OLD POINT FINANCIAL CORP
Form 10-Q
August 09, 2013

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2013

or

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

For the transition period from____________ to___________

Commission File Number: 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 o No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes o No

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

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

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

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

4,959,009 shares of common stock ($5.00 par value) outstanding as of July 31, 2013

OLD POINT FINANCIAL CORPORATION

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PART I – FINANCIAL INFORMATION

Item 1. Financial Statements.

Old Point Financial Corporation and Subsidiaries
Consolidated Balance Sheets

	June 30, 2013 (unaudited)	December 31, 2012
Assets		
Cash and due from banks	$14,012,831	$15,982,070
Interest-bearing due from banks	40,214,328	24,732,329
Federal funds sold	943,365	1,602,847
Cash and cash equivalents	55,170,524	42,317,246
Securities available-for-sale, at fair value	258,583,381	329,455,812
Securities held-to-maturity (fair value approximates $11,402,809 and $573,500)	11,412,681	570,000
Restricted securities	2,378,100	2,561,900
Loans, net of allowance for loan losses of $7,295,952 and $7,324,310	462,211,798	463,808,457
Premises and equipment, net	35,508,997	32,528,350
Bank-owned life insurance	22,256,631	21,824,197
Foreclosed assets, net of valuation allowance of $1,723,658 and $1,870,285	6,559,191	6,573,398
Other assets	12,800,048	7,859,344
Total assets	$866,881,351	$907,498,704
Liabilities & Stockholders' Equity		
Deposits:		
Noninterest-bearing deposits	$177,839,199	$176,740,312
Savings deposits	270,821,034	268,252,782
Time deposits	281,707,695	308,822,642
Total deposits	730,367,928	753,815,736
Overnight repurchase agreements	25,641,883	35,945,800
Term repurchase agreements	410,651	1,279,574
Federal Home Loan Bank advances	25,000,000	25,000,000
Accrued expenses and other liabilities	2,963,605	2,157,558
Total liabilities	784,384,067	818,198,668
Commitments and contingencies		
Stockholders' equity:		
Common stock, $5 par value, 10,000,000 shares authorized;4,959,009 shares issued and outstanding	24,795,045	24,795,045
Additional paid-in capital	16,391,845	16,391,845
Retained earnings	49,724,841	48,304,609
Accumulated other comprehensive loss, net	(8,414,447)	(191,463)
Total stockholders' equity	82,497,284	89,300,036
Total liabilities and stockholders' equity	$866,881,351	$907,498,704

See Notes to Consolidated Financial Statements.

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Old Point Financial Corporation and Subsidiaries
Consolidated Statements of Income

	Three Months Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
	(unaudited)		(unaudited)	
Interest and Dividend Income:				
Interest and fees on loans	$5,891,576	$6,749,689	$11,899,269	$13,818,466
Interest on due from banks	18,782	10,008	32,807	26,280
Interest on federal funds sold	291	460	751	763
Interest on securities:				
Taxable	1,252,486	1,379,414	2,576,536	2,600,900
Tax-exempt	287,389	148,232	551,982	242,209
Dividends and interest on all other securities	26,023	23,815	44,118	45,192
Total interest and dividend income	7,476,547	8,311,618	15,105,463	16,733,810
Interest Expense:				
Interest on savings deposits	68,669	94,184	155,855	188,239
Interest on time deposits	795,843	963,549	1,649,735	1,938,978
Interest on federal funds purchased, securities sold under agreements to repurchase and other borrowings	7,875	15,627	19,441	32,023
Interest on Federal Home Loan Bank advances	305,229	425,046	607,104	850,092
Total interest expense	1,177,616	1,498,406	2,432,135	3,009,332
Net interest income	6,298,931	6,813,212	12,673,328	13,724,478
Provision for loan losses	300,000	1,000,000	500,000	1,200,000
Net interest income, after provision for loan losses	5,998,931	5,813,212	12,173,328	12,524,478
Noninterest Income:				
Income from fiduciary activities	865,689	793,005	1,765,494	1,619,651
Service charges on deposit accounts	1,036,265	1,073,004	2,032,865	2,103,309
Other service charges, commissions and fees	911,619	880,032	1,770,590	1,677,061
Income from bank-owned life insurance	216,519	225,201	431,826	448,881
Income from Old Point Mortgage	217,799	94,311	304,324	125,298
Gain (loss) on sale of available-for-sale securities, net	(20,532)	769,474	(20,532)	1,083,869
Other operating income	56,874	45,821	112,935	90,664
Total noninterest income	3,284,233	3,880,848	6,397,502	7,148,733
Noninterest Expense:				
Salaries and employee benefits	4,805,584	5,219,885	9,726,510	10,180,162
Occupancy and equipment	1,078,684	1,069,180	2,190,883	2,162,933
Data processing	412,884	391,376	834,460	773,903
FDIC insurance	173,914	286,314	356,975	567,152
Customer development	205,372	202,992	411,478	406,888
Legal and audit expense	123,537	224,182	234,661	408,112
Other outside service fees	112,510	140,981	208,888	293,367
Employee professional development	181,367	187,643	312,781	329,984
Postage and courier expense	120,166	118,984	243,031	243,311
Advertising	124,320	146,594	247,370	291,612
Stationery and supplies	95,414	113,304	215,723	217,839
Loss on write-down/sale of foreclosed assets	77,223	380,050	203,676	636,634

Other operating expense	537,800	465,165	1,088,141	984,191
Total noninterest expense	8,048,775	8,946,650	16,274,577	17,496,088
Income before income taxes	1,234,389	747,410	2,296,253	2,177,123
Income tax expense	219,574	109,203	380,121	460,615
Net income	$1,014,815	$638,207	$1,916,132	$1,716,508
Basic Earnings per Share:				
Average shares outstanding	4,959,009	4,959,009	4,959,009	4,959,009
Net income per share of common stock	$0.21	$0.13	$0.39	$0.35
Diluted Earnings per Share:				
Average shares outstanding	4,959,009	4,959,009	4,959,009	4,959,009
Net income per share of common stock	$0.21	$0.13	$0.39	$0.35

See Notes to Consolidated Financial Statements.

