Coastal Banking Company, Inc.

Quarterly Financial Results (Unaudited)

As of March 31, 2015



Coastal Banking Company
Consolidated Balance Sheets

	March 31, 2015 (unaudited)	December 31, 2014 (audited)
Assets		
Cash and due from banks	$ 2,893,005	$ 2,726,911
Interest-bearing deposits in banks	988,540	1,363,282
Federal funds sold	73,891	87,967
Securities available for sale, at fair value	24,101,077	24,836,625
Securities held to maturity, at cost	100,000	—
Restricted equity securities, at cost	7,031,600	5,392,500
Loans held for sale, at fair value	64,102,558	24,491,859
Loans, net of unearned income	270,229,722	272,756,670
Less allowance for loan losses	5,164,722	4,828,899
Loans, net	265,065,000	267,927,771
Premises and equipment, net	7,196,097	7,237,183
Cash surrender value of life insurance	2,423,844	2,402,713
SBA loan servicing rights	1,569,195	1,658,706
Other real estate owned	6,924,678	7,322,404
Loan sales receivable	120,860,580	70,651,624
Other assets	9,277,811	5,831,811
Total assets	$ 513,346,823	$ 421,931,356
Liabilities and Shareholders' Equity		
Deposits:		
Noninterest-bearing	$ 38,431,689	$ 34,929,754
Interest-bearing	286,147,341	250,733,682
Total deposits	324,579,030	285,663,436
Securities sold under agreements to repurchase	3,775,000	—
Other borrowings	126,000,000	83,500,000
Junior subordinated debentures	7,217,000	7,217,000
Other liabilities	12,796,632	7,687,318
Total liabilities	474,367,662	384,067,754
Commitments and contingencies		
Shareholders' Equity:		
Preferred stock, par value $.01; 10,000,000 shares authorized; 9,950 shares issued and outstanding at March 31, 2015 and December 31, 2014	9,950,000	9,950,000
Common stock, par value $.01; 10,000,000 shares authorized; 2,658,787 shares issued and outstanding at March 31, 2015; 2,654,225 shares issued and outstanding at December 31, 2014	26,588	26,542
Additional paid-in capital	41,457,751	41,400,835
Accumulated deficit	(12,930,770)	(13,877,647)
Accumulated other comprehensive income	475,592	363,872
Total shareholders' equity	38,979,161	37,863,602
Total liabilities and shareholders' equity	$ 513,346,823	$ 421,931,356

See accompanying notes to unaudited consolidated financial statements.

Coastal Banking Company
Consolidated Statements of Income
(Unaudited)

	For the three months ending March 31,	
	2015	**2014**
Interest income:		
Interest and fees on loans	$ 4,255,054	$ 3,643,789
Interest on taxable securities	176,504	253,675
Interest on nontaxable securities	28,521	67,599
Interest on deposits in other banks	1,514	1,843
Interest on federal funds sold	26	30
Total interest income	4,461,619	3,966,936
Interest expense:		
Interest on deposits	399,869	454,085
Interest on junior subordinated debentures	42,046	42,139
Interest on other borrowings	145,828	120,218
Total interest expense	587,743	616,442
Net interest income	3,873,876	3,350,494
Provision for loan losses	260,345	255,588
Net interest income after provision for loan losses	3,613,531	3,094,906
Non-interest income:		
Service charges on deposit accounts	50,972	61,181
Other service charges, commissions and fees	102,938	99,674
SBA loan income	82,184	912,058
Mortgage banking income	14,298,859	4,480,229
Income from investment in life insurance contracts	21,130	20,361
Other income	5,350	19,613
Total other income	14,561,433	5,593,116
Non-interest expenses:		
Salaries and employee benefits	13,153,923	5,526,461
Occupancy and equipment expense	866,512	665,611
Data processing fees	354,581	438,889
Other real estate expenses	4,596	346,212
Legal and other professional fees	142,514	171,508
Audit fees	115,084	99,176
Advertising fees	107,406	86,920
FDIC insurance expense	73,302	78,652
Director fees	63,350	68,900
OCC examination fees	32,898	26,782
Other operating	1,266,827	885,644
Total other expenses	16,180,993	8,394,755
Income before income tax	1,993,971	293,267
Income tax expense	823,220	92,557
Net income	$ 1,170,751	$ 200,710
Preferred stock dividends	223,875	167,236
Net income available to common shareholders	$ 946,876	$ 33,474
Basic earnings per common share	$ 0.36	$ .01
Diluted earnings per common share	$ 0.35	$ .01

See accompanying notes to unaudited consolidated financial statements.

Coastal Banking Company
Consolidated Statements of Comprehensive Income
(Unaudited)

	For the three months ending March 31,	
	2015	2014
Net income	$ 1,170,751	$ 200,710
Other comprehensive income, net of tax:		
Net unrealized holding gains arising during period, net of tax of $57,553 and $153,126	111,721	297,246
Total other comprehensive income	111,721	297,246
Comprehensive income	$ 1,282,472	$ 497,956

See accompanying notes to unaudited consolidated financial statements.

Coastal Banking Company
Consolidated Statements of Cash Flows
(Unaudited)

	For the Three Months Ended March 31,	
	2015	**2014**
Cash flows from operating activities:		
Net income	$ 1,170,751	$ 200,710
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation, amortization and accretion	180,614	182,212
Amortization of intangible assets	—	—
Stock-based compensation expense	17,045	25,028
Provision for loan losses	260,345	255,588
Gain on sale of securities available for sale	—	—
Net (increase) in loan sales receivable	(50,208,995)	(27,071,461)
Write downs and (gains)/losses on sale of other real estate owned	(4,686)	239,568
Proceeds from sales of other real estate owned	520,603	855,988
Increase in cash value of life insurance	(21,131)	(20,361)
Originations of mortgage loans held for sale	(750,792,535)	(227,263,874)
Proceeds from sales of mortgage loans held for sale	725,480,695	231,512,524
Net decrease (increase) in interest receivable	42,204	(7,424)
Net increase in interest payable	23,339	20,239
(Gain)/Loss on sale/abandonment of premises and equipment	2,222	(9,522)
SBA loan income	(82,184)	(912,058)
Mortgage banking income	(14,298,859)	(4,480,229)
Net other operating activities	749,129	393,244
Net cash provided by operating activities	(86,961,443)	(26,079,828)
Cash flows from investing activities:		
Net increase in interest-bearing deposits in banks	374,742	(42,969)
Net increase in federal funds sold	14,076	(16,895)
Proceeds from maturities of securities available for sale	819,099	1,162,598
Purchase of securities held to maturity	(100,000)	—
Proceeds from sale of premises and equipment	—	29,379
Net change in restricted equity securities	(1,639,100)	(1,367,300)
Net (increase) decrease in loans	2,484,235	(10,695,634)
Purchase of premises and equipment	(56,027)	(2,649)
Net cash provided by (used in) investing activities	1,897,025	(10,933,470)
Cash flows from financing activities:		
Net (decrease) increase in deposits	38,915,594	(1,798,246)
Net increase in fed funds purchased	3,775,000	—
Proceeds from employee stock purchase plan	39,918	30,785
Proceeds from exercise of stock options	—	10,200
Net increase in other borrowings	42,500,000	35,550,000
Net cash used in financing activities	85,230,512	33,792,739
Net (decrease) increase in cash and due from banks	166,094	(3,220,559)
Cash and due from banks at beginning of period	2,726,911	5,920,153
Cash and due from banks at end of period	$ 2,893,005	$ 2,699,594
Supplemental disclosures of cash flow information:		
Cash paid during the year for:		
Interest expense	$ 564,404	$ 596,203
Federal & State income taxes	$ 14,188	$ 245,520
Noncash Transactions:		
Principal balances of loans transferred to other real estate owned	$ 118,192	$ 1,187,852

See accompanying notes to unaudited consolidated financial statements.

Notes to Consolidated Financial Statements – March 31, 2015 and 2014 (Unaudited) and December 31, 2014

Note 1 - Basis of Presentation

The corporate history of Coastal Banking Company, Inc. (the "Company") is available at www.coastalbanking.com/history.html

On May 2, 2012 the Company filed a Form 15-12G with the Securities and Exchange Commission to terminate the registration of its common stock under Section 12(G) of the Securities Exchange Act of 1934 and thereby suspend its duty to file reports with the SEC under Sections 13 and 15(D) of the Act. As a result, the Form 10Q filed for the period ended March 31, 2012 was the final financial report filed with the SEC by the Company. Management intends to continue to prepare and publish quarterly and annual financial reports with similar information as required in filings with the SEC to ensure that investors have access to timely, meaningful information related to the Company's results. These financial reports will be published on the Company's web site at intervals consistent with the comparable SEC filing deadlines.

The consolidated financial statements include the accounts of the Company and its wholly owned subsidiary, CBC National Bank (the "Bank"). All intercompany accounts and transactions have been eliminated in consolidation.

The financial statements for the interim periods ended March 31, 2015 and March 31, 2014 are unaudited and, in the opinion of management, include all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation. The results of operations for the three months ended March 31, 2015 are not necessarily indicative of the results that may be expected for the year ending December 31, 2015. The financial information as of December 31, 2014 has been derived from the audited financial statements as of that date.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates that affect the amounts of assets and liabilities and changes therein. Actual results could differ from those estimates.

