

OLD POINT FINANCIAL CORP
Form 10-Q
November 08, 2018
UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q
(Mark One)
QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF
1934
For the quarterly period ended September 30, 2018

or

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

For the transition period from _____ to _____

Commission File Number: 000-12896

OLD POINT FINANCIAL CORPORATION
(Exact name of registrant as specified in its charter)

VIRGINIA 54-1265373
(State or other jurisdiction of incorporation or organization) (I.R.S. Employer Identification No.)

1 West Mellen Street, Hampton, Virginia 23663
(Address of principal executive offices) (Zip Code)

(757) 728-1200
(Registrant's telephone number, including area code)

Not Applicable
(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 No

Indicate by check mark whether the registrant has submitted every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes No

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

Large accelerated filer Accelerated filer

Non-accelerated filer Smaller reporting company

Emerging growth company

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

5,183,416 shares of common stock (\$5.00 par value) outstanding as of October 24, 2018

OLD POINT FINANCIAL CORPORATION

FORM 10-Q

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GLOSSARY OF DEFINED TERMS

ALLL	Allowance for Loan and Lease Losses
ASC	Accounting Standards Codification
ASU	Accounting Standards Update
Bank	The Old Point National Bank of Phoebus
CET1	Common Equity Tier 1
Citizens Company	Citizens National Bank Old Point Financial Corporation
CRA	Community Reinvestment Act
ESPP	Employee Stock Purchase Plan
EVE	Economic Value of Equity
FASB	Financial Accounting Standards Board
FHLB	Federal Home Loan Bank
FOMC	Federal Open Market Committee
Federal Reserve	Board of Governors of the Federal Reserve System
FRB	Federal Reserve Bank
GAAP	Generally Accepted Accounting Principles
Incentive Stock Plan	Old Point Financial Corporation 2016 Incentive Stock Plan
IRS	Internal Revenue Service
OAEM	Other Assets Especially Mentioned
OCC	Office of the Comptroller of the Currency
OPM	Old Point Mortgage
OREO	Other Real Estate Owned
SEC	Securities and Exchange Commission
TDR	Troubled Debt Restructuring
Trust	Old Point Trust & Financial Services N.A.
VIE	Variable Interest Entities

PART I – FINANCIAL INFORMATION

Item 1. Financial Statements.

Old Point Financial Corporation and Subsidiaries
Consolidated Balance Sheets

	September 30, 2018	December 31, 2017
	(in thousands except per share data) (unaudited) *	
Assets		
Cash and due from banks	\$ 15,539	\$ 13,420
Interest-bearing due from banks	12,519	908
Federal funds sold	561	84
Cash and cash equivalents	28,619	14,412
Securities available-for-sale, at fair value	142,288	157,121
Restricted securities, at cost	3,869	3,846
Loans held for sale	1,033	779
Loans, net	769,204	729,092
Premises and equipment, net	37,278	37,197
Bank-owned life insurance	26,567	25,981
Goodwill	1,611	621
Other real estate owned, net	133	-
Core deposit intangible, net	418	-
Other assets	14,420	12,777
Total assets	\$ 1,025,440	\$ 981,826
Liabilities & Stockholders' Equity		
Deposits:		
Noninterest-bearing deposits	\$ 240,528	\$ 225,716
Savings deposits	367,085	345,053
Time deposits	233,698	212,825
Total deposits	841,311	783,594
Federal funds purchased	-	10,000
Overnight repurchase agreements	18,116	20,693
Federal Home Loan Bank advances	60,000	67,500
Other borrowings	2,850	-
Accrued expenses and other liabilities	3,588	3,651
Total liabilities	925,865	885,438
Commitments and contingencies		
Stockholders' equity:		
	25,849	25,087

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Common stock, \$5 par value, 10,000,000 shares authorized; 5,183,416 and 5,019,703 shares outstanding (includes 13,689 and 2,245 shares of nonvested restricted stock, respectively)

Additional paid-in capital	20,624	17,270
Retained earnings	56,794	54,738
Accumulated other comprehensive loss, net	(3,692)	(707)
Total stockholders' equity	99,575	96,388
Total liabilities and stockholders' equity	\$1,025,440	\$981,826

See Notes to Consolidated Financial Statements.

* Derived from audited Consolidated Financial Statements

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Old Point Financial Corporation and Subsidiaries
Consolidated Statements of Income

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
	(unaudited, in thousands except per share data)			
Interest and Dividend Income:				
Loans, including fees	\$8,865	\$7,642	\$25,448	\$21,532
Due from banks	68	4	94	12
Federal funds sold	5	1	15	6
Securities:				
Taxable	510	487	1,503	1,474
Tax-exempt	291	385	937	1,232
Dividends and interest on all other securities	75	49	210	98
Total interest and dividend income	9,814	8,568	28,207	24,354
Interest Expense:				
Savings deposits	164	103	409	240
Time deposits	774	560	2,088	1,599
Federal funds purchased, securities sold under agreements to repurchase and other borrowings	41	13	93	26
Federal Home Loan Bank advances	320	161	931	233
Total interest expense	1,299	837	3,521	2,098
Net interest income	8,515	7,731	24,686	22,256
Provision for loan losses	749	1,275	1,849	2,925
Net interest income, after provision for loan losses	7,766	6,456	22,837	19,331
Noninterest Income:				
Fiduciary and asset management fees	904	903	2,803	2,820
Service charges on deposit accounts	1,095	1,001	3,043	2,844
Other service charges, commissions and fees	873	843	2,668	2,562
Bank-owned life insurance	202	198	584	595
Mortgage banking	240	172	617	462
Gain on sale of securities, net	-	2	120	89
Gain on acquisition of Old Point Mortgage	-	-	-	550
Other operating income	59	35	104	114
Total noninterest income	3,373	3,154	9,939	10,036
Noninterest Expense:				
Salaries and employee benefits	5,608	5,104	17,020	15,650
Occupancy and equipment	1,557	1,444	4,521	4,347
Data processing	317	266	993	749
FDIC insurance	160	128	537	322
Customer development	143	153	460	451
Professional services	482	508	1,507	1,401
Employee professional development	195	196	595	651
Other taxes	134	141	446	422
ATM and other losses	103	103	357	435
Loss (gain) on other real estate owned	-	-	86	(18)

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Merger expenses	48	-	644	-
Other operating expenses	680	866	1,895	2,103
Total noninterest expense	9,427	8,909	29,061	26,513
Income before income taxes	1,712	701	3,715	2,854
Income tax expense (benefit)	115	(56)	184	(6)
Net income	\$ 1,597	\$ 757	\$ 3,531	\$ 2,860

Basic earnings per share:

Weighted average shares outstanding	5,182,181	4,993,805	5,127,090	4,985,135
Net income per share of common stock	\$0.31	\$0.15	\$0.69	\$0.57

Diluted earnings per share:

Weighted average shares outstanding	5,182,181	5,003,785	5,127,113	4,997,231
Net income per share of common stock	\$0.31	\$0.15	\$0.69	\$0.57

See Notes to Consolidated Financial Statements.

Old Point Financial Corporation and Subsidiaries
 Consolidated Statements of Comprehensive Income

	Three Months Ended September 30, 2018		Nine Months Ended September 30, 2017	
	2018	2017	2018	2017
	(unaudited, in thousands)			
Net income	\$1,597	\$757	\$3,531	\$2,860
Other comprehensive income (loss), net of tax				
Net unrealized gain (loss) on available-for-sale securities	(803)	59	(2,674)	1,580
Reclassification for gain included in net income	-	(2)	(95)	(59)
Other comprehensive income (loss), net of tax	(803)	57	(2,769)	1,521
Comprehensive income	\$794	\$814	\$762	\$4,381

See Notes to Consolidated Financial Statements.

Old Point Financial Corporation and Subsidiaries
Consolidated Statements of Changes in Stockholders' Equity

	Shares of Common Stock	Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Total
	(unaudited, in thousands except share and per share data)					
NINE MONTHS ENDED SEPTEMBER 30, 2018						
Balance at beginning of period	5,017,458	\$ 25,087	\$ 17,270	\$ 54,738	\$ (707)	\$ 96,388
Net income	-	-	-	3,531	-	3,531
Other comprehensive loss, net of tax	-	-	-	-	(2,769)	(2,769)
Issuance of common stock related to acquisition	149,625	748	3,199	-	-	3,947
Reclassification of the stranded income tax effects of the Tax Cuts and Jobs Act from AOCI	-	-	-	139	(139)	-
Reclassification of net unrealized gains on equity securities from AOCI per ASU 2016-01	-	-	-	77	(77)	-
Employee Stock Purchase Plan share issuance	2,644	14	52	-	-	66
Stock-based compensation expense	-	-	103	-	-	103
Cash dividends (\$0.33 per share)	-	-	-	(1,691)	-	(1,691)
Balance at end of period	5,169,727	\$ 25,849	\$ 20,624	\$ 56,794	\$ (3,692)	\$ 99,575
NINE MONTHS ENDED SEPTEMBER 30, 2017						
Balance at beginning of period	4,961,258	\$ 24,806	\$ 16,427	\$ 56,965	\$ (4,208)	\$ 93,990
Net income	-	-	-	2,860	-	2,860
Other comprehensive income, net of tax	-	-	-	-	1,521	1,521
Exercise of stock options	48,287	241	727	-	-	968
Employee Stock Purchase Plan share issuance	2,523	13	58	-	-	71
Repurchase and retirement of common stock	(4,683)	(23)	(109)	-	-	(132)
Stock-based compensation expense	-	-	9	-	-	9
Cash dividends (\$0.33 per share)	-	-	-	(1,646)	-	(1,646)
Balance at end of period	5,007,385	\$ 25,037	\$ 17,112	\$ 58,179	\$ (2,687)	\$ 97,641

See Notes to Consolidated Financial Statements.

Old Point Financial Corporation and Subsidiaries
Consolidated Statements of Cash Flows

	Nine Months Ended September 30, 2018 2017 (unaudited, dollars in thousands)	
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	\$3,531	\$2,860
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	1,870	2,081
Accretion related to acquisition, net	(199)	-
Provision for loan losses	1,849	2,925
Gain on sale of securities, net	(120)	(89)
Net amortization of securities	1,331	1,727
Increase in loans held for sale, net	(254)	(981)
Net loss on disposal of premises and equipment	9	4
Net (gain) loss on write-down/sale of other real estate owned	86	(18)
Income from bank owned life insurance	(584)	(595)
Stock compensation expense	103	9
Deferred tax benefit	-	(171)
(Increase) decrease in other assets	182	(552)
Decrease in accrued expenses and other liabilities	(387)	(244)
Net cash provided by operating activities	7,417	6,956
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchases of available-for-sale securities	(16,582)	(25,220)
Proceeds from redemption (cash used in purchases) of restricted securities, net	254	(1,920)
Proceeds from maturities and calls of available-for-sale securities	8,750	46,625
Proceeds from sales of available-for-sale securities	12,139	7,030
Paydowns on available-for-sale securities	7,672	7,484
Proceeds from sale of loans held for investment	8,930	-
Net increase in loans held for investment	(8,228)	(99,333)
Proceeds from sales of other real estate owned	211	1,084
Purchases of premises and equipment	(439)	(510)
Cash paid in acquisition	(3,164)	-
Cash acquired in acquisition	2,304	-
Net cash provided by (used in) investing activities	11,847	(64,760)
CASH FLOWS FROM FINANCING ACTIVITIES		
Increase (decrease) in noninterest-bearing deposits	8,499	(5,199)
Increase in savings deposits	14,657	202
Increase (decrease) in time deposits	(9,361)	2,940
Increase (decrease) in federal funds purchased, repurchase agreements and other borrowings, net	(9,727)	5,181
Increase in Federal Home Loan Bank advances	88,000	120,000
Repayment of Federal Home Loan Bank advances	(95,500)	(75,000)
Proceeds from exercise of stock options and ESPP issuance	66	1,039
Repurchase and retirement of common stock	-	(132)

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Cash dividends paid on common stock	(1,691)	(1,646)
Net cash provided by (used in) financing activities	(5,057)	47,385
Net increase (decrease) in cash and cash equivalents	14,207	(10,419)
Cash and cash equivalents at beginning of period	14,412	25,854
Cash and cash equivalents at end of period	\$28,619	\$15,435

SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION

Cash payments for:

Interest	\$3,332	\$2,029
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SUPPLEMENTAL SCHEDULE OF NONCASH TRANSACTIONS

Unrealized gain (loss) on securities available-for-sale	\$(3,603)	\$2,305
Loans transferred to other real estate owned	\$203	\$-

TRANSACTIONS RELATED TO ACQUISITIONS

Assets acquired	\$50,446	\$-
Liabilities assumed	\$44,324	\$-
Common stock issued in acquisition	\$3,947	\$-

See Notes to Consolidated Financial Statements.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

Note 1. Accounting Policies

The accompanying unaudited consolidated financial statements of Old Point Financial Corporation (NASDAQ: OPOF) (the Company) and its subsidiaries have been prepared in accordance with U.S. GAAP for interim financial information. All significant intercompany balances and transactions have been eliminated. In the opinion of management, the accompanying unaudited consolidated financial statements contain all adjustments and reclassifications of a normal and recurring nature considered necessary to present fairly the financial position at September 30, 2018 and December 31, 2017, the statements of income and comprehensive income for the three and nine months ended September 30, 2018 and 2017, and the statements of changes in stockholders' equity and cash flows for the nine months ended September 30, 2018 and 2017. The results of operations for the interim periods are not necessarily indicative of the results that may be expected for the full year.

These consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company's 2017 Annual Report on Form 10-K. Certain previously reported amounts have been reclassified to conform to current period presentation, none of which were material in nature.

PRINCIPLES OF CONSOLIDATION

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries, The Old Point National Bank of Phoebus (the Bank) and Old Point Trust & Financial Services N.A. (Trust). All significant intercompany balances and transactions have been eliminated in consolidation.

BUSINESS COMBINATIONS

On April 1, 2018, the Company acquired Citizens National Bank (Citizens) based in Windsor, Virginia. Refer to Note 2 for further discussion.

NATURE OF OPERATIONS

Old Point Financial Corporation is a holding company that conducts substantially all of its operations through two subsidiaries, the Bank and Trust. The Bank serves individual and commercial customers, the majority of which are in Hampton Roads, Virginia. As of September 30, 2018, the Bank had 19 branch offices. The Bank offers a full range of deposit and loan products to its retail and commercial customers, including mortgage loan products offered through Old Point Mortgage. A full array of insurance products is also offered through Old Point Insurance, LLC in partnership with Morgan Marrow Company. Trust offers a full range of services for individuals and businesses. Products and services include retirement planning, estate planning, financial planning, estate and trust administration, retirement plan administration, tax services and investment management services.

RECENT ACCOUNTING PRONOUNCEMENTS

In February 2016, the FASB issued ASU No. 2016-02, "Leases (Topic 842)." Among other things, in the amendments in ASU 2016-02, lessees will be required to recognize the following for all leases (with the exception of short-term leases) at the commencement date: (1) A lease liability, which is a lessee's obligation to make lease payments arising from a lease, measured on a discounted basis; and (2) A right-of-use asset, which is an asset that represents the lessee's right to use, or control the use of, a specified asset for the lease term. Under the new guidance, lessor accounting is largely unchanged. Certain targeted improvements were made to align, where necessary, lessor accounting with the

lessee accounting model and Topic 606, Revenue from Contracts with Customers. The amendments in this ASU are effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. Early application is permitted upon issuance. Lessees (for capital and operating leases) and lessors (for sales-type, direct financing, and operating leases) must apply a modified retrospective transition approach for leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements. The modified retrospective approach would not require any transition accounting for leases that expired before the earliest comparative period presented. Lessees and lessors may not apply a full retrospective transition approach. The FASB made subsequent amendments to Topic 842 in July 2018 through ASU 2018-10 ("Codification Improvements to Topic 842, Leases") and ASU 2018-11 ("Leases (Topic 842): Targeted Improvements"). Among these amendments is the provision in ASU 2018-11 that provides entities with an additional (and optional) transition method to adopt the new leases standard. Under this new transition method, an entity initially applies the new leases standard at the adoption date and recognizes a cumulative-effect adjustment to the opening balance of retained earnings in the period of adoption. Consequently, an entity's reporting for the comparative periods presented in the financial statements in which it adopts the new leases standard will continue to be in accordance with current GAAP (Topic 840, Leases). As the Company owns the majority of its buildings, management does not anticipate that the ASU will have a material impact; however, the Company will continue to assess any potential impact on its consolidated financial statements.

In June 2016, the FASB issued ASU No. 2016-13, "Financial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments." The amendments in this ASU, among other things, require the measurement of all expected credit losses for financial assets held at the reporting date based on historical experience, current conditions, and reasonable and supportable forecasts. Financial institutions and other organizations will now use forward-looking information to better inform their credit loss estimates. Many of the loss estimation techniques applied today will still be permitted, although the inputs to those techniques will change to reflect the full amount of expected credit losses. In addition, the ASU amends the accounting for credit losses on available-for-sale debt securities and purchased financial assets with credit deterioration. The amendments in this ASU are effective for Securities and Exchange Commission (SEC) filers for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2019. The Company is currently assessing the impact that ASU 2016-13 will have on its consolidated financial statements and has formed a committee to oversee the adoption of the new standard. The ALLL model currently in use by the Company already provides it with the ability to archive prior period information and contains loan balance and charge-off information beginning with September 30, 2011. The committee has reviewed the data included in each monthly archive file and has added fields to enhance its data analysis capabilities under the new standard.

