PEOPLES FINANCIAL CORP /MS/
Form 10-Q
November 13, 2013

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

x **QUARTERLY REPORT PURSUANT TO SECTION 13 or 15 (D) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended September 30, 2013

or

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

Commission File Number 001-12103

PEOPLES FINANCIAL CORPORATION

(Exact name of registrant as specified in its charter)

Mississippi	**64-0709834**
(State or other jurisdiction of	**(I.R.S. Employer**

incorporation or organization)	**Identification No.)**
Lameuse and Howard Avenues, Biloxi, Mississippi	**39533**
(Address of principal executive offices)	**(Zip Code)**

(228) 435-5511

(Registrant s telephone number, including area code)

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

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

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

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

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the last practicable date. Peoples Financial Corporation has only one class of common stock authorized. At October 31, 2013, there were 15,000,000 shares of $1 par value common stock authorized, with 5,123,186 shares issued and outstanding.

Part 1 Financial Information

Item 1: Financial Statements

Peoples Financial Corporation and Subsidiaries

Consolidated Statements of Condition

(in thousands except share data)

	September 30, 2013 (Unaudited)	December 31, 2012 (Audited)
Assets		
Cash and due from banks	$ 34,642	$ 54,020
Available for sale securities	295,075	258,876
Held to maturity securities, fair value of $11,338 at September 30, 2013; $7,225 at December 31, 2012	11,797	7,125
Other investments	3,265	3,450
Federal Home Loan Bank Stock, at cost	3,065	2,380
Loans	396,422	431,083
Less: Allowance for loan losses	11,696	8,857
Loans, net	384,726	422,226
Bank premises and equipment, net of accumulated depreciation	25,693	26,222
Other real estate	9,426	7,008
Accrued interest receivable	2,671	2,895
Cash surrender value of life insurance	17,302	16,861
Prepaid FDIC assessments	264	1,705
Other assets	8,597	2,144
Total assets	$ 796,523	$ 804,912

Peoples Financial Corporation and Subsidiaries

Consolidated Statements of Condition (continued)

(in thousands except share data)

	September 30, 2013 (Unaudited)	December 31, 2012 (Audited)
Liabilities and Shareholders Equity		
Liabilities:		
Deposits:		
Demand, non-interest bearing	$ 118,003	$ 102,609
Savings and demand, interest bearing	233,010	232,401
Time, $100,000 or more	68,419	94,606
Other time deposits	43,532	46,103
Total deposits	462,964	475,719
Federal funds purchased and securities sold under agreements to repurchase	147,630	194,234
Borrowings from Federal Home Loan Bank	67,242	7,912
Employee and director benefit plans liabilities	12,749	12,162
Other liabilities	3,807	4,131
Total liabilities	694,392	694,158
Shareholders Equity:		
Common stock, $1 par value, 15,000,000 shares authorized, 5,123,186 and 5,136,918 shares issued and outstanding at September 30, 2013 and December 31, 2012, respectively	5,123	5,137
Surplus	65,780	65,780
Undivided profits	35,142	34,964
Accumulated other comprehensive income (loss), net of tax	(3,914)	4,873
Total shareholders equity	102,131	110,754
Total liabilities and shareholders equity	$ 796,523	$ 804,912

See notes to consolidated financial statements.

Peoples Financial Corporation and Subsidiaries

Consolidated Statements of Income

(in thousands except per share data)(unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2013	**2012**	**2013**	**2012**
Interest income:				
Interest and fees on loans	$ 4,217	$ 4,637	$ 12,995	$ 13,789
Interest and dividends on securities:				
U.S. Treasuries	139	112	430	281
U.S. Government agencies	828	861	2,307	3,101
Mortgage-backed securities	228	82	458	233
States and political subdivisions	384	376	1,140	1,116
Other investments	6	10	12	15
Interest on federal funds sold	3	3	67	12
Total interest income	5,805	6,081	17,409	18,547
Interest expense:				
Deposits	293	318	928	1,162
Borrowings from Federal Home Loan Bank	43	60	124	179
Federal funds purchased and securities sold under agreements to repurchase	38	81	127	298
Total interest expense	374	459	1,179	1,639
Net interest income	5,431	5,622	16,230	16,908
Provision for allowance for loan losses	542	541	4,619	2,371
Net interest income after provision for allowance for loan losses	$ 4,889	$ 5,081	$ 11,611	$ 14,537

Peoples Financial Corporation and Subsidiaries

Consolidated Statements of Income (continued)

(in thousands except per share data)(unaudited)