Note 2 – Regulatory Oversight, Capital Adequacy, Operating Results and Liquidity

Regulatory Oversight

The Company operates under the supervision and monitoring of the Federal Reserve Bank of Richmond while the Bank's primary regulator is the Office of the Comptroller of the Currency. In 2008 the Company issued preferred stock and warrants to purchase common stock to the US Treasury under the Capital Purchase Program within the Troubled Asset Relief Program (TARP). In February 2013, Coastal Banking Company preferred stock was included in a Treasury Department TARP auction, and that transaction settled on March 11, 2013. As a result, the Company's preferred stock is no longer held by US Treasury. Rather, preferred stock shares are now owned by a small group of private investors.

More detailed information on the status and requirements of the regulatory oversight under which we operate is available at www.coastalbanking.com/regulatoryoversight.html

Capital Adequacy

As of March 31, 2015, the Bank exceeded all of the regulatory capital ratio levels to be categorized as "well capitalized." The actual capital amounts and ratios are presented in the table below:

	Regulatory Levels To Be Well Capitalized (Applies to Bank)	CBC National Bank	Coastal Banking Company
Total risk-based (to risk-weighted assets)	10.00%	20.00%	20.13%
Tier 1 risk-based (to risk-weighted assets)	8.00%	18.73%	18.86%
Common Equity Tier 1 (to risk-weighted assets)	6.50%	18.73%	18.86%
Tier 1 leverage (to total average assets)	5.00%	10.63%	10.72%

During 2013, the Federal Reserve released final United States Basel III regulatory capital rules implementing the global regulatory capital reforms of Basel III and certain changes required by the Dodd-Frank Wall Street Reform and Consumer Protection Act. The FDIC and OCC also approved the final rule during 2013. The rule applies to all banking organizations that are currently subject to regulatory capital requirements, as well as certain savings and loan holding companies. The rule strengthens the definition of regulatory capital, increases risk-based capital requirements, and makes selected changes to the calculation of risk-weighted assets. The rule became effective January 1, 2015, for the Company and most banking organizations subject to a transition period for several aspects of the rule including the new minimum capital ratio requirements, the capital conservation buffer, and the regulatory capital adjustments and deductions. The Company has implemented all of the applicable changes and included them in the filing of the bank's call report for the quarter ending March 31, 2015. The bank has elected to "opt-out" as it pertains to excluding from tier 1 capital the effects of unrealized gains or losses in the investment portfolio.

On December 5, 2008, Coastal issued and sold 9,950 preferred shares of Fixed Rate Cumulative Perpetual Preferred Stock, Series A (the "TARP preferred stock"), along with a Warrant to purchase 205,579 shares of common stock at $7.26 per share to the United States Department of the Treasury (the "Treasury") as part of the Capital Purchase Program ("CPP"). As discussed above, the preferred stock was sold by Treasury through an auction to private investor on March 11, 2013 and as a result the Company is no longer subject to TARP restrictions.

At issue, the preferred stock had an annual 5% cumulative preferred dividend rate for a $12.50 dividend per share, payable quarterly on February 15, May 15, August 15 and November 15. On February 16, 2014 the annual cumulative dividend increased to 9% payable quarterly on the same dates, resulting in an increase of quarterly dividends to $22.50 per share. Dividends compound if they are unpaid when due. On February 15, 2015 the quarterly dividend was paid to shareholders of record on February 5, 2015 in the amount of $223,875 or $22.50 per share of the Fixed Rate Cumulative Preferred Series A Stock. Management is engaged in ongoing efforts to redeem all outstanding shares of this Series A Preferred Stock as soon as practical.

Operating Results

The Company recorded net income of $1,171,000 for the three months ended March 31, 2015 compared to net income of $201,000 for the three months ended March 31, 2014. The increase in year over year earnings for the first quarter was driven primarily by revenues and related profits derived from the Mortgage Banking segment as a direct result of increased lending volume caused by recent decreases to long-term interest rates.

Liquidity

Liquidity represents the ability of a company to convert assets into cash or cash equivalents without significant loss, and the ability to raise additional funds by increasing liabilities. Liquidity management involves monitoring our sources and uses of funds in order to meet our day-to-day cash flow requirements while maximizing profits. Liquidity management is made more complicated because different balance sheet components are subject to varying degrees of management control. For example, the timing of maturities of our investment portfolio is fairly predictable and subject to a high degree of control at the time investment decisions are made. However, net deposit inflows and outflows are far less predictable and are not subject to the same degree of control. Our primary liquidity needs involve the funding of mortgage loans available for sale, new portfolio loans, and maturing deposits.

We meet our liquidity needs through scheduled maturities of loans and investments on the asset side and through pricing policies on the liability side for interest-bearing deposit accounts and with advances from approved borrowing facilities with correspondent banks, the Federal Home Loan Bank of Atlanta, and the Federal Reserve Bank discount window.

As of March 31, 2015, the Company had $224.7 million in total borrowing capacity, of which we had utilized $146.1 million or 65%, leaving remaining available liquidity of $78.6 million. The following tables present available sources of liquidity at March 31, 2015 and December 31, 2014:

	March 31, 2015		
	Total Line of Credit	Funds Borrowed	Funds Available
Available sources of liquidity			
Federal funds purchased lines of credit	$ 34,000,000	$ 3,775,000	$ 30,225,000
Available brokered certificates of deposit	32,453,760	16,340,610	16,113,150
Repurchase agreements secured by investment securities	9,734,693	—	9,734,693
Federal Reserve Borrowing Capacity at Discount Window	22,093,201	—	22,093,201
Federal Home Loan Bank Advance Availability	126,400,000	126,000,000	400,000
Total sources of liquidity	$ 224,681,654	$ 146,115,610	$ 78,566,044

	December 31, 2014		
	Total Line of Credit	Funds Borrowed	Funds Available
Available sources of liquidity			
Federal funds purchased lines of credit	$ 34,000,000	$ —	$ 34,000,000
Available brokered certificates of deposit	28,573,749	13,840,246	14,733,503
Repurchase agreements secured by investment securities	11,427,000	—	11,427,000
Federal Reserve Borrowing Capacity at Discount Window	25,285,608	—	25,285,608
Federal Home Loan Bank Advance Availability	133,403,000	83,500,000	49,930,000
Total sources of liquidity	$ 232,716,357	$ 97,340,246	$ 135,376,111

Additionally, loans available for sale are considered by management as a key source of liquidity as a result of the speed with which these loans are sold and settled for cash. Management expects that, on average, loans originated for sale will be sold and converted to cash within 18 to 20 business days after the loan is originated. The balance of loans available for sale averaged just over $102 million during the first three months of 2015. Accordingly, in the event of a liquidity crisis, we anticipate having the ability to slow or stop loan origination activity to allow the loans available for sale to convert into cash. Another key metric of our liquidity position is the loan-to-total deposit ratio, calculated using loans, net of unearned income, which was 140% at March 31, 2015 and 94% at December 31, 2014. Based on current and expected liquidity needs and sources, management expects the Company to be able to meet all obligations as they become due.

Note 3 –Earnings Per Share

The following table sets forth the computation of basic and diluted earnings per share for the three months ended March 31, 2015 and 2014.

	For the three months ended March 31,	
	2015	2014
Net income	$ 1,170,751	$ 200,710
Preferred stock dividends	223,875	167,236
Net income available to common shareholders	$ 946,876	$ 33,474
Weighted average common shares	2,658,736	2,623,794
Effect of dilutive securities	27,345	24,687
Diluted average common shares	2,686,081	2,648,481
Earnings per common share	$ 0.36	$ .01
Diluted earnings (losses) per common share	$ 0.35	$ .01

Note 4 - Supplemental Segment Information

The Bank has three reportable business segments: community banking, SBA lending, and mortgage banking operations. The Company evaluates performance based on profit and loss from operations before income taxes, not including nonrecurring gains and losses.

All direct costs and revenues generated by each business segment are allocated to the segment; however, there is no allocation of indirect corporate overhead costs to the SBA lending or mortgage banking segments. Additionally, interest expense is allocated to the SBA Lending and Mortgage Banking segments based on the Bank's cost of funds plus a small margin through an intersegment charge. As a result, the interest expense reflected in the SBA Lending and Mortgage Banking segments is significantly lower than would be paid by these two operations in an arm's length, market rate borrowing relationship, and conversely the interest income credited to the Community Bank from this intersegment allocation is much lower than would otherwise be earned by the Bank in arm's length investments or loans. Except as described above, the Company accounts for intersegment revenues and expenses as if the revenue/expense transactions were to third parties at current market prices.

The Company's reportable business segments are strategic business units that offer different products and services to a different customer base. They are managed separately because each segment has different types and levels of credit and interest rate risk.

