THE FARMERS BANK OF APPOMATTOX AND SUBSIDIARY

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As of and for the years ended December 31, 2015 and December 31, 2014

Notice of Annual Meeting

The Annual Meeting of Shareholders will be held at 7:00 p.m. on May 17, 2016 at Appomattox Inn & Suites, 447 Old Courthouse Road, Appomattox, Virginia 24522. All shareholders are invited to attend.

Independent Auditor

Cherry Bekaert LLP
2626 Glenwood Avenue, Suite 200
Raleigh, NC 27608

Corporate Headquarters

The Farmers Bank of Appomattox
223 Main Street
Appomattox, Virginia 24522

Branches

Concord Branch
Brian D. Wilkerson, Manager
10272 Village Highway
Concord, VA 24538

Dillwyn Branch
Stephanie L. Oliver, Manager
16086 N. James Madison Highway
Dillwyn, VA 23936

Farmville Branch
Anabelle R. Milligan, Manager
1508 South Main Street
Farmville, VA 23901

Main Street Branch
Thomas R. Cobb, Manager
223 Main Street
Appomattox, VA 24522

Triangle Plaza Branch
Dianne R. Rudder, Manager
169 Old Courthouse Road
Appomattox, VA 24522

THE PRESIDENT'S MESSAGE

Dear Shareholders,

On behalf of the Board of Directors and management of The Farmers Bank of Appomattox, I am pleased to present our annual report on the financial condition of our Bank for the years ended December 31, 2015 and 2014. While management was faced with many challenges during 2015, it was a successful year as the Bank had substantial growth in both loans and deposits. Total assets grew $8.9 million to $222.9 million and stockholders' equity increased $1.3 million. Management is also pleased to report that the Bank again reported earnings above many of our peers, with net income for 2015 at $2.23 million. This represents a 10.47% increase over 2014 earnings of $2.02 million.

Earnings in 2015 were driven in part by an increase in total interest income of $167 thousand combined with a $108 thousand decrease in total interest expense. The improvement in interest income came as a result of growth in investment and loan balances that overcame falling yields. Investments grew $1.8 million as of year-end 2015, while their tax-equivalent yield decreased 18 basis points ("bps"). Net loans increased $6.1 million (5.10%) to $126.6 million while the loan yield dropped 7 bps to 4.90%. Loan quality remained satisfactory during 2015, with charge-offs remaining low compared to peers. The Bank experienced a loss of $93 thousand on the sale of a Smith Mountain Lake land development participation project, which originated prior to the 2008 economic downturn. Management is pleased that the Bank's earnings were able to recover from this loss and is not aware of any other substantial losses resulting from participation loans.

The Bank also experienced strong deposit growth of $7.3 million as of December 31, 2015 compared to December 31, 2014, with the largest growth in savings and money market accounts. In spite of this growth, the Bank's 2015 service charge income decreased $27 thousand and interest expense decreased $108 thousand. Overall deposit costs fell by 9 bps during 2015 as management continued its practice of pricing deposits and setting fees moderately compared to our competitors.

During 2015, management elected to change the method of accounting for two investments held by the Bank's wholly owned subsidiary, Farmers Bank Financial Services, Inc. As a result of the accounting method change, the Bank recorded income from the subsidiary of $132 thousand, net of income tax. Management believes that the accounting method change will result in a more accurate valuation of the two investments.

Management continued to closely review operating expenses during 2015, which resulted in a 157 bps improvement in the Bank's efficiency ratio, from 64.21% during 2014 to 62.64%. This ratio measures the Bank's operating expense as a percentage of total income; thus the lower the ratio, the better. The Bank's efficiency ratio compares very favorably with its state and national peer group ratios. The Bank's return on average assets of 1.01% as of December 31, 2015 also compared favorably with its peer group average ratio of 0.73 % according to the December 31, 2015 Virginia Bank Performance Report.

Management continually strives to meet the technology expectations of our wide array of customers. During the previous year, we introduced our new mobile banking feature and enhanced our online bill payment option. Our institution also incurred substantial expense to address required disaster recovery and business continuity issues. Cyber Security also became an important focus of management, with the formation of an internal Cyber Security team. This team has worked diligently to take the steps necessary to protect our Bank from outside attacks and has a strategy to address any potential incidents.

We as a company also remain dedicated to making a marked difference in the communities in which we operate. During 2015, we have partnered with Gleaning for the World to assist with their mission of providing for needs around the world. We are thankful for the opportunities we have to give back. We are proud to be able to help small businesses prosper. We are reminded to value each customer and make their banking experience a positive one. As always, I am thankful for our dedicated and talented directors, officers and employees who have helped make 2015 such a productive year. To you, our shareholders, who have supported us throughout the years, we thank you. Please remember to recommend our services to your friends and associates. We would love the opportunity to demonstrate our superior service, expertise and responsiveness. We remain committed to deliver great value for your investment.

Sincerely,

John R. Caldwell

John R. Caldwell
President and Chief Executive Officer

THE FARMERS BANK OF APPOMATTOX AND SUBSIDIARY

Five-year Summary of Selected Financial Data
(In Thousands, Except Per Share Data and Selected Ratios)

	Years Ended December 31				
Income statement data	2015	2014	2013	2012	2011
Interest income	$ 8,501	$ 8,334	$ 8,507	$ 8,764	$ 8,956
Interest expense	1,006	1,114	1,257	1,492	1,775
Net interest income	7,495	7,220	7,250	7,272	7,181
Provision for loan losses	76	118	91	311	337
Net interest income after provision for loan losses	7,419	7,102	7,159	6,961	6,844
Noninterest income	1,266	1,049	1,128	1,110	963
Noninterest expense	5,788	5,624	5,708	5,413	5,438
Income tax expense	671	512	561	670	543
Net income	$ 2,226	$ 2,015	$ 2,018	$ 1,988	$ 1,826
Per share data:					
Basic earnings per share	$ 2.05	$ 1.86	$ 1.86	$ 1.83	$ 1.69
Cash dividends per share	$ .70	$ .70	$ .75	$ .65	$ .65
Book value at year-end	$ 25.76	$ 24.56	$ 22.61	$ 23.17	$ 21.66
Balance sheet data at end of year					
Available-for-sale securities	$ 59,595	$ 65,040	$ 54,703	$ 49,950	$ 41,069
Held to maturity securities	18,447	11,209	12,374	15,641	23,494
Total loans, net	126,559	120,417	119,549	118,022	112,574
Total assets	222,868	213,946	201,344	199,932	186,240
Deposits	192,680	185,420	174,003	169,021	158,482
Stockholders' equity	27,914	26,612	24,502	25,109	23,477
Selected ratios					
Return on average assets	1.01%	0.96%	0.99%	1.01%	0.98%
Return on average equity	8.18	7.75	8.24	8.14	8.26
Dividend payout ratio	34.08	37.64	40.27	35.42	38.58
Average equity to average assets	12.36	12.38	12.02	12.45	11.85

Common Stock Prices and Dividends Paid

The common stock of the Bank is not listed on a registered exchange. However, the investment firm of Davenport and Company, LLC has agreed to execute trades.

