company performs as part of its allowance methodology, the Company ordered appraisals for all loans with balances in excess of $250,000 unless there existed an appraisal that was not older than 18 months and/or deemed to be invalid. The Company uses a ratio analysis for balances less than $250,000. The Company maintains detailed analysis and other information for its allowance methodology, both for internal purposes and for review by its regulators.

Asset Quality – PCI loans

Loans accounted for under FASB ASC 310-30 are generally considered accruing and performing loans as the loans accrete interest income over the estimated life of the loan. Accordingly, acquired impaired loans that are contractually past due are still considered to be accruing and performing loans.

The Company makes an estimate of the total cash flows that it expects to collect from a pool of PCI loans, which include undiscounted expected principal and interest. Over the life of the loan or pool, the Company continues to estimate cash flows expected to be collected. Subsequent decreases in cash flows expected to be collected over the life of the pool are recognized as impairment in the current period through the allowance for loan losses. Subsequent increases in expected cash flows are first used to reverse any existing valuation allowance for that loan or pool. Any remaining increase in cash flows expected to be collected is recognized as an adjustment to the yield over the remaining life of the pool.

Capital Requirements

The determination of capital adequacy depends upon a number of factors, such as asset quality, liquidity, earnings, growth trends and economic conditions. The Company seeks to maintain a strong capital base exceeding regulatory minimums for well capitalized institutions to support its growth and expansion plans, provide stability to current operations and promote public confidence in the Company.

Under the final rule on Enhanced Regulatory Capital Standards, commonly referred to as Basel III which became effective January 1, 2015, the federal banking regulators have defined four tests for assessing the capital strength and adequacy of banks, based on three definitions of capital. “Common equity tier 1 capital” is defined as common equity, retained earnings, and accumulated other comprehensive income (AOCI), less certain intangibles. “Tier 1 capital” is defined as common equity tier 1 capital plus qualifying perpetual preferred stock, tier 1 minority interests, and grandfathered trust preferred securities. “Tier 2 capital” is defined as specific subordinated debt, some hybrid capital instruments and other qualifying preferred stock, non-tier 1 minority interests and a limited amount of the loan loss allowance. “Total capital” is defined as tier 1 capital plus tier 2 capital. Four risk-based capital ratios are computed using the above capital definitions, total assets and risk-weighted assets, and the ratios are measured against regulatory minimums to ascertain adequacy. All assets and off-balance sheet risk items are grouped into categories according to degree of risk and assigned a risk-weighting and the resulting total is risk-weighted assets. “Common equity tier 1 capital ratio” is common equity tier 1 capital divided by risk-weighted assets. “Tier 1 risk-based capital ratio” is tier 1 capital divided by risk-weighted assets. “Total risk-based capital ratio” is total capital divided by risk-weighted assets. The leverage ratio is tier 1 capital divided by total average assets.

The Company’s ratio of total risk-based capital was 13.5% at June 30, 2017 compared with 13.2% at December 31, 2016. The tier 1 risk-based capital ratio was 12.6% at June 30, 2017 and 12.2% at December 31, 2016. The Company’s tier 1 leverage ratio was 9.9% at June 30, 2017 and 9.6% at December 31, 2016. All capital ratios exceed regulatory minimums to be considered well capitalized. BASEL III introduced the common equity tier 1 capital ratio, which was 12.2% at June 30, 2017 and 11.8% at December 31, 2016.

Under Basel III, a capital conservation buffer of 2.5% above the minimum risk-based capital thresholds was established. Dividend and executive compensation restrictions begin if the Company does not maintain the full amount of the buffer. The capital conservation buffer will be phased in between January 1, 2016 and January 1, 2019. At June 30, 2017, the Company had a capital conservation buffer of 5.5%, well above the 2017 required buffer of 1.25%.

Liquidity

Liquidity represents the Company’s ability to meet present and future financial obligations through either the sale or maturity of existing assets or the acquisition of additional funds through liability management. Liquid assets include cash, interest bearing deposits with banks, federal funds sold and certain investment securities. As a result of the Company’s management of liquid assets and the ability to generate liquidity through liability funding, management believes that the Company maintains overall liquidity sufficient to satisfy its depositors’ requirements and meet its customers’ credit needs.