(In thousands)	Community Banking		SBA Lending		Mortgage Banking	
Three months ended March 31,	2015	2014	2015	2014	2015	2014
Interest income	$ 2,276	$ 2,467	$ 679	$ 604	$ 1,506	$ 896
Interest expense	4	244	139	141	403	231
Net interest income	2,272	2,223	540	463	1,103	665
Provision for loan losses	138	139	63	52	59	65
Net interest income after provision	2,134	2,084	477	411	1,044	600
Non interest income	265	195	82	912	14,229	4,486
Non interest expense	2,097	2,539	466	704	13,528	5,152
Net income (loss) before tax expense (benefit)	302	(260)	93	619	1,745	(66)
Income tax expense (benefit)	88	(86)	37	198	698	(20)
Net income (loss) after taxes	$ 214	$ (174)	$ 56	$ 421	$ 1,047	$ (46)

The community banking segment provides traditional banking services offered through the Bank's three full service branch locations in Lady's Island and Port Royal, South Carolina; and Fernandina Beach, Florida. At March 31, 2015 this segment had 67 full time equivalent employees including staff that provides operational and administrative support to the other two reportable segments.

The Small Business Administration lending segment originates SBA loans throughout the southeastern United States through its network of SBA business development officers. These officers serve markets in Jacksonville, Ft. Myers, Tampa, and Vero Beach, Florida; Greensboro, North Carolina; and Beaufort, South Carolina. The majority of loans originated by the division are processed through the SBA 7(a) loan program. Participations in these loans are typically sold to secondary market investors within 30 days of the loan being funded. At March 31, 2015 the division had 15 full time equivalent employees and conducted all loan funding, sales and servicing activity from the Bank's operations center in Fernandina Beach, Florida.

The mortgage banking segment was staffed by 312 full time equivalent employees at March 31, 2015 who originate residential mortgage loans through one of four distinct delivery channels. These channels include (1.) a network of independent mortgage brokers, (2.) a national network of traditional retail mortgage lending branches, (3.) an internet leads based retail loan origination branch, and (4.) retail mortgage lending through the Bank's deposit branch locations. Most of these loans are closed by the Bank and sold to various investors on the secondary market while a limited number of loans are retained in the Bank's loan portfolio. Additionally, during the first three months of 2015, approximately 33% of the loan production was brokered away to other lenders and so were not closed by the Bank. All wholesale and internet retail mortgage banking activity is conducted in the Bank's mortgage banking offices in Atlanta, Georgia, as is the national retail mortgage lending administration function. The national retail lending branches are located in Arizona, Florida, Georgia, Maryland, Michigan, Indiana, Illinois, and Ohio.

Loans on one-to-four family residential mortgages originated by us are sold to various other financial institutions with representations and warranties that are usual and customary for the industry. In addition to these representations and warranties, our loan sale contracts define a condition in which if the borrower fails to make any one of the first four loan payments within 30 days of the due date defined as an Early Payment Default ("EPD"). In the event of an EPD occurrence, we are required to return the premium paid by the investor for the loan as well as pay certain administrative fees. In the event of a breach of any of the representations and warranties related to a loan sold, we could be liable for damages to the investor up to and including a "make whole" demand that involves, at the investor's option, either reimbursing the investor for actual losses incurred on the loan or repurchasing the loan in full. Our maximum exposure to credit loss in the event of a loan repurchase related to a make whole claim would be the unpaid principal balance of the loan to be repurchased along with any premium paid by the investor when the loan was purchased and other minor collection cost reimbursements.

From the September 2007 inception of the mortgage banking division through March 31, 2015, we have sold over 35,000 residential mortgage loans into the secondary market with a principal balance in excess of $7.9 billion. From this population of sold loans, the Bank has received notification from purchasers of a total of thirty-six EPD claims or on average one EPD claim per 986 loans sold. Below are the EPD claims by year of sale-vintage:

Year of Sale	# Loans Sold	# Claims	Claims Rate	$ Loans Sold
2015	1,696	1	0.06%	$ 423,807,376
2014	4,892	2	0.04%	1,151,537,418
2013	5,607	8	0.14%	1,301,421,133
2012	8,104	11	0.14%	1,803,108,311
2011 & prior	15,189	14	0.09%	3,245,925,703
Total	35,488	36	0.10%	$ 7,925,799,941

Beyond the initial payment to the purchasers of $172,000 upon receipt of the EPD claims, the maximum remaining exposure under investor claims of a representation and warranty breach would be the difference between the total loan amount and the liquidated value of the underlying collateral. In the case of our thirty-six EPD claims received since the inception of mortgage banking operations, the aggregate loan balance was $6,936,000 and consisted of 36 single family residences. Original loan-to-value ratios ranged from 65% to 98%, and loans with a loan-to-value ratio over 80% have a mortgage insurance policy in place. If repurchase was required in the future, management believes that the potential amount of loss would not be material and that sufficient reserves exist to fully absorb any loss. Management does not anticipate any material credit risk related to potential EPD claims on loans that have been previously sold and are no longer on the Bank's balance sheet. Because the risk of an EPD claim only exists during the first four payments after a loan is originated, the Bank reports the total of the most recent four months mortgage banking lending volume as off-balance sheet credit risk from EPD claims. As of March 31, 2015, the total off-balance sheet credit risk from EPD claims was $550,432,000.

As discussed above, the representations and warranties in loan sale agreements require that the Bank repurchase loans or indemnify the investors for losses or costs on loans sold under certain limited conditions. Some of these conditions include underwriting errors or omissions, fraud or material misstatements by the borrower in the loan application, or invalid market value on the collateral property due to deficiencies in the appraisal. From the total population of sold loans, over seven years of operations the Bank has been required to settle seventeen make whole claims or on average one claim per 2,088 loans sold at a

total cost of $1,868,000, and has repurchased five loans totaling $1,573,000. Of the five repurchased loans, one has been paid off, and the other four are current and performing in accordance with their loan terms.

Management has recognized the potential risk from costs related to EPD claims and breaches of representations and warranties made in connection with residential loan sales. It is noteworthy that the Bank's loan sale activity began in late 2007 at a time when underwriting requirements had changed and limited documentation conventional (non-government insured) loans were no longer eligible for purchase in the secondary market. Accordingly, the population of conventional loans the Bank has sold was underwritten based on fully documented information. While this will not eliminate all risk of repurchase or indemnification costs, management believes it significantly mitigates that risk as evidenced by the relatively insignificant level of repurchase and indemnification costs incurred to date.

In recognition of risk from potential EPD claims and breaches of representations and warranties, an indemnification reserve has been established and maintained since mortgage banking loan sales began in late 2007 to cover potential costs. Initially management had limited history of costs incurred, so additions to the reserve were made monthly based on a percentage of loan balances sold that month. This approach recognized that the risk of indemnification costs will rise in relation to the level of loans sold. However we also recognize that over time these loans will pay-off as borrowers refinance their loans or sell the properties, but we have no ability to quantify sold loans that have paid off. During 2013 we evaluated the actual loss experience for six years, current business volume and known claims outstanding relative to the indemnification reserve level. Based on that analysis the decision was made to suspend further additions to the reserve balance beginning in August 2013. During September 2014 we updated our analysis of the indemnification reserve considering current business volume, known claims outstanding, trends in presentment of new claims, and recent changes announced by Fannie Mae related to the vintage of future loan repurchase demands. As a result of this analysis the indemnification reserve was reduced by $437,000 to $1,938,000 at September 30, 2014, and reflected as other income. Management believes the reserve level is adequate for potential exposure in connection with loan sale indemnification or EPD claims. Management will monitor the adequacy of the reserve level based on actual loss experience and future business volume levels, and may continue the suspension of additions to the reserve or alternatively decide that further additions to the reserve may be appropriate. However, we can provide no assurance that our methodology will not change and that the balance of this indemnification reserve will prove sufficient to cover actual costs in the future.

The primary source of direct income generated by the mortgage banking division is the gain on sale of mortgage loans which was $14,229,000 for the quarter ended March 31, 2015 compared to $4,486,000 for the quarter ended March 31, 2014. The increase in gain on sale is a result of higher volume caused by a stable to downward trend in long term interest rates which has fueled increasing loan demand for both refinance and purchase money loans. At the peak of refinance activity in 2012, 76.4% of units closed by the mortgage division were for the purpose of refinancing an existing loan and 23.6% were for the purpose of purchasing a home. Management has worked to restructure loan product offerings, geographic sales presence, and pricing incentives to increase the focus on purchase money lending. As a result we have observed a gradual shift from refinance to purchase money lending with refinance lending falling to 53% of total units funded in 2014. Refinance lending increased back to 74% of units funded for the three months ended March 31, 2015 as a result of lower long-term interest rates, reductions in FHA insurance premiums and higher allowable loan to value limits on agency eligible loans. While mortgage loan volume will always be directly impacted by interest rates, purchase money lending has proven to be more resilient to increasing rate environments than has refinance lending, and so by reducing our reliance on refinance lending we expect to be well positioned to maintain profitable funding levels when long term rates begin to rise.

The direct noninterest expenses incurred by the segment were $13,528,000 for the first quarter of 2015, an increase of $8,376,000 over the first quarter 2014 expenses of $5,152,000. The largest contributor to this increase was in salaries and benefits, which were $11,510,000 for first quarter 2015, compared to $3,692,000 for the first quarter 2014, a year over year increase of 212%. This Q1 year over year rise in mortgage banking compensation expense occurred as a result of an increased lending volume of $521.3 million or 217%, from $239.7 million in Q1-2014 to $761.0 million in Q1-2015. Typically lending volume and compensation expense are closely correlated as long as the wholesale/retail mix remains relatively the same as evidenced by the comparable funding mix of 33%/67% in Q1-2014 versus 32%/68% in Q2-2015.