Following are listings of the quarterly high and low sales prices of Bank stock during 2015 and 2014, based on actual sales prices known to the Bank, along with the dividends that were paid during those periods. Prices do not necessarily reflect unreported trades, which may have been at lower or higher prices.

2015	High	Low	Dividends
1st Quarter	$ 23.00	$ 17.50	$ 0.40
2nd Quarter	$ 23.25	$ 19.75	-
3rd Quarter	$ 19.99	$ 18.55	$ 0.30
4th Quarter	$ 18.80	$ 18.48	-

2014	High	Low	Dividends
1st Quarter	$ 17.00	$ 15.85	$ 0.40
2nd Quarter	$ 16.50	$ 15.83	-
3rd Quarter	$ 17.25	$ 16.50	$ 0.30
4th Quarter	$ 18.00	$ 17.25	-

As of December 31, 2015, there were 1,083,660 outstanding shares of Bank common stock, par value $2.00 per share, held by 961 shareholders of record.

The Bank is subject to certain regulatory restrictions pertaining to the amount of dividends that it may pay. The Federal Reserve restricts, without prior approval, the total dividend payments of a member bank in any calendar year to the bank's net income of that year, as defined, combined with its retained net income of the preceding two calendar years, less any required transfers to surplus. At December 31, 2015, retained earnings which are free of such restrictions amounted to approximately $3,930. Please reference Note 11 of the Notes to Consolidated Financial Statements for a discussion of dividend restrictions and capital requirements.

Report of Independent Auditor

The Board of Directors and Stockholders
The Farmers Bank of Appomattox
Appomattox, Virginia

Report on the Consolidated Financial Statements
We have audited the accompanying consolidated financial statements of The Farmers Bank of Appomattox and Subsidiary (the "Bank"), which comprise the consolidated balance sheets as of December 31, 2015 and 2014, and the related consolidated statements of income and comprehensive income, changes in stockholders' equity, and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Consolidated Financial Statements
Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility
Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion
In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of The Farmers Bank of Appomattox and Subsidiary as of December 31, 2015 and 2014, and the results of their operations and their cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Cherry Bekaert LLP

Raleigh, North Carolina
March 18, 2016

THE FARMERS BANK OF APPOMATTOX AND SUBSIDIARY
Consolidated Balance Sheets
December 31, 2015 and 2014
(In thousands, except share and per share data)

Assets	2015	2014
Cash and cash equivalents		
Cash and due from banks	$ 4,338	$ 3,776
Federal funds sold	3,169	3,064
Total cash and cash equivalents	7,507	6,840
Securities		
Available-for-sale, at fair value	59,595	65,040
Held-to-maturity, at amortized cost	18,447	11,209
Loans, net	126,559	120,417
Bank premises and equipment, net	2,554	2,536
Accrued interest receivable	1,155	1,157
Investment in bank-owned life insurance	5,549	5,386
Prepaid pension expense	141	-
Other real estate owned	175	592
Other assets	1,186	769
	215,361	207,106
Total assets	$ 222,868	$ 213,946
Liabilities and Stockholders' Equity		
Deposits		
Demand – noninterest bearing	$ 36,942	$ 30,935
Demand – interest bearing	40,614	38,512
Savings	45,629	43,462
Time:		
Certificates of deposit of $100 and over	35,300	36,282
Other	34,195	36,229
Total deposits	192,680	185,420
Securities sold under repurchase agreements	1,418	1,058
Accrued interest payable	100	114
Deferred income taxes	462	366
Accrued pension expense	-	100
Other liabilities	294	276
Total liabilities	194,954	187,334
Stockholders' equity		
Common stock, $2 par value. Authorized 1,600,000 shares: issued and outstanding 1,083,660 shares	2,167	2,167
Additional paid-in capital	1,000	1,000
Retained earnings	24,956	23,488
Accumulated other comprehensive loss	(209)	(43)
Total stockholders' equity	27,914	26,612
Total liabilities and stockholders' equity	$ 222,868	$ 213,946

See notes to consolidated financial statements

THE FARMERS BANK OF APPOMATTOX AND SUBSIDIARY
Consolidated Statements of Income and Comprehensive Income
December 31, 2015 and 2014
(In thousands, except share and per share data)

	2015	2014
Interest income		
Interest and fees on loans	$ 6,165	$ 6,048
Interest on securities		
U. S. Government agencies	385	356
Obligations of states and political subdivisions – nontaxable	895	809
Obligations of states and political subdivisions – taxable	774	802
Corporate obligations	247	293
Corporate certificates of deposit	27	18
Interest on federal funds sold	8	8
Total interest income	8,501	8,334
Interest expense		
Interest on deposits	580	656
Interest on time certificates of $100 and over	422	451
Interest on securities sold under repurchase agreements	4	7
Total interest expense	1,006	1,114
Net interest income	7,495	7,220
Provision for loan losses	76	118
Net interest income after provision for loan losses	7,419	7,102
Noninterest income		
Service charges on deposit accounts	573	600
Gain on sales, calls or maturities of securities	45	94
Other	648	355
Total noninterest income	1,266	1,049
Noninterest expense		
Salaries and employee benefits	3,240	3,250
Expenses of premises and equipment	478	466
Other operating expenses	2,070	1,908
Total noninterest expense	5,788	5,624
Income before income tax expense	2,897	2,527
Income tax expense	671	512
Net income	2,226	2,015
Other comprehensive income		
Unrealized gains (losses) on available-for-sale securities, net of deferred income tax of ($75) and $725 in 2015 and 2014, respectively	(116)	1,469
Reclassification of gains recognized in net income, net of income tax of $15 and $32 in 2015 and 2014, respectively	(30)	(62)
Change in funded status of pension, net of deferred income tax of ($10) and ($285) in 2015 and 2014, respectively	(20)	(554)
Comprehensive income	$ 2,060	$ 2,868
Per share data:		
Earnings per share	$ 2.05	$ 1.86
Cash dividends per share	$ 0.70	$ 0.70