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Old Point Financial Corporation

Consolidated Statements of Comprehensive Income (Loss)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
	(unaudited)		(unaudited)	
Net income	$1,014,815	$638,207	$1,916,132	$1,716,508
Other comprehensive income (loss), net				
Unrealized gains (losses) on securities, net of reclassification adjustment	(6,496,437)	1,004,031	(8,222,984)	249,407
Comprehensive income (loss)	$(5,481,622)	$1,642,238	$(6,306,852)	$1,965,915

See Notes to Consolidated Financial Statements.

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Old Point Financial Corporation and Subsidiaries

Consolidated Statements of Changes in Stockholders' Equity

(unaudited)	Shares of Common Stock	Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total
SIX MONTHS ENDED JUNE 30, 2013						
Balance at beginning of period	4,959,009	$24,795,045	$16,391,845	$48,304,609	$ (191,463)	$89,300,036
Net income	0	0	0	1,916,132	0	1,916,132
Other comprehensive loss, net of tax	0	0	0	0	(8,222,984)	(8,222,984)
Cash dividends ($0.10 per share)	0	0	0	(495,900)	0	(495,900)
Balance at end of period	4,959,009	$24,795,045	$16,391,845	$49,724,841	$ (8,414,447)	$82,497,284
SIX MONTHS ENDED JUNE 30, 2012						
Balance at beginning of period	4,959,009	$24,795,045	$16,309,983	$45,109,268	$ (349,581)	$85,864,715
Net income	0	0	0	1,716,508	0	1,716,508
Other comprehensive income, net of tax	0	0	0	0	249,407	249,407
Stock compensation expense	0	0	55,330	0	0	55,330
Cash dividends ($0.10 per share)	0	0	0	(495,901)	0	(495,901)
Balance at end of period	4,959,009	$24,795,045	$16,365,313	$46,329,875	$ (100,174)	$87,390,059

See Notes to Consolidated Financial Statements.

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Old Point Financial Corporation and Subsidiaries
Consolidated Statements of Cash Flows

	Six Months Ended June 30,	
	2013	2012
	(unaudited)	
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	$1,916,132	$1,716,508
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	979,896	938,719
Provision for loan losses	500,000	1,200,000
Net (gain) loss on sale of available-for-sale securities	20,532	(1,083,869)
Net amortization of securities	1,318,419	572,773
Net loss on disposal of premises and equipment	16,416	52
Net loss on write-down/sale of foreclosed assets	203,676	636,634
Income from bank owned life insurance	(431,826)	(448,881)
Stock compensation expense	0	55,330
Deferred tax (benefit) expense	(116,994)	20,688
(Increase) decrease in other assets	(522,292)	1,379,570
Increase in other liabilities	806,047	534,406
Net cash provided by operating activities	4,690,006	5,521,930
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchases of available-for-sale securities	(11,377,086)	(186,286,377)
Purchases of held-to-maturity securities	(10,853,837)	0
Proceeds from sales of restricted securities	183,800	341,200
Proceeds from maturities and calls of securities	29,161,524	37,873,835
Decrease in loans made to customers	230,300	41,245,918
Proceeds from sales of foreclosed assets	1,117,240	2,170,889
Purchases of premises and equipment	(4,483,255)	(1,028,992)
Net cash provided by (used in) investing activities	43,279,820	(14,678,372)
CASH FLOWS FROM FINANCING ACTIVITIES		
Increase in noninterest-bearing deposits	1,098,887	9,939,550
Increase in savings deposits	2,568,252	11,483,949
Increase (decrease) in time deposits	(27,114,947)	11,873,082
Decrease in federal funds purchased, repurchase agreements and other borrowings	(11,172,840)	(12,541,091)
Cash dividends paid on common stock	(495,900)	(495,901)
Net cash provided by (used in) financing activities	(35,116,548)	20,259,589
Net increase in cash and cash equivalents	12,853,278	11,103,147
Cash and cash equivalents at beginning of period	42,317,246	24,854,656
Cash and cash equivalents at end of period	$55,170,524	$35,957,803
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION		
Cash payments for:		
Interest	$2,504,764	$3,021,805
Income tax	$450,000	$600,000
SUPPLEMENTAL SCHEDULE OF NONCASH TRANSACTIONS		

Unrealized gain (loss) on securities available-for-sale	$(12,459,065)	$377,890
Loans transferred to foreclosed assets	$866,359	$564,480
Former branch site transferred from fixed assets to foreclosed properties	$506,296	$0

See Notes to Consolidated Financial Statements.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

Note 1. General

The accompanying unaudited consolidated financial statements of Old Point Financial Corporation (the Company) and its subsidiaries have been prepared in accordance with U.S. generally accepted accounting principles (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 positions at June 30, 2013 and December 31, 2012, the results of operations and statements of comprehensive income for the three and six months ended June 30, 2013 and 2012, and the statements of changes in stockholders' equity and statements of cash flows for the six months ended June 30, 2013 and 2012. The results of operations for the interim periods are not necessarily indicative of the results that may be expected for the full year.

These financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company's 2012 annual report on Form 10-K. Certain previously reported amounts have been reclassified to conform to current period presentation.

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). 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 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.

SUBSEQUENT EVENTS

In accordance with ASC 855-10, "Subsequent Events," the Company evaluates subsequent events that have occurred after the balance sheet date but before the financial statements are issued. There are two types of subsequent events: (1) recognized, or those that provide additional evidence about conditions that existed at the date of the balance sheet, including the estimates inherent in the process of preparing financial statements, and (2) nonrecognized, or those that provide evidence about conditions that did not exist at the date of the balance sheet but arose after that date.