Beyond the impact of the noninterest income and expense from this division, the Bank earns interest income at the respective note rates on the balance of loans originated by the division from the time the loan is funded until it is sold to a secondary market investor. The average outstanding daily balance of residential mortgage loans available for sale was $102,026,000 for the three months ended March 31, 2015 and $54,025,000 for the three months ended March 31, 2014. The interest income earned on these loans available for sale was $966,000 and $576,000 for the three months ended March 31, 2015 and 2014 respectively.

Note 5 - Net Interest Income

The Bank's net interest income is determined by the level of our earning assets, primarily loans outstanding, and the management of our net interest margin. For the quarter ended March 31, 2015 net interest income totaled $3,915,000 as compared to $3,391,000 for the quarter ended March 31, 2014 for an increase of $524,000. On a consecutive quarter basis, net interest income was down by $140,000 or 4%, from the $4,055,000 earned during the quarter ended December 31, 2014.

Total interest income increased by $494,000 to $4,460,000 for the three months ended March 31, 2015 compared to $3,966,000

for the three months ended March 31, 2014. On a consecutive quarter basis, total interest income decreased by $162,000 or 4%, from the $4,622,000 earned during the quarter ended December 31, 2014.

The impact of the interest rate environment is seen in the Prime interest rate, which has been set at a historical low rate of 3.25% since December 16, 2008. This historic low Prime interest rate has had an extremely negative impact on the yield earned by the Bank on that portion of the loan portfolio that carry rates based on the Prime interest rate index. At March 31, 2015 and March 31, 2014 the Bank held $123,968,000 and $114,086,000 respectively, in loans carrying rates based on the Prime interest rate index.

In addition to the lower interest rate environment for the first quarter of 2015, net interest income was negatively impacted by the increase in the lower yielding Loans held for sale category from an average of $89,629,000 in the fourth quarter of 2014 to $102,026,000 for the first quarter of 2015, an increase of $12,397,000, or 14%. In addition short term wholesale funding balances increased at a relatively higher cost of funds as compared to other core deposit sources from an average of $74,787,000 for the fourth quarter of 2014 as compared to $79,786,000 for the first quarter of 2015, an increase of $4,999,000, or 6.7%. Average earning assets increased to an average balance of $403,864,000 during the quarter ended March 31, 2015, up by $63,651,000, or 19%, from the average balance during the quarter ended March 31, 2014. The most significant increase in interest income was in interest earned on mortgage loans held for sale, which increased $398,000 to $974,000 during the first quarter of 2015, compared to $576,000 during the first quarter of 2014. Interest and fees earned on portfolio loans increased by $213,000 or 7%, to $3,281,000, in the three months ended March 31, 2015 from $3,068,000 in the three months ended March 31, 2014. Interest income from investment securities decreased $116,000, or 36%, to $205,000 in the three months ended March 31, 2015 compared to $321,000 earned in the three months ended March 31, 2014. On a consecutive quarter basis, interest income from investments decreased $34,000 from $238,000 earned during the quarter ended December 31, 2014. Interest and fees earned on loans increased by $611,000 or 17%, to $4,255,000 for the three month period ended March 31, 2015 compared to $3,644,000 for the same three month period in 2014.

Interest income not recognized on non-accruing loans totaled $39,000 during the three months ended March 31, 2015 as a result of the increasing levels of non-accrual loans. During the first quarter of 2014, we lost income on nonaccrual loans totaling $12,000.

Total interest expense decreased $28,000 or 5%, to $588,000 for the three months ended March 31, 2015 compared to $616,000 for the same period in 2014. On a consecutive quarter basis, total interest expense decreased by $22,000, or 4%, from $610,000 expensed during the quarter ended December 31, 2014.

The net interest margin is a performance metric that reflects how successful the Bank's investment decisions have been relative to its funding choices. It is calculated by dividing the annualized net interest income by the balance of the average earning assets for the period. The net interest margin realized on earning assets decreased by 2 basis points to 3.89% for the three months ended March 31, 2015 when compared to the 3.91% net interest margin earned during the same three months in 2014. On a consecutive quarter basis, the net interest margin decreased by 11 basis points from 4.00% during the quarter ended December 31, 2014. The primary driver of the relatively small decline in net interest margin over these two timeframes is as a result of the increase in the balance of the loans held for sale and loan sales receivable that carry lower interest earning note rates as compared to the other loan categories on our balance sheet.

The net interest rate spread is the difference between the average yield earned by the Bank on loans, investment securities and other earning assets, and the rate paid by the Bank on interest bearing deposits and other borrowings. The net interest rate spread decreased by 11 basis points to 3.69% for the three months ended March 31, 2015 compared to the 3.80% net interest rate spread earned during the same three month period in 2014. On a consecutive quarter basis, the net interest rate spread also decreased by 21 basis points from 3.90% during the quarter ended December 31, 2014 for the same reason as discussed above in regards to net interest margin.

Note 6 - Provision and Allowance for Loan Losses

There are risks inherent in making all loans, including risks with respect to the period of time over which loans may be repaid, risks resulting from changes in economic and industry conditions, risks inherent in dealing with individual borrowers, and, in the case of a collateralized loan, risks resulting from uncertainties about the future value of the collateral. We establish and maintain an allowance for loan losses based on a number of qualitative factors including, among other things, historical experience, evaluation of economic conditions, regular reviews of delinquencies and loan portfolio quality and a number of assumptions about future events, which we believe to be reasonable, but which may not prove to be accurate. We believe that changes in economic and industry conditions capture the impact of general declines in the value of collateral property, and in this way our qualitative factors reflect general declines in collateral values.

To the extent that the recovery of loan balances has become collateral dependent, we obtain appraisals not less than annually, and we reduce these appraised values for selling and holding costs to determine the liquidated value. Any shortfall between the liquidated value and the loan balance is charged against the allowance for loan losses in the month the related appraisal was received. In the ordinary course of managing and monitoring nonperforming loans, information may come to our attention that indicates the collateral value has declined further from the value established in the most recent appraisal. Such other information

may include prices on recent comparable property sales or internet based property valuation estimates. In cases where this other information is deemed reliable, and the impact of a further reduction in collateral value would result in a further loss to the Company, we will record an increase to the allowance to reflect the additional estimated collateral shortfall.

The provision for loan losses is the periodic charge to operating earnings that management believes is necessary to maintain the allowance for possible loan losses at an adequate level. The amounts of these periodic charges are based on management's analysis of the potential risk in the loan portfolio. This analysis includes, among other things, evaluation of the trends in key loan portfolio metrics as follows:

(In thousands)	March 31, 2015	December 31, 2014	September 30, 2014	June 30, 2014	March 31, 2014	December 31, 2013	September 30, 2013	June 30, 2013
Portfolio loans, gross	$ 270,230	272,757	267,393	258,022	253,803	244,543	$ 232,872	$ 235,566
Loans past due > 30 days and still accruing interest	$ 2	806	455	1,720	152	785	$ 261	$ 584
Loans on nonaccrual	$ 4,629	4,330	2,881	2,787	2,045	2,116	$ 3,152	$ 3,673
(as a % of loans, gross)	1.71%	1.59%	1.08%	1.08%	0.81%	0.87%	1.35%	1.56%
Net loan charge offs (recoveries)	$ (76)	72	256	85	249	64	$ 92	$ 412
(as a % of loans, gross)	.03%	0.03%	0.10%	0.03%	0.10%	0.03%	0.04%	0.18%

Portfolio loans, gross addresses the impact on the provision for loan losses from changes in the size and composition of our loan portfolio. In the past we applied various reserve factors to our portfolio based on the risk-rated categories of loans because we had relatively little charge off activity prior to the quarter ended December 31, 2008. As a result of increasing charge off activity over the past four years, we now rely more on historical levels and trends to establish various reserve percentages based on the relative inherent risk for a particular loan type and grade. The inherent risk is established based on peer group data, information from regulatory agencies, the experience of the Bank's lending officers, and recent trends in portfolio losses. These reserve factors are continuously evaluated and subject to change depending on trends in national and local economic conditions, the depth of experience of the Bank's lenders, delinquency trends and other factors. We have made an effort over the last several years to lower the risk profile of our loan portfolio. In doing so, our loan portfolio size decreased during 2012 and the first three quarters of 2013 primarily from reductions in higher risk rated commercial real estate construction loans and since that time we have increased comparably lower risk rated owner occupied residential real estate loans.

