Community Bankers Trust Corp
Form 10-Q
August 07, 2015

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, 2015

or

o **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 o

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 o

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.

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

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

At June 30, 2015, there were 21,828,267 shares of the Company's common stock outstanding.

COMMUNITY BANKERS TRUST CORPORATION

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June 30, 2015

PART I — FINANCIAL INFORMATION

Item 1. ***Financial Statements***

COMMUNITY BANKERS TRUST CORPORATION

CONSOLIDATED BALANCE SHEETS

AS OF JUNE 30, 2015 AND DECEMBER 31, 2014

(dollars in thousands)

	June 30, 2015 (Unaudited)	December 31, 2014
ASSETS		
Cash and due from banks	$ 6,480	$ 8,329
Interest bearing bank deposits	12,389	14,024
Total cash and cash equivalents	18,869	22,353
Securities available for sale, at fair value	262,813	274,568
Securities held to maturity, at cost (fair value of $38,819 and $37,539, respectively)	38,465	36,197
Equity securities, restricted, at cost	8,008	8,816
Total securities	309,286	319,581
Loans held for sale	6,503	200
Loans not covered by FDIC shared-loss agreement	684,080	664,736
Loans covered by FDIC shared-loss agreement	59,034	62,744
Total loans	743,114	727,480
Allowance for loan losses (non-covered loans of $9,962 and $9,365, respectively; covered loans of $386 and $386, respectively)	(10,348)	(9,751)
Net loans	732,766	717,729
FDIC indemnification asset	16,182	18,609
Bank premises and equipment, net	29,775	29,702
Bank premises and equipment held for sale	411	465
Other real estate owned, covered by FDIC shared-loss agreement	1,784	2,019
Other real estate owned, non-covered	4,722	5,724
Bank owned life insurance	21,312	21,004
FDIC receivable under shared-loss agreement	622	669

Core deposit intangibles, net	3,759	4,713
Other assets	13,140	12,966
Total assets	$ 1,159,131	$ 1,155,734
LIABILITIES		
Deposits:		
Noninterest bearing	$ 101,500	$ 84,564
Interest bearing	846,436	834,381
Total deposits	947,936	918,945
Federal funds purchased and securities sold under agreements to repurchase	5,003	14,500
Federal Home Loan Bank advances	81,031	96,401
Long-term debt	7,277	9,680
Trust preferred capital notes	4,124	4,124
Other liabilities	4,581	4,434
Total liabilities	1,049,952	1,048,084
SHAREHOLDERS' EQUITY		
Common stock (200,000,000 shares authorized, $0.01 par value; 21,828,267 and 21,791,523 shares issued and outstanding, respectively)	218	218
Additional paid in capital	145,596	145,321
Retained deficit	(35,548)	(38,553)
Accumulated other comprehensive (loss) income	(1,087)	664
Total shareholders' equity	109,179	107,650
Total liabilities and shareholders' equity	$ 1,159,131	$ 1,155,734

See accompanying notes to unaudited consolidated financial statements

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COMMUNITY BANKERS TRUST CORPORATION

UNAUDITED CONSOLIDATED STATEMENTS OF INCOME

FOR THE THREE AND SIX MONTHS ENDED JUNE 30, 2015 AND 2014

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

	Three months ended		Six months ended	
	June 30, 2015	June 30, 2014	June 30, 2015	June 30, 2014
Interest and dividend income				
Interest and fees on non-covered loans	$ 8,166	$ 7,291	$ 16,072	$ 14,342
Interest and fees on FDIC covered loans	2,269	3,264	4,183	6,225
Interest on federal funds sold	1	—	2	—
Interest on deposits in other banks	17	22	34	35
Interest and dividends on securities				
Taxable	1,355	1,710	2,723	3,408
Nontaxable	525	168	969	324
Total interest and dividend income	12,333	12,455	23,983	24,334
Interest expense				
Interest on deposits	1,486	1,453	2,934	2,861
Interest on borrowed funds	384	244	801	406
Total interest expense	1,870	1,697	3,735	3,267
Net interest income	10,463	10,758	20,248	21,067
Provision for loan losses	—	—	—	—
Net interest income after provision for loan losses	10,463	10,758	20,248	21,067
Noninterest income				
Service charges on deposit accounts	557	561	1,085	1,050
(Loss) gain on securities transactions, net	(8)	24	289	379
Gain on sale of other loans, net	23	27	69	75
Income on bank owned life insurance	188	193	374	385
Other	446	165	786	382
Total noninterest income	1,206	970	2,603	2,271
Noninterest expense				
Salaries and employee benefits	4,406	4,028	8,901	7,951
Occupancy expenses	619	687	1,307	1,335
Equipment expenses	260	260	500	479
FDIC assessment	220	194	457	401
Data processing fees	412	463	854	957
FDIC indemnification asset amortization	1,153	1,478	2,392	2,976
Amortization of intangibles	477	477	954	954
Other real estate expenses	137	100	222	383
Other operating expenses	1,759	1,672	3,375	3,100
Total noninterest expense	9,443	9,359	18,962	18,536
Income before income taxes	2,226	2,369	3,889	4,802

Income tax expense	533	649	884	1,358
Net income	$ 1,693	$ 1,720	$ 3,005	$ 3,444
Dividends paid on preferred stock	—	182	—	247
Net income available to common shareholders	$ 1,693	$ 1,538	$ 3,005	$ 3,197
Net income per share — basic	$ 0.08	$ 0.07	$ 0.14	$ 0.15
Net income per share — diluted	$ 0.08	$ 0.07	$ 0.14	$ 0.15
Weighted average number of shares outstanding				
basic	21,821	21,742	21,810	21,736
diluted	21,958	21,939	21,994	21,972

See accompanying notes to unaudited consolidated financial statements

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COMMUNITY BANKERS TRUST CORPORATION

UNAUDITED CONSOLIDATED STATEMENTS OF COMPREHENSIVE (LOSS) INCOME

FOR THE THREE AND SIX MONTHS ENDED JUNE 30, 2015 AND 2014

(dollars in thousands)

	Three months ended		Six months ended	
	June 30, 2015	June 30, 2014	June 30, 2015	June 30, 2014
Net income	$ 1,693	$ 1,720	$ 3,005	$ 3,444
Other comprehensive (loss) income:				
Unrealized gains on investment securities:				
Change in unrealized (loss) gain in investment securities	(3,976)	1,950	(2,200)	5,696
Tax related to unrealized loss (gain) in investment securities	1,352	(663)	747	(1,937)
Reclassification adjustment for loss (gain) in securities sold	8	(24)	(289)	(379)
Tax related to realized (loss) gain in securities sold	(3)	8	98	129
Cash flow hedge:				
Change in unrealized loss (gain) in cash flow hedge	215	-	(164)	-
Tax related to unrealized (loss) gain in cash flow hedge	(73)	-	57	-
Total other comprehensive (loss) income	(2,477)	1,271	(1,751)	3,509
Total comprehensive (loss) income	$ (784)	$ 2,991	$ 1,254	$ 6,953

See accompanying notes to unaudited consolidated financial statements

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COMMUNITY BANKERS TRUST CORPORATION

UNAUDITED CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

FOR THE SIX MONTHS ENDED JUNE 30, 2015 AND 2014

(dollars and shares in thousands)

	Preferred Stock	Warrants	Common Shares	Stock Amount	Additional Paid in Capital	Retained Deficit	Accumulated Other Comprehensive Income	Total
Balance January 1, 2014	$10,680	$1,037	21,709	$217	$144,656	$(45,822)	$(4,109)	$106,659
Issuance of common stock	—	—	42	1	90	—	—	91
Dividends paid on preferred stock	—	—	—	—	—	(247)	—	(247)
Issuance of stock options	—	—	—	—	93	—	—	93
Redemption of preferred stock	(10,680)	—	—	—	—	—	—	(10,680)
Redemption of warrants on preferred stock	—	(1,037)			257			(780)
Net income	—	—	—	—	—	3,444	—	3,444
Other comprehensive income	—	—	—	—	—	—	3,509	3,509
Balance June 30, 2014	$—	$—	21,751	$218	$145,096	$(42,625)	$(600)	$102,089
Balance January 1, 2015	$—	$—	21,792	$218	$145,321	$(38,553)	$664	$107,650
Issuance of common stock	—	—	36	—	81	—	—	81
Issuance of stock options	—	—	—	—	194	—	—	194
Net income	—	—	—	—	—	3,005	—	3,005
Other comprehensive loss	—	—	—	—	—	—	(1,751)	(1,751)
Balance June 30, 2015	$—	$—	21,828	$218	$145,596	$(35,548)	$(1,087)	$109,179

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, 2015 AND 2014

(dollars in thousands)

	June 30, 2015	June 30, 2014
Operating activities:		
Net income	$ 3,005	$ 3,444
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and intangibles amortization	1,751	1,728
Issuance of common stock and stock options	275	184
Amortization of purchased loan premium	152	727
Amortization of security premiums and accretion of discounts, net	1,325	1,840
Net gain on sale of securities	(289)	(379)
Net loss on sale and valuation of other real estate owned	198	314
Net gain on sale of loans	(69)	(75)
Changes in assets and liabilities:		
(Increase) decrease in loans held for sale	(6,303)	100
Decrease in other assets	2,838	1,695
Increase in accrued expenses and other liabilities	41	521
Net cash provided by operating activities	2,924	10,099
Investing activities:		
Proceeds from available for sale securities	93,444	68,160
Proceeds from held to maturity securities	916	3,602
Proceeds from equity securities	873	586
Purchase of available for sale securities	(85,180)	(66,522)
Purchase of held to maturity securities	(3,221)	—
Purchase of equity securities	(65)	(82)
Proceeds from sale of other real estate owned	1,886	1,379
Improvements of other real estate, net of insurance proceeds	(52)	(178)
Net increase in loans	(20,688)	(37,283)
Principal recoveries of loans previously charged off	1,448	310
Purchase of premises and equipment, net	(870)	(1,915)
Proceeds from sale of loans	3,380	5,274
Net cash used in investing activities	(8,129)	(26,669)
Financing activities:		
Net increase in deposits	28,991	22,475
Net decrease in federal funds purchased and securities sold under agreements to repurchase	(9,497)	(3,460)
Net decrease in Federal Home Loan Bank borrowings	(15,370)	(359)
Cash dividends paid	—	(247)

Proceeds from long-term debt	—	10,680
Redemption of preferred stock and related warrants	—	(11,460)
Payments on long-term debt	(2,403)	—
Net cash provided by financing activities	1,721	17,629
Net (decrease) increase in cash and cash equivalents	(3,484)	1,059
Cash and cash equivalents:		
Beginning of the period	$ 22,353	$ 23,835
End of the period	$ 18,869	$ 24,894
Supplemental disclosures of cash flow information:		
Interest paid	$ 3,765	$ 3,141
Income taxes paid	815	1,364
Transfers of loans to other real estate owned property	741	1,932
Transfer of building premises and equipment to held for sale	—	3,237

See accompanying notes to unaudited consolidated financial statements

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 22 full-service offices in Virginia and Maryland. The Bank also operates two loan production offices 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, 2014. 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, 2015, the statements of changes in shareholders' equity and cash flows for the six months ended June 30, 2015, and the statements of income and comprehensive income for the three and six months ended June 30, 2015. Results for the six month period ended June 30, 2015 are not necessarily indicative of the results that may be expected for the year ending December 31, 2015.