In January 2017, the FASB issued ASU No. 2017-04, "Intangibles—Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment." The amendments in this ASU simplify how an entity is required to test goodwill for impairment by eliminating Step 2 from the goodwill impairment test. Step 2 measures a goodwill impairment loss by comparing the implied fair value of a reporting unit's goodwill with the carrying amount of that goodwill. Instead, under the amendments in this ASU, an entity should perform its annual, or interim, goodwill impairment test by comparing the fair value of a reporting unit with its carrying amount. An entity still has the option to perform the qualitative assessment for a reporting unit to determine if the quantitative impairment test is necessary. Public business entities that are SEC filers should adopt the amendments in this ASU for annual or interim goodwill impairment tests in fiscal years beginning after December 15, 2019. Early adoption is permitted for interim or annual goodwill impairment tests performed on testing dates after January 1, 2017. The Company does not expect the adoption of ASU 2017-04 to have a material impact on its consolidated financial statements.

In March 2017, the FASB issued ASU No. 2017-08, "Receivables—Nonrefundable Fees and Other Costs (Subtopic 310-20), Premium Amortization on Purchased Callable Debt Securities." The amendments in this ASU shorten the amortization period for certain callable debt securities purchased at a premium. Upon adoption of the standard, premiums on these qualifying callable debt securities will be amortized to the earliest call date. Discounts on purchased debt securities will continue to be accreted to maturity. The amendments are effective for fiscal years beginning after December 15, 2018, and interim periods within those fiscal years. Early adoption is permitted, including adoption in an interim period. Upon transition, entities should apply the guidance on a modified retrospective basis, with a cumulative-effect adjustment to retained earnings as of the beginning of the period of adoption and provide the disclosures required for a change in accounting principle. The Company does not expect the adoption of ASU 2017-08 to have a material impact on its consolidated financial statements.

In June 2018, the FASB issued ASU 2018-07, "Compensation- Stock Compensation (Topic 718): Improvements to Nonemployee Share-Based Payment Accounting." The amendments expand the scope of Topic 718 to include share-based payments issued to non-employees for goods or services, which were previously excluded. The amendments will align the accounting for share-based payments to non-employees and employees more similarly. The amendments are effective for fiscal years beginning after December 15, 2018, and interim periods within those fiscal years. Early adoption is permitted. The Company does not expect the adoption of ASU 2018-07 to have a material impact on its consolidated financial statements.

In August 2018, the FASB issued ASU 2018-13, "Fair Value Measurement (Topic 820): Disclosure Framework—Changes to the Disclosure Requirements for Fair Value Measurement." The amendments modify the disclosure requirements in Topic 820 to add disclosures regarding changes in unrealized gains and losses, the range and weighted average of significant unobservable inputs used to develop Level 3 fair value measurements and the narrative description of measurement uncertainty. Certain disclosure requirements in Topic 820 are also removed or modified. The amendments are effective for fiscal years beginning after December 15, 2019, and interim periods within those fiscal years. Certain of the amendments are to be applied prospectively while others are to be applied retrospectively. Early adoption is permitted. The Company does not expect the adoption of ASU 2018-13 to have a material impact on its consolidated financial statements.

ACCOUNTING STANDARDS ADOPTED IN 2018

In January 2016, the FASB issued ASU No. 2016-01, "Financial Instruments - Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities." This ASU requires an entity to, among other things: (i) measure equity investments at fair value through net income, with certain exceptions; (ii) present in OCI the changes in instrument-specific credit risk for financial liabilities measured using the fair value option; (iii) present financial assets and financial liabilities by measurement category and form of financial asset; (iv) calculate the fair value of financial instruments for disclosure purposes based on an exit price and; (v) assess a valuation allowance on deferred tax assets related to unrealized losses of AFS debt securities in combination with other deferred tax assets. The ASU provides an election to subsequently measure certain nonmarketable equity investments at cost less any

impairment and adjusted for certain observable price changes. The ASU also requires a qualitative impairment assessment of such equity investments and amends certain fair value disclosure requirements. This ASU is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2017. The Company adopted ASU No. 2016-01 on January 1, 2018, and during the first quarter of 2018, measured its equity investments at fair value through net income and reclassified \$77 thousand of AOCI to retained earnings, with no effect on total stockholders' equity. During the second quarter of 2018, the Company sold the equity investments, recognizing an additional gain on sale of \$24 thousand, net of tax. The Company also measured the fair value of its loan portfolio and time deposits at September 30, 2018 using an exit price notion (see Note 10. Fair Value Measurements).

In February 2018, the FASB issued ASU 2018-02, "Income Statement – Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income." The amendments provide financial statement preparers with an option to reclassify stranded tax effects within accumulated other comprehensive income (AOCI) to retained earnings in each period in which the effect of the change in the U.S. federal corporate income tax rate in the Tax Cuts and Jobs Act (or portion thereof) is recorded. The amendments are effective for all organizations for fiscal years beginning after December 15, 2018, and interim periods within those fiscal years. Early adoption is permitted. Organizations should apply the proposed amendments either in the period of adoption or retrospectively to each period (or periods) in which the effect of the change in the U.S. federal corporate income tax rate in the Tax Cuts and Jobs Act is recognized. The Company has elected to reclassify the stranded income tax effects from the Tax Cuts and Jobs Act in the consolidated financial statements for the period ending March 31, 2018. The reclassification decreased AOCI and increased retained earnings by \$139 thousand, with no effect on total stockholders' equity.

On January 1, 2018 the Company adopted ASU 2014-09 "Revenue from Contracts with Customers" and all subsequent amendments to the ASU (collectively, "ASC 606"). The majority of the Company's revenues are associated with financial instruments, including loans and securities, to which ASC 606 does not apply. ASC 606 is applicable to certain noninterest revenues including services charges on deposit accounts, interchange fees, merchant services income, trust and asset management income, and the sale of other real estate owned. However, the recognition of these revenue streams, with the exception of interchange income, did not change upon adoption of ASC 606. Substantially all of the Company's revenue is generated from contracts with customers. Noninterest revenue streams in-scope of ASC 606 are discussed below.

Fiduciary and Asset Management Fees

Fiduciary and asset management income is primarily comprised of fees earned from the management and administration of trusts and other customer assets. The Company's performance obligation is generally satisfied over time and the resulting fees are recognized monthly, based upon the applicable fee schedule or contract terms. Payment is generally received immediately or in the following month. The Company does not earn performance-based incentives. Additional services such as tax return preparation services are transactional-based, and the performance obligation is generally satisfied, and related revenue recognized, as incurred. Payment is received shortly after services are rendered.

Service Charges on Deposit Accounts

Service charges on deposit accounts consist of account analysis fees (i.e., net fees earned on analyzed business and public checking accounts), monthly service fees, and other deposit account related fees. The Company's performance obligation for account analysis fees and monthly service fees is generally satisfied, and the related revenue recognized, over the period in which the service is provided. Other deposit account related fees are largely transactional based, and therefore, the Company's performance obligation is satisfied, and related revenue recognized, at a point in time. Payment for service charges on deposit accounts is primarily received immediately or in the following month through a direct charge to customers' accounts.

Other Service Charges, Commissions and Fees

Other service charges, commissions and fees are primarily comprised of debit card income, ATM fees, merchant services income, investment services income, and other service charges. Debit card income is primarily comprised of interchange fees earned whenever the Company's debit and credit cards are processed through card payment networks. During the third quarter of the 2018, the Company entered into a renewal vendor contract and determined, based on an agent capacity, to retrospectively reclassify debit card expenses against debit card revenue creating a net presentation. For the three months and nine months ended September 30, 2018 and 2017, the amounts reclassified were \$274 thousand, \$207 thousand, \$711 thousand, and \$579 thousand, respectively. These reclassifications had no impact on net income for the reporting periods. ATM fees are primarily generated when a Company cardholder uses a non-Company ATM or a non-Company cardholder uses a Company ATM. Merchant services income mainly represents fees charged to merchants to process their debit and credit card transactions, in addition to account management fees. Investment services income relates to commissions earned on brokered trades of investment securities. Other service charges include revenue from processing wire transfers, safe deposit box rentals, cashier's checks, and other services. The Company's performance obligation for other service charges, commission and fees are largely satisfied, and related revenue recognized, when the services are rendered or upon completion. Payment is typically received immediately or in the following month.

Other Operating Income

Other operating income mainly consists of check sales to customers and fees charged for the early redemption of time deposits. Other operating income is largely transactional based, and therefore, the Company's performance obligation

is satisfied, and related revenue recognized, at a point in time. Payment is generally received immediately.

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Note 2. Acquisitions

On April 1, 2018, the Company acquired Citizens. Under the terms of the merger agreement, Citizens stockholders received 0.1041 shares of the Company's common stock and \$2.19 in cash for each share of Citizens common stock, resulting in the Company issuing 149,625 shares of the Company's common stock at a fair value of \$3.9 million, for a total purchase price of \$7.1 million.

The transaction was accounted for using the acquisition method of accounting and, accordingly, assets acquired, liabilities assumed, and consideration exchanged were recorded at estimated fair values on the acquisition date. Fair values are preliminary and subject to refinement for up to one year after the closing date of the acquisition, in accordance with ASC 350, Intangibles-Goodwill and Other. The following table provides a preliminary assessment of the consideration transferred, assets acquired, and liabilities assumed as of the date of the acquisition (dollars in thousands):

	As Recorded by Citizens	Fair Value Adjustments	As Recorded by the Company
Consideration paid:			
Cash			\$ 3,164
Company common stock			3,947
Total purchase price			7,111
Identifiable assets acquired:			
Cash and cash equivalents	\$ 2,304	\$ -	\$ 2,304
Securities available for sale	1,959	-	1,959
Restricted securities, at cost	278	-	278
Loans, net	42,824	(34)	42,790
Premises and equipment	1,070	450	1,520
Other real estate owned	237	(11)	226
Core deposit intangibles	-	440	440
Other assets	1,055	(126)	929
Total assets	\$ 49,727	\$ 719	\$ 50,446
Identifiable liabilities assumed:			
Deposits	\$ 43,754	\$ 246	\$ 44,000
Other liabilities	324	-	324
Total liabilities	\$ 44,078	\$ 246	\$ 44,324
Net assets acquired			\$ 6,122
Preliminary goodwill			\$ 989

Goodwill and intangible assets acquired in a purchase business combination and determined to have an indefinite useful life are not amortized, but tested for impairment at least annually or more frequently if events and circumstances exist that indicate that a goodwill impairment test should be performed. Purchased intangible assets subject to amortization, such as the core deposit intangible asset, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized in the amount by which the carrying amount of the asset exceeds the fair value of the asset.

The acquired loans were recorded at fair value at the acquisition date without carryover of Citizens' allowance for loan losses. The fair value of the loans was determined using market participant assumptions in estimating the amount and timing of both principal and interest cash flows expected to be collected on the loans and then applying a market-based discount rate to those cash flows. In this regard, the acquired loans were segregated into pools based on call code with other key inputs identified such as payment structure, rate type, remaining maturity, and credit risk characteristics including risk rating groups (pass rated loans and adversely classified loans), and past due status.

The acquired loans were divided into loans with evidence of credit quality deterioration which are accounted for under ASC 310-30, Receivables - Loans and Debt Securities Acquired with Deteriorated Credit Quality, (acquired impaired) and loans that do not meet these criteria, which are accounted for under ASC 310-20, Receivables - Nonrefundable Fees and Other Costs, (acquired performing). The fair values of the acquired performing loans were \$42.1 million and the fair value of the acquired impaired loans were \$710 thousand.

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The following table presents the acquired impaired loans receivable at the acquisition date (dollars in thousands):

Contractually required principal and interest payments	\$1,031
Nonaccretable difference	(211)
Cash flows expected to be collected	820
Accretable yield	(110)
Fair value of loans acquired impaired loans	\$710

The amortization and accretion of premiums and discounts associated with the Company's acquisition accounting adjustments related to the Citizens acquisition had the following impact on the Consolidated Statements of Income during the three and nine months ended September 30, 2018 (dollars in thousands). The acquisition occurred on April 1, 2018, therefore the comparative 2017 periods had no impact.

	Three Months Ended September 30, 2018	Nine Months Ended September 30, 2018
Acquired performing loans	\$ 52	\$ 144
Acquired impaired loans	(2)	(1)
Certificate of deposit valuation	39	78
Amortization of core deposit intangible	(11)	(22)
Net impact to income before taxes	\$ 78	\$ 199

Note 3. Securities

Amortized costs and fair values of securities available-for-sale as of the dates indicated are as follows:

	Gross Amortized Cost (in thousands)	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
September 30, 2018				
U.S. Treasury securities	\$9,338	\$ -	\$ (74)	\$9,264
Obligations of U.S. Government agencies	11,278	-	(240)	11,038
Obligations of state and political subdivisions	50,101	50	(1,121)	49,030
Mortgage-backed securities	71,090	-	(3,280)	67,810
Money market investments	1,205	-	-	1,205
Corporate bonds and other securities	3,950	10	(19)	3,941
Total	\$146,962	\$ 60	\$ (4,734)	\$142,288
December 31, 2017				
Obligations of U.S. Government agencies	\$9,530	\$ 27	\$ (122)	\$9,435
Obligations of state and political subdivisions	64,413	489	(137)	64,765
Mortgage-backed securities	75,906	-	(1,610)	74,296
Money market investments	1,194	-	-	1,194
Corporate bonds and other securities	7,049	195	(10)	7,234
Other marketable equity securities	100	97	-	197
Total	\$158,192	\$ 808	\$ (1,879)	\$157,121

The Company has a process in place to identify debt securities that could potentially have a credit or interest-rate related impairment that is other-than-temporary. This process involves monitoring late payments, pricing levels, downgrades by rating agencies, key financial ratios, financial statements, revenue forecasts, and cash flow projections as indicators of credit issues. On a quarterly basis, management reviews all securities to determine whether an other-than-temporary decline in value exists and whether losses should be recognized. Management considers relevant facts and circumstances in evaluating whether a credit or interest-rate related impairment of a security is other-than-temporary. Relevant facts and circumstances considered include: (a) the extent and length of time the fair value has been below cost; (b) the reasons for the decline in value; (c) the financial position and access to capital of the issuer, including the current and future impact of any specific events; and (d) for fixed maturity securities, the Company's intent to sell a security or whether it is more-likely-than-not the Company will be required to sell the security before the recovery of its amortized cost which, in some cases, may extend to maturity, and for equity securities, the Company's ability and intent to hold the security for a period of time that allows for the recovery in value.

The Company has not recorded impairment charges through income on securities for the three or nine months ended September 30, 2018 or the year ended December 31, 2017.

The following table summarizes net realized gains and losses on the sale of investment securities during the periods indicated (dollars in thousands):

	Three Months Ended September 30, 2018		Nine Months Ended September 30, 2017	
Securities Available-for-sale				
Realized gains on sales of securities	\$ -	\$ 2	\$ 131	\$ 89
Realized losses on sales of securities	-	-	(11)	-
Net realized gain	\$ -	\$ 2	\$ 120	\$ 89

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The following table shows the gross unrealized losses and fair value of the Company's investments with unrealized losses that are not deemed to be other-than-temporarily impaired as of September 30, 2018 and December 31, 2017, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position as of the dates indicated:

September 30, 2018

	Less Than Twelve Months		More Than Twelve Months		Total	
	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value
(dollars in thousands)						
Securities Available-for-Sale						
U.S. Treasury securities	\$74	\$9,264	\$-	\$-	\$74	\$9,264
Obligations of U.S. Government agencies	59	7,302	181	3,736	240	11,038
Obligations of state and political subdivisions	441	28,333	680	13,945	1,121	42,278
Mortgage-backed securities	35	2,362	3,245	65,448	3,280	67,810
Corporate bonds	6	2,644	13	287	19	2,931
Total securities available-for-sale	\$615	\$49,905	\$4,119	\$83,416	\$4,734	\$133,321

December 31, 2017

	Less Than Twelve Months		More Than Twelve Months		Total	
	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value
(dollars in thousands)						
Securities Available-for-Sale						
Obligations of U.S. Government agencies	\$11	\$3,189	\$111	\$3,089	\$122	\$6,278
Obligations of state and political subdivisions	32	11,141	105	10,999	137	22,140
Mortgage-backed securities	67	9,742	1,543	64,554	1,610	74,296
Corporate bonds	2	1,098	8	792	10	1,890
Total securities available-for-sale	\$112	\$25,170	\$1,767	\$79,434	\$1,879	\$104,604

The number of investments at an unrealized loss position as of September 30, 2018 and December 31, 2017 were 127 and 77, respectively. Certain investments within the Company's portfolio had unrealized losses for more than twelve months at September 30, 2018 and December 31, 2017, as shown in the tables above. The unrealized losses were caused by increases in market interest rates. Because the Company does not intend to sell the investments and management believes it is unlikely that the Company will be required to sell the investments before recovery of their amortized cost basis, which may be maturity, the Company does not consider the investments to be other-than-temporarily impaired at September 30, 2018 or December 31, 2017.

Restricted Securities

The restricted security category is comprised of stock in the Federal Home Loan Bank of Atlanta (FHLB), the Federal Reserve Bank (FRB), and Community Bankers' Bank (CBB). These stocks are classified as restricted securities because their ownership is restricted to certain types of entities and the securities lack a market. Therefore, FHLB, FRB, and CBB stock are carried at cost and evaluated for impairment. When evaluating these stocks for impairment, their value is determined based on the ultimate recoverability of the par value rather than by recognizing temporary

declines in value. Restricted stock is viewed as a long-term investment and management believes that the Company has the ability and the intent to hold this stock until its value is recovered.