Loans past due greater than 30 days and still accruing interest has proven to be a useful leading indicator of directional trends in future loan losses. As the level of this metric rises, expectations are for a comparable increase in loans moving into a nonaccrual status and ultimately foreclosure resulting in increased losses. This pattern has been observed in the past where increases in loans past due greater than 30 days and still accruing are followed in future quarters with the same directional changes in the level of loans on nonaccrual. The level of loans past due greater than 30 days and still accruing interest totaled $2,000 at March 31, 2015, a decrease of $804,000 or 99% as compared to $806,000 at December 31, 2014. Loans past due greater than 30 days and still accruing had declined to $152,000 at March 31, 2014, the lowest level in over six years, then spiked up to $1.7 million at the end of Q2-2014 before dropping back to the current level of $2,000. Management intends to carefully monitor past due loans and work aggressively to manage loan delinquency levels. While the long term trend in credit quality over the last five years has improved significantly, we continue to experience ups and downs throughout the process. While the weakening loan quality that began in late 2008 will continue to be an area of concern in future periods, the trends are clearly pointing to an improving and stable credit environment.

Loans on nonaccrual has been another leading indicator of potential future losses from loans. We typically place loans on nonaccrual status when they become 90 days past due. In addition to the interest lost when a loan is placed on nonaccrual status, there is an increased probability of a loan on nonaccrual moving into foreclosure with a potential loss outcome. Although it is not shown in the table above, the level of loans on nonaccrual peaked at $25,925,000 at June 30, 2009 and then declined by 50% over the following three quarters to $12,992,000 at March 31, 2010. From that March 31, 2010 low point, loans on nonaccrual gradually increased again to peak at $25,399,000 in mid-2011 which was very near the mid-2009 high point. Once again we saw a downward trend over the following nine quarters; however, after the mid-2011 spike the improvement in nonaccrual balances has generally been sustained. The March 31, 2015 balance of $4,629,000 is a moderate increase of $299,000 over the previous quarter end, however the increase in loans on nonaccrual it is not reflective of new credit problems or general deterioration of the overall portfolio credit quality. Management intends to remain vigilant in our loan monitoring and loss mitigation efforts to either rehabilitate these credits or maximize recovery if required.

Net loan charge offs or recoveries reflect our practice of charging recognized losses to the allowance and adding subsequent recoveries back to the allowance. During the three months ended March 31, 2015, as credit quality in the loan portfolio has continued to improve, we recorded net recoveries of $76,000. This amount represented a decrease of $148,000, or 206%, from the

$72,000 in net charge offs recorded during the prior quarter ended December 31, 2014, and a decrease of $325,000, or 131% from the $249,000 in net charge offs during the same quarter in the prior year.

Prior to the fourth fiscal quarter of 2008, we had very little charge off activity and therefore, had limited historical information upon which to base past estimates. Since 2009 charge off activity has been volatile and difficult to predict, but we continue to assess the implications of trends in recent charge off activity on potential future losses. The recent volatility in the level of quarterly net loan charge offs or recoveries makes it difficult to identify a specific trend or establish reliable future expectations. As a result, there can be no assurance that charge offs of loans in future periods will not increase or exceed the allowance for loan losses as estimated at any point in time or that provisions for loan losses will not be significant to a particular accounting period. Thus, there is a risk that substantial additional increases in the allowance for loan losses could be required, which would result in a decrease in our net income and possibly our capital.

In addition to considering the metrics described above, we evaluate the collectability of individual loans, the balance of impaired loans, economic conditions that may affect the borrower's ability to repay, the amount and quality of collateral securing the loans and a review of specific problem loans. Based on this process and as shown below, the provision charged to expense was $260,000 for the three months ended March 31, 2015 as compared to $256,000 for the three months ended March 31, 2014. On a consecutive quarter basis, the provision was $6,000 or 2%, less than the $266,000 provision charged to expense during the quarter ended December 31, 2014.

(In thousands)	March 31, 2015	December 31, 2014	September 30, 2014	June 30, 2014	March 31, 2014	December 31, 2013	September 30, 2013	June 30, 2013
Provision during quarter ended	$ 260	266	223	473	256	83	171	57
Provision added in excess of (less than) net charge-offs	$ 336	194	(33)	388	7	19	79	(355)
Allowance for loan losses	$ 5,165	4,829	4,635	4,668	4,280	4,273	4,254	4,175
(as a % of loans, gross)	1.91%	1.77%	1.73%	1.81%	1.69%	1.75%	1.83%	1.77%

The difference between the amount of the provision for loan losses and net loan charge offs will result in expansion or shrinkage to the level of the allowance for loan losses. As shown above, during the three months ended March 31, 2015, the current provision for loan losses of $260,000 exceeded the net recoveries against the allowance of $76,000 by $336,000. The result was an increase to the allowance for loan losses of $336,000 to a level of $5,165,000 or 1.91% of gross loans outstanding at March 31, 2015 as compared to $4,829,000 or 1.77% of gross loans outstanding at December 31, 2014.

From a historical perspective, prior to 2008, while the level of loans on nonaccrual was relatively stable, the allowance for loan losses was maintained in the range of 1.2% to 1.3% of the balance of gross loans. As we moved into 2008 and experienced an increase in loans on nonaccrual, it was determined that an increase to the allowance level was appropriate given the projected increased risk of loss, so the allowance was increased to a range of 1.4% to 1.6% during 2008. The weakening of the loan portfolio performance continued into 2009 with actual loss levels that exceeded projections from earlier in 2008, resulting in the decision to increase the allowance level further, to the range of 1.6% to 1.8% in early 2009. With nonaccrual loans reaching a peak in mid-2009, further analysis and projections of potential loan losses in the Bank's existing portfolio supported a further increase in the allowance level to a range of 2.0% to 2.3% of gross loans outstanding, which was sustained through the end of 2012. As we moved into the final two quarters of 2012 and first three quarters of 2013 we experienced significant improvement in loan portfolio performance with most key asset quality metrics improving to levels last reported during 2008. Based on these improving trends and current projections of future potential loses, we have reduced our target allowance level to a range of 1.60% to 1.85% of gross loans outstanding. Management believes that the changes in the level of the allowance for loan losses are directionally consistent with the trends observed in the various asset quality metrics discussed above.

Management continues to carefully monitor past due and nonaccrual loans. Management acknowledges that future asset quality results may vary from our estimates and expectations, resulting in negative asset quality metrics, which could have a material adverse effect on our results of operations and financial condition.

Note 7 - Noninterest Income

Noninterest income for the three months ended March 31, 2015 totaled $14,561,000 as compared to $5,593,000 for the three months ended March 31, 2014. Mortgage banking income was $14,299,000 for the quarter ended March 31, 2015 compared to $4,480,000 for the same period during 2014 for an increase of $9,819,000 or 219%. SBA loan income declined $830,000 or 91% to $82,000 for the three month period ended March 31, 2015 compared to $912,000 for the first quarter of 2014 as a result of management's decision to retain the majority of new production on the bank's balance sheet versus selling this production into the secondary market.

Note 8 - Noninterest Expense

Total noninterest expense for the three months ended March 31, 2015 was $16,181,000 as compared to $8,395,000 for the same period in 2014. The year-over-year increase in noninterest operating expense of $7,786,000 is due largely to increased expenses in the mortgage banking division. Noninterest expenses related to the mortgage banking division increased $8,376,000 or 163%, to $13,528,000 for the first quarter of 2015 compared to expenses of $5,152,000 in the first quarter of 2014.

Salaries and benefits totaled $13,154,000 for the three months ended March 31, 2015 compared to $5,526,000 for the same period a year ago, for an increase of $7,628,000. Salaries and benefits increased $7,818,000 in the mortgage division offset by a $169,000 decrease in the SBA lending division and a $22,000 decrease in the community banking division.

Other real estate expense decreased $341,000 to $5,000 for the first quarter of 2015 compared to $346,000 during the same period of 2014. During 2014 we experienced higher levels of nonperforming assets, which caused the Company to record increased carrying costs on foreclosed properties and losses on the sale of foreclosed properties. While the level of nonperforming assets is still elevated, their related costs have continued to decline in 2015 and will generally trend downward as we continue efforts to further reduce the level of nonperforming assets.

Note 9 – Investment Securities

Investment securities are as follows:

	March 31, 2015			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available for sale				
State and municipal securities	$ 3,157,882	$ 311,226	$ —	$ 3,469,108
Mortgage-backed securities	20,222,601	419,422	(10,054)	20,631,969
	$ 23,380,483	$ 730,648	$ (10,054)	$ 24,101,077
Held to maturity				
Corporate debt securities	$ 100,000	$ —	$ —	$ 100,000
	$ 100,000	$ —	$ —	$ 100,000

	December 31, 2014			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available for sale				
State and municipal securities	$ 3,165,203	$ 294,072	$ —	$ 3,459,275
Mortgage-backed securities	21,120,101	301,808	(44,559)	21,377,350
	$ 24,285,304	$ 595,880	$ (44,559)	$ 24,836,625

Note 10 — Loans and allowance for loan losses

The composition of loans is summarized as follows:

	March 31, 2015	December 31, 2014
Commercial and financial	$ 14,976,755	$ 13,267,236
Agricultural	—	3,747
Real estate – construction, commercial	23,905,579	24,420,805
Real estate – construction, residential	9,356,855	9,356,855
Real estate – mortgage, commercial	99,183,408	97,704,811
Real estate – mortgage, residential	121,281,810	126,418,534
Real estate – mortgage, farmland	261,029	263,847
Consumer installment loans	1,260,882	1,320,835
Other	3,404	—
Gross loans	270,229,722	272,756,670
Less: Allowance for loan losses	5,164,722	4,828,899
Net loans	$ 265,065,000	$ 267,927,771

The Bank grants loans and extensions of credit to individuals and a variety of businesses and corporations located in its general trade areas of Beaufort County, South Carolina, Nassau County, Florida and Thomas County, Georgia. Although the Bank has a diversified loan portfolio, a substantial portion of the loan portfolio is collateralized by improved and unimproved real estate and is dependent upon the real estate market.