	Three Months Ended September 30, 2013	Three Months Ended September 30, 2012	Nine Months Ended September 30, 2013	Nine Months Ended September 30, 2012
Non-interest income:				
Trust department income and fees	$ 368	$ 440	$ 1,062	$ 1,111
Service charges on deposit accounts	1,618	1,472	4,649	4,356
Gain on sales and calls of securities	3	336	258	1,301
Gain (loss) on other investments	36	(48)	45	(84)
Loss on impairment of other investments		(180)		(180)
Increase in cash surrender value of life insurance	121	119	364	366
Other income	160	164	460	450
Total non-interest income	2,306	2,303	6,838	7,320
Non-interest expense:				
Salaries and employee benefits	3,005	2,964	8,996	9,283
Net occupancy	544	610	1,780	1,885
Equipment rentals, depreciation and maintenance	722	731	2,164	2,385
FDIC assessments	162	449	607	1,334
Data processing	305	328	925	1,064
ATM expense	635	519	1,826	1,493
Other expense	1,041	983	2,742	2,694
Total non-interest expense	6,414	6,584	19,040	20,138
Income (loss) before income tax expense (benefit)	781	800	(591)	1,719
Income tax expense (benefit)	(105)	50	(936)	(97)
Net income	$ 886	$ 750	$ 345	$ 1,816
Basic and diluted earnings per share	$ .18	$ .14	$ .07	$ .35

Dividends declared per share	$		$ .10	$		$ .10

See notes to consolidated financial statements.

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Peoples Financial Corporation and Subsidiaries

Consolidated Statements of Comprehensive Income (Loss)

(in thousands)(unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2013	**2012**	**2013**	**2012**
Net income	$ 886	$ 750	$ 345	$ 1,816
Other comprehensive income (loss), net of tax:				
Net unrealized gain (loss) on available for sale securities, net of tax of $981 and $220 for the three months ended September 30, 2013 and 2012, respectively, and $4,439 and $655 for the nine months ended September 30, 2013 and 2012, respectively	(1,904)	427	(8,617)	1,272
Reclassification adjustment for realized gains on available for sale securities called or sold, net of tax of $1 and $114 for the three months ended September 30, 2013 and 2012, respectively, and $88 and $443 for the nine months ended September 30, 2013 and 2012, respectively	(2)	(222)	(170)	(858)
Total other comprehensive income (loss)	(1,906)	205	(8,787)	414
Total comprehensive income (loss)	$ (1,020)	$ 955	$ (8,442)	$ 2,230

See notes to consolidated financial statements.

Peoples Financial Corporation and Subsidiaries

Consolidated Statement of Changes in Shareholders Equity

(in thousands except share data)

	Number of Common Shares	Common Stock	Surplus	Undivided Profits	Accumulated Other Comprehensive Income	Total
Balance, January 1, 2013	5,136,918	$ 5,137	$ 65,780	$ 34,964	$ 4,873	$ 110,754
Net income				345		345
Other comprehensive loss, net of tax					(8,787)	(8,787)
Retirement of common stock	(13,732)	(14)		(167)		(181)
Balance, September 30, 2013	5,123,186	$ 5,123	$ 65,780	$ 35,142	$ (3,914)	$ 102,131

Note: Balances as of January 1, 2013 were audited.

See notes to consolidated financial statements.

Peoples Financial Corporation and Subsidiaries

Consolidated Statements of Cash Flows

(in thousands)(unaudited)

	Nine Months Ended September 30, 2013	2012
Cash flows from operating activities:		
Net income	$ 345	$ 1,816
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	1,331	1,560
Provision for allowance for loan losses	4,619	2,371
Loss on sales of other real estate	59	27
Writedown of other real estate	46	153
Gain on sales of bank premises and equipment	(15)	
(Gain) loss on other investments	(45)	84
Loss on impairment on other investments		180
Gain on sales and calls of securities	(258)	(1,301)
Accretion of held to maturity securities	(2)	(1)
Change in accrued interest receivable	224	267
Increase in cash surrender value of life insurance	(364)	(366)
Change in other assets	756	642
Change in other liabilities	(1,393)	(22)
Net cash provided by operating activities	$ 5,303	$ 5,410

Peoples Financial Corporation and Subsidiaries

Consolidated Statements of Cash Flows (continued)

(in thousands)(unaudited)