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.

Recent Accounting Pronouncements

In April 2015, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2015-05, *Intangibles - Goodwill and Other - Internal-Use Software (Subtopic 350-40): Customer's Accounting for Fees Paid in a Cloud Computing Arrangement.* Existing GAAP does not include explicit guidance about a customer's accounting for fees paid in a cloud computing arrangement. Examples of cloud computing arrangements include: *(a)* software as a service; *(b)* platform as a service; *(c)* infrastructure as a service; and *(d)* other similar hosting arrangements. The ASU provides guidance to customers about whether a cloud computing arrangement includes a software license. If a cloud computing arrangement includes a software license, then the customer should account for the software license element of the arrangement consistent with the acquisition of other software licenses. If a cloud computing arrangement does not include a software license, the customer should account for the arrangement as a service contract. As a result of the ASU, all software licenses within the scope of Subtopic 350-40 will be accounted for consistent with other licenses of intangible assets.

For public business entities, the ASU will be effective for annual periods, including interim periods within those annual periods, beginning after December 15, 2015. Early adoption is permitted. The Company does not expect the adoption of this guidance to have a material impact on its consolidated financial statements.

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

Note 2. Securities

Amortized costs and fair values of securities available for sale and held to maturity at June 30, 2015 and December 31, 2014 were as follows (dollars in thousands):

	June 30, 2015			
		Gross Unrealized		
	Amortized Cost	Gains	Losses	Fair Value
Securities Available for Sale				
U.S. Treasury issue and other U.S. Gov't agencies	$62,479	$47	$(740)	$61,786
U.S. Gov't sponsored agencies	757	—	(28)	729
State, county and municipal	141,240	2,675	(1,946)	141,969
Corporate and other bonds	20,644	11	(114)	20,541
Mortgage backed – U.S. Gov't agencies	4,375	19	(118)	4,276
Mortgage backed – U.S. Gov't sponsored agencies	33,608	16	(112)	33,512
Total Securities Available for Sale	$263,103	$2,768	$(3,058)	$262,813
Securities Held to Maturity				
State, county and municipal	$34,877	$540	$(379)	$35,038
Mortgage backed – U.S. Gov't agencies	3,588	193	—	3,781
Mortgage backed – U.S. Gov't sponsored agencies	—	—	—	—
Total Securities Held to Maturity	$38,465	$733	$(379)	$38,819

	December 31, 2014			
		Gross Unrealized		
	Amortized Cost	Gains	Losses	Fair Value
Securities Available for Sale				
U.S. Treasury issue and other U.S. Gov't agencies	$99,608	$113	$(1,014)	$98,707
State, county and municipal	134,405	3,926	(854)	137,477
Corporate and other bonds	11,921	17	(55)	11,883
Mortgage backed – U.S. Gov't agencies	2,338	18	(98)	2,258
Mortgage backed – U.S. Gov't sponsored agencies	24,096	174	(27)	24,243
Total Securities Available for Sale	$272,368	$4,248	$(2,048)	$274,568
Securities Held to Maturity				
State, county and municipal	$31,677	$1,103	$—	$32,780
Mortgage backed – U.S. Gov't agencies	4,293	238	—	4,531

Mortgage backed – U.S. Gov't sponsored agencies	227	1	—	228
Total Securities Held to Maturity	$ 36,197	$ 1,342	$ —	$ 37,539

The amortized cost and fair value of securities at June 30, 2015 by contractual maturity are shown below. Expected maturities may differ from contractual maturities because issuers may have the right to call or prepay obligations without any penalties.

(dollars in thousands)	Held to Maturity		Available for Sale	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Due in one year or less	$ 1,674	$ 1,695	$ 3,534	$ 3,462
Due after one year through five years	13,622	14,162	67,920	68,614
Due after five years through ten years	14,365	14,271	134,655	134,688
Due after ten years	8,804	8,691	56,994	56,049
Total securities	$ 38,465	$ 38,819	$ 263,103	$ 262,813

Proceeds from sales of securities available for sale were $15.6 million and $22.9 million during the three months ended June 30, 2015 and 2014, respectively, and $56.2 million and $44.6 million during the six months ended June 30, 2015 and 2014, 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, 2015 and 2014 were as follows (dollars in thousands):

	Three Months Ended		Six Months Ended	
	June 30, 2015	June 30, 2014	June 30, 2015	June 30, 2014
Gross realized gains	$ 122	$ 90	$ 575	$ 496
Gross realized losses	(130)	(66)	(286)	(117)
Net securities (losses) gains	$ (8)	$ 24	$ 289	$ 379

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 six months ended June 30, 2015 and 2014.

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, 2015 and December 31, 2014 were as follows (dollars in thousands):

	June 30, 2015		
	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	$8,711	$ (61)	$37,858	$ (679)	$46,569	$ (740)
U.S. Gov't sponsored agencies	729	(28)	-	-	729	(28)
State, county and municipal	60,637	(1,275)	9,837	(671)	70,474	(1,946)
Corporate and other bonds	10,930	(73)	3,386	(41)	14,316	(114)
Mortgage backed – U.S. Gov't agencies	2,012	(31)	1,910	(87)	3,922	(118)
Mortgage backed – U.S. Gov't sponsored agencies	9,283	(112)	-	-	9,283	(112)
Total	$92,302	$ (1,580)	$52,991	$ (1,478)	$145,293	$ (3,058)
Securities Held to Maturity						
State, county and municipal	$19,768	$ (379)	$-	$ -	$19,768	$ (379)

	December 31, 2014					
	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	$47,475	$ (438)	$35,630	$ (576)	$83,105	$ (1,014)
State, county and municipal	3,673	(8)	32,348	(846)	36,021	(854)
Corporate and other bonds	5,756	(21)	3,113	(34)	8,869	(55)
Mortgage backed – U.S. Gov't agencies	—	—	1,899	(98)	1,899	(98)
Mortgage backed – U.S. Gov't sponsored agencies	2,551	(16)	712	(11)	3,263	(27)
Total	$59,455	$ (483)	$73,702	$ (1,565)	$133,157	$ (2,048)

The unrealized losses (impairments) in the investment portfolio at June 30, 2015 and December 31, 2014 are generally a result of market fluctuations that occur daily. The unrealized losses are from 254 securities at June 30, 2015. Of those, 234 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. Twenty investment grade corporate obligations comprise the remaining securities with unrealized losses at June 30, 2015. The Company considers the reason for impairment, length of impairment and ability 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 $55.7 million and $111.3 million at June 30, 2015 and December 31, 2014, respectively, were pledged to secure public deposits and for other purposes required or permitted by law. At each of June 30, 2015 and December 31, 2014, 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 Not Covered by FDIC Shared-loss Agreements (Non-covered Loans) and Related Allowance for Loan Losses

The Company’s non-covered loans, net of deferred fees and costs, at June 30, 2015 and December 31, 2014 were comprised of the following (dollars in thousands):

	June 30, 2015			December 31, 2014		
	Amount	% of Non-Covered Loans		Amount	% of Non-Covered Loans	
Mortgage loans on real estate:						
Residential 1-4 family	$178,426	26.08	%	$168,267	25.31	%
Commercial	284,992	41.66		283,275	42.61	
Construction and land development	59,392	8.69		59,483	8.95	
Second mortgages	7,356	1.08		6,013	0.90	
Multifamily	44,343	6.48		33,812	5.09	
Agriculture	6,654	0.97		7,163	1.08	
Total real estate loans	581,163	84.96		558,013	83.94	

Commercial loans	96,510	14.11	99,783	15.01
Consumer installment loans	5,011	0.73	5,496	0.83
All other loans	1,396	0.20	1,444	0.22
Non-covered loans	$684,080	100.00 %	$664,736	100.00 %

The Company held $14.1 million and $18.3 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, 2015 and December 31, 2014, respectively. As these loans are 100% guaranteed by the USDA, no loan loss provision is required. These loan balances included an unamortized purchase premium of $665,000 and $922,000 at June 30, 2015 and December 31, 2014, respectively. Unamortized purchase premium is recognized 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, 2015 and December 31, 2014, the Company's allowance for credit losses was comprised of the following: (i) specific valuation allowances calculated in accordance with FASB ASC 310, *Receivables,* (ii) general valuation allowances calculated in accordance with FASB Accounting Standards Codification (ASC) 450, *Contingencies*, based on economic conditions and other qualitative risk factors, and (iii) historical valuation allowances calculated using historical loan loss experience. Management identified loans subject to impairment in accordance with ASC 310.

The Purchase and Assumption Agreement into which the Company and the Federal Deposit Insurance Corporation (FDIC) entered in January 2009 that provided for the Company's assumption of all of the deposits and certain other liabilities and acquisition of substantially all assets of Suburban Federal Savings Bank (SFSB) included two shared-loss agreements with respect to certain covered loans and foreclosed real estate assets. See Notes 4 and 5 for more information on the Purchase and Assumption Agreement and the shared-loss agreements. The shared-loss agreement for loans other than those secured by single family, residential 1-4 family mortgages expired March 31, 2014. These loans, which had an outstanding principal balance of $10.0 million and a carrying value of $5.5 million at March 31, 2014, are being accounted for in accordance with FASB ASC 310-30, *Loans and Debt Securities Acquired with Deteriorated Credit Quality,* are commonly referred to as purchased credit impaired loans, and were classified as non-covered loans effective April 1, 2014 (the "PCI loans").

The PCI loans are not classified as nonperforming assets as of June 30, 2015, 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.

The following table reflects the outstanding principal balance and carrying amounts of the PCI loans as of June 30, 2015 and December 31, 2014 (dollars in thousands):

	June 30, 2015		December 31, 2014	
	Unpaid balance	Carrying Value	Unpaid balance	Carrying Value
Mortgage loans on real estate:				
Residential 1-4 family	$2,152	$ 1,013	$ 2,189	$ 1,096
Commercial	2,893	903	3,179	1,148
Construction and land development	3,502	2,384	3,658	2,456
Second mortgages	—	—	31	16
Multifamily	—	—	—	—
Agriculture	—	—	—	—
Total real estate loans	8,547	4,300	9,057	4,716
Total PCI loans	$8,547	$ 4,300	$ 9,057	$ 4,716

The allowance for loan losses related to PCI loans was $98,000 as of June 30, 2015 and was transferred from the allowance for loan losses on covered loans effective April 1, 2014. This allowance was related to commercial real estate loans. There was no other activity in the allowance for loan losses related to PCI loans for the three and six months ended June 30, 2015.