See notes to consolidated financial statements

THE FARMERS BANK OF APPOMATTOX AND SUBSIDIARY
Consolidated Statements of Changes in Stockholders' Equity
Years Ended December 31, 2015 and 2014
(In thousands, except per share data)

	Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Stockholders' Equity
Balances at January 1, 2014	$ 2,167	$ 1,000	$ 22,231	$ (896)	$ 24,502
Net income	-	-	2,015	-	2,015
Cash dividends ($0.70 per share)	-	-	(758)	-	(758)
Other comprehensive loss	-	-	-	853	853
Balances at December 31, 2014	**2,167**	**1,000**	**23,488**	**(43)**	**26,612**
Net income	-	-	2,226	-	2,226
Cash dividends ($0.70 per share)	-	-	(758)	-	(758)
Other comprehensive income	-	-	-	(166)	(166)
Balances at December 31, 2015	**$ 2,167**	**$ 1,000**	**$ 24,956**	**$ (209)**	**$ 27,914**

See notes to consolidated financial statements

THE FARMERS BANK OF APPOMATTOX AND SUBSIDIARY
Consolidated Statements of Cash Flows
Years Ended December 31, 2015 and 2014
(In thousands)

	2015	2014
Cash flow from operating activities:		
Net income	$ 2,226	$ 2,015
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation of bank premises and equipment	186	185
Amortization of intangible asset	-	82
Loss on disposal of equipment	-	1
Net gain on sale, call or maturity of investment securities	(43)	(79)
Net amortization and accretion of premiums and discounts on securities	305	259
Provision for loan losses	76	118
Provision for deferred income taxes	181	50
Increase in cash surrender value of bank-owned life insurance	(163)	(171)
Valuation write-downs of other real estate	93	-
Loss (gain) on the sale of other real estate	(5)	10
Net (increase) decrease in:		
Accrued interest receivable	2	(28)
Prepaid pension expense	(171)	(447)
Other assets	(417)	(61)
Net increase (decrease) in:		
Accrued interest payable	(14)	(12)
Accrued pension expense	(100)	100
Other liabilities	18	(37)
Net cash provided by operating activities	2,174	1,985
Cash flow from investing activities:		
Proceeds from sales of available-for-sale securities	1,667	1,103
Proceeds from maturities and calls of available-for-sale securities	5,591	5,967
Proceeds from maturities and calls of held to maturity securities	2,320	1,147
Net proceeds from the sale of other real estate	329	100
Purchases of available-for-sale securities	(2,248)	(15,438)
Purchases of held to maturity securities	(9,606)	-
Net increase in loans	(6,218)	(986)
Purchases of bank premises and equipment	(204)	(146)
Net cash used in investing activities	(8,369)	(8,253)
Cash flow from financing activities:		
Net increase in demand deposits and savings accounts	10,276	12,110
Net decrease in time deposits	(3,016)	(693)
Net increase (decrease) in securities sold under repurchase agreements	360	(1,342)
Cash dividends paid	(758)	(758)
Net cash provided by financing activities	6,862	9,317
Net increase in cash and cash equivalents	667	3,049
Cash and cash equivalents, beginning of year	6,840	3,791
Cash and cash equivalents, end of year	$ 7,507	$ 6,840

THE FARMERS BANK OF APPOMATTOX AND SUBSIDIARY
Consolidated Statements of Cash Flows
Years Ended December 31, 2015 and 2014
(In thousands)

	2015	2014
Supplemental disclosure of cash flow information		
Interest paid during the period	$ 1,020	$ 1,127
Federal income tax paid during the period	$ 422	$ 525
Supplemental schedule of noncash investing and financing activities		
Transfers from loans to other real estate owned	$ -	$ 7
Unrealized gains (losses) on available-for-sale securities, net of an income tax benefit of $75 and income taxes of $725 in 2015 and 2014, respectively	$ (145)	$ 1,407
Unrecognized net actuarial (loss) in defined benefit plan, net of an income tax benefit of $(82) and $(164) in 2015 and 2014, respectively	$ (20)	$ (554)

See notes to consolidated financial statements

THE FARMERS BANK OF APPOMATTOX AND SUBSIDIARY
Notes to Consolidated Financial Statements
December 31, 2015 and 2014
(In thousands, except share and per-share data)

Note 1 - Summary of significant accounting policies

The accounting and reporting policies of The Farmers Bank of Appomattox and its wholly owned subsidiary, Farmers Bank Financial Services, Inc., conform to accounting principles generally accepted in the United States of America ("GAAP") and general practices within the banking industry. The following is a summary of the more significant accounting policies:

Consolidation

The consolidated financial statements include the accounts of The Farmers Bank of Appomattox and its wholly owned subsidiary (collectively, "the Bank"). The wholly owned subsidiary, Farmers Bank Financial Services, Inc., is utilized to account for the Bank's investment in two insurance companies. All significant intercompany balances and transactions have been eliminated in the consolidation.

Use of Estimates

In preparing the consolidated financial statements, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the dates of the consolidated balance sheets and income and expenses for each year. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant changes in the near term relate to determination of the allowance for loan losses and the fair value of investment securities.

Cash and cash equivalents

For purposes of reporting cash flows, cash and cash equivalents include cash on hand, amounts due from banks and federal funds sold.

Securities

The Bank classifies its securities in two categories: (1) debt securities that the Bank has the positive intent and ability to hold to maturity are classified as "held to maturity securities" and reported at amortized cost. Amortization of premiums and accretion of discounts are adjusted on a basis which approximates the level yield method; and (2) debt and equity securities not classified as held to maturity securities are classified as "available-for-sale securities" and reported at fair value, with unrealized gains and losses excluded from net income and reported in a separate component of stockholders' equity.

Gains or losses on disposition of securities are based on the net proceeds and adjusted carrying values of the securities matured, called or sold, using the specific identification method on a trade date basis. A decline in the market value of any available-for-sale or held to maturity security below cost that is deemed other than temporary is charged to net income, resulting in the establishment of a new cost basis for the security.

Management evaluates securities for other-than-temporary impairment ("OTTI") on at least a quarterly basis, and more frequently when economic or market conditions warrant such an evaluation. For securities in an unrealized loss position, management considers the extent and duration of the unrealized loss, and the financial condition and near-term prospects of the issuer. Management also assesses whether it intends to sell or it is more likely than not it will be required to sell a security in an unrealized loss position before recovery of its amortized cost basis. If either of the criteria regarding intent or requirement to sell is met, the entire difference between amortized cost and fair value is recognized as impairment through earnings.