	Nine Months Ended September 30, 2013	2012
Cash flows from investing activities:		
Proceeds from maturities, sales and calls of available for sale securities	$ 125,329	$ 298,643
Purchases of available for sale securities	(174,169)	(307,299)
Purchases of held to maturity securities	(4,670)	(5,561)
(Purchases) redemption of Federal Home Loan Bank stock	(685)	(225)
Redemption of other investments	230	36
Proceeds from sales of bank premises and equipment	19	
Proceeds from sales of other real estate	1,115	1,150
Insurance proceeds from casualty loss on other real estate	57	
Loans, net change	29,186	(8,894)
Acquisition of bank premises and equipment	(806)	(88)
Investment in cash surrender value of life insurance	(77)	(77)
Net cash used in investing activities	(24,471)	(22,315)
Cash flows from financing activities:		
Demand and savings deposits, net change	16,003	46,442
Time deposits, net change	(28,758)	(16,865)
Cash dividends		(514)
Retirement of common stock	(181)	
Borrowings from Federal Home Loan Bank	212,500	1,557,866
Repayments to Federal Home Loan Bank	(153,170)	(1,560,723)
Federal funds purchased and securities sold under agreements to repurchase, net change	(46,604)	(19,525)
Net cash provided by (used in) financing activities	(210)	6,681
Net decrease in cash and cash equivalents	(19,378)	(10,224)
Cash and cash equivalents, beginning of period	54,020	36,929
Cash and cash equivalents, end of period	$ 34,642	$ 26,705

See notes to consolidated financial statements.

PEOPLES FINANCIAL CORPORATION AND SUBSIDIARIES

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

For the Nine Months Ended September 30, 2013 and 2012

1. Basis of Presentation:

Peoples Financial Corporation (the Company) is a one-bank holding company headquartered in Biloxi, Mississippi. Its two operating subsidiaries are The Peoples Bank, Biloxi, Mississippi (the Bank), and PFC Service Corp. Its principal subsidiary is The Peoples Bank, Biloxi, Mississippi, which provides a full range of banking, financial and trust services to state, county and local government entities and individuals and small and commercial businesses operating in those portions of Mississippi, Louisiana and Alabama which are within a fifty mile radius of the Waveland, Wiggins and Gautier branches, the Bank s three most outlying locations (the trade area).

The accompanying unaudited consolidated financial statements and notes thereto contain all adjustments, consisting only of normal recurring adjustments, necessary to present fairly, in accordance with accounting principles generally accepted in the United States of America (GAAP), the financial position of the Company and its subsidiaries as of September 30, 2013 and the results of their operations and their cash flows for the periods presented. The interim financial information should be read in conjunction with the annual consolidated financial statements and the notes thereto included in the Company s 2012 Annual Report and Form 10-K.

The results of operations for the quarter or nine months ended September 30, 2013, are not necessarily indicative of the results to be expected for the full year.

Use of Estimates - The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reported period. Actual results could differ from those estimates. Material estimates common to the banking industry that are particularly susceptible to significant change in the near term include, but are not limited to, the determination of the allowance for loan losses, the valuation of other real estate acquired in connection with foreclosure or in satisfaction of loans and valuation allowances associated with the realization of deferred tax assets, which are based on future taxable income.

Summary of Significant Accounting Policies - The accounting and reporting policies of the Company conform with GAAP and general practices within the banking industry. There have been no material changes or developments in the application of principles or in our evaluation of the accounting estimates and the underlying assumptions or methodologies that we believe to be Critical Accounting Policies as disclosed in our Form 10-K for the year ended December 31, 2012.

2. Earnings Per Share:

Per share data is based on the weighted average shares of common stock outstanding of 5,123,316 and 5,136,918 for the quarters ended September 30, 2013 and 2012, respectively, and 5,130,811 and 5,136,918 for the nine months ended September 30, 2013 and 2012, respectively.

3. Statements of Cash Flows:

The Company has defined cash and cash equivalents as cash and due from banks. The Company paid $1,198,021 and $1,648,779 for the nine months ended September 30, 2013 and 2012, respectively, for interest on deposits and borrowings. Income tax payments of $810,000 and $615,000 were made during the nine months ended September 30, 2013 and 2012, respectively. Loans transferred to other real estate amounted to $3,695,825 and $2,545,780 during the nine months ended September 30, 2013 and 2012, respectively. Dividends payable of $513,692 as of December 31, 2011 were paid during the first quarter of 2012.

4. Investments:

The amortized cost and fair value of securities at September 30, 2013 and December 31, 2012, are as follows (in thousands):

September 30, 2013	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available for sale securities:				
Debt securities:				
U.S. Treasuries	$ 49,626	$ 106	$ (815)	$ 48,917
U.S. Government agencies	165,761	819	(9,274)	157,306
Mortgage-backed securities	53,257	233	(1,065)	52,425
States and political subdivisions	34,516	1,263	(2)	35,777
Total debt securities	303,160	2,421	(11,156)	294,425
Equity securities	650			650
Total available for sale securities	$ 303,810	$ 2,421	$ (11,156)	$ 295,075
Held to maturity securities:				
States and political subdivisions	$ 11,797	$ 14	$ (473)	$ 11,338
Total held to maturity securities	$ 11,797	$ 14	$ (473)	$ 11,338