The Company is expanding the building of a current branch office. The Company signed a contract with a general contractor on April 19, 2012. The contract entitles the contractor to $2.1 million for Phase I of the construction, which includes site work and construction of the building shell. The Company signed an amendment to the contract with the general contractor on October 16, 2012 for the remainder of the construction. The revised contract entitles the contractor to $12.2 million for the construction of the building. As of the writing of this quarterly report on Form 10-Q, $6.5 million had been disbursed to the contractor. The Company anticipates that the total project will likely cost between $13.0 million and $15.0 million and be completed in the next nine months.

Other than those discussed above, the Company did not identify any recognized or nonrecognized subsequent events that would have required adjustment to or disclosure in the financial statements.

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Note 2. Securities

Amortized costs and fair values of securities held-to-maturity as of the dates indicated are as follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(in thousands)			
June 30, 2013				
Obligations of U.S. Government agencies	$570	$ 3	$ (3)	$570
Obligations of state and political subdivisions	10,843	9	(19)	10,833
Total	$11,413	$ 12	$ (22)	$11,403
December 31, 2012				
Obligations of U.S. Government agencies	$570	$ 4	$ 0	$574

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

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(in thousands)			
June 30, 2013				
Obligations of U.S. Government agencies	$25,372	$ 551	$ (118)	$25,805
Obligations of state and political subdivisions	50,997	160	(2,393)	48,764
Mortgage-backed securities	189,456	0	(7,613)	181,843
Money market investments	801	0	0	801
Corporate bonds	1,399	0	(29)	1,370
Total	$268,025	$ 711	$ (10,153)	$258,583
December 31, 2012				
Obligations of U.S. Government agencies	$35,787	$ 1,314	$ (13)	$37,088
Obligations of state and political subdivisions	43,276	712	(214)	43,774
Mortgage-backed securities	246,132	1,966	(743)	247,355
Money market investments	541	0	0	541
Corporate bonds and other securities	700	0	(2)	698
Total	$326,436	$ 3,992	$ (972)	$329,456

OTHER-THAN-TEMPORARILY IMPAIRED SECURITIES

Management assesses whether the Company intends to sell or it is more-likely-than-not that the Company will be required to sell a security before recovery of its amortized cost basis less any current-period credit losses. For debt securities that are considered other-than-temporarily impaired and that the Company does not intend to sell and will not be required to sell prior to recovery of the amortized cost basis, the Company separates the amount of the impairment into the amount that is credit related (credit loss component) and the amount due to all other factors. The credit loss component is recognized in earnings and is the difference between the security’s amortized cost basis and the present value of its expected future cash flows. The remaining difference between the security’s fair value and the present value of future expected cash flows is due to factors that are not credit related and is recognized in other comprehensive income.

The present value of expected future cash flows is determined using the best-estimate cash flows discounted at the effective interest rate implicit to the security at the date of purchase or the current yield to accrete an asset-backed or floating rate security. The methodology and assumptions for establishing the best-estimate cash flows vary depending on the type of security. The asset-backed securities cash flow estimates are based on bond specific facts and circumstances that may include collateral characteristics, expectations of delinquency and default rates, loss severity and prepayment speeds, and structural support, including subordination and guarantees.

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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 six months ended June 30, 2013 or the year ended December 31, 2012.

TEMPORARILY IMPAIRED SECURITIES

The following table shows the gross unrealized losses and fair value of the Company's investments with unrealized losses that are deemed to be temporarily impaired, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position as of the dates indicated. The Company had no held-to-maturity securities with unrealized losses at December 31, 2012.

	June 30, 2013						
	Less Than Twelve Months		More Than Twelve Months		Total		
	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Number of Securities
	(in thousands)						
Securities Available-for-Sale							
Debt securities:							
Obligations of U.S. Government agencies	$118	$4,890	$ 0	$ 0	$118	$4,890	1
Obligations of state and political subdivisions	2,393	37,905	0	0	2,393	37,905	69
Mortgage-backed securities	7,613	181,843	0	0	7,613	181,843	19
Corporate bonds	29	1,370	0	0	29	1,370	11
Total securities available-for-sale	$10,153	$226,008	$ 0	$ 0	$10,153	$226,008	100
Securities Held-to-Maturity							
Obligations of U.S. Government agencies	$3	$97	$ 0	$ 0	$3	$97	1
Obligations of state and political subdivisions	19	857	0	0	19	857	1
Total securities held-to-maturity	$22	$954	$ 0	$ 0	$22	$954	2

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	December 31, 2012						
	Less Than Twelve Months		More Than Twelve Months		Total		
	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Number of Securities
	(in thousands)						
Securities Available-for-Sale							
Debt securities:							
Obligations of U. S. Government agencies	$13	$5,103	$ 0	$ 0	$13	$5,103	1
Obligations of state and political subdivisions	214	9,535	0	0	214	9,535	24
Mortgage-backed securities	743	104,066	0	0	743	104,066	9
Corporate bonds and other securities	2	700	0	0	2	700	2
Total securities available-for-sale	$972	$119,404	$ 0	$ 0	$972	$119,404	36

Certain investments within the Company's portfolio had unrealized losses at June 30, 2013 and December 31, 2012, 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 June 30, 2013 or December 31, 2012.

Restricted Securities

The restricted security category is comprised of stock in the Federal Home Loan Bank of Atlanta (FHLB) and the Federal Reserve Bank (FRB). 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 and FRB stock is 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.

Note 3. Loans and the Allowance for Loan Losses

The following is a summary of the balances in each class of the Company's loan portfolio as of the dates indicated:

	June 30, 2013	December 31, 2012
	(in thousands)	
Mortgage loans on real estate:		
Residential 1-4 family	$80,553	$77,267
Commercial	273,498	274,613
Construction	13,493	12,005
Second mortgages	12,242	14,315
Equity lines of credit	31,201	32,327
Total mortgage loans on real estate	410,987	410,527
Commercial loans	28,687	25,341
Consumer loans	10,985	13,146
Other	18,849	22,119
Total loans	469,508	471,133
Less: Allowance for loan losses	(7,296)	(7,324)

Loans, net of allowance and deferred fees	$462,212	$463,809

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Overdrawn deposit accounts are reclassified as loans and included in the Other category in the table above. Overdrawn deposit accounts totaled $587 thousand and $1.6 million at June 30, 2013 and December 31, 2012, respectively.