Note 1 - Summary of significant accounting policies (continued)

Securities

For debt securities that do not meet the aforementioned criteria, the amount of impairment is split into two components as follows: 1) OTTI related to credit loss, which must be recognized in the income statement, and 2) OTTI related to other factors, which is recognized in other comprehensive income. The credit loss is defined as the difference between the present value of the cash flows expected to be collected and the amortized cost basis. For equity securities, the entire amount of impairment is recognized through earnings.

Loans and allowance for loan losses

Loans are stated at the amount of unpaid principal, reduced by unearned income and fees on loans and an allowance for loan losses. The allowance for loan losses is a valuation allowance consisting of the cumulative effect of the provision for loan losses, plus any amounts recovered on loans previously charged off, minus loans charged off. The provision for loan losses is charged to expense. Loans are charged against the allowance for loan losses when management believes the collectability of the principal is unlikely.

Modifications to a borrower's debt agreement are considered troubled debt restructurings ("restructurings") if a concession is granted for economic or legal reasons related to a borrower's financial difficulties that otherwise would not be considered. Restructurings are undertaken in order to improve the likelihood of recovery on the loan and may take the form of modifications made with the stated interest rate lower than the current market rate for new debt with similar risk; modifications to the terms and conditions of the loan that fall outside of normal underwriting policies and procedures; or a combination of these modifications. Restructurings can involve loans remaining in nonaccrual status, moving to nonaccrual status, or continuing on accruing status, depending on the individual facts and circumstances of the borrower.

Loans are considered impaired when, based on current information and events, it is probable that the Bank will be unable to collect all amounts due according to the contractual terms of the loan agreement. Impaired loans are measured based on the present value of expected future cash flows, discounted at the loan's effective interest rate or at the fair value of the collateral less the estimated selling costs, if the loan is collateral dependent. Larger groups of homogeneous loans such as real estate mortgage loans, individual consumer loans and home equity loans are evaluated collectively for impairment. Impairment losses are recorded as a charge to the allowance for loan losses.

The allowance for loan losses is an amount management believes will be adequate to absorb probable losses inherent in the loan portfolio. Management determines the adequacy of the allowance based upon reviews of individual credits, delinquencies, current economic conditions, the risk characteristics of the various categories of loans, recent loan loss experience and other pertinent factors. While management uses available information to recognize losses on loans, future additions to the allowance may be necessary based on changes in economic conditions. It is reasonably possible that management's estimate of loan losses and the related allowance may change materially in the near term. However, the amount of that change cannot be estimated. Various regulatory agencies, as an integral part of their examination process, periodically review the Bank's allowance for loan losses. Such agencies may require the Bank to recognize additions to the allowance for loan losses based on their judgments about information available at the time of their examinations.

Note 1 - Summary of significant accounting policies (continued)

Loans and allowance for loan losses

Loans are considered past due when the contractual amounts due with respect to principal and interest are not received within 30 days of their contractual due date. Loans are generally placed in non-accrual status if they are 90 or more days past due unless they are in the process of collection. Interest related to non-accrual loans is recognized on the cash basis. Loans in non-accrual status are generally the collectible portion of bankrupt accounts. Loans are generally charged off when the collection of principal and interest is 90 days or more past due and the loan is considered uncollectible.

Loan origination fees and the corresponding loan origination costs are deferred, and the net amount is amortized over the contractual life of the related loans as an adjustment of yield.

Bank premises and equipment

Bank premises and equipment are stated at cost, net of accumulated depreciation. Depreciation on bank premises and equipment is charged to expense over the estimated useful lives of the assets, principally on the straight-line method. The cost of assets retired and sold and the related accumulated depreciation are eliminated from the accounts, and the resulting gains or losses are included in determining net income. Expenditures for maintenance and repairs are charged to expense as incurred, and improvements and betterments are capitalized.

Other Real Estate Owned

Other real estate owned consists of properties acquired through foreclosure sales or deed in lieu of foreclosure. At the time of the foreclosure, the properties are recorded at the fair value less estimated costs to sell the property. Subsequently these properties are carried at the lower of cost or fair value less the estimated costs to sell the property. Losses from the acquisition of property in full or partial satisfaction of loans are charged against the allowance for loan losses. Subsequent write-downs, if any, are charged to expense. Gains and losses on the sales of foreclosed properties are included in determining net income in the year of the sale.

Defined benefit pension plan

The Bank maintains a noncontributory defined benefit pension plan covering substantially all of its employees. The overfunded or underfunded status of the pension plan is recognized as an asset or liability in the statement of financial position, and changes in the funded status are recognized in comprehensive income. The net periodic pension expense includes a service cost component, interest on the projected benefit obligation, a component reflecting the actual return on plan assets, and the effect of deferring and amortizing certain actuarial gains and losses. The Bank's normal funding policy is to contribute to the pension plan amounts necessary to satisfy the Internal Revenue Service's funding standards and to the extent that they are deductible for federal income tax purposes.

Note 1 - Summary of significant accounting policies (continued)

Bank-owned life insurance

During 2012, the Bank purchased life insurance on key employees in the face amount of $15,397. The policy was recorded at the cash surrender value and reported on the balance sheet. Income generated from the policy is recorded as non-interest income.

Advertising

The Bank expenses advertising costs as incurred. These costs totaled $29 and $22 in 2015 and 2014, respectively.

Income taxes

Income taxes are recorded using the asset and liability method, whereby deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carry-forwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in net income in the period that includes the enactment date.

When tax returns are filed, it is highly certain that some positions taken would be sustained upon examination by the taxing authorities, while others are subject to uncertainty about the merits of the position taken or the amount of the position that would be ultimately sustained. The benefit of a tax position is recognized in the financial statements in the period during which, based on all available evidence, management believes that it is more likely than not that the position will be sustained upon examination, including the resolution of appeals or litigation processes, if any. Tax positions taken are not offset or aggregated with other positions. Tax positions that meet the more-likely-than-not recognition threshold are measured as the largest amount of tax benefit that is more than 50 percent likely of being realized upon settlement with the applicable taxing authority. The portion of the benefits associated with tax positions taken that exceeds the amount measured as described above is reflected as a liability for unrecognized tax benefits in the accompanying balance sheet, along with any associated interest and penalties that would be payable to the taxing authorities upon examination.

Earnings per share

Earnings per share is computed based on the weighted-average number of shares outstanding during each year. The weighted-average number of common shares outstanding was 1,083,660 for 2014 and 2013.