December 31, 2012	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available for sale securities:				
Debt securities:				
U.S. Treasuries	$ 53,661	$ 490	$ (55)	$ 54,096
U.S. Government agencies	147,652	1,810	(364)	149,098
Mortgage-backed securities	16,903	538		17,441
States and political subdivisions	35,433	2,158		37,591
Total debt securities	253,649	4,996	(419)	258,226
Equity securities	650			650
Total available for sale securities	$ 254,299	$ 4,996	$ (419)	$ 258,876
Held to maturity securities:				
States and political subdivisions	$ 7,125	$ 112	$ (12)	$ 7,225
Total held to maturity securities	$ 7,125	$ 112	$ (12)	$ 7,225

The amortized cost and fair value of debt securities at September 30, 2013 (in thousands), by contractual maturity, are shown on the next page. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Amortized Cost	Fair Value
Available for sale securities:		
Due in one year or less	$ 21,798	$ 21,930
Due after one year through five years	59,022	59,258
Due after five years through ten years	74,949	74,516
Due after ten years	94,134	86,296
Mortgage-backed securities	53,257	52,425
Totals	$ 303,160	$ 294,425
Held to maturity securities:		
Due in one year or less	$ 1,012	$ 1,015
Due after one year through five years	1,774	1,772
Due after five years through ten years	5,562	5,425
Due after ten years	3,449	3,126
Totals	$ 11,797	$ 11,338

Available for Sale and Held to Maturity Securities with gross unrealized losses at September 30, 2013 and December 31, 2012, aggregated by investment category and length of time that individual securities have been in a continuous loss position, are as follows (in thousands):

	Less Than Twelve Months		Over Twelve Months		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
September 30, 2013:						
U.S. Treasuries	$ 29,927	$ 815	$	$	$ 29,927	$ 815
U.S. Government agencies	119,480	9,274			119,480	9,274
Mortgage-backed securities	34,788	1,065			34,788	1,065
States and political subdivisions	7,974	475			7,974	475
TOTAL	$ 192,169	$ 11,629	$	$	$ 192,169	$ 11,629
December 31, 2012:						
U.S. Treasuries	$ 9,887	$ 55	$	$	$ 9,887	$ 55
U.S. Government agencies	30,335	364			30,335	364
States and political subdivisions	1,451	12			1,451	12
TOTAL	$ 41,673	$ 431	$	$	$ 41,673	$ 431

At September 30, 2013, 7 of the 12 securities issued by the U.S. Treasury, 25 of the 33 securities issued by U.S. Government agencies, 8 of the 13 mortgage-backed securities and 1 of the 111 securities issued by states and political subdivisions contained unrealized losses.

Management evaluates securities for other-than-temporary impairment on a monthly basis. In performing this evaluation, the length of time and the extent to which the fair value has been less than cost, the fact that the Company s securities are primarily issued by U.S. Treasury and U.S. Government Agencies and the cause of the decline in value are considered. In addition, the Company does not intend to sell and it is not more likely than not that it will be required to sell these securities before maturity. While some available for sale securities have been sold for liquidity purposes or for gains, the Company has traditionally held its securities, including those classified as available for sale, until maturity. As a result of the evaluation of these securities, the Company has determined that the unrealized losses summarized in the tables above are not deemed to be other-than-temporary.

Securities with a fair value of $272,556,976 and $241,879,775 at September 30, 2013 and December 31, 2012, respectively, were pledged to secure public deposits, federal funds purchased and other balances required by law.

Proceeds from the sale of available for sale debt securities were $26,075,225 and $63,339,638 for the nine months ended September 30, 2013 and 2012, respectively. Available for sale debt securities were sold for a realized gain of $257,997 and $1,300,547 for the nine months ended September 30, 2013 and 2012, respectively.

5. Loans:

The composition of the loan portfolio at September 30, 2013 and December 31, 2012, is as follows (in thousands):

	September 30, 2013	December 31, 2012
Gaming	$ 42,567	$ 60,187
Residential and land development	26,810	27,338
Real estate, construction	44,605	52,586
Real estate, mortgage	239,020	246,420
Commercial and industrial	34,864	35,004
Other	8,556	9,548
Total	$ 396,422	$ 431,083

The age analysis of the loan portfolio, segregated by class of loans, as of September 30, 2013 and December 31, 2012, is as follows (in thousands):