The change in the accretable yield balance for the PCI loans for the six months ended June 30, 2015 was as follows (dollars in thousands):

Balance transferred from covered loans, April 1, 2014	$4,773
Accretion	(554)
Reclassification from nonaccretable yield	852
Balance, December 31, 2014	5,071
Accretion	(303)
Reclassification from nonaccretable yield	373
Balance, June 30, 2015	$5,141

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The following table summarizes information related to impaired loans as of June 30, 2015 (dollars in thousands):

With an allowance recorded:	**Recorded Investment (1)**	**Unpaid Principal Balance (2)**	Related Allowance
Mortgage loans on real estate:			
Residential 1-4 family	$ 2,999	$ 3,489	$ 465
Commercial	216	276	28
Construction and land development	4,358	7,130	548
Second mortgages	61	63	11
Multifamily	—	—	—
Agriculture	—	—	—
Total real estate loans	7,634	10,958	1,052
Commercial loans	2	2	—
Consumer installment loans	84	89	14
All other loans	—	—	—
Subtotal impaired loans with a valuation allowance	7,720	11,049	1,066
With no related allowance recorded:			
Mortgage loans on real estate:			
Residential 1-4 family	895	943	—
Commercial	1,521	1,831	—
Construction and land development	394	882	—
Second mortgages	—	—	—
Multifamily	—	—	—
Agriculture	—	—	—
Total real estate loans	2,810	3,656	—
Commercial loans	—	—	—
Consumer installment loans	—	—	—
All other loans	—	—	—
Subtotal impaired loans without a valuation allowance	2,810	3,656	—
Total:			
Mortgage loans on real estate:			
Residential 1-4 family	3,894	4,432	465
Commercial	1,737	2,107	28
Construction and land development	4,752	8,012	548
Second mortgages	61	63	11
Multifamily	—	—	—
Agriculture	—	—	—
Total real estate loans	10,444	14,614	1,052
Commercial loans	2	2	—
Consumer installment loans	84	89	14
All other loans	—	—	—
Total impaired loans	$ 10,530	$ 14,705	$ 1,066

(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

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The following table summarizes information related to impaired loans as of December 31, 2014 (dollars in thousands):

With an allowance recorded:	**Recorded Investment** [(1)]	**Unpaid Principal Balance** [(2)]	Related Allowance
Mortgage loans on real estate:			
Residential 1-4 family	$ 2,754	$ 2,895	$ 463
Commercial	308	470	53
Construction and land development	4,903	7,643	627
Second mortgages	61	63	11
Multifamily	—	—	—
Agriculture	—	—	—
Total real estate loans	8,026	11,071	1,154
Commercial loans	7,521	8,721	520
Consumer installment loans	118	120	20
All other loans	—	—	—
Subtotal impaired loans with a valuation allowance	15,665	19,912	1,694
With no related allowance recorded:			
Mortgage loans on real estate:			
Residential 1-4 family	588	626	—
Commercial	418	550	—
Construction and land development	179	212	—
Second mortgages	—	—	—
Multifamily	—	—	—
Agriculture	—	—	—
Total real estate loans	1,185	1,388	—
Commercial loans	—	—	—
Consumer installment loans	2	3	—
All other loans	—	—	—
Subtotal impaired loans without a valuation allowance	1,187	1,391	—
Total:			
Mortgage loans on real estate:			
Residential 1-4 family	3,342	3,521	463
Commercial	726	1,020	53
Construction and land development	5,082	7,855	627
Second mortgages	61	63	11
Multifamily	—	—	—
Agriculture	—	—	—
Total real estate loans	9,211	12,459	1,154
Commercial loans	7,521	8,721	520
Consumer installment loans	120	123	20
All other loans	—	—	—
Total impaired loans	$ 16,852	$ 21,303	$ 1,694

(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

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The following table summarizes the average recorded investment of impaired loans for the three and six months ended June 30, 2015 and 2014 (dollars in thousands):

	Three months ended		Six months ended	
	June 30, 2015	June 30, 2014	June 30, 2015	June 30, 2014
Mortgage loans on real estate:				
Residential 1-4 family	$ 3,475	$ 4,813	$ 3,617	$ 4,807
Commercial	1,786	2,228	1,232	1,815
Construction and land development	4,750	5,622	4,917	5,609
Second mortgages	61	224	61	224
Multifamily	—	—	—	—
Agriculture	—	—	—	102
Total real estate loans	10,072	12,887	9,827	12,557
Commercial loans	3,706	46	3,762	82
Consumer installment loans	87	97	103	76
All other loans	—	—	—	—
Total impaired loans	$ 13,865	$ 13,030	$ 13,692	$ 12,715

During each of the three and six months ended June 30, 2015, all of the impaired loans were also nonaccruing for which no interest income was recognized. During each of the three and six months ended June 30, 2014, the majority of impaired loans were nonaccruing and no significant amounts of interest income were recognized on accruing impaired loans.

Interest income on nonaccrual loans, if recognized, is recorded using the cash basis method of accounting. Cash basis income of $260,000 and $465,000 was recognized during the three and six months ended June 30, 2015, respectively. Cash basis income of $158,000 and $297,000 was recognized during the three and six months ended June 30, 2014, respectively. For the three months ended June 30, 2015, and 2014, estimated interest income of $225,000 and $230,000, 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, 2015, and 2014, estimated interest income of $420,000 and $454,000, respectively, would have been recorded if all such loans had been accruing interest according to their original contractual terms.

The following table presents non-covered nonaccrual loans, excluding PCI loans, by loan category as of June 30, 2015 and December 31, 2014 (dollars in thousands):

	June 30, 2015	December 31, 2014
Mortgage loans on real estate:		
Residential 1-4 family	$ 3,894	$ 3,342

Commercial	1,737	607
Construction and land development	4,752	4,920
Second mortgages	61	61
Multifamily	—	—
Agriculture	—	—
Total real estate loans	10,444	8,930
Commercial loans	2	7,521
Consumer installment loans	84	120
All other loans	—	—
Total loans	$ 10,530	$ 16,571

Troubled debt restructures and some special mention 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. All impaired loans at June 30, 2015 were also nonaccrual loans. Impaired loans of $16.9 million at December 31, 2014 consisted of $16.6 million in nonaccrual loans, in addition to $118,000 in troubled debt restructures and $163,000 in special mention loans both of which were still accruing.

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The following tables present an age analysis of past due status of non-covered loans, excluding PCI loans, by category as of June 30, 2015 and December 31, 2014 (dollars in thousands):

	June 30, 2015					
	30-89 Days Past Due	90 Days Past Due	Total Past Due	Current	Total Loans	Recorded Investment 90 Days Past Due and Accruing
Mortgage loans on real estate:						
Residential 1-4 family	$ 1,843	$ 3,894	$ 5,737	$ 171,676	$ 177,413	$ —
Commercial	230	1,737	1,967	282,122	284,089	—
Construction and land development	—	4,752	4,752	52,256	57,008	—
Second mortgages	—	61	61	7,295	7,356	—
Multifamily	—	—	—	44,343	44,343	—
Agriculture	—	—	—	6,654	6,654	—
Total real estate loans	2,073	10,444	12,517	564,346	576,863	—
Commercial loans	222	2	224	96,286	96,510	—
Consumer installment loans	14	84	98	4,913	5,011	—
All other loans	—	—	—	1,396	1,396	—
Total loans	$ 2,309	$ 10,530	$ 12,839	$ 666,941	$ 679,780	$ —

	December 31, 2014					
	30-89 Days Past Due	90 Days Past Due	Total Past Due	Current	Total Loans	Recorded Investment 90 Days Past Due and Accruing
Mortgage loans on real estate:						
Residential 1-4 family	$ 298	$ 3,342	$ 3,640	$ 163,531	$ 167,171	$ —
Commercial	200	607	807	281,320	282,127	—
Construction and land development	128	4,920	5,048	51,979	57,027	—
Second mortgages	26	61	87	5,910	5,997	—
Multifamily	—	—	—	33,812	33,812	—
Agriculture	—	—	—	7,163	7,163	—
Total real estate loans	652	8,930	9,582	543,715	553,297	—
Commercial loans	66	7,521	7,587	92,196	99,783	—
Consumer installment loans	10	120	130	5,366	5,496	—
All other loans	—	—	—	1,444	1,444	—
Total loans	$ 728	$ 16,571	$ 17,299	$ 642,721	$ 660,020	$ —

Activity in the allowance for loan losses on non-covered loans, excluding PCI loans, by segment for the three and six months ended June 30, 2015 and 2014 is presented in the following tables (dollars in thousands):

	Three Months Ended June 30, 2015				
	Beginning of Period	Provision Allocation	Charge-offs	Recoveries	End of Period
Mortgage loans on real estate:					
Residential 1-4 family	$2,861	$ 743	$ —	$ 8	$ 3,612
Commercial	2,571	979	—	9	3,559
Construction and land development	1,503	584	(455)	7	1,639
Second mortgages	55	(90)	—	91	56
Multifamily	175	76	—	—	251
Agriculture	70	7	—	—	77
Total real estate loans	7,235	2,299	(455)	115	9,194
Commercial loans	1,650	(2,291)	—	1,202	561
Consumer installment loans	97	(10)	(34)	25	78
All other loans	29	2	—	—	31
Total loans	$9,011	$ —	$ (489)	$ 1,342	$ 9,864

	Three Months Ended June 30, 2014				
	Beginning of Period	Provision Allocation	Charge-offs	Recoveries	End of Period
Mortgage loans on real estate:					
Residential 1-4 family	$3,707	$ (77)	$ —	$ 40	$ 3,670
Commercial	2,964	355	(412)	12	2,919
Construction and land development	1,894	(270)	—	—	1,624
Second mortgages	114	(17)	—	1	98
Multifamily	208	(32)	—	—	176
Agriculture	57	7	—	—	64
Total real estate loans	8,944	(34)	(412)	53	8,551
Commercial loans	1,332	31	—	115	1,478
Consumer installment loans	110	2	(34)	24	102
All other loans	24	1	—	—	25
Total loans	$10,410	$ —	$ (446)	$ 192	$ 10,156

	Six Months Ended June 30, 2015				
	Beginning of Period	Provision Allocation	Charge-offs	Recoveries	End of Period
Mortgage loans on real estate:					
Residential 1-4 family	$3,100	$ 755	$ (300)	$ 57	$ 3,612
Commercial	2,618	926	—	15	3,559
Construction and land development	1,930	146	(455)	18	1,639
Second mortgages	63	(100)	—	93	56
Multifamily	136	115	—	—	251

Agriculture	66	11	—	—	77
Total real estate loans	7,913	1,853	(755)	183	9,194
Commercial loans	1,242	(1,889)	—	1,208	561
Consumer installment loans	85	32	(96)	57	78
All other loans	27	4	—	—	31
Total loans	$9,267	$ —	$ (851)	$ 1,448	$ 9,864