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 charged off because they are considered uncollectible and of such little value that their continuance as bankable assets is not warranted.

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

Credit Quality Information
As of June 30, 2013
(in thousands)

	Pass	OAEM	Substandard	Total
Mortgage loans on real estate:				
Residential 1-4 family	$73,496	$1,746	$ 5,311	$80,553
Commercial	256,142	7,708	9,648	273,498
Construction	10,374	239	2,880	13,493
Second mortgages	11,895	238	109	12,242
Equity lines of credit	30,598	0	603	31,201
Total mortgage loans on real estate	382,505	9,931	18,551	410,987
Commercial loans	27,533	112	1,042	28,687
Consumer loans	10,956	0	29	10,985
Other	18,849	0	0	18,849
Total	$439,843	$10,043	$ 19,622	$469,508

Credit Quality Information
As of December 31, 2012
(in thousands)

	Pass	OAEM	Substandard	Total
Mortgage loans on real estate:				
Residential 1-4 family	$70,961	$1,711	$ 4,595	$77,267
Commercial	258,195	6,781	9,637	274,613
Construction	8,651	254	3,100	12,005
Second mortgages	13,488	242	585	14,315
Equity lines of credit	31,704	239	384	32,327
Total mortgage loans on real estate	382,999	9,227	18,301	410,527

Commercial loans	23,997	209	1,135	25,341
Consumer loans	13,042	0	104	13,146
Other	22,119	0	0	22,119
Total	$442,157	$9,436	$ 19,540	$471,133

As of June 30, 2013 and December 31, 2012 the Company did not have any loans internally classified as Loss or Doubtful.

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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 June 30, 2013

	30 - 59 Days Past Due	60 - 89 Days Past Due	90 or More Days Past Due	Total Past Due	Total Current Loans (1)	Total Loans	Recorded Investment > 90 Days Past Due and Accruing
	(in thousands)						
Mortgage loans on real estate:							
Residential 1-4 family	$1,752	$38	$3,306	$5,096	$75,457	$80,553	$ 258
Commercial	0	200	716	916	272,582	273,498	0
Construction	404	0	2,880	3,284	10,209	13,493	0
Second mortgages	46	35	20	101	12,141	12,242	20
Equity lines of credit	175	75	0	250	30,951	31,201	0
Total mortgage loans on real estate	2,377	348	6,922	9,647	401,340	410,987	278
Commercial loans	54	49	0	103	28,584	28,687	0
Consumer loans	80	40	13	133	10,852	10,985	13
Other	65	9	5	79	18,770	18,849	5
Total	$2,576	$446	$6,940	$9,962	$459,546	$469,508	$ 296

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

Age Analysis of Past Due Loans as of December 31, 2012

	30 - 59 Days Past Due	60 - 89 Days Past Due	90 or More Days Past Due	Total Past Due	Total Current Loans (1)	Total Loans	Recorded Investment > 90 Days Past Due and Accruing
	(in thousands)						
Mortgage loans on real estate:							
Residential 1-4 family	$1,115	$ 0	$3,783	$4,898	$72,369	$77,267	$ 348
Commercial	207	0	724	931	273,682	274,613	0
Construction	140	0	2,925	3,065	8,940	12,005	0
Second mortgages	113	0	544	657	13,658	14,315	60
Equity lines of credit	90	0	287	377	31,950	32,327	0
Total mortgage loans on real estate	1,665	0	8,263	9,928	400,599	410,527	408
Commercial loans	275	13	122	410	24,931	25,341	25
Consumer loans	85	22	11	118	13,028	13,146	11
Other	54	7	3	64	22,055	22,119	3
Total	$2,079	$ 42	$8,399	$10,520	$460,613	$471,133	$ 447

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

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NONACCRUAL LOANS
The Company generally places non-consumer loans 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 loans secured by 1-4 family residential properties are not required to be placed in nonaccrual status. Although consumer loans and loans secured by 1-4 family residential property are not required to be placed in nonaccrual status, the Company may place a consumer loan or loan secured by 1-4 family residential property in nonaccrual status, if necessary to avoid a material overstatement of interest income.

Generally, consumer loans not secured by real estate are placed in nonaccrual status only when part of the principal has been charged off. These loans are charged off or written down to the net realizable value of the collateral when deemed uncollectible, due to bankruptcy or other factors, or when they are past due based on loan product, industry practice, terms and other factors.

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 or cost recovery method, until it qualifies for return to accrual status or is charged off. Generally, management returns a loan to accrual status if (a) all delinquent interest and principal payments become current under the terms of the loan agreement or (b) the loan is both well-secured and in the process of collection and collectability is no longer doubtful.

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

Nonaccrual Loans by Class

	June 30, 2013	December 31, 2012
	(in thousands)	
Mortgage loans on real estate:		
Residential 1-4 family	$3,363	$ 3,663
Commercial	2,965	3,037
Construction	2,880	3,065
Second mortgages	35	484
Equity lines of credit	0	286
Total mortgage loans on real estate	9,243	10,535
Commercial loans	0	97
Consumer loans	0	0
Total	$9,243	$ 10,632

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:

	Six Months Ended June 30,	
	2013	2012
	(in thousands)	
Interest income that would have been recorded under original loan terms	$275	$275

Actual interest income recorded for the period	51	32
Reduction in interest income on nonaccrual loans	$224	$243

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 90 days or more past due and still accruing interest at the report date.