	Number of Days Past Due						
	30 - 59	60 - 89	Greater Than 90	Total Past Due	Current	Total Loans	Loans Past Due Greater Than 90 Days & Still Accruing
September 30, 2013:							
Gaming	$	$	$	$	$ 42,567	$ 42,567	$
Residential and land development	58		20,911	20,969	5,841	26,810	
Real estate, construction	2,403	1,788	2,243	6,434	38,171	44,605	15
Real estate, mortgage	7,374	2,771	5,748	15,893	223,127	239,020	251
Commercial and industrial	1,442	41	8	1,491	33,373	34,864	8
Other	94	7	28	129	8,427	8,556	29
Total	$ 11,371	$ 4,607	$ 28,938	$ 44,916	$ 351,506	$ 396,422	$ 303
December 31, 2012:							
Gaming	$	$ 1,721	$	$ 1,721	$ 58,466	$ 60,187	$
Residential and land development			5,765	5,765	21,573	27,338	
Real estate, construction	3,989	878	6,151	11,018	41,568	52,586	572
Real estate, mortgage	12,012	2,702	7,605	22,319	224,101	246,420	872
Commercial and industrial	1,804	79	107	1,990	33,014	35,004	
Other	127	26	1	154	9,394	9,548	1
Total	$ 17,932	$ 5,406	$ 19,629	$ 42,967	$ 388,116	$ 431,083	$ 1,445

The Company monitors the credit quality of its loan portfolio through the use of a loan grading system. A score of 1 5 is assigned to the loan on factors including repayment ability, trends in net worth and/or financial condition of the borrower and guarantors, employment stability, management ability, loan to value fluctuations, the type and structure of the loan, conformity of the loan to bank policy and payment performance. Based on the total score, a loan grade of A - F is applied. A grade of A will generally be applied to loans for customers that are well known to the Company and that have excellent sources of repayment. A grade of B will generally be applied to loans for customers that have excellent sources of repayment which have no identifiable risk of collection. A grade of C will generally be applied to loans for customers that have adequate sources of repayment which have little identifiable risk of collection. Loans with a grade of C may be placed on the watch list if weaknesses are not resolved which could result in potential loss or for other circumstances that require monitoring. A grade of D will generally be applied to loans for customers that are inadequately protected by current sound net worth, paying capacity of the borrower, or pledged collateral. Loans with a grade of D have unsatisfactory characteristics such as cash flow deficiencies, bankruptcy filing by the borrower or dependence on the sale of collateral for the primary source of repayment, causing more than acceptable levels of risk. Loans 60 to 89 days past due receive a grade of D. A grade of E will generally be applied to loans for customers with weaknesses inherent in the D classification and in which collection or liquidation in full is questionable. In addition, on a monthly basis the Company determines which loans are 90 days or more past due and assigns a grade of E to them. A grade of F is applied to loans which are considered uncollectible and of such little value that their continuance in an active bank is not warranted. Loans with this grade are charged off, even though partial or full recovery may be possible in the future.

An analysis of the loan portfolio by loan grade, segregated by class of loans, as of September 30, 2013 and December 31, 2012, is as follows (in thousands):

	Loans With A Grade Of:					
	A or B	C	D	E	F	Total
September 30, 2013:						
Gaming	$ 26,179	$ 2,500	$	$ 13,888	$	$ 42,567
Residential and land development	4,292	1,544	58	20,916		26,810
Real estate, construction	38,251	784	2,300	3,270		44,605
Real estate, mortgage	205,851	4,476	17,400	11,293		239,020
Commercial and industrial	31,675	684	2,476	29		34,864
Other	8,450	25	52	29		8,556
Total	$ 314,698	$ 10,013	$ 22,286	$ 49,425	$	$ 396,422
December 31, 2012:						
Gaming	$ 27,530	$ 12,300	$ 4,108	$ 16,249	$	$ 60,187
Residential and land development	4,630	1,544	81	21,083		27,338
Real estate, construction	43,318	1,001	2,701	5,566		52,586
Real estate, mortgage	209,479	3,093	21,167	12,681		246,420
Commercial and industrial	32,036	442	2,312	214		35,004
Other	9,449	27	72			9,548
Total	$ 326,442	$ 18,407	$ 30,441	$ 55,793	$	$ 431,083

A loan may be impaired but not on nonaccrual status when the loan is well secured and in the process of collection. Total loans on nonaccrual as of September 30, 2013 and December 31, 2012, are as follows (in thousands):

	September 30, 2013	December 31, 2012
Gaming	$ 12,016	$ 16,249
Residential and land development	20,916	21,083
Real estate, construction	2,863	5,171
Real estate, mortgage	9,800	11,174
Commercial and industrial		214
Total	$ 45,595	$ 53,891

The Company has modified certain loans by granting interest rate concessions to these customers. These loans are in compliance with their modified terms, are currently accruing and the Company has classified them as troubled debt restructurings. Troubled debt restructurings as of September 30, 2013 and December 31, 2012 were as follows (in thousands except for number of contracts):