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Note 4. Loans and the Allowance for Loan Losses

The following is a summary of the balances in each class of the Company's portfolio of loans held for investment as of the dates indicated:

	September 30, 2018	December 31, 2017
	(in thousands)	
Mortgage loans on real estate:		
Residential 1-4 family	\$ 110,133	\$ 101,021
Commercial	312,079	289,682
Construction	32,898	27,489
Second mortgages	17,874	17,918
Equity lines of credit	57,069	56,610
Total mortgage loans on real estate	530,053	492,720
Commercial and industrial loans	67,772	60,398
Consumer automobile loans	125,166	119,251
Other consumer loans	45,732	54,974
Other	10,712	11,197
Total loans, net of deferred fees (1)	779,435	738,540
Less: Allowance for loan losses	(10,231)	(9,448)
Loans, net of allowance and deferred fees and costs (1)	\$ 769,204	\$ 729,092

(1) Net deferred loan fees totaled \$849 thousand and \$916 thousand at September 30, 2018 and December 31, 2017, respectively.

Overdrawn deposit accounts are reclassified as loans and included in the Other category in the table above. Overdrawn deposit accounts, excluding internal use accounts, totaled \$605 thousand and \$424 thousand at September 30, 2018 and December 31, 2017, respectively.

Acquired Loans

The Company had no acquired loans as of December 31, 2017. The outstanding principal balance and the carrying amount of total acquired loans included in the consolidated balance sheet as of September 30, 2018 are as follows:

	September 30, 2018 (in thousands)
Outstanding principal balance	\$ 36,369
Carrying amount	35,811

The outstanding principal balance and related carrying amount of acquired impaired loans, for which the Company applies FASB ASC 310-30 to account for interest earned, as of September 30, 2018 are as follows:

September
30, 2018
(in
thousands)

Outstanding principal balance	\$ 679
Carrying amount	448

The following table presents changes in the accretable yield on acquired impaired loans, for which the Company applies FASB ASC 310-30, at September 30, 2018:

	September 30, 2018 (in thousands)
Balance at January 1, 2018	\$ -
Additions from acquisition of Citizens	110
Accretion	(18)
Other changes, net	-
Balance at end of period	\$ 92

CREDIT QUALITY INFORMATION

The Company uses internally-assigned risk grades to estimate the capability of borrowers to repay the contractual obligations of their loan agreements as scheduled or at all. The Company's internal risk grade system is based on experiences with similarly graded loans. Credit risk grades are updated at least quarterly as additional information becomes available, at which time management analyzes the resulting scores to track loan performance.

The Company's internally assigned risk grades are as follows:

Pass: Loans are of acceptable risk.

Other Assets Especially Mentioned (OAEM): Loans have potential weaknesses that deserve management's close attention.

Substandard: Loans reflect significant deficiencies due to several adverse trends of a financial, economic or managerial nature.

Doubtful: Loans have all the weaknesses inherent in a substandard loan with added characteristics that make collection or liquidation in full based on currently existing facts, conditions and values highly questionable or improbable.

Loss: Loans have been identified for charge-off because they are considered uncollectible and of such little value that their continuance as bankable assets is not warranted.

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The following table presents credit quality exposures by internally assigned risk ratings as of the dates indicated:

Credit Quality Information

As of September 30, 2018

(in thousands)

	Pass	OAEM	Substandard	Doubtful	Total
Mortgage loans on real estate:					
Residential 1-4 family	\$108,270	\$-	\$ 1,863	\$ -	\$110,133
Commercial	284,698	8,144	19,237	-	312,079
Construction	32,409	71	418	-	32,898
Second mortgages	17,535	-	339	-	17,874
Equity lines of credit	56,770	-	299	-	57,069
Total mortgage loans on real estate	499,682	8,215	22,156	-	530,053
Commercial and industrial loans	65,170	2,143	459	-	67,772
Consumer automobile loans	124,765	-	401	-	125,166
Other consumer loans	45,597	-	135	-	45,732
Other	10,712	-	-	-	10,712
Total	\$745,926	\$10,358	\$ 23,151	\$ -	\$779,435

Credit Quality Information

As of December 31, 2017

(in thousands)

	Pass	OAEM	Substandard	Doubtful	Total
Mortgage loans on real estate:					
Residential 1-4 family	\$98,656	\$-	\$ 2,365	\$ -	\$101,021
Commercial	264,275	10,526	14,881	-	289,682
Construction	26,694	74	721	-	27,489
Second mortgages	17,211	431	276	-	17,918
Equity lines of credit	56,318	-	292	-	56,610
Total mortgage loans on real estate	463,154	11,031	18,535	-	492,720
Commercial and industrial loans	58,091	1,469	838	-	60,398
Consumer automobile loans	119,211	-	40	-	119,251
Other consumer loans	54,926	-	48	-	54,974
Other	11,197	-	-	-	11,197
Total	\$706,579	\$12,500	\$ 19,461	\$ -	\$738,540

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AGE ANALYSIS OF PAST DUE LOANS BY CLASS

All classes of loans are considered past due if the required principal and interest payments have not been received as of the date such payments were due. Interest and fees continue to accrue on past due loans until the date the loan is placed in nonaccrual status, if applicable. The following table includes an aging analysis of the recorded investment in past due loans as of the dates indicated. Also included in the table below are loans that are 90 days or more past due as to interest and principal and still accruing interest, because they are well-secured and in the process of collection. Loans in nonaccrual status that are also past due are included in the aging categories in the table below.

Age Analysis of Past Due Loans as of September 30, 2018

	30 - 59 Days Past Due (in thousands)	60 - 89 Days Past Due	90 or More Days Past Due	Acquired Impaired	Total Current Loans ⁽¹⁾	Total Loans	Recorded Investment > 90 Days Past Due and Accruing
Mortgage loans on real estate:							
Residential 1-4 family	\$460	\$655	\$860	\$ 347	\$107,811	\$110,133	\$ 429
Commercial	445	710	4,707	101	306,116	312,079	149
Construction	-	-	418	-	32,480	32,898	-
Second mortgages	119	149	189	-	17,417	17,874	96
Equity lines of credit	790	91	1,011	-	55,177	57,069	962
Total mortgage loans on real estate	1,814	1,605	7,185	448	519,001	530,053	1,636
Commercial loans	214	600	559	-	66,399	67,772	419
Consumer automobile loans	1,221	196	52	-	123,697	125,166	51
Other consumer loans	778	886	2,198	-	41,870	45,732	2,198
Other	76	10	10	-	10,616	10,712	10
Total	\$4,103	\$3,297	\$10,004	\$ 448	\$761,583	\$779,435	\$ 4,314

⁽¹⁾ For purposes of this table, Total Current Loans includes loans that are 1 - 29 days past due.

In the table above, the past due totals include student loans and small business loans with principal and interest amounts that are 97 - 100% guaranteed by the federal government. The past due principal portion of these guaranteed loans totaled \$3.9 million at September 30, 2018.

Age Analysis of Past Due Loans as of December 31, 2017

	30 - 59 Days Past Due (in thousands)	60 - 89 Days Past Due	90 or More Days Past Due	Total Current Loans ⁽¹⁾	Total Loans	Recorded Investment > 90 Days Past Due and Accruing
Mortgage loans on real estate:						
Residential 1-4 family	\$229	\$153	\$1,278	\$99,361	\$101,021	\$ 261
Commercial	194	771	1,753	286,964	289,682	-
Construction	-	-	721	26,768	27,489	-
Second mortgages	15	-	163	17,740	17,918	45
Equity lines of credit	75	19	53	56,463	56,610	-

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Total mortgage loans on real estate	513	943	3,968	487,296	492,720	306
Commercial loans	709	-	1,060	58,629	60,398	471
Consumer automobile loans	517	122	41	118,571	119,251	41
Other consumer loans	2,222	544	2,360	49,848	54,974	2,360
Other	84	9	4	11,100	11,197	4
Total	\$4,045	\$1,618	\$7,433	\$725,444	\$738,540	\$ 3,182

⁽¹⁾ For purposes of this table, Total Current Loans includes loans that are 1 - 29 days past due.

In the table above, the other consumer loans category includes student loans with principal and interest amounts that are 97 - 98% guaranteed by the federal government. The past due principal portion of these guaranteed loans totaled \$4.2 million at December 31, 2017.

Although the portions of the student and small business loan portfolios that are 90 days or more past due would normally be considered impaired, the Company does not include these loans in its impairment analysis. Because the federal government has provided guarantees of repayment of these student and small business loans in an amount ranging from 97% to 100% of the total principal and interest of the loans, management does not expect significant increases in delinquencies of these loans to have a material effect on the Company.

NONACCRUAL LOANS

The Company generally places commercial loans (including construction loans and commercial loans secured and not secured by real estate) in nonaccrual status when the full and timely collection of interest or principal becomes uncertain, part of the principal balance has been charged off and no restructuring has occurred or the loan reaches 90 days past due, unless the credit is well-secured and in the process of collection.

Under regulatory rules, consumer loans, which are loans to individuals for household, family and other personal expenditures, and consumer loans secured by real estate (including residential 1 - 4 family mortgages, second mortgages, and equity lines of credit) are not required to be placed in nonaccrual status. Although consumer loans and consumer loans secured by real estate are not required to be placed in nonaccrual status, the Company may elect to place these loans in nonaccrual status, if necessary to avoid a material overstatement of interest income. Generally, consumer loans secured by real estate are placed in nonaccrual status only when payments are 120 days past due.

Generally, consumer loans not secured by real estate are placed in nonaccrual status only when part of the principal has been charged off. If a charge-off has not occurred sooner for other reasons, a consumer loan not secured by real estate will generally be placed in nonaccrual status when payments are 120 days past due. These loans are charged off or written down to the net realizable value of the collateral when deemed uncollectible, when classified as a "loss," when repayment is unreasonably protracted, when bankruptcy has been initiated, or when the loan is 120 days or more past due unless the credit is well-secured and in the process of collection.

When management places a loan in nonaccrual status, the accrued unpaid interest receivable is reversed against interest income and the loan is accounted for by the cash basis or cost recovery method, until it qualifies for return to accrual status or is charged off. Generally, loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured, or when the borrower has resumed paying the full amount of the scheduled contractual interest and principal payments for at least six months.

The following table presents loans in nonaccrual status by class of loan as of the dates indicated:

Nonaccrual Loans by Class

	September 30, 2018	December 31, 2017
	(in thousands)	
Mortgage loans on real estate		
Residential 1-4 family	\$ 1,283	\$ 1,447
Commercial	10,498	9,468
Construction	418	721
Second mortgages	203	118
Equity lines of credit	299	292
Total mortgage loans on real estate	12,701	12,046
Commercial loans	308	836
Total	\$ 13,009	\$ 12,882

No acquired impaired loans were on nonaccrual status at September 30, 2018.

The following table presents the interest income that the Company would have earned under the original terms of its nonaccrual loans and the actual interest recorded by the Company on nonaccrual loans for the periods presented:

Nine Months
Ended

	September 30, 2018 2017 (in thousands)	
Interest income that would have been recorded under original loan terms	\$ 388	\$ 311
Actual interest income recorded for the period	249	179
Reduction in interest income on nonaccrual loans	\$ 139	\$ 132

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TROUBLED DEBT RESTRUCTURINGS

The Company's loan portfolio includes certain loans that have been modified in a troubled debt restructuring (TDR), where economic concessions have been granted to borrowers who are experiencing financial difficulties. These concessions typically result from the Company's loss mitigation activities and could include reduction in the interest rate below current market rates for borrowers with similar risk profiles, payment extensions, forgiveness of principal, forbearance or other actions intended to maximize collection. The Company defines a TDR as nonperforming if the TDR is in nonaccrual status or is 90 days or more past due and still accruing interest at the report date.

When the Company modifies a loan, management evaluates any possible impairment as stated in the impaired loan section below.

The following table presents TDRs during the periods indicated, by class of loan. There were no troubled debt restructurings in the three or nine months ended September 30, 2018 or the three months ended September 30, 2017.

Troubled Debt Restructurings by Class
For the Nine Months Ended September 30, 2017

	Recorded Number of Modifications	Recorded Investment Prior to Modification	Recorded Investment After Modification	Current Investment on September 30, 2017
(dollars in thousands)				
Mortgage loans on real estate:				
Residential 1-4 family	1	\$ 142	\$ 142	\$ 141
Commercial	2	3,663	3,663	3,653
Total	3	\$ 3,805	\$ 3,805	\$ 3,794

Of the loans restructured in the nine months ended September 30, 2017 one was given a below-market rate for debt with similar risk characteristics and two were granted terms that the Company would not otherwise extend to borrowers with similar risk characteristics. At September 30, 2018 and December 31, 2017, the Company had no outstanding commitments to disburse additional funds on any TDR. At September 30, 2018 the Company had no loans secured by residential 1 - 4 family real estate that were in the process of foreclosure. At December 31, 2017, residential 1 - 4 family real estate loans totaling \$77 thousand were in the process of foreclosure.

In the three and nine months ended September 30, 2018 and 2017, there were no defaulting TDRs where the default occurred within twelve months of restructuring. The Company considers a TDR in default when any of the following occurs: the loan, as restructured, becomes 90 days or more past due; the loan is moved to nonaccrual status following the restructure; the loan is restructured again under terms that would qualify it as a TDR if it were not already so classified; or any portion of the loan is charged off.

All TDRs are factored into the determination of the allowance for loan losses and included in the impaired loan analysis, as discussed below.

IMPAIRED LOANS

A loan is considered impaired when, based on current information and events, it is probable that the Company will be unable to collect all amounts when due from the borrower in accordance with the contractual terms of the loan. Impaired loans include nonperforming loans and loans modified in a TDR. When management identifies a loan as impaired, the impairment is measured based on the present value of expected future cash flows, discounted at the loan's effective interest rate, except when the sole or remaining source of repayment for the loan is the operation or liquidation of the collateral. In these cases, management uses the current fair value of the collateral, less selling costs, when foreclosure is probable, instead of the discounted cash flows. If management determines that the value of the impaired loan is less than the recorded investment in the loan (net of previous charge-offs, deferred loan fees or costs and unamortized premium or discount), impairment is recognized through a specific allocation in the allowance or a charge-off to the allowance.

When the ultimate collectability of the total principal of an impaired loan is in doubt and the loan is in nonaccrual status, all payments are applied to principal under the cost-recovery method. For financial statement purposes, the recorded investment in the loan is the actual principal balance reduced by payments that would otherwise have been applied to interest. When reporting information on these loans to the applicable customers, the unpaid principal balance is reported as if payments were applied to principal and interest under the original terms of the loan agreements. Therefore, the unpaid principal balance reported to the customer would be higher than the recorded investment in the loan for financial statement purposes. When the ultimate collectability of the total principal of the impaired loan is not in doubt and the loan is in nonaccrual status, contractual interest is credited to interest income when received under the cash-basis method.

The following table includes the recorded investment and unpaid principal balances (a portion of which may have been charged off) for impaired loans, exclusive of acquired impaired loans, with the associated allowance amount, if applicable, as of the dates presented. Also presented are the average recorded investments in the impaired loans and the related amount of interest recognized for the periods presented. The average balances are calculated based on daily average balances.

Impaired Loans by Class

	As of September 30, 2018				For the nine months ended September 30, 2018	
	Unpaid Principal Balance	Recorded Investment Without Allowance	Recorded Investment With Allowance	Associated Allowance	Average Recorded Investment	Interest Recognized
Mortgage loans on real estate:						
Residential 1-4 family	\$2,139	\$1,924	\$ 93	\$ 47	\$2,123	\$ 63
Commercial	15,099	12,921	607	113	14,471	403
Construction	511	418	93	19	718	6
Second mortgages	547	397	131	14	510	11
Equity lines of credit	300	49	250	22	324	1
Total mortgage loans on real estate	18,596	15,709	1,174	215	18,146	484
Commercial loans	396	80	228	14	493	6
Other consumer loans	45	-	-	-	58	1
Total	\$19,037	\$15,789	\$ 1,402	\$ 229	\$18,697	\$ 491

Impaired Loans by Class

As of December 31, 2017 For the Year Ended

December 31, 2017

	Recorded Investment			Associated Allowance	Average Recorded Investment	Interest Income Recognized
	Unpaid Principal Balance	Without Allowance	With Allowance			
Mortgage loans on real estate:						
Residential 1-4 family	\$2,873	\$2,499	\$ 316	\$ 52	\$2,525	\$ 90
Commercial	15,262	11,622	1,644	1	13,541	579
Construction	814	721	92	18	406	23
Second mortgages	473	318	135	14	464	20
Equity lines of credit	293	53	239	10	261	-
Total mortgage loans on real estate	19,715	15,213	2,426	95	17,197	712
Commercial loans	1,115	836	-	-	1,388	30
Other consumer loans	-	-	-	-	41	-
Total	\$20,830	\$16,049	\$ 2,426	\$ 95	\$18,626	\$ 742

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MONITORING OF LOANS AND EFFECT OF MONITORING FOR THE ALLOWANCE FOR LOAN LOSSES

Loan officers are responsible for continual portfolio analysis and prompt identification and reporting of problem loans, which includes assigning a risk grade to each applicable loan at its origination and revising such grade as the situation dictates. Loan officers maintain frequent contact with borrowers, which should enable the loan officer to identify potential problems before other personnel. In addition, meetings with loan officers and upper management are held to discuss problem loans and review risk grades. Nonetheless, in order to avoid over-reliance upon loan officers for problem loan identification, the Company's loan review system provides for review of loans and risk grades by individuals who are independent of the loan approval process. Risk grades and historical loss rates (determined by migration analysis) by risk grades are used as a component of the calculation of the allowance for loan losses.