Loans exhibiting one or more of the following attributes are placed on a nonaccrual status:

a.) Principal and/or interest is 90 days or more delinquent, unless the obligation is (i) well secured by collateral with a realizable value sufficient to discharge the debt including accrued interest in full, and (ii) in the process of collection, which is reasonably expected to result in repayment of the debt or in its restoration to a current status.

b.) A borrower's financial condition has deteriorated to such an extent, or some condition exists, that makes collection of interest and/or principal in full unlikely in management's opinion.

c.) Foreclosure or legal action has been initiated as a result of default by the borrower on the terms of the debt.

The following is a summary of current, past due and nonaccrual loans:

	March 31, 2015						
(In thousands)	30-59 Days Past Due	60-89 Days Past Due	Greater than 90 Days Past Due & Accruing	Nonaccrual	Total Past Due & Nonaccrual	Current Loans	Total Loans
Commercial and financial	$ —	—	$ —	$ 19	$ 19	$ 14,958	$ 14,977
Agricultural	—	—	—	—	—	—	—
Real estate – construction, commercial	—	—	—	452	452	23,454	23,906
Real estate – construction, residential	—	—	—	210	210	9,147	9,357
Real estate – mortgage, commercial	—	—	—	2,476	2,476	96,707	99,183
Real estate – mortgage, residential	—	—	—	1,472	1,472	119,810	121,282
Real estate – mortgage, farmland	—	—	—	—	—	261	261
Consumer installment loans	2	—	—	—	2	1,259	1,261
Other	—	—	—	—	—	3	3
	$ 2	$ —	$ —	$ 4,629	$ 4,631	$ 265,599	$ 270,230

	December 31, 2014						
(In thousands)	30-59 Days Past Due	60-89 Days Past Due	Greater than 90 Days Past Due & Accruing	Nonaccrual	Total Past Due & Nonaccrual	Current Loans	Total Loans
Commercial and financial	$ 7	—	$ —	$ 91	$ 98	$ 13,169	$ 13,267
Agricultural	—	—	—	—	—	4	4
Real estate – construction, commercial	451	—	—	210	661	23,760	24,421
Real estate – construction, residential	54	—	—	—	54	9,303	9,357
Real estate – mortgage, commercial	—	—	—	2,555	2,555	95,150	97,705
Real estate – mortgage, residential	294	—	—	1,474	1,768	124,650	126,418
Real estate – mortgage, farmland	—	—	—	—	—	264	264
Consumer installment loans	—	—	—	—	—	1,321	1,321
	$ 806	$ —	$ —	$ 4,330	$ 5,136	$ 267,621	$ 272,757

Other Risk Elements in the Loan Portfolio

The following is a summary of other risk elements in the loan portfolio:

	Loans with Interest Only Payments			
(In thousands)	March 31, 2015		December 31, 2014	
Commercial and financial	$ 2,894	8%	$ 3,247	8%
Real estate – construction, commercial	9,047	24%	9,070	21%
Real estate – construction, residential	3,187	8%	4,857	11%
Real estate – mortgage, commercial	5,412	14%	5,442	13%
Real estate – mortgage, residential	17,641	46%	19,719	47%
Consumer installment loans	73	—%	81	—%
Other	4	—%	4	—%
	$ 38,258		$ 42,420	

As shown above, we have a moderate concentration of interest only loans in our portfolio, and such loans are generally regarded as carrying a higher risk profile than fully amortizing loans. It is important to note that none of the interest only loans in our portfolio allow negative amortization, nor do we have any loans with capitalized interest reserves.

Balances within the major loans receivable categories and geographic concentration of the loan portfolio are presented below:

	Geographic Concentration of Loan Portfolio			
	March 31, 2015			
(In thousands)	Florida	Georgia	South Carolina	Other
Commercial and financial	$ 7,386	$ 2,371	$ 3,452	$ 1,703
Agricultural	—	—	3	—
Real estate – construction, commercial	9,691	2,151	11,321	1,628
Real estate – construction, residential	3,527	1,504	3,249	192
Real estate – mortgage, commercial	47,558	16,142	31,993	3,554
Real estate – mortgage, residential	46,243	39,822	28,404	6,813
Real estate – mortgage, farmland	—	261	—	—
Consumer installment loans	403	261	477	121
	$ 114,808	$ 62,512	$ 78,899	$ 14,011

	Geographic Concentration of Loan Portfolio			
	December 31, 2014			
(In thousands)	Florida	Georgia	South Carolina	Other
Commercial and financial	$ 6,346	$ 2,333	$ 3,604	$ 984
Agricultural	—	—	4	—
Real estate – construction, commercial	9,025	2,232	11,511	1,653
Real estate – construction, residential	3,459	2,420	3,450	28
Real estate – mortgage, commercial	47,911	15,417	31,324	3,053
Real estate – mortgage, residential	48,560	41,045	28,599	8,214
Real estate – mortgage, farmland	—	264	—	—
Consumer installment loans	424	274	549	74
	$ 115,725	$ 63,985	$ 79,041	$ 14,006

We also monitor and evaluate several other loan portfolio characteristics at a total portfolio level rather than by major loan category. These characteristics include:

Junior Liens – Loans secured by liens in subordinate positions tend to have a higher risk profile than loans secured by liens in the first or senior position. At March 31, 2015 the Company held $17,781,000 of loans secured by junior liens, which represented approximately 6.6% of the total net loan portfolio. Net loan recoveries were $79,000 during the three months ended March 31, 2015 for all loans secured by junior liens for an annualized net recovery rate of 1.77%. At December 31, 2014 the Company held $17,681,000 of loans secured by junior liens which represented approximately 6.5% of the total net loan portfolio.

High Loan to Value Ratios – Typically the Company will not originate a new loan with a loan to value (LTV) ratio in excess of 100%. However, declines in collateral values can result in the case of an existing loan renewal with an LTV ratio in excess of 100% based on the current appraised value of the collateral. In such cases the borrower may be asked to pledge additional collateral or to renew the loan for a lesser amount. If the borrower lacks the ability to pay down the loan or provide additional collateral, but has the ability to continue to service the debt, the loan will be renewed with an LTV ratio in excess of 100%. At March 31, 2015 the loan portfolio included 57 loans with an aggregate balance of $18,138,000 or 6.8% of the net loan portfolio, with LTV ratios in excess of 100%. At December 31, 2014 the loan portfolio included 59 loans with an aggregate balance of $20,053,000 or 7.4% of the net loan portfolio, with LTV ratios in excess of 100%.

Restructured Loans – Historically, the Company has followed a conservative approach by classifying any loan as restructured whenever the terms of a loan were adjusted to the benefit of any borrower in financial distress, regardless of the status of the loan at the time of restructuring. In some cases we have restructured loans for borrowers who were not delinquent, but for various reasons these borrowers were experiencing financial distress that raised a doubt about their continued ability to make payments under current terms. By adjusting the terms of the loan to better fit the borrower's current financial condition, expectations are that the loan will avoid a future default. In other cases we have restructured loans for borrowers who were in default at the time the loan terms were restructured. The expectation is that by adjusting the terms of such loans, the borrower may begin to make payments again based on the improved loan terms.

The types of changes that are made for troubled borrowers to restructure their obligations may include one or more of the following:

- Deferral of one or more scheduled loan payments to a future date
- Temporary or permanent reduction of the loan interest rate
- Conversion from principal and interest payment term to an interest only payment term on a temporary basis, or until maturity
- Forgiveness of accrued but uncollected interest
- Extension of loan maturity date
- Reduction in principal due under the loan agreement

The potential financial effects of restructuring troubled debts includes a reduction in the level of interest income collected, a complete loss of interest income, or a loss of some portion of the original loan principal. All troubled debt restructurings are tested for impairment. If a loan is considered to be collateral dependent, the measurement of impairment is based on the fair value of the collateral, net of estimated liquidation costs. If the loan is not considered to be collateral dependent, the present value of expected future cash flows is used to determine any amount of impairment. Any impairment is then charged to the allowance for loan and lease losses or designated as a specific reserve, and as such will be considered as a component of the reserve calculation.

The following table provides a summary of all loans that are currently designated as restructured for regulatory purposes.

	March 31, 2015			December 31, 2014		
Troubled debt restructurings	**Number of loans**	**Recorded Investment**	**Unpaid Principal Balance**	**Number of loans**	**Recorded Investment**	**Unpaid Principal Balance**
Real estate – construction	—	$ —	$ —	—	$ —	$ —
Real estate – mortgage	12	6,560,912	6,678,032	12	6,659,886	7,018,289
Total troubled debt restructurings	12	$ 6,560,912	$ 6,678,032	12	$ 6,659,886	$ 7,018,289

The following table provides the payment status as of March 31, 2015 and 2014 of all loans that were restructured in the twelve month periods ending on those respective dates.