	Number of Contracts	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment	Related Allowance
September 30, 2013:				
Real estate, construction	2	$ 900	$ 900	$ 276
Real estate, mortgage	3	9,048	9,048	827
Commercial and industrial	1	680	680	
Total	6	$ 10,628	$ 10,628	$ 1,103
December 31, 2012:				
Real estate, construction	3	$ 1,095	$ 1,095	$ 340
Real estate, mortgage	3	9,054	9,054	957
Commercial and industrial	1	702	702	
Total	7	$ 10,851	$ 10,851	$ 1,297

Impaired loans, which include loans classified as nonaccrual and troubled debt restructurings, segregated by class of loans, as of September 30, 2013 and December 31, 2012, are as follows (in thousands):

	Unpaid Principal Balance	Recorded Investment	Related Allowance	Average Recorded Investment	Interest Income Recognized
September 30, 2013:					
With no related allowance recorded:					
Gaming	$ 10,786	$ 10,786	$	$ 11,712	$
Residential and land development	4,430	4,430		4,478	
Real estate, construction	2,448	2,448		2,144	13
Real estate, mortgage	9,741	9,141		9,114	10
Commercial and industrial	680	680		692	17
Total	$ 28,085	$ 27,485	$	$ 28,140	$ 40
With a related allowance recorded:					
Gaming	$ 1,704	$ 1,230	$ 626	$ 1,346	$
Residential and land development	17,590	16,486	3,149	16,536	
Real estate, construction	1,315	1,315	424	1,255	14
Real estate, mortgage	9,707	9,707	1,338	9,812	212
Total	$ 30,316	$ 28,738	$ 5,537	$ 28,949	$ 226
Total by class of loans:					
Gaming	$ 12,490	$ 12,016	$ 626	$ 13,058	$
Residential and land development	22,020	20,916	3,149	21,014	
Real estate, construction	3,763	3,763	424	3,399	27
Real estate, mortgage	19,448	18,848	1,338	18,926	222
Commercial and industrial	680	680		692	17
Total	$ 58,401	$ 56,223	$ 5,537	$ 57,089	$ 266

	Unpaid Principal Balance	Recorded Investment	Related Allowance	Average Recorded Investment	Interest Income Recognized
December 31, 2012:					
With no related allowance recorded:					
Gaming	$ 14,528	$ 14,528	$	$ 14,869	$
Residential and land development	21,837	20,733		21,288	
Real estate, construction	4,635	4,580		3,833	
Real estate, mortgage	9,971	9,935		9,821	
Commercial and industrial	892	892		791	23
Total	$ 51,863	$ 50,668	$	$ 50,602	$ 23
With a related allowance recorded:					
Gaming	$ 1,721	$ 1,721	$ 1,100	$	$
Residential and land development	350	350	70	350	
Real estate, construction	1,694	1,686	663	1,314	8
Real estate, mortgage	10,893	10,293	1,229	10,199	319
Commercial and industrial	24	24	12		
Total	$ 14,682	$ 14,074	$ 3,074	$ 11,863	$ 327
Total by class of loans:					
Gaming	$ 16,249	$ 16,249	$ 1,100	$ 14,869	$
Residential and land development	22,187	21,083	70	21,638	
Real estate, construction	6,329	6,266	663	5,147	8
Real estate, mortgage	20,864	20,228	1,229	20,020	319
Commercial and industrial	916	916	12	791	23
Total	$ 66,545	$ 64,742	$ 3,074	$ 62,465	$ 350

6. Allowance for Loan Losses:

Transactions in the allowance for loan losses for the quarters and nine months ended September 30, 2013 and 2012, and the balances of loans, individually and collectively evaluated for impairment as of September 30, 2013 and 2012, are as follows (in thousands):

	Gaming	Residential and Land Development	Real Estate, Construction	Real Estate, Mortgage	Commercial and Industrial	Other	Total
For the Nine Months Ended September 30, 2013:							
Allowance for Loan Losses:							
Beginning Balance	$ 1,541	$ 200	$ 967	$ 5,273	$ 593	$ 283	$ 8,857
Charge-offs	(474)		(947)	(623)	(21)	(173)	(2,238)
Recoveries	65	67	79	150	24	73	458
Provision	(143)	3,068	586	999	4	105	4,619
Ending Balance	$ 989	$ 3,335	$ 685	$ 5,799	$ 600	$ 288	$ 11,696
For the Quarter Ended September 30, 2013:							
Allowance for Loan Losses:							
Beginning Balance	$ 986	$ 3,343	$ 1,330	$ 5,588	$ 627	$ 276	$ 12,150
Charge-offs			(900)	(342)	(21)	(43)	(1,306)
Recoveries	65		79	148	2	16	310
Provision	(62)	(8)	176	405	(8)	39	542
Ending Balance	$ 989	$ 3,335	$ 685	$ 5,799	$ 600	$ 288	$ 11,696
Allowance for loan losses, September 30, 2013:							
Ending balance: individually evaluated for impairment	$ 626	$ 3,149	$ 651	$ 2,128	$ 330	$ 33	$ 6,917
Ending balance: collectively evaluated for impairment	$ 363	$ 186	$ 34	$ 3,671	$ 270	$ 255	$ 4,779
Total Loans, September 30, 2013:							
Ending balance: individually evaluated for impairment	$ 13,888	$ 20,974	$ 5,570	$ 28,693	$ 2,505	$ 80	$ 71,710
Ending balance: collectively evaluated for impairment	$ 28,679	$ 5,836	$ 39,035	$ 210,327	$ 32,359	$ 8,476	$ 324,712