Equity Method Investment

During the year ended December 31, 2015, the Bank elected to adopt the equity method of accounting for two investments in limited liability corporations that had previously been accounted for as cost method investments. The Bank determined that it had the ability to exercise significant influence over the investees, as the Bank has representation on both limited liability corporations' board of directors. In conjunction with the change in accounting principle, the Bank has reported a $200 thousand gain on the investment in noninterest income for the year ended December 31, 2015.

THE FARMERS BANK OF APPOMATTOX AND SUBSIDIARY
Notes to Consolidated Financial Statements
December 31, 2015 and 2014
(In thousands, except share and per-share data)

Note 1 - Summary of significant accounting policies (continued)

Comprehensive income

Accounting Standards Codification ("ASC") 220-10, *Comprehensive Income*, requires the Bank to classify items of "Other Comprehensive Income" (such as net unrealized gains (losses) on available-for-sale securities) by their nature in a financial statement and present the accumulated balance of other comprehensive income separately from retained earnings and surplus in the equity section of a statement of financial position. The Bank's other comprehensive income consists of the change in the net unrealized gains (losses) on securities available-for-sale, net of income taxes, and the change in the funded status of the Bank's defined benefit pension plan, net of income taxes.

Note 2 - Restrictions on cash

To comply with Federal Reserve regulations, the Bank is required to maintain certain average cash reserve balances. The daily average cash reserve requirements were approximately $1,799 and $1,617 for the specified review weeks in December 2015 and 2014, respectively.

Note 3 - Securities

The amortized costs, gross unrealized gains, gross unrealized losses and fair values of securities are as follows:

	December 31, 2015			
	Amortized Costs	Gross Unrealized Gains	Gross Unrealized Losses	Fair Values
Available-for-sale				
U.S. Government agencies	$ 11,970	$ 164	$ (42)	$ 12,092
Obligations of states and political subdivisions - nontaxable	22,392	576	(120)	22,848
Obligations of states and political subdivisions - taxable	13,236	714	-	13,950
Corporate	7,891	138	(67)	7,962
Corporate certificates of deposit	2,739	4	-	2,743
	$ 58,228	$ 1,596	$ (229)	$ 59,595
Held to maturity				
U.S. Government agencies	$ 5,008	$ 66	$ (35)	$ 5,039
Obligations of states and political subdivisions - nontaxable	9,483	261	(11)	9,733
Obligations of states and political subdivisions - taxable	3,956	241	(11)	4,186
	$ 18,447	$ 568	$ (57)	$ 18,958

(In thousands, except share and per-share data)

Note 3 – Securities (continued)

	December 31, 2014			
	Amortized Costs	Gross Unrealized Gains	Gross Unrealized Losses	Fair Values
Available-for-sale				
U.S. Government agencies	$ 13,446	$ 148	$ (96)	$ 13,498
Obligations of states and political subdivisions - nontaxable	25,231	516	(89)	25,658
Obligations of states and political subdivisions - taxable	13,256	904	-	14,160
Corporate	8,034	217	(22)	8,229
Corporate certificates of deposit	3,486	9	-	3,495
	$ 63,453	$ 1,794	$ (207)	$ 65,040
Held to maturity				
U.S. Government agencies	$ 2,016	$ 98	$ -	$ 2,114
Obligations of states and political subdivisions - nontaxable	5,229	297	-	5,526
Obligations of states and political subdivisions - taxable	3,964	326	-	4,290
	$ 11,209	$ 721	$ -	$ 11,930

The amortized costs and fair values of securities at December 31, 2015, by contractual maturity, are shown below. Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Available-for-Sale		Held to Maturity	
	Amortized Cost	Fair Values	Amortized Cost	Fair Values
Due in one year or less	$ 4,840	$ 4,850	$ 1,736	$ 1,750
Due after one year through five years	30,339	31,359	8,769	9,163
Due after five years through ten years	20,280	20,552	7,942	8,045
Due after ten years	2,769	2,834	-	-
	$ 58,228	$ 59,595	$ 18,447	$ 18,958

The amortized costs of securities pledged to collateralize public deposits and securities sold under repurchase agreements and for other purposes as required or permitted by law were approximately $8,808 and $10,263 (fair value of $9,062 and $10,547, respectively) at December 31, 2015 and 2014, respectively.

(In thousands, except share and per-share data)

Note 3 – Securities (continued)

During 2015 and 2014, the Bank sold available-for-sale securities with amortized costs totaling $1,639 and $1,061, respectively. Gross realized gains on these sales were $28 and $53, respectively, while gross realized losses were $0 and $10, respectively. Also during 2015 and 2014, the Bank had called and matured securities with amortized costs totaling $7,896 and $7,028, respectively. Gross realized gains on the called and matured securities were $17 and $41, respectively, while gross realized losses were $2 and $5, respectively.

The following table shows the gross unrealized losses and fair value of the Bank's investments, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position, at December 31, 2015 and 2014:

	Less Than 12 Months		12 Months or Greater		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
December 31, 2015:						
U. S. Government agencies	$ 7,936	$ (52)	$ 1,575	$ (25)	$ 9,511	$ (77)
Obligations of state and political subdivisions	2,477	(23)	2,104	(119)	4,581	(142)
Corporate	3,702	(67)	-	-	3,702	(67)
Total	$ 14,115	$ (142)	$ 3,679	$ (144)	$ 17,794	$ (286)

	Less Than 12 Months		12 Months or Greater		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
December 31, 2014:						
U. S. Government agencies	$ 493	$ (3)	$ 6,496	$ (93)	$ 6,989	$ (96)
Obligations of state and political subdivisions	520	(1)	4,813	(88)	5,333	(89)
Corporate	2,056	(7)	542	(15)	2,598	(22)
Total	$ 3,069	$ (11)	$ 11,851	$ (196)	$ 14,920	$ (207)

As of December 31, 2015 and 2014, the Bank held $17,794 and $14,920, respectively, in securities with unrealized losses. These unrealized losses are all related to the change in market interest rates and not to the credit quality of the issuers. When analyzing an issuer's financial condition, management considers whether the securities are issued by the federal government or its agencies, whether downgrades by bond rating agencies have occurred, and industry analysts' reports. As management has the ability and intent to hold debt securities for the foreseeable future, no declines are deemed to be other-than-temporary.