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	Six Months Ended June 30, 2014				
	Beginning of Period	Provision Allocation	Charge-offs	Recoveries	End of Period
Mortgage loans on real estate:					
Residential 1-4 family	$3,853	$ (120)	$ (110)	$ 47	$ 3,670
Commercial	2,333	917	(412)	81	2,919
Construction and land development	2,252	(629)	—	1	1,624
Second mortgages	101	(5)	—	2	98
Multifamily	151	25	—	—	176
Agriculture	81	(17)	—	—	64
Total real estate loans	8,771	171	(522)	131	8,551
Commercial loans	1,546	(187)	—	119	1,478
Consumer installment loans	101	17	(76)	60	102
All other loans	26	(1)	—	—	25
Total loans	$10,444	$ —	$ (598)	$ 310	$ 10,156

The following tables present information on the non-covered loans evaluated for impairment in the allowance for loan losses as of June 30, 2015 and December 31, 2014 (dollars in thousands):

	June 30, 2015			
	Allowance for Loan Losses			
	Individually Evaluated for Impairment	Collectively Evaluated for Impairment (1)	Related to PCI loans	Total
Mortgage loans on real estate:				
Residential 1-4 family	$564	$ 3,048	$ —	$3,612
Commercial	58	3,501	98	3,657
Construction and land development	548	1,091	—	1,639
Second mortgages	10	46	—	56
Multifamily	—	251	—	251
Agriculture	—	77	—	77
Total real estate loans	1,180	8,014	98	9,292
Commercial loans	6	555	—	561
Consumer installment loans	15	63	—	78
All other loans	—	31	—	31
Total loans	$1,201	$ 8,663	$ 98	$9,962

	June 30, 2015			
	Recorded Investment in Loans			
	Individually Evaluated for Impairment	Collectively Evaluated for Impairment (1)	Related to PCI loans	Total
Mortgage loans on real estate:				
Residential 1-4 family	$6,930	$ 170,483	$ 1,013	$178,426

Commercial	4,976	279,113	903	284,992
Construction and land development	4,753	52,255	2,384	59,392
Second mortgages	61	7,295	—	7,356
Multifamily	—	44,343	—	44,343
Agriculture	—	6,654	—	6,654
Total real estate loans	16,720	560,143	4,300	581,163
Commercial loans	213	96,297	—	96,510
Consumer installment loans	83	4,928	—	5,011
All other loans	—	1,396	—	1,396
Total loans	$17,016	$ 662,764	$ 4,300	$684,080

	December 31, 2014			
	Allowance for Loan Losses			
	Individually Evaluated for Impairment	Collectively Evaluated for Impairment (1)	Related to PCI loans	Total
Mortgage loans on real estate:				
Residential 1-4 family	$598	$ 2,502	$ —	$3,100
Commercial	54	2,564	98	2,716
Construction and land development	628	1,302	—	1,930
Second mortgages	11	52	—	63
Multifamily	—	136	—	136
Agriculture	—	66	—	66
Total real estate loans	1,291	6,622	98	8,011
Commercial loans	529	713	—	1,242
Consumer installment loans	20	65	—	85
All other loans	—	27	—	27
Total loans	$1,840	$ 7,427	$ 98	$9,365

	December 31, 2014			
	Recorded Investment in Loans			
	Individually Evaluated for Impairment	Collectively Evaluated for Impairment (1)	Related to PCI loans	Total
Mortgage loans on real estate:				
Residential 1-4 family	$7,307	$ 159,864	$ 1,096	$168,267
Commercial	5,122	277,005	1,148	283,275
Construction and land development	5,096	51,931	2,456	59,483
Second mortgages	61	5,936	16	6,013
Multifamily	—	33,812	—	33,812
Agriculture	—	7,163	—	7,163
Total real estate loans	17,586	535,711	4,716	558,013
Commercial loans	7,757	92,026	—	99,783
Consumer installment loans	124	5,372	—	5,496
All other loans	—	1,444	—	1,444
Total loans	$25,467	$ 634,553	$ 4,716	$664,736

(1) The category “Individually Evaluated for Impairment” includes loans individually evaluated for impairment and determined not to be impaired. These loans totalled $6.5 million and $8.6 million at June 30, 2015 and December 31, 2014, respectively. The allowance for loans losses allocated to these loans was $135,000 and $146,000 at June 30, 2015 and December 31, 2014, respectively.

Non-covered 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 $14.1 million and $18.3 million at June 30, 2015 and December 31, 2014, 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.

The following tables present the composition of non-covered loans, excluding PCI loans, by credit quality indicator at June 30, 2015 and December 31, 2014 (dollars in thousands):

	June 30, 2015				
	Pass	Special Mention	Substandard	Doubtful	Total
Mortgage loans on real estate:					
Residential 1-4 family	$164,921	$6,919	$ 5,573	$ —	$177,413
Commercial	271,762	10,705	1,622	—	284,089
Construction and land development	51,549	707	4,752	—	57,008
Second mortgages	5,786	1,509	61	—	7,356
Multifamily	44,343	—	—	—	44,343
Agriculture	6,275	379	—	—	6,654
Total real estate loans	544,636	20,219	12,008	—	576,863
Commercial loans	95,281	1,016	213	—	96,510
Consumer installment loans	4,891	36	84	—	5,011
All other loans	1,396	—	—	—	1,396
Total loans	$646,204	$21,271	$ 12,305	$ —	$679,780

	December 31, 2014				
	Pass	Special Mention	Substandard	Doubtful	Total
Mortgage loans on real estate:					
Residential 1-4 family	$153,699	$7,540	$ 5,932	$ —	$167,171
Commercial	268,391	10,363	3,373	—	282,127
Construction and land development	51,473	620	4,934	—	57,027
Second mortgages	4,636	1,300	61	—	5,997
Multifamily	33,812	—	—	—	33,812
Agriculture	7,163	—	—	—	7,163
Total real estate loans	519,174	19,823	14,300	—	553,297
Commercial loans	90,035	1,991	7,757	—	99,783
Consumer installment loans	5,351	21	124	—	5,496
All other loans	1,444	—	—	—	1,444
Total loans	$616,004	$21,835	$ 22,181	$ —	$660,020

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.

During the three and six months ended June 30, 2015, the Company modified one residential 1-4 family loan that was considered to be a TDR. The Company extended the terms and lowered the interest rate for this loan, which had a pre- and post-modification balance of $68,000. During the three and six months ended June 30, 2014, there were no loans modified that were considered to be TDRs.

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, 2015 and 2014.

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, 2015, the Company had 1-4 family mortgages in the amount of $141.8 million pledged as collateral to the Federal Home Loan Bank for a total borrowing capacity of $119.2 million.

Note 4. Loans Covered by FDIC Shared-loss Agreements (Covered Loans) and Related Allowance for Loan Losses

On January 30, 2009, the Company entered into a Purchase and Assumption Agreement with the FDIC to assume all of the deposits and certain other liabilities and acquire substantially all assets of 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 “covered 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. The shared-loss agreement related to loans other than those secured by single family, residential 1-4 family mortgages expired March 31, 2014. These loans, which had an outstanding principal balance of $10.0 million and a carrying value of $5.5 million at March 31, 2014, were transferred to non-covered loans effective April 1, 2014 (the PCI loans). See Note 3 for further details.

As of June 30, 2015 and December 31, 2014, the outstanding contractual balance of the covered loans was $88.8 million and $94.9 million, respectively. The carrying amount, by loan type, as of these dates is as follows (dollars in thousands):

	June 30, 2015			December 31, 2014		
	Amount	% of Covered Loans		Amount	% of Covered Loans	
Mortgage loans on real estate:						
Residential 1-4 family	$55,715	94.38	%	$59,075	94.15	%

Second mortgages	3,042	5.15		3,393	5.41	
Multifamily	277	0.47		276	0.44	
Total real estate loans	59,034	100.00		62,744	100.00	
Total covered loans	$59,034	100.00	%	$62,744	100.00	%

The allowance for loan losses related to the PCI loans of $98,000 was transferred to the non-covered allowance for loan losses effective April 1, 2014, and was related to commercial real estate loans. The remaining allowance for loan losses on covered loans of $386,000 at December 31, 2014 related to residential 1-4 family loans. There was no other activity in the allowance for loan losses on covered loans for the three and six months ended June 30, 2015 and 2014.

The following table presents information on the covered loans collectively evaluated for impairment in the allowance for loan losses at June 30, 2015 and December 31, 2014 (dollars in thousands):

	June 30, 2015		December 31, 2014	
	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	$386	$ 55,715	$ 386	$ 59,075
Second mortgages	—	3,042	—	3,393
Multifamily	—	277	—	276
Total real estate loans	386	59,034	386	62,744
Total covered loans	$386	$ 59,034	$ 386	$ 62,744

The change in the accretable yield balance for the six months ended June 30, 2015 and for the year ended December 31, 2014, is as follows (dollars in thousands):

Balance, January 1, 2014	$51,515
Accretion	(10,650)
Reclassification from nonaccretable yield	9,919
Transfer of PCI loans to non-covered loans	(4,773)
Balance, December 31, 2014	46,011
Accretion	(4,154)
Reclassification to nonaccretable yield	4,627
Balance, June 30, 2015	$46,484

The covered loans were not classified as nonperforming assets as of June 30, 2015, 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 covered loans.

Note 5. FDIC Agreements and FDIC Indemnification Asset

On January 30, 2009, the Company entered into a Purchase and Assumption Agreement with the FDIC to assume all of the deposits and certain other liabilities and acquire substantially all assets of SFSB. Under the shared-loss agreements that are part of that agreement, the FDIC will reimburse the Bank for 80% of losses arising from covered loans and foreclosed real estate assets, on the first $118 million in losses on such covered loans and foreclosed real estate assets, and for 95% of losses on covered loans and foreclosed real estate assets thereafter. Under the shared-loss agreements, a “loss” on a covered loan or foreclosed real estate is defined generally as a realized loss incurred through a permitted disposition, foreclosure, short-sale or restructuring of the covered loan or foreclosed real estate. The reimbursements for losses on single family, residential 1-4 family mortgage assets are to be made quarterly through March 2019 for losses incurred through January 2019, and the reimbursements for losses on other covered assets were made quarterly through March 2014. The shared-loss agreements provide for indemnification from the first dollar of losses without any threshold requirement. The reimbursable losses from the FDIC are based on the book value of the relevant loan as determined by the FDIC at the date of the transaction, January 30, 2009. New loans made after that date are not covered by the shared-loss agreements. The fair value of the shared-loss agreements is detailed below.

The Company is accounting for the shared-loss agreements with the FDIC as an indemnification asset pursuant to the guidance in FASB ASC 805, *Business Combinations*. The FDIC indemnification asset is required to be measured in the same manner as the asset or liability to which it relates. The FDIC indemnification asset is measured separately from the covered loans and other real estate owned assets (OREO) because it is not contractually embedded in the covered loan and OREO and is not transferable should the Company choose to dispose of them. Fair value was estimated using projected cash flows available for loss sharing based on the credit adjustments estimated for each loan pool and other real estate owned and the loss sharing percentages outlined in the shared-loss agreements. These cash flows were discounted to reflect the uncertainty of the timing and receipt of the loss sharing reimbursement from the FDIC.