	March 31, 2015		March 31, 2014	
	Number of loans	**Recorded Investment**	**Number of loans**	**Recorded Investment**
Restructured loans less than 30 days past due				
Real estate – mortgage	1	$ 730,932	1	$ 394,020
Total restructured loans less than 30 days past due	1	$ 730,932	1	$ 394,020
Total restructured loans 30 days or more past due	—	—	—	—
Restructured loans on nonaccrual	—	—	—	—
Total restructured loans on nonaccrual	—	—	—	—

Loans classified as Special Mention or Substandard – Management evaluates all loan relationships periodically in order to assess the financial strength of the borrower and the value of any underlying collateral. Loans that are found to have a potential or actual weakness are classified as special mention or substandard and subject to increased monitoring by management. This typically includes frequent contact with the borrower to actively manage the borrowing relationship as needed to rehabilitate or mitigate the weakness identified. A summary of loan credit quality is presented below:

(In thousands)	March 31, 2015			
	Pass	**Special Mention**	**Substandard**	**Total**
Commercial and financial	$ 13,909	$ 1,034	$ 34	$ 14,977
Agricultural	—	—	—	—
Real estate – construction, commercial	23,454	—	452	23,906
Real estate – construction, residential	9,147	—	210	9,357
Real estate – mortgage, commercial	94,745	1,891	2,547	99,183
Real estate – mortgage, residential	118,181	1,629	1,472	121,282
Real estate – mortgage, farmland	261	—	—	261
Consumer installment loans	1,261	—	—	1,261
Other	1	—	2	3
	$ 260,959	$ 4,554	$ 4,717	$ 270,230

(In thousands)	December 31, 2014			
	Pass	**Special Mention**	**Substandard**	**Total**
Commercial and financial	$ 12,056	$ 1,100	$ 111	$ 13,267
Agricultural	4	—	—	4
Real estate – construction, commercial	23,759	452	210	24,421
Real estate – construction, residential	9,357	—	—	9,357
Real estate – mortgage, commercial	92,949	2,128	2,628	97,705
Real estate – mortgage, residential	123,308	1,579	1,531	126,418
Real estate – mortgage, farmland	264	—	—	264
Consumer installment loans	1,319	—	2	1,321
	$ 263,016	$ 5,259	$ 4,482	$ 272,757

Management has established an allowance for loan losses through a provision for loan losses charged to expense on the statement of earnings. Additions to the allowance for loan losses are made periodically to maintain the allowance at an appropriate level based on management's analysis of the potential risk in the loan portfolio. The allowance for loan losses represents an amount, which is believed to be adequate to absorb probable losses on existing loans that may become uncollectible. Management's judgment as to the adequacy of the allowance for loan losses is based upon a number of assumptions about future events, which are believed to be reasonable, but which may or may not prove to be accurate. To the extent that the recovery of loan balances has become collateral dependent, the Bank obtains appraisals not less than annually, and then reduces these appraised values by the amount estimated for selling and holding costs to determine the liquidated value. Any shortfall between the liquidated value and the loan balance is charged against the allowance for loan losses in the month the related appraisal was received. Losses will undoubtedly vary from management estimates, and there is a possibility that charge-offs can reduce this allowance. Management's determination of the allowance for loan losses is based on evaluations of the collectability of loans, including consideration of factors such as the balance of impaired loans, the quality, mix, and size of the overall loan portfolio, economic conditions that may affect the borrower's ability to repay, commercial and residential real estate market trends, the amount and quality of collateral securing the loans, the Bank's historical loan loss experience, and a review of specific problem loans. Management also considers subjective issues such as changes in the lending policies and procedures, changes in the local/national economy, changes in volume or type of credits, changes in volume/severity of problem loans, quality of loan review and board of director oversight, concentrations of credit, and peer group comparisons.

An analysis of the activity in the allowance for loan losses is presented below:

	For the Three Months Ended March 31,	
	2015	2014
Balance, beginning of year	$ 4,828,899	$ 4,273,099
Provision for loan losses	260,345	255,588
Loans charged off	(51,608)	(453,179)
Recoveries of loans previously charged off	127,085	204,910
Balance, end of period	$ 5,164,723	$ 4,280,418

Note 11 — SBA Loan Servicing Rights

Loan Servicing Rights (LSR) are initially booked at an estimated original fair value during the current quarter. At quarter end the estimated original fair value is determined by an independent evaluation at loan level detail, less accumulated amortization with any resulting adjustment to SBA loan income. Amortization is recorded over the expected life of the loan as a component of SBA loan income. Under the amortization method, loan servicing rights are amortized in proportion to, and over the period of, estimated servicing income. The LSR asset is evaluated for impairment at the end of each quarter, by obtaining a current fair value from an independent third party. For the period ended March 31, 2015, the carrying value of the SBA LSRs was $1,569,000 and the fair value of the SBA LSRs was $1,981,000. As of December 31, 2014, the carrying value of the SBA LSRs was $1,659,000 and the fair value of the SBA LSRs was $1,970,000. As a result of the quarterly independent valuation process, no valuation allowance was required at either period end. The related balance of SBA loans participated and serviced for others was $80,341,000 at March 31, 2015 and $82,474,000 at December 31, 2014.

The fair value of loan servicing rights typically rises as market interest rates increase and declines as market interest rates decrease; however, the extent to which this occurs depends in part on (1) the magnitude of changes in market interest rates, and (2) the differential between the then current market interest rates for mortgage loans and the mortgage interest rates included in the loan-servicing portfolio. Since sales of mortgage servicing rights tend to occur in private transactions and the precise terms and conditions of the sales are typically not readily available, there is a limited market to refer to in determining the fair value of loan servicing rights. As such, like other participants in the SBA loan servicing business, we determine value of loan servicing rights by estimating the present value of the future income stream attained from all of the servicing related cash flows. The value is the sum on the present value of these future income streams, which is impacted by assumptions on prepayment speeds, age and type of the underlying mortgage, and the rate at which these cash flows are discounted. The present value of the portfolio's expected stream of future cash flows is determined though a loan level analysis utilizing assumptions that would be used by other market participants. The valuation incorporates a five step process. Three income elements that include servicing value, remittance value, and additional income are determined as a present value of the respective estimated cash flows from each loan. Finally, the servicing cost, also expressed as a dollar amount per loan, is valued. The net servicing value for each loan is then determined by subtracting the servicing cost from the three income values.

Note 12 — Other Real Estate Owned

A summary of other real estate owned is presented as follows:

	Three Months Ended March 31,	
	2015	2014
Balance, beginning of year	$ 7,322,404	$ 11,544,720
Additions	118,192	1,187,852
Disposals	(520,603)	(855,988)
Valuation write downs and gains/(losses) on sales	4,686	(239,569)
Balance, end of period	$ 6,924,679	$ 11,637,015

Expenses related to other real estate owned include the following:

	Three Months Ended March 31,	
	2015	2014
Net (gain)/loss on sales of real estate	$ (4,686)	$ 66,399
Valuation write downs	—	173,169
Operating expenses, net	3,172	106,644
	$ (1,514)	$ 346,212

Other real estate owned represents collateral property taken back from borrowers in partial or full satisfaction of their defaulted debt obligation to the Company. We track our historical experience of loans that ultimately convert to other real estate owned by collateral type and by geographic exposure as shown on the following tables:

	Book Value of Other Real Estate at March 31, 2015			
(In thousands)	Florida	Georgia	South Carolina	Total
Residential	$ 224	$ —	$ 111	$ 335
Commercial	2,489	39	1,159	3,687
Finished lots	263	—	551	814
Raw land	1,834	—	255	2,089
	$ 4,810	$ 39	$ 2,076	$ 6,925

	Number of Parcels at March 31, 2015			
	Florida	Georgia	South Carolina	Total
Residential	1	—	1	2
Commercial	3	1	8	12
Finished lots	6	—	38	44
Raw land	5	—	1	6
	15	1	48	64

	Book Value of Other Real Estate at December 31, 2014			
(In thousands)	Florida	Georgia	South Carolina	Total
Residential	$ 223	$ —	$ 159	$ 382
Commercial	2,410	—	1,627	4,037
Finished lots	263	—	551	814
Raw land	1,834	—	255	2,089
	$ 4,730	$ —	$ 2,592	$ 7,322

	Number of Parcels at December 31, 2014			
	Florida	Georgia	South Carolina	Total
Residential	1	—	3	4
Commercial	2	—	9	11
Finished lots	6	—	38	44
Raw land	5	—	1	6
	14	—	51	65

During the three months ended March 31, 2015 we sold 3 other real estate owned properties with a total book value of $516,000. The net proceeds from these sales were $521,000 which resulted in a net recovery of approximately 74% of the original loan amounts and 101% of the book value of the other real estate sold. During the three months ended March 31, 2014 we sold a total of 5 other real estate owned properties with a total book value of $922,000. The net proceeds from these sales were $856,000 which resulted in a net recovery of approximately 51% of the original loan amounts and 93% of the book value of the other real estate sold.