	Gaming	Residential and Land Development	Real Estate, Construction	Real Estate, Mortgage	Commercial and Industrial	Other	Total
For the Nine Months Ended September 30, 2012:							
Allowance for Loan Losses:							
Beginning Balance	$ 457	$ 1,081	$ 937	$ 4,800	$ 557	$ 304	$ 8,136
Charge-offs	(275)	(1,103)	(474)	(1,243)	(203)	(224)	(3,522)
Recoveries					27	76	103
Provision	313	223	31	1,543	117	144	2,371
Ending Balance	$ 495	$ 201	$ 494	$ 5,100	$ 498	$ 300	$ 7,088
For the Quarter Ended September 30, 2012:							
Allowance for Loan Losses:							
Beginning Balance	$ 474	$ 203	$ 449	$ 4,876	$ 457	$ 284	$ 6,743
Charge-offs				(141)	(43)	(45)	(229)
Recoveries					13	20	33
Provision	21	(2)	45	365	71	41	541
Ending Balance	$ 495	$ 201	$ 494	$ 5,100	$ 498	$ 300	$ 7,088
Allowance for loan losses, September 30, 2012:							
Ending balance: individually evaluated for impairment	$	$	$ 431	$ 1,798	$ 268	$ 38	$ 2,535
Ending balance: collectively evaluated for impairment	$ 495	$ 201	$ 63	$ 3,302	$ 230	$ 262	$ 4,553
Total Loans, September 30, 2012:							
Ending balance: individually evaluated for impairment	$ 24,816	$ 21,322	$ 8,714	$ 36,072	$ 2,787	$ 79	$ 93,790
Ending balance: collectively evaluated for impairment	$ 36,711	$ 6,242	$ 45,755	$ 211,739	$ 31,456	$ 9,643	$ 341,546

7. Deposits:

At September 30, 2013, time deposits of $100,000 or more include brokered deposits of $5,000,000, which mature in 2017.

8. Fair Value Measurements and Disclosures:

The Company utilizes fair value measurements to record fair value adjustments to certain assets and liabilities and to determine fair value disclosures. Available for sale securities are recorded at fair value on a recurring basis.

Additionally, from time to time, the Company may be required to record other assets at fair value on a non-recurring basis, such as impaired loans and ORE. These non-recurring fair value adjustments typically involve application of lower of cost or market accounting or write-downs of individual assets. Additionally, the Company is required to disclose, but not record, the fair value of other financial instruments.

Fair Value Hierarchy

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 market 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.

Level 3 - Valuation is generated from model-based techniques that use at least one significant assumption not observable in the market. These unobservable assumptions reflect estimates of assumptions that market participants would use in pricing the asset or liability. Valuation techniques include the use of option pricing models, discounted cash flow models and similar techniques.

Following is a description of valuation methodologies used to determine the fair value of financial assets and liabilities.

Cash and Due from Banks

The carrying amount shown as cash and due from banks approximates fair value.

Available for Sale Securities

The fair value of available for sale securities is based on quoted market prices. The Company s available for sale securities are reported at their estimated fair value, which is determined utilizing several sources. The primary source is Interactive Data Corporation, which utilizes pricing models that vary based on asset class and include available trade, bid and other market information and whose methodology includes broker quotes, proprietary models and vast descriptive databases. The other source for determining fair value is matrix pricing, which is a mathematical technique used widely in the industry to value debt securities without relying exclusively on quoted prices for the specific securities but rather by relying on the securities relationship to other benchmark securities. All of the Company s available for sale securities are Level 2 assets.

Held to Maturity Securities

The fair value of held to maturity securities is based on quoted market prices.

Other Investments

The carrying amount shown as other investments approximates fair value.

Federal Home Loan Bank Stock

The carrying amount shown as Federal Home Loan Bank Stock approximates fair value.