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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 period indicated, by class of loan:

Troubled Debt Restructurings by Class
For the Six Months Ended June 30, 2013
(dollars in thousands)

	Number of Modifications	Recorded Investment Prior to Modification	Recorded Investment After Modification	Current Investment on June 30, 2013
Mortgage loans on real estate:				
Residential 1-4 family	3	$ 676	$ 676	$ 673
Commercial	1	207	207	203
Total	4	$ 883	$ 883	$ 876

Troubled Debt Restructurings by Class
For the Six Months Ended June 30, 2012
(dollars in thousands)

	Number of Modifications	Recorded Investment Prior to Modification	Recorded Investment After Modification	Current Investment on June 30, 2012
Mortgage loans on real estate:				
Commercial	2	$ 3,019	$ 2,461	$ 2,373
Second mortgages	1	111	145	140
Total	3	$ 3,130	$ 2,606	$ 2,513

The four loans restructured in the first six months of 2013 were all given below-market rates for debt with similar risk characteristics. The restructurings during the first six months of 2012 were given principal reductions, with the principal forgiveness on all loans in the table totaling $525 thousand. One loan restructured during the first six months of 2012 was also given a below-market rate for debt with similar risk characteristics.

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As of June 30, 2013 and June 30, 2012, there were no TDRs for which there was a payment default where the default occurred within twelve months of restructuring. A TDR is considered in default when it is 90 days or more past due or has been charged off.

The TDRs in the tables above are factored into the determination of the allowance for loan losses as of the periods indicated. These loans are 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 due from the borrower in accordance with the contractual terms of the loan. Impaired loans include nonperforming commercial 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 an allowance estimate 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.

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The following table includes the recorded investment and unpaid principal balances (a portion of which may have been charged off) for 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
(in thousands)

	As of June 30, 2013				For the six months ended June 30, 2013	
	Unpaid Principal Balance	Recorded Investment Without Valuation Allowance	Recorded Investment With Valuation Allowance	Associated Allowance	Average Recorded Investment	Interest Income Recognized
Mortgage loans on real estate:						
Residential 1-4 family	$4,546	$872	$ 3,415	$ 237	$4,738	$ 16
Commercial	13,702	3,683	7,082	1,261	10,910	269
Construction	3,639	0	2,880	360	2,891	0
Second mortgages	183	43	136	47	745	4
Equity lines of credit	50	50	0	0	193	1
Total mortgage loans on real estate	$22,120	$4,648	$ 13,513	$ 1,905	$19,477	$ 290
Commercial loans	0	0	0	0	12	0
Consumer loans	16	16	0	0	18	1
Total	$22,136	$4,664	$ 13,513	$ 1,905	$19,507	$ 291

Impaired Loans by Class
(in thousands)

	As of December 31, 2012				For the year ended December 31, 2012	
	Unpaid Principal Balance	Recorded Investment Without Valuation Allowance	Recorded Investment With Valuation Allowance	Associated Allowance	Average Recorded Investment	Interest Income Recognized
Mortgage loans on real estate:						
Residential 1-4 family	$4,100	$681	$ 3,235	$ 226	$2,354	$ 136
Commercial	12,459	3,741	5,817	180	10,151	242
Construction	3,782	3,064	0	0	3,320	(9)
Second mortgages	695	583	47	5	542	12
Equity lines of credit	370	286	0	0	391	(2)
Total mortgage loans on real estate	$21,406	$8,355	$ 9,099	$ 411	$16,758	$ 379
Commercial loans	117	0	97	33	104	(14)
Consumer loans	17	17	0	0	26	1
Total	$21,540	$8,372	$ 9,196	$ 444	$16,888	$ 366

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 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 losses inherent in the loan portfolio. For purposes of determining the allowance for loan losses, the Company has segmented certain loans in the portfolio by product type. 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.

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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.

To determine the balance of the allowance account for each segment of the loan portfolio, management pools each segment by risk grade individually and applies a historical loss percentage. At June 30, 2013 and December 31, 2012, the historical loss percentage was based on losses sustained in each segment of the portfolio over the previous eight quarters.

Management also provides an allocated component of the allowance for loans that are classified as impaired. An allocated allowance is established when the discounted value of 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.

THE COMPANY’S ESTIMATION PROCESS

The allowance for loan losses is the accumulation of various components that are calculated based on independent methodologies. Management’s estimate is based on certain observable, historical data that management believes are most reflective of the underlying credit losses being estimated. In addition, impaired loans are separately identified for evaluation and are measured based on the present value of expected future cash flows, the observable market price of the loans or the fair value of the collateral. Also, various qualitative factors are applied to each segment of the loan portfolio.

ALLOWANCE FOR LOAN LOSSES BY SEGMENT

The total allowance reflects management’s estimate of loan losses inherent in the loan portfolio at the balance sheet date. The Company considers the allowance for loan losses of $7.3 million adequate to cover loan losses inherent in the loan portfolio at June 30, 2013.

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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 Six Months Ended June 30, 2013	Commercial	Real Estate Construction	Real Estate - Mortgage	Consumer	Other	Total
Allowance for Loan Losses:						
Balance at the beginning of period	$677	$ 187	$6,179	$ 204	$77	$7,324
Charge-offs	(106)	(100)	(413)	(66)	(79)	(764)
Recoveries	43	3	121	34	35	236
Provision for loan losses	(339)	429	421	(22)	11	500
Ending balance	$275	$ 519	$6,308	$ 150	$44	$7,296
Ending balance individually evaluated for impairment	$0	$ 360	$1,545	$ 0	$0	$1,905
Ending balance collectively evaluated for impairment	275	159	4,763	150	44	5,391
Ending balance	$275	$ 519	$6,308	$ 150	$44	$7,296
Loan Balances:						
Ending balance individually evaluated for impairment	$0	$ 2,880	$15,281	$ 16	$0	$18,177
Ending balance collectively evaluated for impairment	28,687	10,613	382,213	10,969	18,849	451,331
Ending balance	$28,687	$ 13,493	$397,494	$ 10,985	$18,849	$469,508