The Company’s results of operations are significantly affected by its ability to manage effectively the interest rate sensitivity and maturity of its interest earning assets and interest bearing liabilities. A summary of the Company’s liquid assets at June 30, 2017 and December 31, 2016 was as follows (dollars in thousands):

	June 30, 2017	December 31, 2016
Cash and due from banks	$ 11,342	$ 13,828
Interest bearing bank deposits	29,908	7,244
Federal funds sold	152	—
Available for sale securities, at fair value, unpledged	175,450	170,898
Total liquid assets	$ 216,852	$ 191,970
Deposits and other liabilities	$ 1,168,750	$ 1,135,280
Ratio of liquid assets to deposits and other liabilities	18.55 %	16.91 %

Off-Balance Sheet Arrangements and Contractual Obligations

A summary of the contract amount of the Company's exposure to off-balance sheet and balance sheet risk as of June 30, 2017 and December 31, 2016, is as follows (dollars in thousands):

	June 30, 2017	December 31, 2016
Commitments with off-balance sheet risk:		
Commitments to extend credit	$ 129,597	$ 134,517
Standby letters of credit	6,399	7,151
Total commitments with off-balance sheet risks	$ 135,996	$ 141,668

44

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Company evaluates each customer’s credit worthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Company upon extension of credit, is based on management’s credit evaluation of the counterparty. Collateral held varies but may include accounts receivable, inventory, property and equipment, and income-producing commercial properties.

Unfunded commitments under lines of credit are commitments for possible future extensions of credit to existing customers. Those lines of credit may be drawn upon only to the total extent to which the Company is committed.

Standby letters of credit are conditional commitments issued by the Company to guarantee the performance of a customer to a third party. Those guarantees are primarily issued to support public and private borrowing arrangements, including commercial paper, bond financing, and similar transactions. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to clients. The Company holds certificates of deposit, deposit accounts, and real estate as collateral supporting those commitments for which collateral is deemed necessary.

On November 7, 2014, the Company entered into an interest rate swap with a total notional amount of $30 million. The Company designated the swap as a cash flow hedge intended to protect against the variability in the expected future cash flows on the designated variable rate borrowings. The swap hedges the interest rate risk, wherein the Company will receive an interest rate based on the three month LIBOR from the counterparty and pays an interest rate of 1.69% to the same counterparty calculated on the notional amount for a term of five years. The Company intends to sequentially issue a series of three month fixed rate debt as part of a planned roll-over of short term debt for five years. The forecasted funding will be provided through one of the following wholesale funding sources: a new FHLB advance, a new repurchase agreement, or a pool of brokered CDs, based on whichever market offers the most advantageous pricing at the time that pricing is first initially determined for the effective date of the swap and each reset period thereafter. Each quarter when the Company rolls over the three month debt, it will decide at that time which funding source to use for that quarterly period.

The fair value of the Company’s cash flow hedge was an unrealized loss of $39,000 and $70,000 at June 30, 2017 and December 31, 2016, respectively, which was recorded in other liabilities. The Company’s cash flow hedge is deemed to be effective. Therefore, the loss was recorded as a component of other comprehensive income recorded in the Company’s Consolidated Statements of Comprehensive Income.

Item 3. ***Quantitative and Qualitative Disclosures About Market Risk***

Market risk is the risk of loss in a financial instrument arising from adverse changes in market rates or prices such as interest rates, foreign currency exchange rates, commodity prices and equity prices. The Company’s primary market risk exposure is interest rate risk. The ongoing monitoring and management of interest rate risk is an important component of the Company’s asset/liability management process, which is governed by policies established by its Board of Directors that are reviewed and approved annually. The Board of Directors delegates responsibility for carrying out asset/liability management policies to the Asset/Liability Committee (ALCO) of the Bank. In this capacity, ALCO develops guidelines and strategies that govern the Company’s asset/liability management related activities, based upon estimated market risk sensitivity, policy limits and overall market interest rate levels and trends.

Interest rate risk represents the sensitivity of earnings to changes in market interest rates. As interest rates change, the interest income and expense streams associated with the Company’s financial instruments also change, affecting net interest income, the primary component of the Company’s earnings. ALCO uses the results of a detailed and dynamic simulation model to quantify the estimated exposure of net interest income to sustained interest rate changes. While ALCO routinely monitors simulated net interest income sensitivity over various periods, it also employs additional tools to monitor potential longer-term interest rate risk.

The simulation model captures the impact of changing interest rates on the interest income received and interest expense paid on all assets and liabilities reflected on the Company’s balance sheet. The simulation model is prepared and results are analyzed at least quarterly. This sensitivity analysis is compared to ALCO policy limits, which specify a maximum tolerance level for net interest income exposure over a one-year horizon, assuming no balance sheet growth, given a 400 basis point upward shift and a 400 basis point downward shift in interest rates. The downward shift of 300 or 400 basis points is included in the analysis, although less meaningful in the current rate environment, because all results are monitored regardless of likelihood. A parallel shift in rates over a 12-month period is assumed.

The following table represents the change to net interest income given interest rate shocks up and down 100, 200, 300 and 400 basis points at June 30, 2017 (dollars in thousands):

	June 30, 2017	
	%	$
Change in Yield curve		
+400 bp	2.8	1,246
+300 bp	2.2	982
+200 bp	1.6	685
+100 bp	0.8	358
most likely	—	—
-100 bp	(1.2)	(539)
-200 bp	(3.5)	(1,556)
-300 bp	(3.7)	(1,615)
-400 bp	(3.7)	(1,618)

At June 30, 2017, the Company’s interest rate risk model indicated that, in a rising rate environment of 400 basis points over a 12 month period, net interest income could increase by 2.8%. For the same time period, the interest rate risk model indicated that in a declining rate environment of 400 basis points, net interest income could decrease by 3.7%. While these percentages are subjective based upon assumptions used within the model, management believes the balance sheet is appropriately balanced with acceptable risk to changes in interest rates.