Because the acquired loans are subject to shared-loss agreements and a corresponding indemnification asset exists to represent the value of expected payments from the FDIC, increases and decreases in loan accretable yield due to changing loss expectations will also have an impact on the valuation of the FDIC indemnification asset. Improvement in loss expectations will typically increase loan accretable yield and decrease the value of the FDIC indemnification asset and, in some instances, result in an amortizable premium on the FDIC indemnification asset. Increases in loss expectations will typically be recognized as impairment in the current period through allowance for loan losses, resulting in additional noninterest income for the amount of the increase in the FDIC indemnification asset.

In addition to the premium amortization, the balance of the FDIC indemnification asset is affected by expected payments from the FDIC. Under the terms of the shared-loss agreements, the FDIC will reimburse the Company for loss events incurred related to the covered loan portfolio. These events include such things as future writedowns due to decreases in the fair market value of OREO, net loan charge-offs and recoveries, and net gains and losses on OREO sales.

As discussed above, the shared-loss agreement for assets other than single family, residential 1-4 family mortgage assets expired March 2014. However, under the terms of the shared-loss agreement, the Company is required to reimburse the FDIC for recoveries of previously reimbursed loss events related to these assets until March 2017. The FDIC indemnification asset related to those assets was zero at March 31, 2014.

The following table presents the balances of the FDIC indemnification asset at June 30, 2015 and December 31, 2014 (dollars in thousands):

	Anticipated Expected Losses	Estimated Loss Sharing Value	Amortizable Premium (Discount) at Present Value	FDIC Indemnification Asset Total
January 1, 2014	$ 13,514	$ 10,811	$ 14,598	$ 25,409
Increases:				
Writedown of OREO property to FMV	34	27		27
Decreases:				
Net amortization of premium			(5,795)	(5,795)
Reclassifications to FDIC receivable:				
Net loan charge-offs and recoveries	(87)	(69)		(69)
OREO sales	(1,085)	(868)		(868)
Reimbursements requested from FDIC	(118)	(95)		(95)
Reforecasted Change in Anticipated Expected Losses	(6,707)	(5,365)	5,365	—
December 31, 2014	5,551	4,441	14,168	18,609
Increases:				
Writedown of OREO property to FMV	—	—		—

Decreases:				
Net amortization of premium			(2,392)	(2,392)
Reclassifications to FDIC receivable:				
Net loan charge-offs and recoveries	53	42		42
OREO sales	(82)	(66)		(66)
Reimbursements requested from FDIC	(14)	(11)		(11)
Reforecasted Change in Anticipated Expected Losses	(410)	(328)	328	—
June 30, 2015	$ 5,098	$ 4,078	$ 12,104	$ 16,182

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Note 6. Other real estate owned

The following table presents the balances of other real estate owned, covered by FDIC shared-loss agreements, and other real estate owned, non-covered, at June 30, 2015 and December 31, 2014 (dollars in thousands):

	June 30, 2015		December 31, 2014	
	Other real estate owned, covered by FDIC shared-loss agreements	Other real estate owned, non-covered	Other real estate owned, covered by FDIC shared-loss agreements	Other real estate owned, non-covered
Residential 1-4 family	$ 1,784	$ 63	$ 2,019	$ 320
Commercial	—	829	—	1,868
Construction and land development	—	3,830	—	3,536
Total other real estate owned	$ 1,784	$ 4,722	$ 2,019	$ 5,724

At June 30, 2015, the Company had $707,000 in residential 1-4 family non-covered loans that were in the process of foreclosure and $2.8 million in residential 1-4 family covered loans that were in in process of foreclosure.

Note 7. Deposits

The following table provides interest bearing deposit information, by type, as of June 30, 2015 and December 31, 2014 (dollars in thousands):

	June 30, 2015	December 31, 2014
NOW	$ 124,234	$ 123,682
MMDA	110,577	101,784
Savings	86,114	78,478
Time deposits less than $250,000	414,015	416,628
Time deposits $250,000 and over	111,496	113,809
Total interest bearing deposits	$ 846,436	$ 834,381

Note 8. 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, 2015 and 2014 (dollars in thousands):

	Three months ended June 30, 2015			
	Unrealized Gain (Loss) on Securities	Defined Benefit Pension Plan	Gain (Loss) on Cash Flow Hedge	Total Other Comprehensive (Loss) Income
Beginning balance	$ 2,427	$ (811)	$ (226)	$ 1,390
Other comprehensive (loss) income before reclassifications	(2,624)	-	142	(2,482)
Amounts reclassified from AOCI	5	-	-	5
Net current period other comprehensive (loss) income	(2,619)	-	142	(2,477)
Ending balance	$ (192)	$ (811)	$ (84)	$ (1,087)

	Three months ended June 30, 2014		
	Unrealized Gain (Loss) on Securities	Defined Benefit Pension Plan	Total Other Comprehensive (Loss) Income)
Beginning balance	$ (1,716)	$ (155)	$ (1,871)
Other comprehensive income before reclassifications	1,287	-	1,287
Amounts reclassified from AOCI	(16)	-	(16)
Net current period other comprehensive income	1,271	-	1,271
Ending balance	$ (445)	$ (155)	$ (600)

	Six months ended June 30, 2015			
	Unrealized Gain (Loss) on Securities	Defined Benefit Pension Plan	Gain (Loss) on Cash Flow Hedge	Total Other Comprehensive (Loss) Income
Beginning balance	$ 1,452	$ (811)	$ 23	$ 664
Other comprehensive loss before reclassifications	(1,453)	-	(107)	(1,560)
Amounts reclassified from AOCI	(191)	-	-	(191)
Net current period other comprehensive loss	(1,644)	-	(107)	(1,751)
Ending balance	$ (192)	$ (811)	$ (84)	$ (1,087)

	Six months ended June 30, 2014		
	Unrealized Gain (Loss) on Securities	Defined Benefit Pension Plan	Total Other Comprehensive (Loss) Income
Beginning balance	$ (3,954)	$ (155)	$ (4,109)
Other comprehensive income before reclassifications	3,759	-	3,759
Amounts reclassified from AOCI	(250)	-	(250)
Net current period other comprehensive income	3,509	-	3,509
Ending balance	$ (445)	$ (155)	$ (600)

The following tables present the effects of reclassifications out of AOCI on line items of consolidated income for the three and six months ended June 30, 2015 and 2014 (dollars in thousands):

Details about AOCI Components	Amount Reclassified from AOCI Three months ended June 30, 2015	June 30, 2014	Affected Line Item in the Unaudited Consolidated Statement of Income
Unrealized loss (gain) on securities available for sale	$ 8	$ (24)	(Loss) gain on securities transactions, net
	(3)	8	Income tax expense
	$ 5	$ (16)	Net of tax

Details about AOCI Components	Amount Reclassified from AOCI Six months ended June 30, 2015	June 30, 2014	Affected Line Item in the Unaudited Consolidated Statement of Income
Unrealized gain on securities available for sale	$ (289)	$ (379)	(Loss) gain on securities transactions, net
	98	129	Income tax expense
	$ (191)	$ (250)	Net of tax

Note 9. 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, 2015.

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, 2015			
	Total	Level 1	Level 2	Level 3
Investment securities available for sale				
U.S. Treasury issue and other U.S. Gov't agencies	$61,786	$58,851	$2,935	$ -
U.S. Gov't sponsored agencies	729	-	729	-
State, county and municipal	141,969	6,695	135,274	-
Corporate and other bonds	20,541	2,301	18,240	-
Mortgage backed – U.S. Gov't agencies	4,276	-	4,276	-
Mortgage backed – U.S. Gov't sponsored agencies	33,512	17,937	15,575	-
Total investment securities available for sale	262,813	85,784	177,029	-
Loans held for sale	6,503	-	6,503	-
Total assets at fair value	$269,316	$85,784	$183,532	$ -
Cash flow hedge	$128	$-	$128	$ -
Total liabilities at fair value	$128	$-	$128	$ -

	December 31, 2014			
	Total	Level 1	Level 2	Level 3
Investment securities available for sale				
U.S. Treasury issue and other U.S. Gov't agencies	$98,707	$94,464	$4,243	$ -
State, county and municipal	137,477	5,596	131,881	-
Corporate and other bonds	11,883	-	11,883	-
Mortgage backed – U.S. Gov't agencies	2,258	-	2,258	-
Mortgage backed – U.S. Gov't sponsored agencies	24,243	-	24,243	-
Total investment securities available for sale	274,568	100,060	174,508	-
Loans held for sale	200	-	200	-
Cash flow hedge	23	-	23	-
Total assets at fair value	$274,791	$100,060	$174,731	$ -
Total liabilities at fair value	$-	$-	$-	$ -

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. 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.

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.

Level 1 securities include those traded on an active exchange, such as the New York Stock Exchange, U.S. Treasury securities that are traded by dealers or brokers in active over-the-counter markets and money market funds. Level 2 securities include mortgage-backed securities issued by government sponsored entities, municipal bonds and corporate debt securities.

Loans held for sale

The carrying amounts of loans held for sale approximate fair value.

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, 2015 and December 31, 2014 (dollars in thousands):

	June 30, 2015			
	Total	Level 1	Level 2	Level 3
Impaired loans, non-covered	$8,105	$ —	$ —	$8,105
Other real estate owned (OREO), non-covered	4,722	—	—	4,722
Other real estate owned (OREO), covered	1,784	—	—	1,784
Total assets at fair value	$14,611	$ —	$ —	$14,611
Total liabilities at fair value	$—	$ —	$ —	$—

	December 31, 2014			
	Total	Level 1	Level 2	Level 3
Impaired loans, non-covered	$14,286	$ —	$ —	$14,286
Other real estate owned (OREO), non-covered	5,724	—	—	5,724
Other real estate owned (OREO), covered	2,019	—	—	2,019
Total assets at fair value	$22,029	$ —	$ —	$22,029
Total liabilities at fair value	$—	$ —	$ —	$—

Impaired loans, non-covered

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, 2015 and December 31, 2014, 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 12 months old. 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. Internally prepared estimates generally result from current market data and actual sales data related to the Company’s collateral or where the collateral is located. 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, covered and non-covered

Other real estate owned (OREO) assets are adjusted to fair value less estimated selling costs upon transfer of the related loans to OREO property. 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 selling 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 recognized 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, 2015				
	Carrying Value	**Estimated Fair Value**	Level 1	Level 2	Level 3
Financial assets:					
Securities held to maturity	$38,465	$ 38,819	$ —	$38,819	$—
Loans, non-covered	674,118	682,363	—	669,862	12,501
Loans, covered	58,648	63,972	—	—	63,972
FDIC indemnification asset	16,182	3,941	—	—	3,941
Financial liabilities:					
Interest bearing deposits	846,436	848,670	—	848,670	—
Long-term borrowings	92,432	92,460	—	92,460	—

	December 31, 2014				
	Carrying Value	**Estimated Fair Value**	Level 1	Level 2	Level 3
Financial assets:					
Securities held to maturity	$36,197	$ 37,539	$ —	$37,539	$—
Loans, non-covered	655,371	661,806	—	642,645	19,161
Loans, covered	62,358	69,483	—	—	69,483
FDIC indemnification asset	18,609	4,242	—	—	4,242
Financial liabilities:					
Interest bearing deposits	834,381	836,658	—	836,658	—
Long-term borrowings	110,205	110,218	—	110,218	—

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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, 2015. 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.