For the Year Ended December 31, 2012	Commercial	Real Estate - Construction	Real Estate - Mortgage	Consumer	Other	Total
Allowance for Loan Losses:						
Balance at the beginning of period	$ 1,011	$ 323	$6,735	$ 300	$129	$8,498
Charge-offs	(138)	(831)	(2,554)	(259)	(187)	(3,969)
Recoveries	67	30	162	70	66	395
Provision for loan losses	(263)	665	1,836	93	69	2,400
Ending balance	$ 677	$ 187	$6,179	$ 204	$77	$7,324
Ending balance individually evaluated for impairment	$ 33	$ 0	$411	$ 0	$0	$444
Ending balance collectively evaluated for impairment	644	187	5,768	204	77	6,880
Ending balance	$ 677	$ 187	$6,179	$ 204	$77	$7,324
Loan Balances:						
Ending balance individually evaluated for impairment	$ 97	$ 3,064	$14,390	$ 17	$0	$17,568
Ending balance collectively evaluated for impairment	25,244	8,941	384,132	13,129	22,119	453,565
Ending balance	$ 25,341	$ 12,005	$398,522	$ 13,146	$22,119	$471,133

CHANGES IN ACCOUNTING METHODOLOGY

There were no changes in the Company's accounting methodology for the allowance for loan losses in the first six months of 2013.

Note 4. Share-Based Compensation

Share-based compensation arrangements include stock options, restricted stock awards, performance-based awards, stock appreciation rights and employee stock purchase plans. 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.

Historically, the Company has only granted share-based compensation in the form of stock options. There were no options granted in the first six months of 2013.

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On March 9, 2008, the Company's 1998 Stock Option Plan expired. Options to purchase 154,460 shares of common stock were outstanding under the Company's 1998 Stock Option Plan at June 30, 2013. The exercise price of each option equals the market price of the Company's common stock on the date of the grant and each option's maximum term is ten years.

Stock option activity for the six months ended June 30, 2013 is summarized below:

	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life (in years)	Aggregate Intrinsic Value (in thousands)
Options outstanding, January 1, 2013	156,960	$ 21.63		
Granted	0	0		
Exercised	0	0		
Canceled or expired	(2,500)	21.94		
Options outstanding, June 30, 2013	154,460	$ 21.63	2.96	$ 0
Options exercisable, June 30, 2013	154,460	$ 21.63	2.96	$ 0

The aggregate intrinsic value of a stock option in the table above represents the total pre-tax intrinsic value (the amount by which the current market value of the underlying stock exceeds the exercise price of the option) that would have been received by the option holders had all option holders exercised their options on June 30, 2013. This amount changes based on changes in the market value of the Company's common stock. As of June 30, 2013, the outstanding options had no intrinsic value because the exercise prices of all outstanding options were above the market value of a share of the Company's common stock.

No options were exercised during the six months ended June 30, 2013.

As of June 30, 2013, all outstanding stock options were fully vested and there was no unrecognized stock-based compensation expense.

Note 5. Pension Plan

The Company provides pension benefits for eligible participants through a non-contributory defined benefit pension plan. The plan was frozen effective September 30, 2006; therefore, no additional participants will be added to the plan. The components of net periodic pension plan cost are as follows for the periods indicated:

Three months ended June 30,	2013	2012
	Pension Benefits	
Interest cost	$62,983	$71,750
Expected return on plan assets	(88,399)	(97,500)
Amortization of net loss	74,524	56,250
Net periodic pension plan cost	$49,108	$30,500

Six months ended June 30,	2013	2012
	Pension Benefits	
Interest cost	$125,966	$143,500
Expected return on plan assets	(176,798)	(195,000)
Amortization of net loss	149,048	112,500
Net periodic pension plan cost	$98,216	$61,000

At June 30, 2013, management had not yet determined the amount, if any, that the Company will contribute to the plan in the year ending December 31, 2013.

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Note 6. Stockholders' Equity and Earnings per Share

STOCKHOLDERS' EQUITY – 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 June 30, 2013	Three Months Ended June 30, 2012	Six Months Ended June 30, 2013	Six Months Ended June 30, 2012	Affected Line Item on Consolidated Statement of Income
	(in thousands)				
Available-for-sale securities					
Realized gains (losses) on sales of securities	$(21)	$769	$(21)	$1,084	Gain (loss) on sale of available-for-sale securities, net
Tax effect	(7)	262	(7)	369	Income tax expense
	$(14)	$507	$(14)	$715	Net of tax

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

	Unrealized Gains (Losses) on Securities	Defined Benefit Pension Plans	Accumulated Other Comprehensive Loss
	(in thousands)		
SIX MONTHS ENDED JUNE 30, 2013			
Balance at beginning of period	$1,993	$(2,184)	$ (191)
Net change for the period	(8,223)	0	(8,223)
Balance at end of period	$(6,230)	$(2,184)	$ (8,414)

	Unrealized Gains (Losses) on Securities	Defined Benefit Pension Plans	Accumulated Other Comprehensive Loss
	(in thousands)		
SIX MONTHS ENDED JUNE 30, 2012			
Balance at beginning of period	$1,526	$(1,875)	$ (349)
Net change for the period	249	0	249
Balance at end of period	$1,775	$(1,875)	$ (100)

The following table presents the change in each component of other comprehensive income on a pre-tax and after-tax basis for the periods indicated.

	Six Months Ended June 30, 2013		
	Pretax	Tax Expense (Benefit)	Net-of-Tax
	(in thousands)		
Unrealized losses on securities			
Unrealized holding losses arising during the period	$(12,480)	$(4,243)	$(8,237)
Less reclassification adjustment for losses recognized in income	(21)	(7)	(14)
Net unrealized losses on securities	(12,459)	(4,236)	(8,223)
Total decrease in other comprehensive loss	$(12,459)	$(4,236)	$(8,223)

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	Six Months Ended June 30, 2012		
	Pretax	Tax Expense (Benefit)	Net-of-Tax
	(in thousands)		
Unrealized gains on securities			
Unrealized holding gains arising during the period	$1,461	$ 497	$ 964
Less reclassification adjustment for gains recognized in income	1,084	369	715
Net unrealized gains on securities	377	128	249
Total increase in other comprehensive loss	$377	$ 128	$ 249

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 Company did not include an average of 156 thousand potential common shares attributable to outstanding stock options in the diluted earnings per share calculation for the first six months of 2013 because they were antidilutive.