The preceding sensitivity analysis does not represent a forecast and should not be relied upon as being indicative of expected operating results. These hypothetical estimates are based upon numerous assumptions, including the nature and timing of interest rate levels such as yield curve shape, prepayments on loans and securities, deposit decay rates, pricing decisions on loans and deposits, reinvestment or replacement of asset and liability cash flows. While assumptions are developed based upon current economic and local market conditions, the Company cannot make any assurances about the predictive nature of these assumptions, including how customer preferences or competitor influences might change.

Also, as market conditions vary from those assumed in the sensitivity analysis, actual results will also differ due to factors such as prepayment and refinancing levels likely deviating from those assumed, the varying impact of interest rate change, caps or floors on adjustable rate assets, the potential effect of changing debt service levels on customers with adjustable rate loans, depositor early withdrawals and product preference changes, and other internal and external variables. Furthermore, the sensitivity analysis does not reflect actions that ALCO might take in response to, or in anticipation of, changes in interest rates.

Item 4. ***Controls and Procedures***

Evaluation of Disclosure Controls and Procedures

As of the end of the period covered by this Form 10-Q, the Company’s management, with the participation of the Company’s chief executive officer and its chief financial officer (“the Certifying Officers”), conducted evaluations of the Company’s disclosure controls and procedures. As defined under Section 13a-15(e) of the Securities Exchange Act of 1934, as amended (the “Exchange Act”), the term “disclosure controls and procedures” means controls and other procedures of an issuer that are designed to ensure that information required to be disclosed by the issuer in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the SEC’s rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by an issuer in the reports that it files or submits under the Exchange Act is accumulated and communicated to the issuer’s management, including the Certifying Officers, to allow timely decisions regarding required disclosures.

Based on this evaluation, the Certifying Officers have concluded that the Company’s disclosure controls and procedures were effective to ensure that material information is recorded, processed, summarized and reported by management of the Company on a timely basis in order to comply with the Company’s disclosure obligations under the Exchange Act and the rules and regulations promulgated under it.

Internal Control over Financial Reporting

The management of the Company is responsible for establishing and maintaining adequate internal control over financial reporting. The Company’s internal control over financial reporting is a process designed under the supervision of the Certifying Officers to provide reasonable assurance regarding the reliability of financial reporting and the preparation of the Company’s financial statements for external purposes in accordance with U.S. generally accepted accounting principles. There were no changes in the Company’s internal control over financial reporting identified in connection with the evaluation of it that occurred during the Company’s last fiscal quarter that materially affected, or are reasonably likely to materially affect, internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. *Legal Proceedings*

There are no material pending legal proceedings, other than ordinary routine litigation incidental to the Company’s business, to which the Company, including its subsidiaries, is a party or of which the property of the Company is subject.

Item 1A. *Risk Factors*

As of the date of this report, there were no material changes to the risk factors previously disclosed in the Company’s Annual Report on Form 10-K for the year ended December 31, 2016.

Item 2. *Unregistered Sales of Equity Securities and Use of Proceeds*

None.

Item 3. *Defaults upon Senior Securities*

None.

Item 4. ***Mine Safety Disclosures***

Not applicable

Item 5. ***Other Information***

None.

Item 6. ***Exhibits***

Exhibit No.	**Description**
31.1	Rule 13a-14(a)/15d-14(a) Certification for Chief Executive Officer*
31.2	Rule 13a-14(a)/15d-14(a) Certification for Chief Financial Officer*
32.1	Section 1350 Certifications*
101	Interactive Data File with respect to the following materials from the Company's Quarterly Report on Form 10-Q for the period ended June 30, 2017 formatted in Extensible Business Reporting Language (XBRL): (i) the Unaudited Consolidated Balance Sheets, (ii) the Unaudited Consolidated Statements of Income, (iii) the Unaudited Consolidated Statements of Comprehensive Income, (iv) the Unaudited Consolidated Statements of Changes in Shareholders' Equity, (v) the Unaudited Consolidated Statements of Cash Flows, and (vi) Notes to Unaudited Consolidated Financial Statements*

* Filed herewith.

SIGNATURES

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

COMMUNITY BANKERS TRUST CORPORATION
(Registrant)

/s/ Rex L. Smith, III
Rex L. Smith, III
President and Chief Executive Officer
(principal executive officer)

Date: August 8, 2017

/s/ Bruce E. Thomas
Bruce E. Thomas
Executive Vice President and Chief Financial Officer
(principal financial officer)

Date: August 8, 2017