(In thousands, except share and per-share data)

Note 4 - Loans and allowance for loan losses

A summary of loans, net is as follows:

	December 31	
	2015	2014
Commercial loans	$ 10,104	$ 8,556
Real estate construction loans	6,364	6,979
Real estate mortgage loans	87,318	85,562
Consumer loans	23,601	20,236
Total loans, gross	127,387	121,333
Less unearned income and fees	(207)	(225)
Loans, net of unearned income and fees	127,180	121,108
Less allowance for loan losses	(621)	(691)
Loans, net	$ 126,559	$ 120,417

Following is a breakdown of real estate mortgage loans:

	December 31	
Real estate mortgage loans:	2015	2014
Commercial mortgage loans	$ 21,301	$ 19,709
1 – 4 family residential mortgages	49,590	48,004
Home equity lines of credit	14,288	15,520
Other mortgages	2,139	2,329
Total real estate mortgage loans	$ 87,318	$ 85,562

Loan origination / Risk management. The Bank has certain lending policies and procedures in place that are designed to maximize loan income within an acceptable level of risk. Management reviews and approves these policies and procedures on a regular basis. A reporting system supplements the review process by providing management with frequent reports related to loan production, loan quality, concentrations of credit, loan delinquencies and non-performing and potential problem loans. Diversification in the loan portfolio is a means of managing risk associated with fluctuations in economic conditions. The primary categories of loans originated by the Bank are real estate mortgage loans, real estate construction and land development loans, commercial loans and consumer loans.

Note 4 - Loans and allowance for loan losses (continued)

Real estate mortgage loans are primarily underwritten as cash flow loans and secondarily as loans secured by real estate. Commercial real estate mortgage loans are subject to underwriting standards and processes similar to commercial loans where evaluation of the borrower's ability to operate profitably and repay their obligations as agreed is critical to the underwriting process. Commercial real estate lending typically involves higher loan principal amounts, and the repayment of these loans is generally dependent on the successful operation of the property securing the loan or the business conducted on the property securing the loan. Commercial real estate loans may be more adversely affected by conditions in the real estate markets or in the general economy.

Real estate construction and land development loans are generally based upon estimates of costs and value associated with the complete project. These loans often involve the disbursement of substantial funds, with repayment dependent on the ultimate success of the project. Management is aware that cost estimates may be inaccurate; thus, physical inspections of the property during the construction phase to assess whether the estimated percentage of completeness is in line with the requested loan advance are critical to the loan management process. Sources of repayment for these types of loans may be pre-committed permanent loans from approved long-term lenders, sales of developed property, or some other interim loan commitment provided while permanent financing is being obtained. These loans are considered to have higher risks than other real estate loans due to their ultimate repayment being sensitive to interest rate changes, governmental regulation of the property, general economic conditions, and the availability of permanent financing.

Residential real estate mortgage loans are primarily underwritten based on an assessment of the borrower's credit history and estimated ability to repay the mortgage loan based on a comparison of the borrower's verified income and current obligations, including the requested loan. The value of the property securing the loan is generally determined by an independent real estate appraisal. The Bank generally lends up to 80% of the value of the property, thus mitigating the risk associated with these loans. Home equity loans are also underwritten utilizing a maximum loan-to-value percentage of 80%.

Commercial loans are underwritten after evaluating and understanding the borrower's ability to operate profitably and prudently expand its business. Once it is determined that the borrower's management possesses sound ethics and solid business acumen, the Bank's management examines current and projected cash flows to determine the ability of the borrower to repay their obligations as agreed. Commercial loans are primarily made based on the identified cash flows of the borrower and secondarily on the underlying collateral provided by the borrower. Management is aware that the cash flows of the borrower may not match projections and collateral securing these loans may fluctuate in value. Most commercial loans are secured by the assets being financed or other business assets such as inventory or equipment and may incorporate a personal guarantee. Some smaller amount, short-term loans are made on an unsecured basis.

The Bank typically originates consumer loans utilizing an independent, third-party credit bureau report to supplement the underwriting process. Consumer loans are primarily made based on an assessment of the borrower's credit history and the estimated ability to repay the borrower's obligations based on a comparison of the borrower's stated income to existing obligations, including the loan being requested. These loans are generally secured by the asset being purchased, secured by unencumbered assets already owned by the borrower or unsecured. The risk associated with consumer loans is minimized by the relatively small amount of the loans spread among a large number of borrowers.

(In thousands, except share and per-share data)

Note 4 - Loans and allowance for loan losses (continued)

The Bank maintains an independent loan administration department that reviews all loan documentation for accuracy, completeness, and compliance with Bank policies and procedures. Results of these reviews are presented to management. The loan administration process complements and reinforces the risk identification and assessment decisions made by lenders.

In the ordinary course of business, the Bank has granted loans to certain directors, executive officers, and their affiliates (collectively referred to as “related parties”). These loans were made on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with other unaffiliated persons and do not involve more than normal risk of collectability. Activity in related party loans in 2015 and 2014 is presented in the following table:

	2015	2014
Balance of related party loans, January 1	$ 384	$ 29
Principal additions	689	394
Principal reductions	(86)	(39)
Balance of related party loans, December 31	$ 987	$ 384

Non-accrual loans, segregated by type of loan, as of December 31, 2015 and 2014, were as follows:

	2015	2014
1-4 family residential real estate mortgages	$ 116	$ -
Home equity loans	-	19
Real estate construction loans	13	-
Consumer loans	292	102
Total non-accrual loans	$ 421	$ 121

Had non-accrual loans performed in accordance with their original contract terms, the Bank would have recognized additional interest income, net of income tax, of approximately $24 in 2015 and $8 in 2014.

(In thousands, except share and per-share data)

Note 4 - Loans and allowance for loan losses (continued)

An age analysis of past due loans, segregated by type of loan, as of December 31, 2015 and 2014 is as follows:

	Loans 30-89 Days Past Due	Loans 90 or more Days Past Due	Total Past Due Loans	Current Loans	Total Loans	Accruing Loans 90 or More Days Past Due
December 31, 2015:						
Real estate mortgage loans:						
Commercial mortgages	$ 96	$ -	$ 96	$ 21,138	$ 21,234	$ -
1-4 family res. mortgages	1,519	116	1,635	47,719	49,354	-
Home equity lines of credit	49	-	49	14,245	14,294	-
Other mortgages	-	-	-	2,138	2,138	-
Real estate construction loans	-	13	13	6,333	6,346	-
Commercial loans	138	-	138	9,976	10,114	-
Consumer loans	1,465	294	1,759	21,941	23,700	2
Total	$ 3,267	$ 423	$ 3,690	$ 123,490	$ 127,180	$ 2
December 31, 2014:						
Real estate mortgage loans:						
Commercial mortgages	$ 258	$ 21	$ 279	$ 19,361	$ 19,640	$ 21
1-4 family res. mortgages	1,737	88	1,825	45,953	47,778	88
Home equity lines of credit	54	19	73	15,451	15,524	-
Other mortgages	36	-	36	2,292	2,328	-
Real estate construction loans	-	-	-	6,950	6,950	-
Commercial loans	119	-	119	8,448	8,567	-
Consumer loans	1,282	217	1,499	18,822	20,321	115
Total	$ 3,486	$ 345	$ 3,831	$ 117,277	$ 121,108	$ 224