Note 7. Recent Accounting Pronouncements

In February 2013, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2013-02, “Comprehensive Income (Topic 220): Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income.” The amendments in this ASU require an entity to present (either on the face of the statement where net income is presented or in the notes) the effects on the line items of net income of significant amounts reclassified out of accumulated other comprehensive income. In addition, the amendments require a cross-reference to other disclosures currently required for other reclassification items to be reclassified directly to net income in their entirety in the same reporting period. Public companies should apply these amendments for fiscal years, and interim periods within those years, beginning on or after December 15, 2012. The Company has included the required disclosures from ASU 2013-02 in its consolidated financial statements.

Note 8. 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 and FASB ASU 2011-04, 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 company, 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.

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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 and equity 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 June 30, 2013 Using (in thousands)		
Description	Balance	Quoted Prices in Active Markets for Identical Assets	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)

		(Level 1)		
Available-for-sale securities				
Obligations of U.S. Government agencies	$25,805	$0	$ 25,805	$ 0
Obligations of state and political subdivisions	48,764	0	48,764	0
Mortgage-backed securities	181,843	0	181,843	0
Money market investments	801	0	801	0
Corporate bonds	1,370	0	1,370	0
Total available-for-sale securities	$258,583	$0	$ 258,583	$ 0

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Description	Balance	Fair Value Measurements at December 31, 2012 Using (in thousands) Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Available-for-sale securities				
Obligations of U.S. Government agencies	37,088	0	37,088	0
Obligations of state and political subdivisions	43,774	0	43,774	0
Mortgage-backed securities	247,355	0	247,355	0
Money market investments	541	0	541	0
Corporate bonds	698	0	698	0
Total available-for-sale securities	$329,456	$0	$ 329,456	$ 0

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

Loans are designated as impaired when, in the judgment of management based on current information and events, it is probable that all amounts due according to the contractual terms of the loan agreement will not be collected. 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. 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.

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Foreclosed assets

Loans are transferred to foreclosed assets when the collateral securing them is foreclosed on. The measurement of loss associated with foreclosed assets 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 foreclosed assets below the original book value are recorded in the period incurred and expensed against current earnings.

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 interest rate of the loan 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 June 30, 2013 Using (in thousands)		
	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Impaired loans				
Mortgage loans on real estate:				
Residential 1-4 family	$3,006	$0	$ 0	$ 3,006
Commercial	2,776	0	0	2,776
Construction	2,520	0	0	2,520
Second mortgages	88	0	0	88
Total	$8,390	$0	$ 0	$ 8,390
Foreclosed assets				
Residential 1-4 family	$521	$0	$ 0	$ 521
Commercial	2,286	0	0	2,286
Construction	3,752	0	0	3,752
Total	$6,559	$0	$ 0	$ 6,559

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Description	Fair Value	Carrying Value at December 31, 2012 Using (in thousands) Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
Impaired loans				
Mortgage loans on real estate:				
Residential 1-4 family	$3,009	$0	$ 0	$ 3,009
Commercial	2,271	0	0	2,271
Second mortgages	42	0	0	42
Total mortgage loans on real estate	$5,322	$0	$ 0	$ 5,322
Commercial loans	64	0	0	64
Total	$5,386	$0	$ 0	$ 5,386
Foreclosed assets				
Residential 1-4 family	$676	$0	$ 0	$ 676
Commercial	2,094	0	0	2,094
Construction	3,804	0	0	3,804
Total	$6,574	$0	$ 0	$ 6,574

The following table displays quantitative information about Level 3 Fair Value Measurements as of the date indicated (dollars in thousands):

Description	Fair Value at June 30, 2013 (in thousands)	Quantitative Information About Level 3 Fair Value Measurements Valuation Techniques	Unobservable Input	Range (Average)
Impaired loans				
Residential 1-4 family real estate	3,006	Market comparables	Selling costs	5% - 6% (5%)
			Liquidation discount	1.25%
Commercial real estate	2,776	Market comparables	Selling costs	6% - 20% (10%)
			Age of appraisal	46%
Construction	2,520	Market comparables	Selling costs	20%
			Liquidation discount	1.25%
Second mortgages	88	Market comparables	Selling costs	6%

			Liquidation discount	1.25%
Foreclosed assets				
Residential 1-4 family	521	Market comparables	Selling costs	6% - 10% (6%)
Commercial	2,286	Market comparables	Selling costs	6% - 10% (6%)
Construction	3,752	Market comparables	Selling costs	6% - 10% (6%)

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Description	Fair Value at December 31, 2012 (in thousands)	Quantitative Information About Level 3 Fair Value Measurements Valuation Techniques	Unobservable Input	Range (Average)
Impaired loans				
Residential 1-4 family real estate	3,009	Market comparables	Differences in comparables	0% - 5% (5%)
			Selling costs	4.75% - 6% (6%)
Commercial real estate	2,271	Market comparables	Selling costs	0% - 6% (4%)
Second mortgages	42	Market comparables	Selling costs	6%
Commercial loans	64	Market comparables	Differences in comparables	25%
Foreclosed assets				
Residential 1-4 family	676	Market comparables	Selling costs	6% - 10% (6%)
Commercial	2,094	Market comparables	Selling costs	6% - 10% (6%)
Construction	3,804	Market comparables	Selling costs	6% - 10% (6%)

ASC 825, "Financial Instruments," requires disclosure about fair value of financial instruments for interim periods and excludes certain financial instruments and all non-financial instruments from its disclosure requirements. Accordingly, the aggregate fair value amounts presented may not necessarily represent the underlying fair value of the Company's assets.

The following methods and assumptions were used by the Company in estimating fair value disclosures for financial instruments:

CASH AND CASH EQUIVALENTS
The carrying amounts of cash and short-term instruments, including interest-bearing due from banks, approximate fair values.