ALLOWANCE FOR LOAN LOSSES

Management has an established methodology to determine the adequacy of the allowance for loan losses that assesses the risks and probable losses inherent in the loan portfolio. The Company segments the loan portfolio into categories as defined by Schedule RC-C of the Federal Financial Institutions Examination Council Consolidated Reports of Condition and Income Form 041 (Call Report). Loans are segmented into the following pools: commercial, real estate-construction, real estate-mortgage, consumer and other loans. The Company also sub-segments the real estate-mortgage segment into four classes: residential 1-4 family, commercial real estate, second mortgages and equity lines of credit.

The Company uses an internally developed risk evaluation model in the estimation of the credit risk process. The model and assumptions used to determine the allowance are independently validated and reviewed to ensure that the theoretical foundation, assumptions, data integrity, computational processes and reporting practices are appropriate and properly documented.

Each portfolio segment has risk characteristics as follows:

Commercial: Commercial loans carry risks associated with the successful operation of a business or project, in addition to other risks associated with the ownership of a business. The repayment of these loans may be dependent upon the profitability and cash flows of the business. In addition, there is risk associated with the value of collateral other than real estate which may depreciate over time and cannot be appraised with as much precision.

Real estate-construction: Construction loans carry risks that the project will not be finished according to schedule, the project will not be finished according to budget and the value of the collateral may at any point in time be less than the principal amount of the loan. Construction loans also bear the risk that the general contractor, who may or may not be the loan customer, may be unable to finish the construction project as planned because of financial pressure unrelated to the project.

Real estate-mortgage: Residential mortgage loans and equity lines of credit carry risks associated with the continued credit-worthiness of the borrower and changes in the value of the collateral. Commercial real estate loans carry risks associated with the successful operation of a business if owner occupied. If non-owner occupied, the repayment of these loans may be dependent upon the profitability and cash flow from rent receipts.

Consumer loans: Consumer loans carry risks associated with the continued credit-worthiness of the borrowers and the value of the collateral. Consumer loans are more likely than real estate loans to be immediately adversely affected by job loss, divorce, illness or personal bankruptcy.

Other loans: Other loans are loans to mortgage companies, loans for purchasing or carrying securities, and loans to insurance, investment and finance companies. These loans carry risks associated with the successful operation of a business. In addition, there is risk associated with the value of collateral other than real estate which may depreciate over time, depend on interest rates or fluctuate in active trading markets.

Each segment of the portfolio is pooled by risk grade or by days past due. Consumer loans not secured by real estate and made to individuals for household, family and other personal expenditures are segmented into pools based on

days past due, while all other loans, including loans to consumers that are secured by real estate, are segmented by risk grades. A historical loss percentage is then calculated by migration analysis and applied to each pool. The migration analysis applied to all pools is able to track the risk grading and historical performance of individual loans throughout a number of periods set by management, which provides management with information regarding trends (or migrations) in a particular loan segment. At September 30, 2018 and December 31, 2017 management used eight twelve-quarter migration periods.

Management also provides an allocated component of the allowance for loans that are specifically identified that may be impaired, and are individually analyzed for impairment. An allocated allowance is established when the present value of expected future cash flows from the impaired loan (or the collateral value or observable market price of the impaired loan) is lower than the carrying value of that loan.

Based on credit risk assessments and management's analysis of qualitative factors, additional loss factors are applied to loan balances. These additional qualitative factors include: economic conditions, trends in growth, loan concentrations, changes in certain loans, changes in underwriting, changes in management and changes in the legal and regulatory environment.

Acquired loans are recorded at their fair value at acquisition date without carryover of the acquiree's previously established ALL, as credit discounts are included in the determination of fair value. The fair value of the loans is determined using market participant assumptions in estimating the amount and timing of both principal and interest cash flows expected to be collected on the loans and then applying a market-based discount rate to those cash flows. During evaluation upon acquisition, acquired loans are also classified as either acquired impaired or acquired performing.

Acquired impaired loans reflect credit quality deterioration since origination, as it is probable at acquisition that the Company will not be able to collect all contractually required payments. These acquired impaired loans are accounted for under ASC 310-30, Receivables – Loans and Debt Securities Acquired with Deteriorated Credit Quality. The acquired impaired loans are segregated into pools based on loan type and credit risk. Loan type is determined based on collateral type, purpose, and lien position. Credit risk characteristics include risk rating groups, nonaccrual status, and past due status. For valuation purposes, these pools are further disaggregated by maturity, pricing characteristics, and re-payment structure. Acquired impaired loans are written down at acquisition to fair value using an estimate of cash flows deemed to be collectible. Accordingly, such loans are no longer classified as nonaccrual even though they may be contractually past due because the Company expects to fully collect the new carrying values of such loans, which is the new cost basis arising from purchase accounting.

Acquired performing loans are accounted for under ASC 310-20, Receivables – Nonrefundable Fees and Other Costs. The difference between the fair value and unpaid principal balance of the loan at acquisition date (premium or discount) is amortized or accreted into interest income over the life of the loans. If the acquired performing loan has revolving privileges, it is accounted for using the straight-line method; otherwise, the effective interest method is used.

ALLOWANCE FOR LOAN LOSSES BY SEGMENT

The total allowance reflects management's estimate of losses inherent in the loan portfolio at the balance sheet date. The Company considers the allowance for loan losses of \$10.2 million adequate to cover probable loan losses inherent in the loan portfolio at September 30, 2018.

The following table presents, by portfolio segment, the changes in the allowance for loan losses and the recorded investment in loans for the periods presented. Allocation of a portion of the allowance to one category of loans does not preclude its availability to absorb losses in other categories.

ALLOWANCE FOR LOAN LOSSES AND RECORDED INVESTMENT IN LOANS

(in thousands)

For the Nine Months Ended September 30, 2018	Commercial	Real Estate - Construction	Real Estate - Mortgage (1)	Consumer (2)	Other	Total
Allowance for Loan Losses:						
Balance at the beginning of period	\$ 1,889	\$ 541	\$5,217	\$1,644	\$157	\$9,448
Charge-offs	(81)	-	(729)	(502)	(267)	(1,579)
Recoveries	136	-	127	189	61	513
Provision for loan losses	405	(401)	1,336	214	295	1,849
Ending balance	\$ 2,349	\$ 140	\$5,951	\$1,545	\$246	\$10,231
Ending balance individually evaluated for impairment	\$ 14	\$ 19	\$196	\$-	\$-	\$229
Ending balance collectively evaluated for impairment	2,335	121	5,755	1,545	246	10,002
Ending balance acquired impaired loans	-	-	-	-	-	-
Ending balance	\$ 2,349	\$ 140	\$5,951	\$1,545	\$246	\$10,231
Loan Balances:						
Ending balance individually evaluated for impairment	\$ 308	\$ 511	\$16,372	\$-	\$-	\$17,191
Ending balance collectively evaluated for impairment	67,363	32,387	480,436	170,898	10,712	761,796
Ending balance acquired impaired loans	101	-	347	-	-	448
Ending balance	\$ 67,772	\$ 32,898	\$497,155	\$170,898	\$10,712	\$779,435

For the Year Ended December 31, 2017	Commercial	Real Estate - Construction	Real Estate - Mortgage (1)	Consumer	Other	Total
Allowance for Loan Losses:						
Balance at the beginning of period	\$ 1,493	\$ 846	\$5,267	\$455	\$184	\$8,245
Charge-offs	(807)	-	(1,934)	(279)	(267)	(3,287)
Recoveries	37	104	45	56	88	330
Provision for loan losses	1,166	(409)	1,839	1,412	152	4,160
Ending balance	\$ 1,889	\$ 541	\$5,217	\$1,644	\$157	\$9,448
Ending balance individually evaluated for impairment	\$ -	\$ 18	\$77	\$-	\$-	\$95
Ending balance collectively evaluated for impairment	1,889	523	5,140	1,644	157	9,353

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Ending balance	\$ 1,889	\$ 541	\$5,217	\$ 1,644	\$157	\$9,448
Loan Balances:						
Ending balance individually evaluated for impairment	\$ 836	\$ 813	\$16,826	\$-	\$-	\$18,475
Ending balance collectively evaluated for impairment	59,562	26,676	448,405	174,225	11,197	720,065
Ending balance	\$ 60,398	\$ 27,489	\$465,231	\$174,225	\$11,197	\$738,540

(1) The real estate-mortgage segment includes residential 1 – 4 family, commercial real estate, second mortgages and equity lines of credit.

(2) The consumer segment includes consumer automobile loans.

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Note 5. Low-Income Housing Tax Credits

The Company was invested in 4 separate housing equity funds at both September 30, 2018 and December 31, 2017. The general purpose of these funds is to encourage and assist participants in investing in low-income residential rental properties located in the Commonwealth of Virginia; develop and implement strategies to maintain projects as low-income housing; deliver Federal Low Income Housing Credits to investors; allocate tax losses and other possible tax benefits to investors; and preserve and protect project assets.

The investments in these funds were recorded as other assets on the consolidated balance sheets and were \$3.3 million and \$3.5 million at September 30, 2018 and December 31, 2017, respectively. The expected terms of these investments and the related tax benefits run through 2033. Total projected tax credits to be received for 2018 are \$494 thousand, which is based on the most recent quarterly estimates received from the funds. Additional capital calls expected for the funds totaled \$248 thousand at September 30, 2018 and \$1.1 million at December 31, 2017, respectively, and are recorded in accrued expenses and other liabilities on the corresponding consolidated balance sheet.

	Three Months Ended September 30,		Nine Months Ended September 30,		Affected Line Item on Consolidated Statements of Income
	2018	2017	2018	2017	
	(in thousands)				
Tax credits and other tax benefits					
Amortization of operating losses	\$80	\$77	\$240	\$255	Other operating expenses
Tax benefit of operating losses*	17	26	50	87	Income tax expense (benefit)
Tax credits	137	113	384	346	Income tax expense (benefit)
Total tax benefits	\$154	\$139	\$434	\$433	

* Computed using a 21% tax rate for 2018 and a 34% tax rate for 2017

Note 6. Borrowings

The Company classifies all borrowings that will mature within a year from the date on which the Company enters into them as short-term borrowings. Short-term borrowings sources consist of federal funds purchased, overnight repurchase agreements (which are secured transactions with customers that generally mature within one to four days), and advances from the FHLB.

The Company maintains federal funds lines with several correspondent banks to address short-term borrowing needs. At September 30, 2018 and December 31, 2017 the remaining credit available from these lines totaled \$55.0 million and \$45.0 million, respectively. The Company has a collateral dependent line of credit with the FHLB with remaining credit availability of \$248.0 million and \$217.0 as of September 30, 2018 and December 31, 2017, respectively.

SHORT-TERM BORROWINGS

The following table presents total short-term borrowings as of the dates indicated:

	September		December	
	30,		31,	2017
	2018			
	(in thousands)			
Federal funds purchased	\$-		\$	10,000
Overnight repurchase agreements	18,116		20,693	
FHLB advances	23,000		47,500	
Total short-term borrowings	\$41,116		\$	78,193
Maximum month-end outstanding balance	\$99,898		\$	79,819
Average outstanding balance during the period	\$72,371		\$	53,165
Average interest rate (year-to-date)	1.11	%	0.72	%
Average interest rate at end of period	1.32	%	1.27	%

LONG-TERM BORROWINGS

The Company had long-term FHLB advances totaling \$37.0 million outstanding at September 30, 2018 and \$20.0 million outstanding at December 31, 2017. Scheduled maturity dates of the advances at September 30, 2018 range from February 28, 2019 to August 27, 2021, and the interest rates range from 1.54% to 2.89%.

The Company also obtained a loan maturing on April 1, 2023 from a correspondent bank during the second quarter of 2018 to provide partial funding for the Citizens acquisition. The terms of the loan include a LIBOR based interest rate that adjusts monthly and quarterly principal curtailments. At September 30, 2018 the outstanding balance was \$2.9 million, and the then-current interest rate was 4.58%.

The loan agreement with the lender contains financial covenants including minimum return on average asset ratio and Bank capital leverage ratio, maintenance of a well-capitalized position as defined by regulatory guidance and a maximum level of non-performing assets as a percentage of capital plus the allowance for loan losses. The Company was in compliance with each covenant at September 30, 2018.

Note 7. Commitments and Contingencies**CREDIT-RELATED FINANCIAL INSTRUMENTS**

The Company is a party to credit-related financial instruments with off-balance-sheet risk in the normal course of business in order to meet the financing needs of its customers. These financial instruments include commitments to extend credit, standby letters of credit and commercial letters of credit. Such commitments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the consolidated balance sheets.

The Company's exposure to credit loss is represented by the contractual amount of these commitments. The Company follows the same credit policies in making such commitments as it does for on-balance-sheet instruments.

The following financial instruments whose contract amounts represent credit risk were outstanding at September 30, 2018 and December 31, 2017:

	September 30, 2018	December 31, 2017
	(in thousands)	
Commitments to extend credit:		
Home equity lines of credit	\$71,545	\$56,486
Commercial real estate, construction and development loans committed but not funded	33,166	19,526
Other lines of credit (principally commercial)	88,797	68,101
Total	\$193,508	\$144,113
Letters of credit	\$3,831	\$3,331

Note 8. Share-Based Compensation

The Company has adopted an employee stock purchase plan and offers share-based compensation through its equity compensation plan. Share-based compensation arrangements may include stock options, restricted and unrestricted stock awards, restricted stock units, performance units and stock appreciation rights. Accounting standards require all share-based payments to employees to be valued using a fair value method on the date of grant and to be expensed based on that fair value over the applicable vesting period. The Company accounts for forfeitures during the vesting period as they occur.

The 2016 Incentive Stock Plan (the Incentive Stock Plan) permits the issuance of up to 300,000 shares of common stock for awards to key employees and non-employee directors of the Company and its subsidiaries in the form of stock options, restricted stock, restricted stock units, stock appreciation rights, stock awards and performance units. As of September 30, 2018 only restricted stock has been granted under the Incentive Stock Plan.

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Restricted stock activity for the nine months ended September 30, 2018 is summarized below:

	Shares	Weighted Average Grant Date Fair Value
Nonvested, January 1, 2018	2,245	\$ 33.60
Issued	11,444	26.32
Vested	-	-
Forfeited	-	-
Nonvested, September 30, 2018	13,689	\$ 27.51

The weighted average period over which nonvested awards are expected to be recognized is 1.50 years.

The fair value of restricted stock granted during the nine months ended September 30, 2018 was \$301 thousand.

The remaining unrecognized compensation expense for nonvested restricted stock shares totaled \$257 thousand as of September 30, 2018.

Stock-based compensation expense was \$50 thousand and \$103 thousand for the three and nine months ended September 30, 2018, respectively. Stock-based compensation expense for the three and nine months ended September 30, 2017 was \$9 thousand.

Under the Company's Employee Stock Purchase Plan (ESPP), substantially all employees of the Company and its subsidiaries can authorize a specific payroll deduction from their base compensation for the periodic purchase of the Company's common stock. Shares of stock are issued quarterly at a discount to the market price of the Company's stock on the day of purchase, which can range from 0-15% and was set at 5% for 2017 and for the first nine months of 2018.

2,644 shares were purchased under the ESPP during the nine months ended September 30, 2018. At September 30, 2018, the Company had 242,809 remaining shares reserved for issuance under this plan.

Note 9. Stockholders' Equity and Earnings per Share

STOCKHOLDERS' EQUITY – Accumulated Other Comprehensive Loss

The following table presents information on amounts reclassified out of accumulated other comprehensive loss, by category, during the periods indicated:

	Three Months Ended September 30,	Nine Months Ended September 30,	2017	2018	2017	Affected Line Item on Consolidated Statements of Income
Available-for-sale securities						
Realized gains on sales of securities	\$-	\$ 2	\$ 120	\$ 89		Gain on sale of securities, net
Tax effect	-	-	25	30		Income tax expense (benefit)
	\$-	\$ 2	\$ 95	\$ 59		

The following tables present the changes in accumulated other comprehensive loss, by category, net of tax, for the periods indicated:

	Unrealized Gains (Losses) on Available-for-Sale Securities (in thousands)	Defined Benefit Plans	Accumulated Other Comprehensive Loss
Three Months Ended September 30, 2018			
Balance at beginning of period	\$ (2,889)	\$ -	\$ (2,889)
Net other comprehensive loss	(803)	\$ -	(803)
Balance at end of period	\$ (3,692)	\$ -	\$ (3,692)
Three Months Ended September 30, 2017			
Balance at beginning of period	\$ (275)	\$ (2,469)	\$ (2,744)
Net other comprehensive income	57	-	57
Balance at end of period	\$ (218)	\$ (2,469)	\$ (2,687)

Unrealized Gains (Losses) on Available-for-Sale Securities	Defined Benefit Plans	Accumulated Other Comprehensive Loss
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(in thousands)

Nine Months Ended September 30, 2018

Balance at beginning of period	\$ (707)	\$ -	\$ (707)
Net other comprehensive loss	(2,769)	-	(2,769)
Reclassification of the income tax effects of the Tax Cuts and Jobs Act from AOCI	(139)	-	(139)
Reclassification of net unrealized gains on equity securities from AOCI per ASU 2016-01	(77)	-	(77)
Balance at end of period	\$ (3,692)	\$ -	\$ (3,692)

Nine Months Ended September 30, 2017

Balance at beginning of period	\$ (1,739)	\$ (2,469)	\$ (4,208)
Net other comprehensive income	1,521	-	1,521
Balance at end of period	\$ (218)	\$ (2,469)	\$ (2,687)

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The following tables present the change in each component of accumulated other comprehensive loss on a pre-tax and after-tax basis for the periods indicated.