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.

Securities held for investment

For securities held for investment, fair values are based on quoted market prices or dealer quotes.

Restricted securities

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

Loans held for sale

The carrying amounts of loans held for sale approximate fair value.

Loans not covered by FDIC shared-loss agreement (non-covered loans)

The fair value of loans, excluding PCI 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. The fair value of non-covered loans that are PCI loans is estimated using the same methodology described below for covered loans.

Loans covered by FDIC shared-loss agreement (covered loans) and PCI loans

Fair values for covered loans and 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.

FDIC indemnification asset

Loss sharing assets are measured separately from the related covered assets as they are not contractually embedded in the covered assets and are not transferable with the assets should the Company choose to dispose of them. Fair value is estimated using projected cash flows related to the obligations under the shared-loss agreements based on the expected reimbursements for losses and the applicable loss sharing percentages. These expected reimbursements do not include reimbursable amounts related to future covered expenditures. These cash flows were discounted to reflect the uncertainty of the timing and receipt of the loss sharing reimbursement from the FDIC. A reduction in loss expectations has resulted in the estimated fair value of the FDIC indemnification asset being lower than its carrying value. This creates a premium that is amortized over the life of the asset and is reflected in Note 5.

Accrued interest receivable

The carrying amounts of accrued interest receivable approximate fair value.

Financial Liabilities

Noninterest bearing deposits

The carrying amount of noninterest bearing deposits approximates fair value.

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 and securities sold under agreements to repurchase

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

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 analyzes 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.

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 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 10. Earnings Per Common Share

Basic earnings per common share (EPS) is computed by dividing net income or loss available to common shareholders 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, 2015 and 2014 (dollars and shares in thousands, except per share data):

	Net Income Available to Common Shareholders (Numerator)	Weighted Average Common Shares (Denominator)	Per Common Share Amount
For the three months ended June 30, 2015			
Basic EPS	$ 1,693	21,821	$ 0.08
Effect of dilutive stock awards	—	137	—
Diluted EPS	$ 1,693	21,958	$ 0.08
For the three months ended June 30, 2014			
Basic EPS	$ 1,538	21,742	$ 0.07
Effect of dilutive stock awards	—	197	—
Diluted EPS	$ 1,538	21,939	$ 0.07
For the six months ended June 30, 2015			
Basic EPS	$ 3,005	21,810	$ 0.14
Effect of dilutive stock awards	—	184	—
Diluted EPS	$ 3,005	21,994	$ 0.14
For the six months ended June 30, 2014			
Basic EPS	$ 3,197	21,736	$ 0.15
Effect of dilutive stock awards	—	236	—
Diluted EPS	$ 3,197	21,972	$ 0.15

There were no antidilutive exclusions from the computation of diluted earnings per common share for the three and six months ended June 30, 2015. Antidilutive common shares issuable under awards or options of 36,000 were excluded from the computation of diluted earnings per common share during the three and six months ended June 30, 2014.

Note 11. 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, 2015 and 2014 (dollars in thousands):

	Three months ended June 30		Six months ended June 30	
	2015	2014	2015	2014
Interest cost	$ 47	$ 56	$ 95	$ 111
Expected return on plan assets	(88)	(99)	(177)	(198)
Amortization of prior service cost	1	1	2	2
Recognized net actuarial loss	11	3	22	6
Net periodic benefit	$ (29)	$ (39)	$ (58)	$ (79)

Note 12. 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. As of June 30, 2015, the Company had $160,000 of cash pledged as collateral.

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 is deemed to be effective. At June 30, 2015, the fair value of the Company’s cash flow hedge was an unrealized loss of $128,000 and was recorded in other liabilities. The loss was recorded as a component of other comprehensive income.

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, 2015 and results of operations of Community Bankers Trust Corporation (the "Company") for the three and six months ended June 30, 2015 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, 2014.

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 22 full-service offices in Virginia and Maryland. The Bank also operates two loan production offices 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.

For 2015, the Company is strategically prepared to grow and expand organically throughout Virginia and Maryland. The Company opened new branch offices in Bowie, Maryland on January 12, 2015 and in the Bon Air area of Richmond, Virginia on August 3, 2015. The Company recently fully staffed an existing loan production office in Fairfax, Virginia with three new lenders. Additionally, four other lenders have been added to its small business and commercial banking groups. While this increases salary costs in the short term, it is expected to add significant value with both future loan production and growth in low cost deposits.

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, gains from loan sales, transactions involving bank-owned property, 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, 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;

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- 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 loan pools under the shared-loss agreements;
- 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, 2014 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 Non-covered 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 quarterly 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. 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 Bank's allowance for loan losses and may require the Bank 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 and general 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.

A loan is considered impaired when, based on current information and events, management believes that it is more likely than not that the Bank 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, availability of current financial information, 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.

Large groups of smaller-balance homogeneous loans are collectively evaluated for impairment. Accordingly, the Company does not separately identify individual consumer and residential loans for impairment disclosures.

Accounting for Certain Loans or Debt Securities 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 allowance for loan losses.

The Company's acquired loans from the Suburban Federal Savings Bank (SFSB) transaction (the "covered loans"), subject to FASB ASC Topic 805, *Business Combinations*, are 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 shared-loss agreement with the Federal Deposit Insurance Corporation (FDIC) related to the acquisition of SFSB for loans other than those secured by single family, residential 1-4 family mortgages expired March 31, 2014. These loans will continue to be accounted for in accordance with FASB ASC 310-30 as purchased credit impaired loans and were classified as non-covered loans effective April 1, 2014 (the "PCI loans").

The covered loans and PCI loans are subject to the credit review standards described above for non-covered loans. If and when credit deterioration occurs subsequent to the date that the covered loans were acquired, a provision for credit loss for covered loans will be charged to earnings for the full amount without regard to the shared-loss agreements.

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.

FDIC Indemnification Asset

The Company is accounting for the shared-loss agreements as an indemnification asset pursuant to the guidance in FASB ASC 805. The FDIC indemnification asset is required to be measured in the same manner as the asset or liability to which it relates. The FDIC indemnification asset is measured separately from the covered loans and other real estate owned (OREO) assets because it is not contractually embedded in the covered loan and OREO assets and is not transferable should the Company choose to dispose of them. Fair value was estimated using projected cash flows available for loss sharing based on the credit adjustments estimated for each loan pool and OREO and the loss sharing percentages outlined in the shared-loss agreements. These cash flows were discounted to reflect the uncertainty of the timing and receipt of the loss sharing reimbursement from the FDIC.

Because the acquired loans are subject to shared-loss agreements and a corresponding indemnification asset exists to represent the value of expected payments from the FDIC, increases and decreases in loan accretable yield due to changing loss expectations will also have an impact to the valuation of the FDIC indemnification asset. Improvement in loss expectations will typically increase loan accretable yield and decrease the value of the FDIC indemnification asset and, in some instances, result in an amortizable premium on the FDIC indemnification asset. Increases in loss expectations will typically be recognized as impairment in the current period through allowance for loan losses while resulting in additional noninterest income for the amount of the increase in the FDIC indemnification asset.

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. 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 various state income taxes. All years from 2011 through 2014 are open to examination by the respective tax authorities.

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.

RESULTS OF OPERATIONS

Overview

Net income was $1.7 million for the second quarter of 2015, compared with $1.7 million in the second quarter of 2014. Net income available to common shareholders was $1.7 million in the second quarter of 2015, compared with $1.5 million in the second quarter of 2014. Earnings per common share, basic and fully diluted, were $0.08 per share for the second quarter of 2015, compared with $0.07 per share for the second quarter of 2014.

Net income was $3.0 million for the six months ended June 30, 2015 compared with $3.4 million for the first half of 2014. Net income available to common shareholders equaled $3.0 million for the first half of 2015 versus $3.2 million for the same period in 2014. The decline in net income over the respective time periods was the result of lower net interest income coupled with a modest increase in operating expenses, most notably personnel expenses. Earnings per common share, basic and fully diluted, were $0.14 per share and $0.15 per share for the six months ended June 30, 2015 and 2014, respectively.

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 declined $295,000, or 2.7%, from the second quarter of 2014 to the second quarter of 2015. Interest income declined $122,000, or 1.0%, when comparing these time periods. Interest income on the non-covered loan portfolio increased $875,000, or 12.0%. Average non-covered loan balances increased $75.2 million when comparing the second quarter of 2014 to the second quarter of 2015, while the average loan yield declined only two basis points to 4.77% for the second quarter of 2015. This increase was more than offset by a $995,000, or 30.5%, decline in covered loan interest income over the same time frame. This decline was partially the result of fewer significant cash payments received on covered loans related to pools that had previously been written down to a zero carrying value. During the second quarter of 2014, these significant cash payments totalled $706,000 and, during the second quarter of 2015, these payments totalled $475,000. The remainder of the decrease was due to normal amortization within the portfolio. As a result, the yield on the covered loan portfolio fell from 19.62% for the second quarter of 2014 to 15.07% for the second quarter of 2015.

Interest expense increased $173,000, or 10.2%, when comparing the second quarter of 2014 and the second quarter of 2015. Interest expense on deposits increased $33,000, or 2.3%, while interest expense on borrowings increased $140,000, or 57.4%. The slight increase in deposit cost was driven by higher cost time deposits. Average FHLB advances increased $14.4 million, and the expense associated with the borrowings increased $138,000, from the second quarter of 2014 to the second quarter of 2015. This increase in interest expense was also influenced by the $30.0 million notional value swap entered into during the fourth quarter of 2014. Consequently, the average cost of FHLB and other borrowings increased 46 basis points from 0.80% for the second quarter of 2014 to 1.26% for the second quarter of 2015. Other interest expense was attributed to the third-party loan that the Company closed in the second quarter of 2014 for which the proceeds were used to pay off the Company’s then outstanding TARP investment. Pre-tax interest on the loan equalled $84,000 for the second quarter of 2015, versus $81,000 in the second quarter of 2014.

The tax equivalent net interest margin declined 28 basis points from 4.35% in the second quarter of 2014 to 4.07% in the second quarter of 2015. Likewise, the net interest spread decreased from 4.29% to 3.98% over the same time period. The decline in margin was precipitated by the reduction in cash basis covered loan income, which helped drive overall loan yields down 64 basis points.