Loans are considered impaired when, based on current information and events, it is probable the Bank will be unable to collect all amounts due in accordance with the original contractual terms of the loan agreement, including scheduled principal and interest payments. Impairment is evaluated in total for smaller-balance loans of a similar nature and on an individual loan basis for other loans. If a loan is impaired, a specific valuation allowance is allocated, if necessary, so that the loan is reported net, at the present value of estimated future cash flows using the loan's existing rate or at the fair value of collateral if repayment is expected solely from the collateral. Interest payments on impaired loans are typically applied to principal unless collectability of the principal amount is reasonably assured, in which case interest is recognized on a cash basis. Impaired loans, or portions thereof, are charged off when deemed uncollectible.

(In thousands, except share and per-share data)

Note 4 - Loans and allowance for loan losses (continued)

The following table provides a breakdown of the Bank's impaired loans by loan type and recorded investment amounts as of December 31, 2015 and 2014. The Bank received interest payments totaling $76 and $76 on these loans during 2015 and 2014, respectively.

	Impaired Loans with no Allowance	Impaired Loans with Allowance	Total Impaired Loans	Related Allowance	Average Impaired Loans
December 31, 2015:					
Real estate mortgage loans:					
Commercial mortgages	$ 81	$ 224	$ 305	$ 41	$ 159
1-4 family residential mortgages	1,640	-	1,640	-	1,200
Home equity lines of credit	63	58	121	12	119
Other mortgages	-	-	-	-	8
Real estate construction loans	127	-	127	-	88
Commercial loans	131	-	131	-	157
Consumer loans	529	43	572	13	234
Total	$ 2,571	$ 325	$ 2,896	$ 66	$ 1,964
December 31, 2014:					
Real estate mortgage loans:					
Commercial mortgages	$ 132	$ -	$ 132	$ -	$ 144
1-4 family residential mortgages	1,164	-	1,164	-	1,165
Home equity lines of credit	51	58	109	12	112
Other mortgages	13	-	13	-	15
Real estate construction loans	-	-	-	-	-
Commercial loans	147	20	167	2	189
Consumer loans	183	17	200	5	169
Total	$ 1,690	$ 95	$ 1,785	$ 19	$ 1,794

Credit Quality Indicators. As part of the ongoing monitoring of the credit quality of the Bank's loan portfolio, management reviews certain credit quality indicators including (i) commercial loans with an outstanding balance of $200 or greater; (ii) loans which are past due more than 30 days; (iii) loan charge-offs and recoveries; (iv) non-accrual loans and (v) the general economic conditions in the Bank's market and surrounding areas. Commercial loans with a balance of $200 or greater are reviewed quarterly to determine whether the loan should be classified. Management reviews all loans which are past due more than 30 days and two or more payments on a monthly basis. These loans are discussed with the Board of Directors at its monthly meeting. Loan charge-offs and recoveries and non-accrual loans are also reported to the Board of Directors on a monthly basis. The local general economic conditions are detailed in a written report presented to the Board of Directors on a quarterly basis. This report is also included in the Bank's quarterly classified loan report. Management utilizes sources such as the local newspapers; local, state and national economic statistics (such as unemployment statistics); and other internet articles to prepare this report.

(In thousands, except share and per-share data)

Note 4 - Loans and allowance for loan losses (continued)

The Bank utilizes a risk rating matrix to assign a risk grade to each of its loans. A description of the general characteristics of the risk grades is as follows:

Excellent / Satisfactory – These loans range from having minimal to acceptable credit risk.

Watch – These loans have acceptable credit risk but are beginning to develop potential weaknesses that may be temporary in nature but must be watched.

Other Assets Especially Mentioned ("OAEM") – These loans have potential weaknesses that deserve management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan at some future date.

Substandard – These loans are inadequately protected by the net worth or paying capacity of the borrower, and repayment may become dependent on liquidation of the underlying collateral. These loans have well-defined weaknesses, with the Bank likely sustaining a loss if the deficiencies are not corrected.

Doubtful – These loans have all of the weaknesses inherent in those classified as substandard with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of the currently existing facts, conditions and values, highly questionable and improbable.

Loss – These loans are in a non-accrual status and in the process of collateral liquidation.

The following table provides a breakdown of the Bank's loans by risk grade as of December 31, 2015 and 2014.

	Real estate mortgage loans	Real estate construction loans	Commercial loans	Consumer loans	Total
December 31, 2015					
Excellent / Satisfactory	$ 80,850	$ 6,023	$ 9,892	$ 22,686	$ 119,451
Watch	335	85	-	1	421
OAEM	1,336	-	60	4	1,400
Substandard	4,499	238	162	1,009	5,908
Doubtful	-	-	-	-	-
Loss	-	-	-	-	-
Total	$ 87,020	$ 6,346	$ 10,114	$ 23,700	$ 127,180
December 31, 2014					
Excellent / Satisfactory	$ 77,348	$ 5,670	$ 7,248	$ 19,862	$ 110,128
Watch	934	822	-	77	1,833
OAEM	2,353	135	1,005	74	3,567
Substandard	4,600	323	314	308	5,545
Doubtful	35	-	-	-	35
Loss	-	-	-	-	-
Total	$ 85,270	$ 6,950	$ 8,567	$ 20,321	$ 121,108

Note 4 - Loans and allowance for loan losses (continued)

The allowance for loan losses is a reserve established through a provision for loan losses charged to expense, which represents management's best estimate of probable losses inherent within the existing portfolio of loans. The Bank's allowance for loan loss methodology includes allowance allocations calculated in accordance with ASC Topic 310, "*Receivables*" and allowance allocations calculated in accordance with ASC Topic 450, "*Contingencies.*" Accordingly, the methodology is based on historical loss experience by type of credit, specific homogeneous risk pools and specific loss allocations with adjustments for current events and conditions. The Bank's process for determining the appropriate level of the allowance for loan losses is designed to account for credit deterioration as it occurs. The provision for loan losses reflects loan quality trends, including the levels of and trends related to non-accrual loans, past-due loans, potential problem loans, criticized loans and charge-offs and recoveries, among other factors. Portions of the allowance may be allocated for specific credits; however, the entire allowance is available for any credit that, in management's judgment, should be charged off. While management utilizes its best judgment and information available, the ultimate adequacy of the allowance is dependent upon a variety of factors beyond management's control, including, among other things, the performance of the Bank's loan portfolio, the economy, changes in interest rates and the view of the regulatory authorities toward loan classifications.