	Three Months Ended September 30, 2018		
	Pretax	Tax	Net-of-Tax
	(in thousands)		
Unrealized losses on available-for-sale securities:			
Unrealized holding losses arising during the period	\$(1,017)	\$(214)	\$(803)
Reclassification adjustment for gains recognized in income	-	-	-
Total change in accumulated other comprehensive loss, net	\$(1,017)	\$(214)	\$(803)

	Three Months Ended September 30, 2017		
	Pretax	Tax	Net-of-Tax
	(in thousands)		
Unrealized gains on available-for-sale securities:			
Unrealized holding gains arising during the period	\$89	\$30	\$ 59
Reclassification adjustment for gains recognized in income	(2)	-	(2)
Total change in accumulated other comprehensive loss, net	\$87	\$30	\$ 57

	Nine Months Ended September 30, 2018		
	Pretax	Tax	Net-of-Tax
	(in thousands)		
Unrealized losses on available-for-sale securities:			
Unrealized holding losses arising during the period	\$(3,385)	\$(711)	\$(2,674)
Reclassification adjustment for gains recognized in income	(120)	(25)	(95)
Total change in accumulated other comprehensive loss, net	\$(3,505)	\$(736)	\$(2,769)

	Nine Months Ended September 30, 2017		
	Pretax	Tax	Net-of-Tax
	(in thousands)		
Unrealized gains on available-for-sale securities:			
Unrealized holding gains arising during the period	\$2,394	\$814	\$ 1,580
Reclassification adjustment for gains recognized in income	(89)	(30)	(59)
Total change in accumulated other comprehensive loss, net	\$2,305	\$784	\$ 1,521

EARNINGS PER COMMON SHARE

Basic earnings per share is computed by dividing net income by the weighted average number of common shares outstanding during the period. Diluted earnings per share is computed using the weighted average number of common shares outstanding during the period, including the effect of dilutive potential common shares attributable to outstanding stock options.

The following is a reconciliation of the denominators of the basic and diluted EPS computations for the three and nine months ended September 30, 2018 and 2017:

	Net Income Available to Common Stockholders (Numerator) (in thousands except per share data)	Weighted Average Common Shares (Denominator)	Per Share Amount
Three Months Ended September 30, 2018			
Net income, basic	\$1,597	5,182	\$ 0.31
Potentially dilutive common shares - stock options	-	-	-
Potentially dilutive common shares - employee stock purchase program	-	-	-
Diluted	\$1,597	5,182	\$ 0.31
Three Months Ended September 30, 2017			
Net income, basic	\$757	4,994	\$ 0.15
Potentially dilutive common shares - stock options	-	10	-
Potentially dilutive common shares - employee stock purchase program	-	-	-
Diluted	\$757	5,004	\$ 0.15
Nine Months Ended September 30, 2018			
Net income, basic	\$3,531	5,127	\$ 0.69
Potentially dilutive common shares - stock options	-	-	-
Potentially dilutive common shares - employee stock purchase program	-	-	-
Diluted	\$3,531	5,127	\$ 0.69
Nine Months Ended September 30, 2017			
Net income, basic	\$2,860	4,985	\$ 0.57
Potentially dilutive common shares - stock options	-	12	-
Potentially dilutive common shares - employee stock purchase program	-	-	-
Diluted	\$2,860	4,997	\$ 0.57

The Company had no antidilutive shares outstanding in the nine months ended September 30, 2018 and 2017. Nonvested restricted common shares, which carry all rights and privileges of a common share with respect to the stock, including the right to vote, were included in the basic and diluted per common share calculations.

Note 10. Fair Value Measurements

The Company uses fair value measurements to record fair value adjustments to certain assets and liabilities and to determine fair value disclosures. In accordance with the "Fair Value Measurements and Disclosures" topics of FASB

ASU 2010-06, FASB ASU 2011-04, and FASB ASU 2016-01, the fair value of a financial instrument is the price that would be received in the sale of an asset or transfer of a liability in an orderly transaction between market participants at the measurement date. Fair value is best determined based upon quoted market prices. However, in many instances, there are no quoted market prices for the Company's various financial instruments. In cases where quoted market prices are not available, fair values are based on estimates using present value or other valuation techniques. Those techniques are significantly affected by the assumptions used, including the discount rate and estimate of future cash flows. Accordingly, the fair value estimates may not be realized in an immediate settlement of the instrument.

The fair value guidance provides a consistent definition of fair value, which focuses on exit price in an orderly transaction (that is, not a forced liquidation or distressed sale) between market participants at the measurement date under current market conditions. If there has been a significant decrease in the volume and level of activity for the asset or liability, a change in valuation technique or the use of multiple valuation techniques may be appropriate. In such instances, determining the price at which willing market participants would transact at the measurement date under current market conditions depends on the facts and circumstances and requires the use of significant judgment. The fair value can be a reasonable point within a range that is most representative of fair value under current market conditions.

In estimating the fair value of assets and liabilities, the Company relies mainly on two models. The first model, used by the Company's bond accounting service provider, determines the fair value of securities. Securities are priced based on an evaluation of observable market data, including benchmark yield curves, reported trades, broker/dealer quotes, and issuer spreads. Pricing is also impacted by credit information about the issuer, perceived market movements, and current news events impacting the individual sectors. For assets other than securities and for all liabilities, fair value is determined using the Company's asset/liability modeling software. The software uses current yields, anticipated yield changes, and estimated duration of assets and liabilities to calculate fair value.

In accordance with ASC 820, "Fair Value Measurements and Disclosures," the Company groups its financial assets and financial liabilities generally measured at fair value into 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.

Level 1: Valuation is based on quoted prices in active markets for identical assets or liabilities that the reporting entity has the ability to access at the measurement date. Level 1 assets and liabilities generally include debt and equity securities that are traded in an active exchange market. Valuations are obtained from readily available pricing sources for market transactions involving identical assets or liabilities.

Level 2: Valuation is based on inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. The valuation may be based on quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the asset or liability.

Level 3: Valuation is based on unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. Level 3 assets and liabilities include financial instruments whose value is determined using pricing models, discounted cash flow methodologies, or similar techniques, as well as instruments for which determination of fair value requires significant management judgment or estimation.

An instrument's categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement.

ASSETS MEASURED AT FAIR VALUE ON A RECURRING BASIS

Debt securities with readily determinable fair values that are classified as "available-for-sale" are recorded at fair value, with unrealized gains and losses excluded from earnings and reported in other comprehensive income. Securities available-for-sale are recorded at fair value on a recurring basis. Fair value measurement is based upon quoted market prices, when available (Level 1). If quoted market prices are not available, fair values are measured utilizing independent valuation techniques of identical or similar securities for which significant assumptions are derived primarily from or corroborated by observable market data. Third party vendors compile prices from various sources and may determine the fair value of identical or similar securities by using pricing models that consider observable market data (Level 2). In certain cases where there is limited activity or less transparency around inputs to the valuation, securities are classified within Level 3 of the valuation hierarchy. Currently, all of the Company's available-for-sale securities are considered to be Level 2 securities.

The following table presents the balances of certain assets measured at fair value on a recurring basis as of the dates indicated:

	Fair Value Measurements at September 30, 2018 Using		
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Available-for-sale securities			
U.S. Treasury securities	\$9,264	\$-	\$9,264
			\$ -

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Obligations of U.S. Government agencies	11,038	-	11,038	-
Obligations of state and political subdivisions	49,030	-	49,030	-
Mortgage-backed securities	67,810	-	67,810	-
Money market investments	1,205	-	1,205	-
Corporate bonds	3,941	-	3,941	-
Total available-for-sale securities	\$142,288	\$-	\$142,288	\$-

Fair Value Measurements at
December 31, 2017 Using
Quoted

Prices

in

Active

Markets

for Significant

Identifiable

Assets

(Level 1)

Inputs

(Level 2)

Inputs

(Level 3)

Significant

Unobservable

Inputs

(Level 3)

Available-for-sale securities

Obligations of U.S. Government agencies	\$9,435	\$-	\$9,435	\$-
Obligations of state and political subdivisions	64,765	-	64,765	-
Mortgage-backed securities	74,296	-	74,296	-
Money market investments	1,194	-	1,194	-
Corporate bonds	7,234	-	7,234	-
Other marketable equity securities	197	-	197	-
Total available-for-sale securities	\$157,121	\$-	\$157,121	\$-

ASSETS MEASURED AT FAIR VALUE ON A NONRECURRING BASIS

Under certain circumstances, adjustments are made to the fair value for assets and liabilities although they are not measured at fair value on an ongoing basis.

Impaired loans

A loan is considered impaired when, based on current information and events, it is probable that the Company will be unable to collect all amounts when due from the borrower in accordance with the contractual terms of the loan agreement. The measurement of fair value and loss associated with impaired loans can be based on the observable market price of the loan, the fair value of the collateral securing the loan, or the present value of the loan's expected future cash flows, discounted at the loan's effective interest rate. Collateral may be in the form of real estate or business assets including equipment, inventory, and accounts receivable, with the vast majority of the collateral in real estate.

The value of real estate collateral is determined utilizing an income, market, or cost valuation approach based on an appraisal conducted by an independent, licensed appraiser outside of the Company. In the case of loans with lower balances, the Company may obtain a real estate evaluation instead of an appraisal. Evaluations utilize many of the same techniques as appraisals, and are typically performed by independent appraisers. Once received, appraisals and evaluations are reviewed by trained staff independent of the lending function to verify consistency and reasonability. Appraisals and evaluations are based on significant unobservable inputs, including but not limited to: adjustments made to comparable properties, judgments about the condition of the subject property, the availability and suitability of comparable properties, capitalization rates, projected income of the subject or comparable properties, vacancy rates, projected depreciation rates, and the state of the local and regional economy. The Company may also elect to make additional reductions in the collateral value based on management's best judgment, which represents another source of unobservable inputs. Because of the subjective nature of collateral valuation, impaired loans are considered Level 3.

Impaired loans may be secured by collateral other than real estate. The value of business equipment is based upon an outside appraisal if deemed significant, or the net book value on the applicable business' financial statements if not considered significant using observable market data. Likewise, values for inventory and accounts receivable collateral are based on financial statement balances or aging reports (Level 3). If a loan is not collateral-dependent, its impairment may be measured based on the present value of expected future cash flows, discounted at the loan's effective interest rate. Because the loan is discounted at its effective rate of interest, rather than at a market rate, the loan is not considered to be held at fair value and is not included in the tables below. Collateral-dependent impaired loans allocated to the allowance for loan losses are measured at fair value on a nonrecurring basis. Any fair value adjustments are recorded in the period incurred as part of the provision for loan losses on the Consolidated Statements of Income.

Other Real Estate Owned (OREO)

Loans are transferred to OREO when the collateral securing them is foreclosed on. The measurement of gain or loss associated with OREOs is based on the fair value of the collateral compared to the unpaid loan balance and anticipated costs to sell the property. If there is a contract for the sale of a property, and management reasonably believes the transaction will be consummated in accordance with the terms of the contract, fair value is based on the sale price in that contract (Level 1). If management has recent information about the sale of identical properties, such as when selling multiple condominium units on the same property, the remaining units would be valued based on the observed market data (Level 2). Lacking either a contract or such recent data, management would obtain an appraisal or evaluation of the value of the collateral as discussed above under Impaired Loans (Level 3). After the asset has been booked, a new appraisal or evaluation is obtained when management has reason to believe the fair value of the property may have changed and no later than two years after the last appraisal or evaluation was received. Any fair value adjustments to OREOs below the original book value are recorded in the period incurred and expensed against current earnings.

Loans Held For Sale

Loans held for sale are carried at the lower of cost or fair value. These loans currently consist of residential loans originated for sale in the secondary market. Fair value is based on the price secondary markets are currently offering for similar loans using observable market data which is not materially different than cost due to the short duration between origination and sale (Level 2). Gains and losses on the sale of loans are recorded within the mortgage segment and are reported on a separate line item on the Company's Consolidated Statements of Income.

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The following table presents the assets carried on the consolidated balance sheets for which a nonrecurring change in fair value has been recorded. Assets are shown by class of loan and by level in the fair value hierarchy, as of the dates indicated. Certain impaired loans are valued by the present value of the loan's expected future cash flows, discounted at the loan's effective interest rate rather than at a market rate. These loans are not carried on the consolidated balance sheets at fair value and, as such, are not included in the table below.

	Carrying Value at September 30, 2018 Using Quoted Prices in Active Markets for Significant Identifiable Assets			Fair Value (in thousands)
	Other Observable Inputs (Level 1)	Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
Impaired loans				
Mortgage loans on real estate:				
Residential 1-4 family	\$45	\$-	\$ -	\$ 45
Commercial	326	-	-	326
Construction	74	-	-	74
Equity lines of credit	229	-	-	229
Total	\$674	\$-	\$ -	\$ 674
Loans				
Loans held for sale	\$1,033	\$-	\$ 1,033	\$ -
Other real estate owned				
Commercial real estate	\$-	\$-	\$ -	\$ -
Construction	133	-	-	133
Total	\$133	\$-	\$ -	\$ 133

	Carrying Value at December 31, 2017 Using Quoted Prices in Active Markets for Significant Identifiable Assets			Fair Value (in thousands)
	Other Observable Inputs (Level 1)	Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
Impaired loans				

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Mortgage loans on real estate:

Residential 1-4 family	\$264	\$-	\$ -	\$ 264
Construction	74	-	-	74
Equity lines of credit	229	-	-	229
Total	\$567	\$-	\$ -	\$ 567

Loans

Loans held for sale	\$779	\$-	\$ 779	\$ -
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The following table displays quantitative information about Level 3 Fair Value Measurements as of the dates indicated:

Quantitative Information About Level 3 Fair Value Measurements

	Fair Value at September 30, 2018 (dollars in thousands)	Valuation Techniques	Unobservable Input	Range (Weighted Average)	
Impaired loans					
Residential 1-4 family real estate	\$ 45	Market comparables	Selling costs	7.25	%
			Liquidation discount	4.00	%
Commercial real estate	\$ 326	Market comparables	Selling costs	7.73	%
			Liquidation discount	7.64	%
Construction	\$ 74	Market comparables	Selling costs	7.25	%
			Liquidation discount	4.00	%
Equity lines of credit	\$ 229	Market comparables	Selling costs	0.00% - 7.25% (6.70	%)
			Liquidation discount	0.00% - 4.00% (3.70	%)
Other real estate owned					
Construction	\$ 133	Market comparables	Selling costs	7.25	%
			Liquidation discount	4.00	%

Quantitative Information About Level 3 Fair Value Measurements

	Fair Value at December 31, 2017 (dollars in thousands)	Valuation Techniques	Unobservable Input	Range (Weighted Average)	
Impaired loans					
Residential 1-4 family real estate	\$ 264	Market comparables	Selling costs	7.25	%
			Liquidation discount	0.00% - 4.00% (2.91	%)
Construction	\$ 74	Market comparables	Selling costs	7.25	%
			Liquidation discount	4.00	%
Equity lines of credit	\$ 229	Market comparables	Selling costs	7.25	%
			Liquidation discount	4.00	%

The estimated fair values, and related carrying or notional amounts, of the Company's financial instruments as of the dates indicated are as follows:

Carrying Value	Fair Value Measurements at September 30, 2018 Using		
	Quoted Prices in Active Markets for	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)

deposits as of December 31, 2017 were measured using an entry price notion.

Note 11. Segment Reporting

The Company operates in a decentralized fashion in three principal business segments: The Old Point National Bank of Phoebus (the Bank), Old Point Trust & Financial Services, N. A. (Trust), and the Company as a separate segment (for purposes of this Note, the Parent). Revenues from the Bank's operations consist primarily of interest earned on loans and investment securities and service charges on deposit accounts. Trust's operating revenues consist principally of income from fiduciary activities. The Parent's revenues are mainly fees and dividends received from the Bank and Trust companies. The Company has no other segments.

The Company's reportable segments are strategic business units that offer different products and services. They are managed separately because each segment appeals to different markets and, accordingly, requires different technologies and marketing strategies.