For the first half of 2015, net interest income decreased $819,000, or 3.9%, when compared to the first six months of 2014. Interest income declined $351,000, or 1.4%, over this time frame while interest expense increased $468,000, or 14.3%. Interest income on the non-covered loan portfolio increased $1.7 million, or 12.1%. Average non-covered loan balances increased $75.9 million, or 12.6%, for the first six months of 2015 versus the same period in 2014, while the average loan yield declined only two basis points to 4.77% for the first half of 2015. This increase partially offset a $2.0 million, or 32.8%, decline in covered loan interest income over the same time frame. Part of the decline in this income was related to significant cash payments on loans related to pools previously written down to a zero carrying value. Significant cash payments equalled $1.1 million in the first half of 2014 and $475,000 in the first half of 2015, all of which were received during the second quarter. As mentioned above, the remainder of the decrease was due to normal amortization within the portfolio. As a result, the yield on the covered loan portfolio fell from 18.00% for the first six months of 2014 to 13.74% for the same period in 2015.

Interest expense increased $468,000, or 14.3%, when comparing the first six months of 2014 and the first six months of 2015. Deposit costs increased a modest $73,000, or 2.6%, over this time frame while interest expense on FHLB borrowings increased $300,000, or 92.9%, over the same time frame. Average FHLB advances increased $16.8 million for the first six months of 2015 compared with the first six months of 2014. The increase in the associated FHLB interest expense was the result of the swap noted above. The average cost of FHLB and other borrowings increased 48 basis points from 0.80% for the six months ended June 30, 2014 to 1.28% for the first six months of 2015. Other interest expense was attributed to the third-party loan mentioned above. The pre-tax interest on the loan, which closed in the second quarter of 2014, equalled $176,000 for the first half of 2015, versus $81,000 for the first six months of 2014.

The tax equivalent net interest margin declined 34 basis points from 4.32% in the first half of 2014 to 3.98% in the first half of 2015. Likewise, the net interest spread decreased from 4.26% to 3.90% over the same time period. As previously discussed, the decline in the margin was influenced by the reduction in cash basis covered loan income, which helped drive overall loan yields down 65 basis points.

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, 2015 and 2014. The tables also set 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 table, as loans carrying a zero yield.

(dollars in thousands)	Three months ended June 30, 2015			Three months ended June 30, 2014		
	Average Balance Sheet	Interest Income/ Expense	Average Rates Earned/ Paid	Average Balance Sheet	Interest Income/ Expense	Average Rates Earned/ Paid
ASSETS:						
Loans, non-covered, including fees	$ 686,293	$ 8,166	4.77 %	$ 611,065	$ 7,291	4.79 %
FDIC covered loans, including fees	60,388	2,269	15.07	66,722	3,264	19.62
Total loans	746,681	10,435	5.61	677,787	10,555	6.25
Interest bearing bank balances	20,874	17	0.33	28,795	22	0.31
Federal funds sold	3,473	1	0.10	1,379	-	0.10
Securities (taxable)	212,681	1,355	2.55	269,566	1,710	2.54
Securities (tax exempt) [(1)]	74,762	795	4.25	22,436	255	4.55
Total earning assets	1,058,471	12,603	4.78	999,963	12,542	5.03
Allowance for loan losses	(9,732)			(10,802)		
Non-earning assets	99,028			117,948		
Total assets	$ 1,147,767			$ 1,107,109		
LIABILITIES AND SHAREHOLDERS' EQUITY						
Demand - interest bearing	$ 225,643	$ 169	0.30 %	$ 199,829	$ 148	0.30 %
Savings	84,576	66	0.31	77,057	66	0.34
Time deposits	525,372	1,251	0.96	558,797	1,239	0.89
Total interest bearing deposits	835,591	1,486	0.71	835,683	1,453	0.70
Short-term borrowings	283	-	0.62	73	1	0.61
FHLB and other borrowings	95,437	300	1.26	81,056	162	0.80
Long-term debt	8,069	84	4.11	8,098	81	3.98
Total interest bearing liabilities	939,380	1,870	0.80	924,910	1,697	0.74
Noninterest bearing deposits	93,623			73,738		
Other liabilities	4,061			4,526		
Total liabilities	1,037,064			1,003,174		
Shareholders' equity	110,703			103,935		
Total liabilities and shareholders' equity	$ 1,147,767			$ 1,107,109		
Net interest earnings		$ 10,733			$ 10,845	
Interest spread			3.98 %			4.29 %
Net interest margin			4.07 %			4.35 %

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

(dollars in thousands)	Six months ended June 30, 2015			Six months ended June 30, 2014		
	Average Balance Sheet	Interest Income/ Expense	Average Rates Earned/ Paid	Average Balance Sheet	Interest Income/ Expense	Average Rates Earned/ Paid
ASSETS:						
Loans, non-covered, including fees	$ 679,247	$ 16,072	4.77 %	$ 603,381	$ 14,342	4.79 %
FDIC covered loans, including fees	61,406	4,183	13.74	69,731	6,225	18.00
Total loans	740,653	20,255	5.51	673,112	20,567	6.16
Interest bearing bank balances	18,137	34	0.38	22,586	35	0.31
Federal funds sold	3,735	2	0.10	693	-	0.10
Securities (taxable)	219,311	2,723	2.48	274,404	3,408	2.48
Securities (tax exempt) [1]	68,177	1,468	4.31	21,244	491	4.61
Total earning assets	1,050,013	24,482	4.70	992,039	24,501	4.98
Allowance for loan losses	(9,713)			(10,878)		
Non-earning assets	100,882			115,838		
Total assets	$ 1,141,182			$ 1,096,999		
LIABILITIES AND SHAREHOLDERS' EQUITY						
Demand - interest bearing	$ 223,518	$ 323	0.29 %	$ 195,341	$ 291	0.30 %
Savings	82,116	126	0.31	76,333	132	0.35
Time deposits	526,042	2,485	0.95	557,340	2,438	0.88
Total interest bearing deposits	831,676	2,934	0.71	829,014	2,861	0.70
Short-term borrowings	904	2	0.54	601	2	0.52
FHLB and other borrowings	97,959	623	1.28	81,145	323	0.80
Long-term debt	8,560	176	4.09	4,071	81	3.98
Total interest bearing liabilities	939,099	3,735	0.80	914,831	3,267	0.72
Noninterest bearing deposits	88,065			71,180		
Other liabilities	4,152			4,225		
Total liabilities	1,031,316			990,236		
Shareholders' equity	109,866			106,763		
Total liabilities and shareholders' equity	$ 1,141,182			$ 1,096,999		
Net interest earnings		$ 20,747			$ 21,234	
Interest spread			3.90 %			4.26 %
Net interest margin			3.98 %			4.32 %

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

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 Non-covered 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 covered and PCI loan portfolios 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 in either the three or six month periods ended June 30, 2015 or 2014 with respect to either its non-covered loan portfolio or its FDIC covered loan portfolio. With respect to the non-covered loan portfolio, this was the direct result of nominal charge-offs and the ongoing stabilization of asset quality.

There were net recoveries of $853,000 in the second quarter of 2015, compared with net charge-offs of $254,000 in the second quarter of 2014. Total charge-offs for the second quarter of 2015 were $489,000 compared with $446,000 in the second quarter of 2014. Recoveries of previously charged-off loans were $1.3 million for the second quarter of 2015 compared with $192,000 in the first quarter of 2014.

There were net recoveries of $597,000 in the six months ended June 30, 2015, compared with net charge-offs of $288,000 in the six months ended June 30, 2014. Total charge-offs for the first six months of 2015 were $851,000 compared with $598,000 for the same period in 2014. Recoveries of previously charged-off loans were $1.4 million in the six months ended June 30, 2015 compared with $310,000 for the same period in 2014.

Noninterest Income

Noninterest income increased $236,000, or 24.3%, from the second quarter of 2014 to the second quarter of 2015. Other operating income increased $281,000, or 170.3%, from the quarter ended June 30, 2014 to the quarter ended June 30, 2015. A vast improvement in mortgage income was the sole driver of this increase. In June 2014, the Company began a wholesale mortgage operation to complement and expand the existing mortgage origination division. This has contributed significant growth to the mortgage operation in 2015. Mortgage income increased $232,000, or 773.3%, when comparing the second quarter of 2015 with the second quarter of 2014. This improvement more than offset any decline in other noninterest income categories.

For the six months ended June 30, 2015, noninterest income totaled $2.6 million, which was a $332,000, or 14.6%, improvement from the first six months of 2014. Other noninterest income increased principally because of mortgage income. Mortgage income was $73,000 for the first six months of 2014 increasing $337,000, or 461.6%, to $410,000 for the first six months of 2015.

Noninterest Expense

Noninterest expenses increased $84,000, or 0.9%, when comparing the second quarter of 2014 with the same period in 2015. The single largest increase was in salaries and benefits which rose $378,000, or 9.4%, over this time frame. The overall increase in salaries and benefits expense was related to increased staffing in 2015, most notably income producing lenders. Other operating expense increased $87,000, or 5.2%, when comparing the second quarter of 2014 with the second quarter of 2015. Credit expense increased $197,000, or 140.7%, which was driven in part by the legal fees related to the resolution of a $7.4 million commercial loan relationship, as well as filing fees and appraisal expenses. Within the other operating expense category, supplies expense declined $35,000, or 24.0%, and external audit fees declined $85,000, or 61.6%, over the same time frame.

The Company benefitted from a $325,000, or 22.0%, decline in the indemnification asset amortization from the second quarter of 2014 to the second quarter of 2015. Occupancy expenses and data processing fees declined $68,000, or 9.9%, and $51,000, or 11.0%, respectively, during this time frame. The improvement in occupancy expenses was driven by lower rental expense following the closing of the Landover Hills branch in the fourth quarter of 2014. The reduction in data processing fees was the result of account consolidation and improved vendor contract pricing.

Noninterest expenses increased $426,000, or 2.3%, when comparing the first six months of 2014 and 2015. The majority of the increase was evidenced in two categories: salaries and benefits expense and other operating expenses. Salaries and benefits expense increased $950,000, or 11.9%, during the first six months of 2015 when compared with the first six months of 2014. This increase was the result of increased staffing and the related benefits from the addition of new lending team members over the last year to boost production. Other operating expenses increased $275,000, or 8.9%, over the same time frame. This increase was primarily driven by an increase in credit related expenses and advertising expenses. Credit expense increased $263,000, or 110.5%, and was driven in part by the legal fees for the resolution of the commercial loan relationship mentioned above. Within the other operating expense category, state taxes declined $100,000, or 87.0%, and external audit fees declined $97,000, or 43.7%. These declines off set a $167,000 increase in advertising expenses over the same time frame. The increase in advertising expenses was partially attributed to new promotional materials for new deposit products. The reduction in state taxes was the result of reincorporating the Company from Delaware to Virginia at the beginning of 2014.