Loans

The fair value of fixed rate 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 for the remaining maturities. The cash flows considered in computing the fair value of such loans are segmented into categories relating to the nature of the contract and collateral based on contractual principal maturities. Appropriate adjustments are made to reflect probable credit losses. Cash flows have not been adjusted for such factors as prepayment risk or the effect of the maturity of balloon notes. The fair value of floating rate loans is estimated to be its carrying value. At each reporting period, the Company determines which loans are impaired. Accordingly, the Company s impaired loans are reported at their estimated fair value on a non-recurring basis. An allowance for each impaired loan, which are generally collateral-dependent, is calculated based on the fair value of its collateral. The fair value of the collateral is based on appraisals performed by third-party valuation specialists. Factors including the assumptions and techniques utilized by the appraiser are considered by Management. If the recorded investment in the impaired loan exceeds the measure of fair value of the collateral, a valuation allowance is recorded as a component of the allowance for loan losses. When the fair value of the collateral is based on an observable market price, the Company records the impaired loan as a non-recurring Level 2 asset. When an appraised value is not available or Management determines 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 a non-recurring Level 3 asset.

Other Real Estate

In the course of lending operations, Management may determine that it is necessary to foreclose on the related collateral. Other real estate acquired through foreclosure is carried at fair value, less estimated costs to sell. The fair value of the collateral is based on appraisals performed by third-party valuation specialists. Factors including the assumptions and techniques utilized by the appraiser are considered by Management. If the current appraisal is more than one year old and/or the loan balance is more than $200,000, a new appraisal is obtained. Otherwise, the Bank s in-house property evaluator and Management will determine the fair value of the collateral, based on comparable sales, market conditions, Management s plans for disposition and other estimates of fair value obtained from principally independent sources, adjusted for estimated selling costs. When the fair value of the property is based on observable market price, the Company records the other real estate as a non-recurring Level 2 asset. When an appraised value is not available or Management determines the fair value of the other real estate is further impaired below the appraised value and there is no observable market price, the Company records the other real estate as a non-recurring Level 3 asset.

Cash Surrender Value of Life Insurance

The carrying amount of cash surrender value of bank-owned life insurance approximates fair value.

Deposits

The fair value of non-interest bearing demand and interest bearing savings and demand deposits is the amount reported in the financial statements. The fair value of time deposits is estimated by discounting the cash flows using current rates of time deposits with similar remaining maturities. The cash flows considered in computing the fair value of such deposits are based on contractual maturities, since approximately 98% of time deposits provide for automatic renewal at current interest rates.

Federal Funds Purchased and Securities Sold under Agreements to Repurchase

The carrying amount shown as federal funds purchased and securities sold under agreements to repurchase approximates fair value.

Borrowings from Federal Home Loan Bank

The fair value of FHLB fixed rate borrowings is estimated using discounted cash flows based on current incremental borrowing rates for similar types of borrowing arrangements. The Company has no FHLB variable rate borrowings.

Commitments to Extend Credit and Standby Letters of Credit

Because commitments to extend credit and standby letters of credit are generally short-term and at variable rates, the contract value and estimated value associated with these instruments are immaterial.

The balances of available for sale securities, which are the only assets measured at fair value on a recurring basis, by level within the fair value hierarchy and by investment type, as of September 30, 2013 and December 31, 2012 are as follows (in thousands):

		Fair Value Measurements Using		
	Total	Level 1	Level 2	Level 3
September 30, 2013:				
U.S. Treasuries	$ 48,917	$	$ 48,917	$
U.S. Government agencies	157,306		157,306	
Mortgage-backed securities	52,425		52,425	
States and political subdivisions	35,777		35,777	
Equity securities	650		650	
Total	$ 295,075	$	$ 295,075	$
December 31, 2012:				
U.S. Treasuries	$ 54,096	$	$ 54,096	$
U.S. Government agencies	149,098		149,098	
Mortgage-backed securities	17,441		17,441	
States and political subdivisions	37,591		37,591	
Equity securities	650		650	
Total	$ 258,876	$	$ 258,876	$

Impaired loans, which are measured at fair value on a non-recurring basis, by level within the fair value hierarchy as of September 30, 2013 and December 31, 2012 are as follows (in thousands):

		Fair Value Measurements Using		
	Total	Level 1	Level 2	Level 3
September 30, 2013	$ 23,498	$	$	$ 23,498

December 31, 2012	16,030	16,030

The following table presents a summary of changes in the fair value of impaired loans which are measured using level 3 inputs (in thousands):

	For the Nine Months Ended September 30, 2013	For the Year Ended December 31, 2012
Balance, beginning of period	$ 16,030	$ 14,770
Additions to impaired loans and troubled debt restructurings	16,464	2,960
Principal payments, charge-offs and transfers to other real estate	(6,533)	(1,654)
Change in allowance for loan losses on impaired loans	(2,463)	(46)