Information about reportable segments, and reconciliation of such information to the consolidated financial statements as of and for the three and nine months ended September 30, 2018 and 2017 follows:

	Three Months Ended September 30, 2018				
	Bank	Trust	Parent	Eliminations	Consolidated
	(in thousands)				
Revenues					
Interest and dividend income	\$9,788	\$26	\$1,767	\$ (1,767	) \$ 9,814
Income from fiduciary activities	-	904	-	-	904
Other income	2,258	226	50	(65	) 2,469
Total operating income	12,046	1,156	1,817	(1,832	) 13,187
Expenses					
Interest expense	1,265	-	34	-	1,299
Provision for loan losses	749	-	-	-	749
Salaries and employee benefits	4,754	747	107	-	5,608
Other expenses	3,485	287	112	(65	) 3,819
Total operating expenses	10,253	1,034	253	(65	) 11,475
Income before taxes	1,793	122	1,564	(1,767	) 1,712
Income tax expense (benefit)	122	26	(33	) -	115
Net income	\$1,671	\$96	\$1,597	\$ (1,767	) \$ 1,597
Capital expenditures	\$123	\$(1	) \$-	\$ -	\$ 122
Total assets	\$1,019,780	\$6,084	\$102,459	\$ (102,883	) \$ 1,025,440
Three Months Ended September 30, 2017					
	Bank	Trust	Parent	Eliminations	Consolidated
	(in thousands)				
Revenues					
Interest and dividend income	\$8,550	\$18	\$898	\$ (898	) \$ 8,568
Income from fiduciary activities	-	903	-	-	903
Other income	2,068	198	50	(65) 2,251
Total operating income	10,618	1,119	948	(963) 11,722

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Expenses					
Interest expense	837	-	-	-	837
Provision for loan losses	1,275	-	-	-	1,275
Salaries and employee benefits	4,343	657	104	-	5,104
Other expenses	3,457	253	160	(65)	3,805
Total operating expenses	9,912	910	264	(65)	11,021
Income before taxes	706	209	684	(898)	701
Income tax expense (benefit)	(55)	) 72	(73)	) -	(56)
Net income	\$761	\$137	\$757	\$ (898)	) \$ 757
Capital expenditures	\$60	\$6	\$-	\$ -	\$ 66
Total assets	\$948,377	\$6,141	\$97,645	\$ (97,666)) \$ 954,497

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	Nine Months Ended September 30, 2018				
	Bank	Trust	Parent	Eliminations	Consolidated
	(in thousands)				
Revenues					
Interest and dividend income	\$28,136	\$69	\$4,578	\$ (4,576)	\$ 28,207
Income from fiduciary activities	-	2,803	-	-	2,803
Other income	6,404	748	180	(196)	7,136
Total operating income	34,540	3,620	4,758	(4,772)	38,146
Expenses					
Interest expense	3,455	-	66	-	3,521
Provision for loan losses	1,849	-	-	-	1,849
Salaries and employee benefits	14,455	2,242	323	-	17,020
Other expenses	10,470	822	945	(196)	12,041
Total operating expenses	30,229	3,064	1,334	(196)	34,431
Income before taxes	4,311	556	3,424	(4,576)	3,715
Income tax expense (benefit)	173	118	(107)	-	184
Net income	\$4,138	\$438	\$3,531	\$ (4,576)	\$ 3,531
Capital expenditures	\$439	\$-	\$-	\$-	\$ 439
Total assets	\$1,019,780	\$6,084	\$102,459	\$ (102,883)	\$ 1,025,440

	Nine Months Ended September 30, 2017				
	Bank	Trust	Parent	Eliminations	Consolidated
	(in thousands)				
Revenues					
Interest and dividend income	\$24,300	\$52	\$3,251	\$ (3,249)	\$ 24,354
Income from fiduciary activities	-	2,820	-	-	2,820
Other income	6,554	708	150	(196)	7,216
Total operating income	30,854	3,580	3,401	(3,445)	34,390
Expenses					
Interest expense	2,097	-	-	1	2,098
Provision for loan losses	2,925	-	-	-	2,925
Salaries and employee benefits	13,252	2,068	330	-	15,650
Other expenses	9,881	766	412	(196)	10,863
Total operating expenses	28,155	2,834	742	(195)	31,536
Income before taxes	2,699	746	2,659	(3,250)	2,854
Income tax expense (benefit)	(60)	255	(201)	-	(6)
Net income	\$2,759	\$491	\$2,860	\$ (3,250)	\$ 2,860
Capital expenditures	\$504	\$6	\$-	\$-	\$ 510

Total assets \$948,377 \$6,141 \$97,645 \$ (97,666) \$ 954,497

The accounting policies of the segments are the same as those described in the summary of significant accounting policies reported in the Company's 2017 Annual Report on Form 10-K. The Company evaluates performance based on profit or loss from operations before income taxes, not including nonrecurring gains or losses.

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

Management's discussion and analysis is presented to aid the reader in understanding and evaluating the financial condition and results of operations of Old Point Financial Corporation and its subsidiaries (collectively, the Company). This discussion and analysis should be read with the consolidated financial statements, the notes to the financial statements, and the other financial data included in this report, as well as the Company's Annual Report on Form 10-K and management's discussion and analysis for the year ended December 31, 2017. Highlighted in the discussion are material changes from prior reporting periods and any identifiable trends affecting the Company. Results of operations for the three and nine months ended September 30, 2018 and 2017 are not necessarily indicative of results that may be attained for any other period. Amounts are rounded for presentation purposes while some of the percentages presented are computed based on unrounded amounts.

Caution About Forward-Looking Statements

In addition to historical information, certain statements in this report which use language such as "believes," "expects," "plans," "may," "will," "should," "projects," "contemplates," "anticipates," "forecasts," "intends" and similar expressions, may identify forward-looking statements. For this purpose, any statement that is not a statement of historical fact may be deemed to be a forward-looking statement. These forward-looking statements are based on the beliefs of the Company's management, as well as estimates and assumptions made by, and information currently available to, management. These statements are inherently uncertain, and there can be no assurance that the underlying estimates, assumptions or beliefs will prove to be accurate. Actual results could differ materially from historical results or those anticipated by such statements. Forward-looking statements in this report include, without limitation: statements regarding future financial performance and profitability; future impacts of the Tax Cuts and Jobs Act on the Company's operations; performance of the investment and loan portfolios, including performance of the consumer auto loan portfolio and the purchased student loan portfolio and expected trends in the quality of the loan portfolio; the effects of diversifying the loan portfolio; strategic business and growth initiatives; management's efforts to reposition the balance sheet; deposit growth; levels and sources of liquidity; the securities portfolio; use of proceeds from the sale of securities; future levels of charge-offs or net recoveries; the impact of increases in NPAs on future earnings; write-downs and expected sales of other real estate owned; income taxes; monetary policy actions of the Federal Open Market Committee; and changes in interest rates.

Factors that could have a material adverse effect on the operations and future prospects of the Company include, but are not limited to: the possibility that any of the anticipated benefits of the acquisition of Citizens will not be realized or will not be realized within the expected time period; expected revenue synergies and cost savings from the acquisition of Citizens may not be fully realized or realized within the expected timeframe; revenues following the acquisition of Citizens may be lower than expected; customer and employee relationships and business operations may be disrupted by the acquisition of Citizens. Other factors that could have a material adverse effect on the operations and future prospects of the Company include, but are not limited to, changes in: interest rates and yields; general economic and business conditions, including unemployment levels; demand for loan products; the performance of the Company's dealer lending program; the legislative/regulatory climate; monetary and fiscal policies of the U.S. government, including policies of the U.S. Treasury and the Federal Reserve Board and any changes associated with the current administration; the quality or composition of the loan or securities portfolios; changes in the volume and mix of interest-earning assets and interest-bearing liabilities; the effects of management's investment strategy and strategy to manage the net interest margin; the U.S. government's guarantee of repayment of student or small business loans purchased by the Company; the level of net charge-offs on loans; deposit flows; competition; demand for financial services in the Company's market area; implementation of new technologies; the Company's ability to develop and maintain secure and reliable electronic systems; any interruption or breach of security in the Company's information systems or those of the Company's third party vendors or other service providers; reliance on third parties for key services; the use of inaccurate assumptions in management's modeling systems; technological risks and developments and cyber-attacks, threats and events; the real estate market; accounting principles, policies and guidelines; and other factors detailed in the Company's publicly filed documents, including the Company's 2017 Annual Report on Form 10-K. These risks and uncertainties should be considered in evaluating the forward-looking

statements contained herein, and readers are cautioned not to place undue reliance on such statements, which speak only as of date of the report.

These risks and uncertainties, in addition to the risks and uncertainties identified in the Company's 2017 Annual Report on Form 10-K, should be considered in evaluating the forward-looking statements contained herein, and readers are cautioned not to place undue reliance on such statements. Any forward-looking statement speaks only as of the date on which it is made, and the Company undertakes no obligation to update any forward-looking statement to reflect events or circumstances after the date on which it is made. In addition, past results of operations are not necessarily indicative of future results. We undertake no obligation to update or revise any forward-looking statement to reflect events or circumstances arising after the date on which the statement was made, except as otherwise required by law.

Available Information

The Company maintains a website on the Internet at www.oldpoint.com. The Company makes available free of charge, on or through its website, its proxy statements, annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and any amendments to those reports as soon as reasonably practicable after such material is electronically filed with the Securities and Exchange Commission (SEC). This reference to the Company's Internet address shall not, under any circumstances, be deemed to incorporate the information available at such Internet address into this Form 10-Q or other SEC filings. The information available on the Company's Internet website is not part of this Form 10-Q or any other report filed by the Company with the SEC. The public may read and copy any documents the Company files with or furnishes to the SEC at the SEC's Public Reference Room at 100 F Street, N.E., Washington, D.C. 20549. The public may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. The Company's SEC filings can also be obtained on the SEC's website on the Internet at www.sec.gov.

About Old Point Financial Corporation

The Company is the parent company of The Old Point National Bank of Phoebus (the Bank) and Old Point Trust & Financial Services, N. A. (Trust). The Bank is a locally managed community bank serving the Hampton Roads localities of Chesapeake, Hampton, Isle of Wight County, Newport News, Norfolk, Virginia Beach, Williamsburg/James City County and York County. The Bank currently has 19 branch offices. Trust is a wealth management services provider.

On April 1, 2018, the Company acquired Citizens National Bank (Citizens). Under the terms of the merger agreement, Citizens stockholders received 0.1041 shares of Company stock and \$2.19 in cash for each share of Citizens stock. Systems integration was completed in May 2018.

Critical Accounting Policies and Estimates

The accounting and reporting policies of the Company are in accordance with U.S. GAAP and conform to general practices within the banking industry. The Company's financial position and results of operations are affected by management's application of accounting policies, including estimates, assumptions, and judgments made to arrive at the carrying value of assets and liabilities and amounts reported for revenues, expenses, and related disclosures. Different assumptions in the application of these policies could result in material changes in the Company's consolidated financial position and/or results of operations. The Company evaluates its critical accounting estimates and assumptions on an ongoing basis and updates them, as needed. Management has discussed the Company's critical accounting policies and estimates with the Audit Committee of the Board of Directors.

The critical accounting and reporting policies include the Company's accounting for the allowance for loan losses, acquired loans, and goodwill and intangible assets. Accordingly, the Company's significant accounting policies are discussed in this Item 2 and in Note 4 of the Notes to the Consolidated Financial Statements included in this quarterly report on Form 10-Q, and are discussed in further detail in the Company's 2017 Annual Report on Form 10-K.

Executive Overview

The Company's net income for the quarter ended September 30, 2018 was \$1.6 million, or \$0.31 per diluted share, which compares to net income of \$757 thousand, or \$0.15 per diluted share, for the third quarter of 2017. This increase was principally attributable to higher average loan balances and lower provision for loan losses, as evidenced by the \$1.3 million increase period over period in net interest income after the provision for loan losses.

For the nine months ended September 30, 2018 net income was \$3.5 million, or \$0.69 per diluted share. This compares to net income of \$2.9 million, or \$0.57 per diluted share, for the first nine months of 2017. This increase was primarily attributable to year over year increases in net interest income after the provision for loan losses of \$3.5 million offset by a \$2.5 million increase in noninterest expense.

Highlights are as follows:

Net interest income after provision for loan losses for the three and nine months ended September 30, 2018 increased 20.3% and 18.1%, respectively, from the same periods of 2017.

Annualized return on average assets for the third quarter of 2018 was 0.62% compared to 0.32% for the third quarter of 2017. Annualized return on average assets for the nine months ended September 30, 2018 was 0.46% compared to 0.41% for the first nine months of 2017.

The net interest margin for the third quarter of 2018 was 3.67% compared to 3.68% for the same period of 2017. The net interest margin for the nine months ended September 30, 2018 was 3.60% compared to 3.67% during the first nine months of 2017.

Non-performing assets as a percentage of total assets increased to 1.70% at September 30, 2018 from 1.64% at December 31, 2017.

Total assets increased to \$1.0 billion, representing growth of \$43.6 million, or 5.1%, from December 31, 2017 and \$72.9 million, or 7.7%, from September 30, 2017, reflecting the acquisition of Citizens.

Net Interest Income

The principal source of earnings for the Company is net interest income. Net interest income is the difference between interest and fees generated by earning assets and interest expense paid to fund them. Changes in the volume and mix of interest-earning assets and interest-bearing liabilities, as well as their respective yields and rates, have a significant impact on the level of net interest income. The net interest margin is calculated by dividing tax-equivalent net interest income by average earning assets.

For the third quarter of 2018, net interest income was \$8.5 million, an increase of \$784 thousand or 10.1% from the third quarter of 2017. Net interest income, on a fully tax-equivalent basis, for the third quarter of 2018, was \$8.6 million, an increase of 8.1% from the third quarter of 2017. Both increases were primarily due to higher interest and fees on loans resulting from growth in average loan balances. Average loans increased \$82.4 million, or 11.9%, from the third quarter of 2017. The increase was due to both the acquisition of Citizens and organic growth. The average loan yield for the quarter increased by 15 basis points compared to the same period of 2017. The average tax-equivalent yield on earning assets for the third quarter of 2018 was 4.23% compared to 4.06% for the third quarter of 2017. The average rate on interest-bearing liabilities for the quarter ended September 30, 2018 was 0.76%, up from 0.53% for the same period of 2017. Higher deposit and borrowing rates as well as increases in average time deposit and FHLB advance balances relative to lower cost deposits are responsible for this increase. The tax-equivalent net interest margin for the third quarter of 2018 was 3.67%, down slightly from 3.68% in the third quarter of 2017.

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For the nine months ended September 30, 2018, net interest income was \$24.7 million, an increase of \$2.4 million or 10.9% compared to the prior year period. Net interest income, on a fully tax-equivalent basis, was \$25.0 million for the nine months ended September 30, 2018, compared to \$23.0 million for the nine months ended September 30, 2017, an increase of 8.7%. As in the quarterly comparison, the increases were driven principally by higher average loan balances primarily due to organic growth. Average outstanding loans for the nine months ended September 30, 2018 increased \$109.8 million, or 16.7%, compared to the first nine months of 2017. The average tax-equivalent yield increased to 4.11% compared to 4.00% for the first nine months of 2017. Higher rates on deposits and borrowings as well as an increased reliance on borrowings relative to last year lead to an increase of 22 basis points in the average rate on interest-bearing liabilities when comparing the first nine months of 2018 to 2017. The tax-equivalent net interest margin for the first nine months of 2018 was 3.60% compared to 3.67% for the same period of 2017.

The following tables show analyses of average earning assets, interest-bearing liabilities and rates and yields for the periods indicated. Nonaccrual loans are included in loans outstanding.

AVERAGE BALANCE SHEETS, NET INTEREST INCOME AND RATES

	For the quarter ended September 30,					
	2018			2017		
	Average Balance	Interest Income/ Expense	Yield/ Rate**	Average Balance	Interest Income/ Expense	Yield/ Rate**
	(dollars in thousands)					
ASSETS						
Loans*	\$ 777,179	\$ 8,880	4.57 %	\$ 694,783	\$ 7,673	4.42 %
Investment securities:						
Taxable	94,674	510	2.15 %	101,612	487	1.92 %
Tax-exempt*	47,458	368	3.10 %	64,662	584	3.61 %
Total investment securities	142,132	878	2.47 %	166,274	1,071	2.58 %
Interest-bearing due from banks	13,389	68	2.03 %	1,093	4	1.46 %
Federal funds sold	950	5	2.11 %	457	1	0.88 %
Other investments	3,869	75	7.75 %	3,132	49	6.26 %
Total earning assets	937,519	\$ 9,906	4.23 %	865,739	\$ 8,798	4.06 %
Allowance for loan losses	(10,184)			(9,128)		
Other non-earning assets	103,231			97,420		
Total assets	\$ 1,030,566			\$ 954,031		
LIABILITIES AND STOCKHOLDERS' EQUITY						
Time and savings deposits:						
Interest-bearing transaction accounts	\$ 28,001	\$ 2	0.03 %	\$ 27,705	\$ 2	0.03 %
Money market deposit accounts	243,556	140	0.23 %	231,785	90	0.16 %
Savings accounts	88,345	22	0.10 %	84,220	11	0.05 %
Time deposits	235,443	774	1.31 %	207,491	560	1.08 %
Total time and savings deposits	595,345	938	0.63 %	551,201	663	0.48 %
Federal funds purchased, repurchase agreements and other borrowings	32,800	41	0.50 %	27,046	13	0.19 %
Federal Home Loan Bank advances	60,000	320	2.13 %	50,707	161	1.27 %
Total interest-bearing liabilities	688,145	1,299	0.76 %	628,954	837	0.53 %
Demand deposits	238,592			222,429		
Other liabilities	3,382			5,006		
Stockholders' equity	100,447			97,642		
Total liabilities and stockholders' equity	\$ 1,030,566			\$ 954,031		

Net interest margin	\$ 8,607	3.67 %	\$ 7,961	3.68 %
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*Computed on a fully tax-equivalent basis using a 21% rate for 2018 and a 34% rate for 2017; the tax-equivalent adjustment to interest income was \$92 thousand and \$230 thousand for the three months ended September 30, 2018 and 2017, respectively.