Other noteworthy changes in noninterest expenses over this time frame included FDIC indemnification asset amortization, other real estate expense, and data processing fees. FDIC indemnification asset amortization declined $584,000, or 19.6%, while other real estate expenses and data processing fees declined $161,000, or 42.0%, and $103,000, or 10.8%, respectively. The improvement in other real estate expense was driven by increased rental income related to other real estate owned (OREO) property coupled with lower losses taken on the disposition of OREO property.

Income Taxes

Income tax expense was $533,000 for the three months ended June 30, 2015, compared with income tax expense of $649,000 for the second quarter of 2014. Income tax expense was $884,000 for the first six months of 2015 compared with $1.4 million for the first six months of 2014. The effective tax rate for the second quarter of 2015 was 23.9% versus 27.4% for the second quarter of 2014. The effective tax rate for the first six months of 2015 was 22.7% compared with 28.3% for the first six months of 2014. This decline in the effective tax rate was due to an increased level of nontaxable income related to an increased volume of municipal securities.

FINANCIAL CONDITION

General

During the first six months of 2015, total assets increased $3.4 million to $1.159 billion at June 30, 2015. Total loans were $743.1 million at June 30, 2015, increasing $15.6 million since December 31, 2014. Total non-covered loans were $684.0 million at June 30, 2015 and $664.7 million at December 31, 2014. The majority of the non-covered loan growth was in the residential 1-4 family loan category as well as the multifamily loan segment. Residential 1-4 family loans grew $10.2 million, or 6.0%, and multifamily loans grew $10.5 million or 31.1%, since year end.

The Company's securities portfolio, excluding equity securities, declined $9.5 million, or 3.1%, from $310.8 million at December 31, 2014 to $301.3 million at June 30, 2015. Realized losses of $8,000 occurred during the second quarter of 2015 through sales and call activity, and net gains on the sales of securities aggregated $289,000 for the first six months of 2015. This compares with $24,000 of net gains taken in the second quarter of 2014 and $379,000 during the first six months of 2014.

The Company had cash and cash equivalents of $18.9 million and $22.4 million at June 30, 2015 and December 31, 2014, respectively. There were $5.0 million in federal funds purchased at June 30, 2015 versus $14.5 million at

December 31, 2014.

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 $263.0 million at June 30, 2015 and $274.6 million at December 31, 2014. At June 30, 2015, the Company had a net unrealized loss on the AFS portfolio of $290,000 compared with a net unrealized gain of $2.2 million at December 31, 2014. Municipal securities comprised 54% of the total AFS portfolio at June 30, 2015. These securities exhibit more price volatility in a changing interest rate environment because of their longer weighted average life, than other categories contained within the rest of the portfolio.

Interest bearing deposits at June 30, 2015 were $846.4 million, an increase of $12.1 million, or 1.44%, from December 31, 2014. MMDA and savings account balances increased $8.8 million and $7.6 million, or 8.6% and 9.7%, respectively, over the same time period. Retail time deposit account balances increased $3.3 million, or 0.7%, during the first half of 2015, while brokered time deposits declined $8.2 million, or 11.2%, since year end. Management has focused on changing the deposit mix from higher cost time deposit products to lower cost transactional products. The Company has been successful with its solid growth in interest free demand deposits and other transactional accounts mentioned above.

FHLB advances were $81.0 million at June 30, 2015, compared with $96.4 million at December 31, 2014. During the second quarter of 2015, $15.2 million in FHLB advances matured. Total deposit growth of $32.9 million during the second quarter of 2015 afforded the reduction in FHLB advances. Long term debt totaled $7.3 million at June 30, 2015, declining by $2.4 million, or 24.8%, since December 31, 2014. This borrowing, initially in the amount of $10.7 million, was obtained in April 2014, and the proceeds were used to redeem the Company’s remaining outstanding TARP preferred stock. The Company has repaid $3.4 million of this debt and should have the loan fully paid within the next two years.

Shareholders' equity was $109.2 million at June 30, 2015 and $107.7 million at December 31, 2014, respectively. Shareholders' equity increased $1.5 million, or 1.4%, from year end 2014 as the result of a decline in other comprehensive income related to net losses in the investment portfolio and net income of $3.0 million in the first half of 2015.

Asset Quality – non-covered assets, 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.

Non-covered 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 Non-covered Loans* in the Critical Accounting Policies section above for further discussion.

The Company maintains a list of non-covered 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. Non-covered nonperforming assets totaled $15.3 million at June 30, 2015 and net recoveries were $597,000 for the six months ended June 30, 2015. This compares with nonperforming assets of $22.3 million and net charge-offs of $1.2 million at and for the year ended December 31, 2014.

Nonperforming non-covered loans were $10.5 million at June 30, 2015, a decrease from $16.6 million at December 31, 2014. The $6.0 million decrease in nonperforming loans since December 31, 2014 was the net result of $3.2 million in additions to nonperforming loans and $9.2 million in reductions. With respect to the reductions to nonperforming loans, $7.5 million were payoffs, $7.4 million of which was related to one nonaccrual commercial relationship. Other reductions consisted of $837,000 of payments to existing credits, $781,000 of charge-offs, and $38,000 of loans returned to accruing status.

The allowance for loan losses equaled 93.68% of non-covered nonaccrual loans at June 30, 2015 compared with 55.92% at December 31, 2014. The ratio of the allowance for loan losses to total nonperforming assets was 64.67% at June 30, 2015, compared with 41.57% at December 31, 2014. The ratio of nonperforming assets to loans and OREO continued to decline. The ratio was 2.21% at June 30, 2015 versus 3.35% at December 31, 2014.

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 restructured 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, 2015 and December 31, 2014, total impaired non-covered loans equaled $10.5 million and $16.9 million, respectively.

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

	June 30, 2015		December 31, 2014	
Nonaccrual loans	$ 10,530		$ 16,571	
Loans past due 90 days and accruing interest	—		—	
Total nonperforming non-covered loans	10,530		16,571	
OREO – non-covered	4,722		5,724	
Total nonperforming non-covered assets	$ 15,252		$ 22,295	
Accruing troubled debt restructure loans	$ 4,594		$ 6,195	
Balances				
Specific reserve on impaired loans	1,066		1,694	
General reserve related to unimpaired loans	8,798		7,573	
Total allowance for loan losses	$ 9,864		$ 9,267	
Average loans during the year, net of unearned income	$ 679,247		$ 621,213	
Impaired loans	10,530		16,852	
Non-impaired loans	669,250		643,168	
Total loans, net of unearned income	$ 679,780		$ 660,020	
Ratios				
Allowance for loan losses to loans	1.45	%	1.40	%
Allowance for loan losses to nonperforming assets	64.67		41.57	
Allowance for loan losses to nonaccrual loans	93.68		55.92	
General reserve to non-impaired loans	1.31		1.18	
Nonaccrual loans to loans	1.55		2.51	
Nonperforming assets to loans and OREO	2.21		3.35	
Net (recoveries) charge-offs to average loans	(0.18	)	0.19	

The Company performs troubled debt restructures (TDR) and other various loan workouts whereby an existing loan may be restructured into multiple new loans. At June 30, 2015, the Company had 18 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. Four of these loans were restructured using multiple new loans. The aggregated outstanding principal of TDR loans at June 30, 2015 was $6.6 million, of which $2.0 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 note 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 covered loans, at June 30, 2015 and December 31, 2014 is below (dollars in thousands):

	June 30, 2015	December 31, 2014
Mortgage loans on real estate:		
Residential 1-4 family	$ 3,894	$ 3,342
Commercial	1,737	607
Construction and land development	4,752	4,920
Second mortgages	61	61
Multifamily	—	—
Agriculture	—	—
Total real estate loans	10,444	8,930
Commercial loans	2	7,521
Consumer installment loans	84	120
All other loans	—	—
Total loans	$ 10,530	$ 16,571

At June 30, 2015, the Company had eight 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, 2015 was $4.8 million. These loans have either been charged-down or sufficiently reserved against to equal the current expected realizable value.

The Company charged off $455,000 related to one of these relationships during the first six months of 2015. The total amount of the allowance for loan losses attributed to all eight relationships was $548,000, or 11.5% of the total credit exposure outstanding. The Company establishes its reserves as described above in *Allowance for Loan Losses on Non-covered 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 12 months. The Company orders an automated valuation for balances between $100,000 and $250,000 and uses a ratio analysis for balances less than $100,000. The Company maintains detailed analysis and other information for its allowance methodology, both for internal purposes and for review by its regulators.

Asset Quality – covered assets and 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 covered 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 14.9% at June 30, 2015 compared with 14.7% at December 31, 2014. The tier 1 risk-based capital ratio was 13.7% at June 30, 2015 and 13.5% at December 31, 2014. The Company’s tier 1 leverage ratio was 9.9% at June 30, 2015 and 9.4% at December 31, 2014. All capital ratios exceed regulatory minimums to be considered well capitalized. As discussed above, Basel III introduced the common equity tier 1 capital ratio, which was 13.2% at June 30, 2015.

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.

On its March 31, 2015 regulatory Call Report, the Bank made the one-time AOCI opt-out election, which allows banks under $250 billion in assets that make the one-time opt-out election to remove the impact of certain unrealized capital gains and losses from the calculation of regulatory capital. There is no opportunity to change methodology in future periods.

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, 2015 and December 31, 2014 was as follows (dollars in thousands):

	June 30, 2015	December 31, 2014
Cash and due from banks	$ 6,480	$ 8,329
Interest bearing bank deposits	12,389	14,024
Available for sale securities, at fair value, unpledged	244,044	199,067
Total liquid assets	$ 262,913	$ 221,420
Deposits and other liabilities	$ 1,049,952	$ 1,048,084
Ratio of liquid assets to deposits and other liabilities	25.04 %	21.13 %

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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, 2015 and December 31, 2014, is as follows (dollars in thousands):

	June 30, 2015	December 31, 2014
Commitments with off-balance sheet risk:		
Commitments to extend credit	$ 85,580	$ 87,017
Standby letters of credit	7,181	7,358
Total commitments with off-balance sheet risks	$ 92,761	$ 94,375

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. For the avoidance of doubt, 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.

At June 30, 2015, the fair value of the Company's cash flow hedge was an unrealized loss of $128,000, 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, 2015 (dollars in thousands):

	Change in net interest income			
	%		$	
Change in Yield curve				
+400 bp	(1.7	)%	(639	)
+300 bp	(1.8	)%	(666	)
+200 bp	(1.3	)%	(474	)
+100 bp	(1.0	)%	(374	)
most likely	0	%	—	
-100 bp	1.8	%	665	
-200 bp	(0.2	)%	(83	)
-300 bp	(0.5	)%	(198	)
-400 bp	(0.5	)%	(201	)

At June 30, 2015, 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 decrease by 1.7%. 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 0.5%. 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, 2014.

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, 2015 formatted in Extensible Business Reporting Language (XBRL): (i) the Consolidated Balance Sheets, (ii) the Unaudited Consolidated Statements of Income, (iii) the Unaudited Consolidated Statements of Comprehensive (Loss) 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 7, 2015

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

Date: August 7, 2015