RESTRICTED SECURITIES
The restricted security category is comprised of FHLB and Federal Reserve Bank stock. These stocks are classified as restricted securities because their ownership is restricted to certain types of entities and they lack a market. When the FHLB or Federal Reserve Bank repurchases stock, they repurchase at the stock's book value. Therefore, the carrying amounts of restricted securities approximate fair value.

LOANS RECEIVABLE
The fair value of a loan is based on its interest rate in relation to its risk profile, in comparison to what an investor could earn on a different investment with a similar risk profile. Variations in risk tolerance between lenders, and thus in risk pricing, can result in the same loan being priced differently at different institutions. A bank's experience with the type of lending (such as commercial real estate) can also impact its assessment of the riskiness of a loan. A comprehensive picture of competitors' rates in relation to borrower risk profiles is not available. Since the rate and risk profile are the primary factors in determining the fair value of a loan, both of which are unobservable in the market, the Company classifies loans as Level 3 in the fair value hierarchy. Instead, the Company uses a model which estimates market value based on the loan's interest rate (regardless of its risk level) and rates for debt of similar maturities where market data is available. Fair values for non-performing loans are estimated as described above.

BANK-OWNED LIFE INSURANCE

Bank-owned life insurance represents insurance policies on certain current and former officers of the Company. The cash value of the policies is estimated using information provided by the insurance carrier. The insurance carrier uses actuarial data to estimate the value of each policy, based on the age and health of the insured relative to other individuals about whom the carrier has information. Health information can be broken down into quantitative, observable inputs, such as smoking habits, blood pressure, and weight, which, along with the insured's age, can be compared to observable data the insurance carrier has available. The carrier can then estimate the cash value of each policy. Since the cash value represents the amount of cash the Company would receive when the policies are paid, the cash value closely approximates the fair value of the policies. Accordingly, bank-owned life insurance is classified as Level 2.

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DEPOSIT LIABILITIES
The fair value of demand deposits, savings and certain money market deposits is the amount payable on demand at the reporting date. The fair value of certificates of deposits is estimated by discounting the future cash flows using the rates currently offered for deposits of similar remaining maturities. Information about the rates paid by other institutions for deposits of similar terms is readily available, and rates are mainly influenced by the term of the deposit itself. As a result, fair value calculations are based on observable inputs, and are classified as Level 2.

SHORT-TERM BORROWINGS
The carrying amounts of federal funds purchased, overnight repurchase agreements, and other short-term borrowings maturing within 90 days approximate their fair values. Since the contractual terms of these borrowings provide all information necessary to calculate the amounts that will be due at maturity, these liabilities are classified as Level 2.

LONG-TERM BORROWINGS
The fair values of the Company's long-term borrowings are estimated based on the current cost to repay the debt in full, discounted to current values and including any prepayment penalties that may apply. As the contractual terms of the borrowing provide all the necessary inputs for this calculation, long-term borrowings are classified as Level 2.

ACCRUED INTEREST
The calculation of accrued interest is based on readily observable information, such as the rate and term of the underlying asset or liability. Since these amounts are expected to be realized quickly (generally within 30 to 90 days), the carrying value approximates fair value and is classified as Level 2.

COMMITMENTS TO EXTEND CREDIT AND IRREVOCABLE LETTERS OF CREDIT
The fair value of commitments is estimated using the fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the present credit-worthiness of the counterparties. For fixed-rate loan commitments, fair value also considers the difference between current levels of interest rates and the committed rates. The fair value of letters of credit is based on fees currently charged for similar agreements or on the estimated cost to terminate them or otherwise settle the obligations with the counterparties at the reporting date. At June 30, 2013 and December 31, 2012, the fair value of fees charged for loan commitments and irrevocable letters of credit was immaterial.

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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 June 30, 2013 Using (in thousands) Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets				
Cash and cash equivalents	$55,171	$55,171	$ 0	$ 0
Securities available-for-sale	258,583	0	258,583	0
Securities held-to-maturity	11,413	0	11,403	0
Restricted securities	2,378	0	2,378	0
Loans, net of allowances for loan losses	462,212	0	0	467,676
Bank owned life insurance	22,257	0	22,257	0
Accrued interest receivable	2,593	0	2,593	0
Liabilities				
Deposits	$730,368	$0	$ 734,412	$ 0
Overnight repurchase agreements	25,642	0	25,642	0
Term repurchase agreements	411	0	411	0
Federal Home Loan Bank advances	25,000	0	27,992	0
Accrued interest payable	366	0	366	0

	Carrying Value	Fair Value Measurements at December 31, 2012 Using (in thousands) Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets				
Cash and cash equivalents	$42,317	$42,317	$ 0	$ 0
Securities available-for-sale	329,456	0	329,456	0
Securities held-to-maturity	570	0	574	0
Restricted securities	2,562	0	2,562	0

Loans, net of allowances for loan losses	463,809	0	0	466,492
Bank owned life insurance	21,824	0	21,824	0
Accrued interest receivable	2,420	0	2,420	0
Liabilities				
Deposits	$753,816	$0	$757,923	$0
Overnight repurchase agreements	35,946	0	35,946	0
Term repurchase agreements	1,280	0	1,282	0
Federal Home Loan Bank advances	25,000	0	28,681	0
Accrued interest payable	439	0	439	0

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Note 9. 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 interest 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 six months ended June 30, 2013 and 2012 follows:

	Three Months Ended June 30, 2013				
	Bank	Trust	Unconsolidated Parent	Eliminations	Consolidated
Revenues					
Interest and dividend income	$7,466,917	$9,933	$ 1,095,279	$(1,095,582)	$7,476,547
Income from fiduciary activities	0	865,689	0	0	865,689
Other income	2,299,848	133,972	50,100	(65,376)	2,418,544
Total operating income	9,766,765	1,009,594	1,145,379	(1,160,958)	10,760,780
Expenses					
Interest expense	1,177,919	0	0	(303)	1,177,616
Provision for loan losses	300,000	0			