**Annualized

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AVERAGE BALANCE SHEETS, NET INTEREST INCOME AND RATES

	For the nine months ended September 30,					
	2018			2017		
	Average Balance	Interest Income/ Expense	Yield/ Rate**	Average Balance	Interest Income/ Expense	Yield/ Rate**
	(dollars in thousands)					
ASSETS						
Loans*	\$767,101	\$25,492	4.43 %	\$657,310	\$21,627	4.39 %
Investment securities:						
Taxable	94,907	1,503	2.11 %	104,059	1,474	1.89 %
Tax-exempt*	51,717	1,186	3.06 %	69,274	1,867	3.59 %
Total investment securities	146,624	2,689	2.45 %	173,333	3,341	2.57 %
Interest-bearing due from banks	6,481	94	1.93 %	1,502	12	1.07 %
Federal funds sold	1,164	15	1.72 %	1,096	6	0.73 %
Other investments	4,160	210	6.73 %	2,075	98	6.30 %
Total earning assets	925,530	\$28,500	4.11 %	835,316	\$25,084	4.00 %
Allowance for loan losses	(10,052)			(8,851)		
Other non-earning assets	98,819			102,726		
Total assets	\$1,014,297			\$929,191		
LIABILITIES AND STOCKHOLDERS' EQUITY						
Time and savings deposits:						
Interest-bearing transaction accounts	\$28,159	\$8	0.04 %	\$28,121	\$7	0.03 %
Money market deposit accounts	238,520	347	0.19 %	234,446	202	0.11 %
Savings accounts	87,596	54	0.08 %	82,160	31	0.05 %
Time deposits	227,914	2,088	1.22 %	206,150	1,599	1.03 %
Total time and savings deposits	582,189	2,497	0.57 %	550,877	1,839	0.45 %
Federal funds purchased, repurchase agreements and other borrowings	30,442	93	0.41 %	24,684	26	0.14 %
Federal Home Loan Bank advances	68,223	931	1.82 %	25,879	233	1.20 %
Total interest-bearing liabilities	680,854	3,521	0.69 %	601,440	2,098	0.47 %
Demand deposits	231,916			226,103		
Other liabilities	3,243			5,477		
Stockholders' equity	98,284			96,171		
Total liabilities and stockholders' equity	\$1,014,297			\$929,191		
Net interest margin		\$24,979	3.60 %		\$22,986	3.67 %

*Computed on a fully tax-equivalent basis using a 21% rate for 2018 and a 34% rate for 2017; the tax-equivalent adjustment to interest income was \$293 thousand and \$730 thousand for the nine months ended September 30, 2018 and 2017, respectively.

**Annualized

Provision for Loan Losses

The provision for loan losses is a charge against earnings necessary to maintain the allowance for loan losses at a level consistent with management's evaluation of the portfolio. This expense is based on management's estimate of probable credit losses inherent to the loan portfolio. Management's evaluation included credit quality trends, collateral values, discounted cash flow analysis, loan volumes, geographic, borrower and industry concentrations, the findings of internal credit quality assessments and results from external regulatory examinations. These factors, as well as identified impaired loans, historical losses and current economic and business conditions, were used in developing

estimated loss factors for determining the loan loss provision. Based on its analysis of the adequacy of the allowance for loan losses, management concluded that the provision was appropriate.

The provision for loan losses was \$1.8 million in the first nine months of 2018, compared to \$2.9 million in the first nine months of 2017. For the three months ended September 30, 2018 and 2017, the Company recorded \$749 thousand and \$1.3 million, respectively.

The decline in the provision for loan losses for the three and nine months ended September 30, 2018 versus the same periods in 2017 was largely due to a decline in net loan growth, exclusive of the loans acquired in the Citizens acquisition. The loans acquired from Citizens were recorded at fair value at the acquisition date without carrying over the associated allowance for loan losses previously established by Citizens. Impacts of the decline in organic loan growth were offset by increases in specific reserves.

Net loans charged off as a percent of average loans on an annualized basis were 0.19% for the first nine months of 2018, or \$1.4 million, compared to 0.42%, or \$2.2 million, in the first nine months of 2017. In the three months ended September 30, 2018 and 2017, net loans charged off as a percent of total loans on an annualized basis were 0.24% and 0.59%, respectively.

Noninterest Income

Noninterest income was \$3.4 million and \$9.9 million, respectively, in the three and nine months ended September 30, 2018, an increase of \$219 thousand or 6.9% from the third quarter of 2017 and a decrease \$97 thousand or 1.0% from the nine months ended September 30, 2017. The declines between the 2017 and 2018 nine-month periods resulted primarily from a nonrecurring gain of \$550 thousand associated with the acquisition in the second quarter of 2017 of the outstanding interest in Old Point Mortgage, LLC.

Service charges on deposit accounts increased \$94 thousand, or 9.4%, when comparing the third quarters of 2018 and 2017 and increased \$199 thousand, or 7.0%, when comparing the nine months ended September 30, 2018 and 2017. Other service charges, commission, and fees increased \$30 thousand, or 3.6%, when comparing the third quarters of 2018 and 2017 and increased \$106 thousand, or 4.1%, when comparing the first nine months of 2018 and 2017, which was partially offset by lower fiduciary and asset management fees. Gains on sales of securities were \$120 thousand and \$89 thousand for the nine months ended September 30, 2018 and 2017, respectively, and \$2 thousand for the three months ended September 30, 2017 with no gain or loss activity for the comparable 2018 period.

Noninterest Expense

Noninterest expense increased \$2.5 million or 9.6% when comparing the nine months ended September 30, 2018 to the same period in 2017 and increased \$518 thousand or 5.8% when comparing the third quarters of 2018 and 2017. Both the linked quarter and year ago quarter increases were mostly due to higher salaries and employee benefits associated with normal market driven adjustments, but also included the addition of salaries and related severance payments associated with the acquisitions of Citizens and OPM, non-recurring merger expenses, and losses on OREO.

Merger expenses totaled \$48 thousand for the third quarter of 2018 and \$644 thousand for the first nine months of 2018. There were no merger expenses for the comparative periods.

Total salaries and benefits costs increased \$504 thousand, or 9.9%, when comparing the third quarters of 2018 and 2017 and increased \$1.4 million, or 8.8%, when comparing the first nine months of 2018 and 2017. Data processing expenses increased \$51 thousand, or 19.2%, in the third quarter of 2018 relative to the third quarter of 2017 and increased \$244 thousand, or 32.6%, in the nine months ended September 30, 2018 compared to the same period in 2017. Several factors lead to these increases including the Citizens acquisition and increased processing expenses for debit cards and electronic banking services. FDIC insurance expense was also significantly elevated for the three and nine months ended September 30, 2018, increasing \$32 thousand, or 25.0%, and \$215 thousand, or 66.8%, respectively. Trailing twelve month earnings are a significant factor in the insurance premium calculation, so the substantial net loss recorded by the Company in the fourth quarter of 2017 resulting from the termination of the pension plan and the deferred tax asset write-down precipitated by the Tax Cuts and Jobs Act increased the premium considerably.

The Company's income tax expense for the third quarter and first nine months of 2018 increased \$171 thousand and \$190 thousand, respectively, when compared to the same periods in 2017. In addition to overall higher net income, the increases were due to non-deductible merger expenses and lower income from tax-exempt sources outweighing the benefit of a lower statutory federal income tax rate. The Company's effective tax rate remains low due to its investments in tax-exempt securities and bank-owned life insurance and its receipt of federal income tax credits for its investment in certain housing projects. The effective federal income tax rates for the three and nine months ended September 30, 2018 were 6.72% and 4.95%, respectively; the effective tax rates for the three and nine months ended September 30, 2017 were (7.99)% and (0.21)%, respectively.

Balance Sheet Review

Unless otherwise noted, all comparisons in this section are between balances at December 31, 2017 and September 30, 2018.

Total assets as of September 30, 2018 were \$1.0 billion, an increase of \$43.6 million or 4.4%. The acquisition of Citizens is responsible for substantially all of the year-to-date growth. The fair value of assets acquired was \$50.4 million as of the date of acquisition. Net loans held for investment increased \$40.1 million, or 5.5%. Excluding the \$42.8 million fair value of acquired loans at the date of acquisition loans held for investment declined modestly. The Company sold an \$8.8 million pool of consumer automobile loans during the first quarter and has experienced accelerated payoffs in recent months. Cash and cash equivalents increased \$14.2 million, or 98.6%, and securities available-for-sale declined \$14.8 million, or 9.4%.

Total deposits increased \$57.7 million, or 7.4%, to \$841.3 million at September 30, 2018. This includes the addition of deposits from the acquisition of Citizens, the fair value of which was \$44.0 million at the date of acquisition. Noninterest-bearing deposits increased \$14.8 million, or 6.6%, savings deposits increased \$22.0 million, or 6.4%, and time deposits increased \$20.9 million, or 9.8%. Total borrowings decreased \$17.2 million, or 17.5%.

Average assets for the first nine months of 2018 were \$1.0 billion compared to \$929.2 million for the first nine months of 2017, an increase of 9.2%. Comparing the first nine months of 2018 to the first nine months of 2017, average loans grew \$109.8 million, and average investment securities declined \$26.7 million. Total average deposits increased \$37.1 million, and average borrowings increased \$48.1 million.

The Company's holdings of "Alt-A" type mortgage loans such as adjustable rate and nontraditional type loans were inconsequential, amounting to less than 1.0% of the Company's loan portfolio as of September 30, 2018.

The Company does not have a formal program for subprime lending. The Company is required by law to comply with the requirements of the Community Reinvestment Act (the CRA), which imposes on financial institutions an affirmative and ongoing obligation to meet the credit needs of their local communities, including low- and moderate-income borrowers. In order to comply with the CRA and meet the credit needs of its local communities, the Company finds it necessary to make certain loans with subprime characteristics.

Liquidity

Liquidity is the ability of the Company 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, investments in securities and loans maturing within one year. The Company's internal sources of such liquidity are deposits, loan and investment repayments and securities available-for-sale. As of September 30, 2018, the Bank's unpledged, available-for-sale securities totaled \$70.2 million. The Company's primary external source of liquidity is advances from the FHLB.

A major source of the Company's liquidity is its large, stable deposit base. In addition, secondary liquidity sources are available through the use of borrowed funds if the need should arise, including secured advances from the FHLB. As of the end of the third quarter of 2018, the Company had \$87.0 million in additional FHLB borrowing availability based on loans and securities currently available for pledging, less advances currently outstanding. The Company believes that the availability at the FHLB is sufficient to meet future cash-flow needs. The Company also has available short-term, unsecured borrowed funds in the form of federal funds lines of credit with correspondent banks. As of the end of the third quarter of 2018, the Company had \$55.0 million available in federal funds lines to address any short-term borrowing needs.

As disclosed in the Company's consolidated statements of cash flows, net cash provided by operating activities was \$7.4 million, net cash provided by investing activities was \$11.8 million and net cash used in financing activities was \$5.1 million for the nine months ended September 30, 2018. Combined, this contributed to a \$14.2 million increase in cash and cash equivalents for the nine months ended September 30, 2018.

Management is not aware of any market or institutional trends, events or uncertainties that are expected to have a material effect on the liquidity, capital resources or operations of the Company. Nor is management aware of any current recommendations by regulatory authorities that would have a material effect on liquidity, capital resources or operations.

Based on the Company's management of liquid assets, the availability of borrowed funds, and the Company's ability to generate liquidity through liability funding, management believes that the Company maintains overall liquidity sufficient to satisfy its depositors' requirements and to meet its customers' future borrowing needs.

Notwithstanding the foregoing, the Company's ability to maintain sufficient liquidity may be affected by numerous factors, including economic conditions nationally and in the Company's markets. Depending on its liquidity levels, its capital position, conditions in the capital markets and other factors, the Company may from time to time consider the issuance of debt, equity, other securities or other possible capital markets transactions, the proceeds of which could provide additional liquidity for the Company's operations.

Nonperforming Assets

Nonperforming assets consist of nonaccrual loans, loans past due 90 days or more and accruing interest, restructured loans that are accruing interest and not performing according to their modified terms, and OREO. OREO consists of real estate from a foreclosure on loan collateral.

The majority of the loans past due 90 days or more and accruing interest are small business or student loans with principal and interest amounts that are 97 - 100% guaranteed by the federal government. When a loan changes from "past due 90 days or more and accruing interest" status to "nonaccrual" status, the loan is reviewed for impairment. In most cases, if the loan is considered impaired, then the difference between the value of the collateral and the principal amount outstanding on the loan is charged off. If the Company is waiting on an appraisal to determine the collateral's value or is in negotiations with the borrower or other parties that may affect the value of the collateral, management allocates funds to the allowance for loan losses to cover the anticipated deficiency, based on information available to management at that time.

In the case of TDRs, the restructuring may be to modify to an unsecured loan (e.g., a short sale) that the borrower can afford to repay. In these circumstances, the entire balance of the loan would be specifically allocated for, unless the present value of expected future cash flows was more than the current balance on the loan. It would not be charged off if the loan documentation supports the borrower's ability to repay the modified loan.

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The following table presents information on nonperforming assets, as of the dates indicated:

NONPERFORMING ASSETS

	September 30, 2018 (in thousands)	December 31, 2017	Increase (Decrease)
Nonaccrual loans			
Commercial	\$308	\$836	\$ (528)
Real estate-construction	418	722	(304)
Real estate-mortgage (1)	12,283	11,324	959
Total nonaccrual loans	\$13,009	\$12,882	\$ 127
Loans past due 90 days or more and accruing interest			
Commercial	\$419	\$471	\$ (52)
Real estate-mortgage (1)	1,636	306	1,330
Consumer loans (2)	2,249	2,401	(152)
Other	10	4	6
Total loans past due 90 days or more and accruing interest	\$4,314	\$3,182	\$ 1,132
Restructured loans			
Commercial	\$80	\$98	\$ (18)
Real estate-construction	93	92	1
Real estate-mortgage (1)	12,197	14,781	(2,584)
Total restructured loans	\$12,370	\$14,971	\$ (2,601)
Less nonaccrual restructured loans (included above)	8,121	8,561	(440)
Less restructured loans currently in compliance (3)	4,249	6,410	(2,161)
Net nonperforming, accruing restructured loans	\$-	\$-	\$ -
Nonperforming loans	\$17,323	\$16,064	\$ 1,259
Other real estate owned			
Real estate-construction	\$133	\$-	\$ 133
Nonfarm nonresidential properties	-	-	-
Total other real estate owned	\$133	\$-	\$ 133
Total nonperforming assets	\$17,456	\$16,064	\$ 1,392

(1) The real estate-mortgage segment includes residential 1 – 4 family, commercial real estate, second mortgages and equity lines of credit.

(2) Amounts listed include student loans with principal and interest amounts that are 97 - 98% guaranteed by the federal government. The portion of these guaranteed loans that is past due 90 days or more totaled \$2.0 million at September 30, 2018 and \$2.3 million at December 31, 2017.

(3) As of September 30, 2018 and December 31, 2017, all of the Company's restructured accruing loans were performing in compliance with their modified terms.

Nonperforming assets as of September 30, 2018 were \$17.5 million, \$1.4 million higher than nonperforming assets as of December 31, 2017. Nonaccrual loans increased \$127 thousand when comparing the balances as of September 30, 2018 to December 31, 2017. See Note 4 of the Notes to the Consolidated Financial Statements included in this quarterly report on Form 10-Q for additional information about the change in nonaccrual loans. Management has set

aside specific allocations on those loans where it is deemed appropriate based on the information available to management at this time regarding the cash flow, anticipated financial performance, and collateral securing these loans. Management believes that the collateral and/or discounted cash flow on these loans will be sufficient to cover balances for which it has no specific allocation.

The majority of the balance of nonaccrual loans at September 30, 2018 was related to a few large credit relationships. Of the \$13.0 million of nonaccrual loans at September 30, 2018, \$10.4 million, or approximately 78.8%, was comprised of four credit relationships. All loans in these relationships have been analyzed to determine whether the cash flow of the borrower and the collateral pledged to secure the loans is sufficient to cover outstanding principal balances. The Company has set aside specific allocations for those loans without sufficient cash flow or collateral and charged off any balance that management does not expect to collect.

Loans past due 90 days or more and accruing interest increased \$1.1 million. As of September 30, 2018, \$2.4 million of the \$4.3 million of loans past due 90 days or more and accruing interest were government-guaranteed small business and student loans on which the Company expects to experience minimal losses. Because the federal government has provided guarantees of repayment of these loans in an amount ranging from 97% to 100% of the total principal and interest of the loans, management does not expect even significant increases in past due student loans to have a material effect on the Company.

Total restructured loans decreased by \$2.6 million from December 31, 2017 to September 30, 2018 primarily due to paydowns and charge-offs. All accruing TDRs are performing in accordance with their modified terms and have been evaluated for impairment, with any necessary reserves recorded as needed.

The Company acquired one OREO property in the first quarter of 2018 through a real estate foreclosure and two properties in the second quarter of 2018 through the Citizens acquisition; however, only one of the three properties remained as of September 30, 2018.

Management believes the Company has excellent credit quality review processes in place to identify problem loans quickly. This allows management to work with problem loan relationships to identify any payment shortfall and assist these borrowers to improve performance or correct the problems.

Allowance for Loan Losses

The allowance for loan losses is based on several components. The first component of the allowance for loan losses is determined based on specifically identified loans that may become impaired. These loans are individually analyzed for impairment and include nonperforming loans and both performing and nonperforming TDRs. This component may also include loans considered impaired for other reasons, such as outdated financial information on the borrower or guarantors or financial problems of the borrower, including operating losses, marginal working capital, inadequate cash flow, or business interruptions. Changes in TDRs and nonperforming loans affect the dollar amount of the allowance. Increases in the impairment allowance for TDRs and nonperforming loans are reflected as an increase in the allowance for loan losses except in situations where the TDR or nonperforming loan does not require a specific allocation (i.e. the discounted present value of expected future cash flows or the collateral value is considered sufficient).