The Bank's special asset group is charged with the administration and liquidation of other real estate owned. Our approach has been to manage each property individually in such a way as to maximize our net proceeds upon sale. Management continues to evaluate other methods to liquidate these properties more quickly, but such methods typically result in a much lower recovery relative to the original loan amount. Management attempts to balance the desire to aggressively drive down the level of nonperforming assets with the objective to maximize recovery levels from liquidation of these assets.

Note 13 — Deposits

Total deposits increased by $38,916,000 or 14%, to a total of $324,579,000 at March 31, 2015 from $285,663,000 at December 31, 2014. This increase was primarily from the addition of brokered deposits with terms of four to thirteen weeks that were used to fund the growth in the balance of mortgage loans available for sale and the related loan sales receivable. Noninterest-bearing demand deposits increased $3,502,000 or 10%, while interest-bearing deposits increased $35,414,000 or 14%. The Company has continued its use of brokered deposits, which typically carry substantially lower interest rates than comparable term core retail deposits. Brokered deposits are issued in individual's names and in the names of trustees with balances participated out to others. Core retail deposits are deposits which are gathered in the normal course of business, without the use of a broker. Core reciprocal deposits are gathered in the same manner as core retail deposits, but the funds are participated out to other banks through use of the CDARS reciprocal transactions program. The CDARS program allows depositors to obtain FDIC insurance for deposits up to $50 million by exchanging the portions of their deposits in excess of FDIC insurance limitations with other financial institutions participating in the CDARS program. In return, we receive an equal amount of deposits back from other CDARS participating financial institutions, such that there is no net change in the level of total deposits on our balance sheet.

Balances and percentages within the major deposit categories are as follows:

	March 31, 2015			
(In thousands)	Core Retail Deposits	Core CDAR's Deposits	Brokered Deposits	Total Deposits
Noninterest-bearing demand deposits	$ 38,431	$ —	$ —	$ 38,431
Interest-bearing demand deposits	124,452	—	—	124,452
Savings deposits	4,721	—	—	4,721
Certificates of deposit $100,000 and over	39,690	24,882	39,270	103,842
Other time deposits	34,313	2,479	16,341	53,133
	$ 241,607	$ 27,361	$ 55,611	$ 324,579

	December 31, 2014			
(In thousands)	Core Retail Deposits	Core CDAR's Deposits	Brokered Deposits	Total Deposits
Noninterest-bearing demand deposits	$ 34,930	$ —	$ —	$ 34,930
Interest-bearing demand deposits	117,750	—	—	117,750
Savings deposits	4,510	—	—	4,510
Certificates of deposit $100,000 and over	41,050	35,826	—	76,876
Other time deposits	36,589	1,168	13,840	51,597
	$ 234,829	$ 36,994	$ 13,840	$ 285,663

Note 14 - Other Borrowings

Other Borrowings of $126,000,000 at March 31, 2015 are composed of advances from the Federal Home Loan Bank of Atlanta (FHLB) and represent an increase of $42,500,000 from advances totaling $83,500,000 at December 31, 2014.

FHLB advances outstanding and related terms at March 31, 2015 and December 31, 2014 are shown in the following tables:

		FHLB Advances Outstanding March 31, 2015		
Type advance	Balance	Interest rate	Maturity date	Convertible date
Fixed rate	$ 11,000,000	0.19%	April 3, 2015	
Fixed rate	5,000,000	0.19%	April 13, 2015	
Fixed rate	5,000,000	0.20%	April 15, 2015	
Fixed rate	5,000,000	0.21%	April 16, 2015	
Fixed rate	5,000,000	0.21%	April 17, 2015	
Fixed rate	5,000,000	0.21%	April 23, 2015	
Fixed rate	10,000,000	0.19%	April 23, 2015	
Fixed rate	10,000,000	0.19%	April 23, 2015	
Fixed rate	5,000,000	0.19%	April 27, 2015	
Fixed rate	10,000,000	0.19%	May 28, 2015	
Fixed rate	5,000,000	2.09%	August 10, 2015	
Variable rate overnight advance	38,000,000	0.36%		
Fixed rate	5,000,000	1.95%	August 9, 2016	
Fixed rate	2,000,000	2.84%	August 9, 2017	
Convertible fixed rate advance	2,000,000	3.69%	September 7, 2017	June 7, 2015
Fixed rate	3,000,000	2.94%	August 9, 2018	
Total	$ 126,000,000			

		FHLB Advances Outstanding December 31, 2014		
Type advance	Balance	Interest rate	Maturity date	Convertible date
Fixed rate	$ 10,000,000	0.18%	January 5, 2015	
Fixed rate	5,000,000	0.23%	January 26, 2015	
Fixed rate	10,000,000	0.20%	January 28, 2015	
Fixed rate	5,000,000	0.20%	January 28, 2015	
Fixed rate	10,000,000	0.19%	January 28, 2015	
Fixed rate	5,000,000	2.09%	August 10, 2015	
Fixed rate	5,000,000	1.95%	August 9, 2016	
Fixed rate	2,000,000	2.84%	August 9, 2017	
Convertible fixed rate advance	2,000,000	3.69%	September 7, 2017	March 7, 2015
Fixed rate	3,000,000	2.94%	August 9, 2018	
Variable rate overnight advance	26,500,000	0.36%		
Total	$ 83,500,000	0.71%		

Note 15 - Junior Subordinated Debentures

In May 2004, Coastal Banking Company Statutory Trust I issued $3.0 million of trust preferred securities with a maturity of July 23, 2034. The proceeds from the issuance of the trust preferred securities were used by the Trust to purchase $3,093,000 of the Company's junior subordinated debentures, which pay interest at a floating rate equal to 3 month LIBOR plus 275 basis points. The Company used the proceeds from the sale of the junior subordinated debentures to strengthen the capital position of the Bank and to accommodate current and future growth. The current regulatory rules allow certain amounts of junior subordinated debentures to be included in the calculation of regulatory capital, and have been included in the Tier I calculation accordingly. The debentures and related accrued interest represent the sole asset of the Trust.

The Company has entered into contractual arrangements which, taken collectively, fully and unconditionally guarantee payment of: (i) accrued and unpaid distributions required to be paid on the trust preferred securities; (ii) the redemption price with respect to any trust preferred securities called for redemption by Trust I, and (iii) payments due upon a voluntary or involuntary dissolution, winding up, or liquidation of the Trust I. The trust preferred securities must be redeemed upon maturity of the debentures on July 23, 2034, or upon earlier redemption as provided in the indenture. The Company has the right to redeem the

debentures purchased by the Trust I in whole or in part, on or after July 23, 2009. As specified in the indentures, if the debentures are redeemed prior to maturity, the redemption price will be the unpaid principal amount, plus any accrued unpaid interest.

In June 2006, Coastal Banking Company Statutory Trust II issued $4.0 million of trust preferred securities with a maturity of September 30, 2036. The proceeds from the issuance of the trust preferred securities were used by the Trust to purchase $4,124,000 of the Company's junior subordinated debentures, which pay interest at a floating rate equal to 3 month LIBOR plus 160 basis points. The Company used the proceeds from the sale of the junior subordinated debentures to strengthen the capital position of the Bank and to accommodate current and future growth. The current regulatory rules allow certain amounts of junior subordinated debentures to be included in the calculation of regulatory capital, and have been included in the Tier I calculation accordingly. The debentures and related accrued interest represent the sole asset of the Trust.

The Company has entered into contractual arrangements which, taken collectively, fully and unconditionally guarantee payment of: (i) accrued and unpaid distributions required to be paid on the trust preferred securities; (ii) the redemption price with respect to any trust preferred securities called for redemption by Trust II, and (iii) payments due upon a voluntary or involuntary dissolution, winding up, or liquidation of the Trust II. The trust preferred securities must be redeemed upon maturity of the debentures on September 30, 2036, or upon earlier redemption as provided in the indenture. The Company has the right to redeem the debentures purchased by the Trust II in whole or in part, on or after September 30, 2011. As specified in the indentures, if the debentures are redeemed prior to maturity, the redemption price will be the unpaid principal amount, plus any accrued unpaid interest.

As of March 31, 2015, the Company has paid all interest payments due on all trust preferred securities.

Note 16 – Employee Stock Purchase Plan

On February 27, 2013 the Board of Directors approved the adoption of the Coastal Banking Company Employee Stock Purchase Plan (the "Plan") effective April 1, 2013, and set aside 250,000 shares of common stock for issuance under the Plan. The Plan allows eligible full time employees to direct an after-tax deduction from their pay to be accumulated and disbursed once per quarter to purchase newly issued common stock in the Company at a 5% discount to fair market value on the final day of each calendar quarter. Total shares purchased through the plan were 4,562 for the three month period ending March 31, 2015 and 15,828 for the year ending December 31, 2014. The 5% discount to fair market value is considered compensation cost to the Company and it was $2,099 for the three month period ended March 31, 2015 and $6,005 for the year ended December 31, 2014.

Note 17 – Reclassifications

Certain amounts reported as of December 31, 2014, or the periods ended March 31, 2014, have been reclassified to conform with the presentation of March 31, 2015. These reclassifications had no effect on previously reported net loss or shareholders' equity.