The majority of the Company's TDRs and nonperforming loans are collateralized by real estate. When reviewing loans for impairment, the Company obtains current appraisals when applicable. If the Company is waiting on an appraisal to determine the collateral's value or is in negotiations with the borrower or other parties that may affect the value of the collateral, any loan balance that is in excess of the estimated appraised value is allocated in the allowance. As of September 30, 2018 and December 31, 2017, the impaired loan component of the allowance for loan losses was \$229 thousand and \$95 thousand, respectively.

The second component of the allowance consists of qualitative factors and includes items such as economic conditions, growth trends, loan concentrations, changes in certain loans, changes in underwriting, changes in management and legal and regulatory changes.

Historical loss is the final component of the allowance for loan losses and is calculated based on the migration of loans from performing to charge-off over a period of time that management deems appropriate to provide a reasonable estimate of losses inherent in the loan portfolio. For the last five quarterly calculations including the September 30, 2018 calculation, the historical loss was based on eight migration periods of twelve quarters each.

Both the historical loss and qualitative factor components of the allowance are applied to loans evaluated collectively for impairment. The portfolio is segmented based on the loan classifications set by the Federal Financial Institutions Examination Council in the instructions for the call report applicable to the Bank. Consumer loans not secured by real estate and made to individuals for household, family and other personal expenditures are segmented into pools based

on whether the loan's payments are current (including loans 1 – 29 days past due), or are 30 – 59 days past due, 60 – 89 days past due, or 90 days or more past due. All other loans, including loans to consumers that are secured by real estate, are segmented by the Company's internally assigned risk grades: substandard, other assets especially mentioned (OAEM, rated just above substandard), and pass (all other loans).

On a combined basis, the historical loss and qualitative factor components amounted to \$10.0 million as of September 30, 2018 and \$9.4 million at December 31, 2017.

The allowance for loan losses was 1.31% of total loans on September 30, 2018 and 1.28% on December 31, 2017. As of September 30, 2018, the allowance for loan losses was 59.1% of nonperforming loans and 58.6% of nonperforming assets; this compares to 58.8% of both nonperforming loans and nonperforming assets as of December 31, 2017. Management believes it has provided an adequate reserve for nonperforming loans at September 30, 2018.

Acquired loans are recorded at their fair value at acquisition date without carryover of the acquiree's previously established ALL, as credit discounts are included in the determination of fair value. The fair value of the loans is determined using market participant assumptions in estimating the amount and timing of both principal and interest cash flows expected to be collected on the loans and then applying a market-based discount rate to those cash flows. During evaluation upon acquisition, acquired loans are also classified as either acquired impaired (or PCI) or acquired performing.

Acquired impaired loans reflect credit quality deterioration since origination, as it is probable at acquisition that the Company will not be able to collect all contractually required payments. These acquired impaired loans are accounted for under ASC 310-30, Receivables – Loans and Debt Securities Acquired with Deteriorated Credit Quality. The acquired impaired loans are segregated into pools based on loan type and credit risk. Loan type is determined based on collateral type, purpose, and lien position. Credit risk characteristics include risk rating groups, nonaccrual status, and past due status. For valuation purposes, these pools are further disaggregated by maturity, pricing characteristics, and re-payment structure. Acquired impaired loans are written down at acquisition to fair value using an estimate of cash flows deemed to be collectible.

A loan will be removed from a pool (at its carrying value) only if the loan is sold, foreclosed, or assets are received in full satisfaction of the loan. For purposes of removing the loan from the pool, the carrying value is deemed to equal the amount of principal cash flows received in lieu of the loan balance. This treatment ensures that the percentage yield calculation used to recognize accretable yield on the pool of loans is not affected.

Quarterly, management will evaluate acquired impaired loans based on updated future expected cash flows. The excess of the cash flows expected to be collected over a pool's carrying value is considered to be the accretable yield and is recognized as interest income over the estimated life of the loan or pool using the effective yield method. The accretable yield may change due to changes in the timing and amounts of expected cash flows; these changes are disclosed in Note 4 "Loans and Allowance for Loan Losses."

The excess of the undiscounted contractual balances due over the cash flows expected to be collected is considered to be the nonaccretable difference, which represents the estimate of credit losses expected to occur and was considered in determining the fair value of loan at the acquisition date. Any subsequent increases in expected cash flows over those expected at the acquisition date in excess of fair value are adjusted through an increase in the accretable yield on a prospective basis; any decreases in expected cash flows attributable to credit deterioration are recognized by recording a provision for loan losses.

The Company's policy is to remove an individual loan from a pool based on comparing the amount received from its resolution with its contractual amount. Any difference between these amounts is absorbed by the nonaccretable difference for the entire pool. This removal method assumes that the amount received from resolution approximates pool performance expectations. The remaining accretable yield balance is unaffected and any material change in remaining effective yield caused by this removal method is addressed by the quarterly cash flow evaluation process for each pool. For loans that are resolved by payment in full, there is no release of the nonaccretable difference for the pool because there is no difference between the amount received at resolution and the contractual amount of the loan. The acquired impaired loans are and will continue to be subject to the Company's internal and external credit review and monitoring. If further credit deterioration is experienced, such deterioration will be measured and the provision for loan losses will be increased.

Acquired performing loans are accounted for under ASC 310-20, Receivables – Nonrefundable Fees and Other Costs. The difference between the fair value and unpaid principal balance of the loan at acquisition date (premium or discount) is amortized or accreted into interest income over the life of the loans. If the acquired performing loan has revolving privileges, it is accounted for using the straight-line method; otherwise, the effective interest method is used. The adequacy of the remaining discount as compared to the reserve that would be required under the Company's allowance for loan loss methodology is evaluated quarterly. Should the methodology reserve exceed the remaining discount, additional provision would be recognized.

Capital Resources

Total stockholders' equity as of September 30, 2018 was \$99.6 million, an increase of \$3.2 million or 3.3% from \$96.4 million at December 31, 2017. The increase was the result of the issuance of common stock related to the Citizens acquisition and increased retained earnings offsetting an increase in the net unrealized loss on available-for-sale securities, a component of accumulated other comprehensive loss on the consolidated balance sheets. The increase in the unrealized loss position was driven by increases in market rates during the quarter.

The maintenance of appropriate levels of capital is a management priority and is monitored on a regular basis. The Company's principal goals related to the maintenance of capital are to provide adequate capital to support the Company's risk profile consistent with the board approved risk appetite, provide financial flexibility to support future growth and client needs, comply with relevant laws, regulations, and supervisory guidance, and provide a competitive return to stockholders. Risk-based capital ratios, which include CET1 capital, Tier 1 capital and Total capital are calculated based on regulatory guidance related to the measurement of capital and risk-weighted assets.

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The Economic Growth, Regulatory Relief and Consumer Protection Act of 2018 (EGRRCPA), enacted in May 2018, contains a variety of provisions that will affect regulations applicable to the Company and the Bank. Certain provisions of the EGRRCPA were effective immediately, while others depend upon future rulemaking by federal banking regulatory agencies. The EGRRCPA required action by the Federal Reserve Board to expand the applicability of its small bank holding company policy statement, which, among other things, exempts certain bank holding companies from reporting consolidated regulatory capital ratios and from minimum regulatory capital requirements that apply to other bank holding companies. In August 2018, the Federal Reserve Board issued an interim final rule provisionally expanding the applicability of the small bank holding company policy statement to bank holding companies with consolidated total assets of less than \$3 billion. The statement previously applied only to bank holding companies with consolidated total assets of less than \$1 billion. As a result of the interim final rule, which was effective upon its issuance, the Company expects that it will be treated as a small bank holding company and will no longer be subject to regulatory capital requirements. Comments on the interim final rule closed on October 29, 2018.

The following is a summary of the Company's capital ratios at September 30, 2018 and December 31, 2017. As shown below, these ratios were all well above the recommended regulatory minimum levels.

	2018		2017	
	Regulatory Minimums	September 30, 2018	Regulatory Minimums	December 31, 2017
Common Equity Tier 1 Capital to Risk-Weighted Assets	4.50	% 11.37	% 4.50	% 11.18
Tier 1 Capital to Risk-Weighted Assets	6.00	% 11.37	% 6.00	% 11.18
Tier 1 Leverage to Average Assets	4.00	% 9.84	% 4.00	% 9.98
Total Capital to Risk-Weighted Assets	8.00	% 12.53	% 8.00	% 12.28
Capital Conservation Buffer	1.88	% 4.53	% 1.25	% 4.28
Risk-Weighted Assets (in thousands)		\$ 890,740		\$ 863,187

Book value per share was \$19.26 at September 30, 2018 as compared to \$19.50 at September 30, 2017. Cash dividends were \$1.7 million or \$0.33 per share in the first nine months of 2018 and \$1.6 million or \$0.33 per share in the first nine months of 2017.

Contractual Obligations

In the normal course of business there are various outstanding contractual obligations of the Company that will require future cash outflows. In addition, there are commitments and contingent liabilities, such as commitments to extend credit that may or may not require cash outflows.

The Company obtained a loan maturing on April 1, 2023 from a correspondent bank during the second quarter of 2018 to provide partial funding for the Citizens acquisition. The terms of the loan include a LIBOR based interest rate that adjusts monthly and quarterly principal curtailments. At September 30, 2018 the outstanding balance was \$2.9 million, and the then-current interest rate was 4.48%.

The loan agreement with the lender contains financial covenants including minimum return on average asset ratio and Bank capital leverage ratio, maintenance of a well-capitalized position as defined by regulatory guidance and a maximum level of non-performing assets as a percentage of capital plus the allowance for loan losses. The Company was in compliance with each covenant at September 30, 2018.

Other than the loan discussed immediately above, as of September 30, 2018, there have been no material changes outside the ordinary course of business in the Company's contractual obligations disclosed in the Company's 2017 Annual Report on Form 10-K.

Off-Balance Sheet Arrangements

As of September 30, 2018, there were no material changes in the Company's off-balance sheet arrangements disclosed in the Company's 2017 Annual Report on Form 10-K.

Item 3. Quantitative and Qualitative Disclosures About Market Risk.

Market risk is the risk of loss arising from adverse changes in the fair value of financial instruments due to changes in interest rates, exchange rates, and equity prices. The Company's primary component of market risk is interest rate volatility. Fluctuations in interest rates will impact the amount of interest income and expense the Company receives or pays on a significant portion of its assets and liabilities and the market value of its interest-earning assets and interest-bearing liabilities, excluding those which have a very short-term until maturity. Management is responsible for reviewing the interest rate sensitivity position of the Company and establishing policies to monitor and limit exposure to this risk.

Three complementary modeling techniques are utilized to measure and monitor the exposure to interest rate risk: static gap analysis, earnings simulation analysis, and economic value of equity (EVE) analysis. Static gap measures the aggregate dollar volume of rate-sensitive assets relative to rate-sensitive liabilities re-pricing over various time horizons. This metric does not effectively capture the re-pricing characteristics or embedded optionality of the Company's assets and liabilities, so it is not relied upon or addressed here. Earnings simulation measures the potential effect of changes in market interest rates on future net interest income. This analysis incorporates management's assumptions for product pricing and pre-payment expectations and is the Company's preferred tool to assess its interest rate sensitivity in the short- to medium-term. The simulation utilizes a "static" balance sheet approach, which assumes that management makes no changes to the composition of the balance sheet to mitigate the impact of interest rate changes. EVE modeling estimates the fair value of assets and liabilities in different interest rate environments using discounted cash flow analysis. The net economic value of equity is the economic value of all assets minus the economic value of all liabilities. This measure provides an indication of the future earnings capacity of the balance sheet, and the change in EVE over different rate scenarios is a measure of long-term interest rate risk. The Company places less emphasis on EVE results due to the inherent imprecision of cash flow estimations and the limited utility of a static balance sheet assumption over the long-term.

The Company determines the overall magnitude of interest sensitivity risk and then formulates policies governing asset generation and pricing, funding sources and pricing, and off-balance sheet commitments. These decisions are based on management's expectations regarding future interest rate movements, the state of the national and regional economy, and other financial and business risk factors.

When the Company is liability sensitive, net interest income should improve if interest rates fall since liabilities will reprice faster than assets (depending on the optionality or prepayment speeds of the assets). Conversely, if interest rates rise, net interest income should decline. When the Company is asset sensitive, net interest income should improve if interest rates rise and fall if rates fall. The rate change model assumes that these changes will occur gradually over the course of a year. The earnings simulation results for the September 30, 2018 calculation indicate a moderately asset-sensitive position. The results for the September 30, 2017 calculation are seemingly incongruous, as net interest income was projected to decrease with both rising and falling rates. This was a result of the persistent low-rate environment. Rates on certain deposits and other funding liabilities could not realistically decrease materially, so they were more sensitive to rising rates than falling rates.

The table below shows the Company's interest rate sensitivity for the periods and rate scenarios presented (dollars in thousands):

	Change In Net Interest Income			
	As of September 30,			
	2018		2017	
Change in interest Rates	%	\$	%	\$
+300 basis points	1.62 %	574	(0.29)%	(92)
+200 basis points	1.15 %	407	(0.08)%	(26)
+100 basis points	0.59 %	208	0.10 %	30
Unchanged	0.00 %	-	0.00 %	-
-50 basis points	(0.44)%	(156)	(0.77)%	(242)
-100 basis points	(1.17)%	(414)	(1.52)%	(478)

Item 4. Controls and Procedures.

Disclosure Controls and Procedures. Management evaluated, with the participation of the Company's Chief Executive Officer and Chief Financial Officer, the effectiveness of the Company's disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934, as amended (the Exchange Act)) as of the end of the period covered by this report. Based on that evaluation, the Company's Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures are effective as of the end of the period covered by this report to ensure that information required to be disclosed in the reports that the Company 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 and that such information is accumulated and communicated to management, including the Company's Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

In designing and evaluating its disclosure controls and procedures, management recognized that disclosure controls and procedures, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the disclosure controls and procedures are met. The design of any disclosure controls and procedures also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions.

Internal Control over Financial Reporting. Management is responsible for establishing and maintaining adequate internal control over financial reporting (as defined in Rule 13a-15(f) under the Exchange Act). No changes in the

Company's internal control over financial reporting occurred during the fiscal quarter ended September 30, 2018 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting. Because of its inherent limitations, a system of internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

PART II - OTHER INFORMATION

Item 1. Legal Proceedings.

There are no pending legal proceedings to which the Company, or any of its subsidiaries, is a party or to which the property of the Company or any of its subsidiaries is subject that, in the opinion of management, may materially impact the financial condition of the Company.

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Item 1A. Risk Factors.

There have been no material changes in the risk factors faced by the Company from those disclosed in the Company's 2017 Annual Report on Form 10-K and quarterly report on Form 10-Q for the period ended September 30, 2018.

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

Pursuant to the Company's equity compensation plans, participants may pay the exercise price of certain awards or satisfy tax withholding requirements associated with awards by surrendering shares of the Company's common stock that the participants already own. Shares surrendered by participants of these plans are repurchased at current market value pursuant to the terms of the applicable awards. During the three months ended September 30, 2018, the Company did not repurchase any shares related to the exercise of awards.

During the three months ended September 30, 2018, the Company did not repurchase any shares pursuant to the Company's stock repurchase program. The Company is authorized to repurchase, during any given calendar year, up to an aggregate of 5 percent of the shares of the Company's common stock outstanding as of January 1 of that calendar year.

Item 3. Defaults Upon Senior Securities.

None.

Item 4. Mine Safety Disclosures.

None.

Item 5. Other Information.

The Company has made no changes to the process by which security holders may recommend nominees to its board of directors, which is discussed in the Company's Proxy Statement for the Company's 2018 Annual Meeting of Stockholders.

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Item 6. Exhibits.

Exhibit No.	Description
2.1	<u>Agreement and Plan of Reorganization, dated as of October 27, 2017, by and among Old Point Financial Corporation, The Old Point National Bank of Phoebus, and Citizens National Bank (incorporated by reference to Exhibit 2.1 to Form 8-K filed November 2, 2017)</u>
3.1	<u>Articles of Incorporation of Old Point Financial Corporation, as amended effective June 22, 2000 (incorporated by reference to Exhibit 3.1 to Form 10-K filed March 12, 2009)</u>
3.1.1	<u>Articles of Amendment to Articles of Incorporation of Old Point Financial Corporation, effective May 26, 2016 (incorporated by reference to Exhibit 3.1.1 to Form 8-K filed May 31, 2016)</u>
3.2	<u>Bylaws of Old Point Financial Corporation, as amended and restated August 9, 2016 (incorporated by reference to Exhibit 3.2 to Form 10-Q filed August 10, 2016)</u>
31.1	<u>Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002</u>
31.2	<u>Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002</u>
32.1	<u>Certification of Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002</u>
101	The following materials from Old Point Financial Corporation's quarterly report on Form 10-Q for the quarter ended September 30, 2018, formatted in XBRL (Extensible Business Reporting Language), filed herewith: (i) Consolidated Balance Sheets (unaudited for September 30, 2018), (ii) Consolidated Statements of Income (unaudited), (iii) Consolidated Statements of Comprehensive Income (unaudited), (iv) Consolidated Statements of Changes in Stockholders' Equity (unaudited), (v) Consolidated Statements of Cash Flows (unaudited), and (vi) Notes to Consolidated Financial Statements (unaudited)

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.

OLD POINT FINANCIAL CORPORATION

November 8, 2018 /s/Robert F. Shuford, Sr.
 Robert F. Shuford, Sr.
 Chairman, President & Chief Executive Officer
 (Principal Executive Officer)

November 8, 2018 /s/Jeffrey W. Farrar
 Jeffrey W. Farrar
 Chief Financial Officer & Senior Vice President/Finance
 (Principal Financial & Accounting Officer)