The Bank's allowance for loan losses consists of three elements: (i) specific valuation allowances determined in accordance with ASC Topic 310 based on probable losses on specific loans; (ii) historical valuation allowances determined in accordance with ASC Topic 450 based on historical loan loss experience for similar loans with similar characteristics and trends, adjusted, as necessary, to reflect the impact of current conditions; and (iii) general valuation allowances determined in accordance with ASC Topic 450 based on general economic conditions and other qualitative risk factors both internal and external to the Bank.

The allowances for loan losses on specific loans are based on a regular analysis and evaluation of the specific loans. On a quarterly basis, commercial and industrial loans and commercial real estate loans with a balance of $200 or greater are evaluated. Certain of these loans with potential problems are given an internal classification which reflects management's assessment of the borrower's ability to repay the loan, the estimated value of the underlying collateral and the economic environment and industry in which the borrower operates. The regular analysis and evaluation of problem loans is performed by the loan officers and independently reviewed and approved by the Chief Compliance Officer. Generally, specific allowances are based on the difference between the estimated value of the underlying collateral and the balance of the loan if the loan is deemed collateral dependent. The specific allowances are determined by the Chief Compliance Officer.

The Bank also determines specific valuation allowances for certain past- due loans and non-accrual loans. Estimated loss ratios are applied to the balances of these loans collectively to determine the amount of the allowance. Loans past-due sixty or more days are grouped in pools of similar loans with similar characteristics which currently include consumer, commercial and industrial and real estate loans. The estimated loss ratio is applied to each pool of past-due loans less any loans in the pool for which a specific allowance valuation has already been determined. Likewise, non-accrual loans are grouped into pools of secured and unsecured loans, from which non-accrual loans with specific valuation allowances are subtracted prior to application of the historical loss ratios.

(In thousands, except share and per-share data)

Note 4 - Loans and allowance for loan losses (continued)

Historical valuation allowances are calculated based on the historical loss experience of specific types of loans. Management calculates historical loss ratios for pools of similar loans with similar characteristics based on the proportion of net charged-off loans to the total populations of loans in the pool. The historical loss ratios are updated quarterly based on the charge-off loan totals for the most recent twelve quarters. The historical valuation allowance is established for each pool of similar loans based on the product of the historical loss ratio and the total dollar amount of loans in the pool less those loans in the pool for which a specific valuation allowance has been determined. The Bank's pools of similar loans currently include consumer, commercial and industrial, real estate and real estate construction loans.

A general valuation allowance based on general economic conditions is also calculated. An economic analysis is performed by the Chief Compliance Officer based on such factors as the Bank's market area industries; local, state and national unemployment statistics; general local economic conditions; and local real estate market conditions. The Bank has identified five categories of economic conditions ranging from "very good economic conditions" to "major problematic economic conditions," and a loss rate is estimated for each category. The economic allowance is calculated by applying the estimated loss rate to the total loan population less loans for which a specific valuation has been determined.

The following table details activity in the allowance for loan losses by loan category for the years ended December 31, 2015 and 2014. Allocation of a portion of the allowance to one category of loans does not preclude its availability to absorb losses in other categories.

	Real estate mortgage loans	Real estate construction loans	Commercial loans	Consumer loans	Total
Balance, December 31, 2014	$ 295	$ 88	$ 32	$ 276	$ 691
Charged-off loans	-	-	(12)	(185)	(197)
Loan recoveries	4	-	5	42	51
Provision for loan losses	(36)	(65)	-	177	76
Balance, December 31, 2015	$ 263	$ 23	$ 25	$ 310	$ 621
Allowance for loan losses allocated to:					
Loans individually evaluated for Impairment	$ 53	$ -	$ -	$ 13	$ 66
Loans collectively evaluated for Impairment	210	23	25	297	555
Allowance for loan losses, Dec. 31, 2015	$ 263	$ 23	$ 25	$ 310	$ 621

(In thousands, except share and per-share data)

Note 4 - Loans and allowance for loan losses (continued)

	Real estate mortgage loans	Real estate construction loans	Commercial loans	Consumer loans	Total
Balance, December 31, 2013	$ 291	$ 87	$ 32	$ 283	$ 693
Charged-off loans	(10)	-	(4)	(171)	(185)
Loan recoveries	-	-	12	53	65
Provision for loan losses	14	1	(8)	111	118
Balance, December 31, 2014	$ 295	$ 88	$ 32	$ 276	$ 691
Allowance for loan losses allocated to:					
Loans individually evaluated for Impairment	$ 12	$ -	$ 2	$ 5	$ 19
Loans collectively evaluated for Impairment	283	88	30	271	672
Allowance for loan losses, Dec. 31, 2014	$ 295	$ 88	$ 32	$ 276	$ 691

The Bank's total loans related to each balance in the allowance for loan losses by loan type and disaggregated on the basis of the Bank's impairment methodology as of December 31, 2015 and 2014 were as follows:

	Real estate mortgage loans	Real estate construction loans	Commercial loans	Consumer loans	Total
December 31, 2015:					
Loans individually evaluated for Impairment	$ 1,950	$ 114	$ 131	$ 278	$ 2,473
Loans collectively evaluated for Impairment	85,070	6,232	9,983	23,422	124,707
Total loans evaluated for impairment	$ 87,020	$ 6,346	$ 10,114	$ 23,700	$127,180
December 31, 2014:					
Loans individually evaluated for Impairment	$ 1,418	$ -	$ 167	$ 200	$ 1,785
Loans collectively evaluated for Impairment	83,852	6,950	8,400	20,121	119,323
Total loans evaluated for impairment	$ 85,270	$ 6,950	$ 8,567	$ 20,321	$121,108

Note 5 – Troubled Debt Restructurings

ASC 310-40-20 defines a troubled debt restructuring as a restructuring of debt where a creditor for economic or legal reasons related to a debtor's financial difficulties grants a concession to the debtor that it would not otherwise consider. The concession is granted by the creditor in an attempt to protect as much of its investment as possible. The concession either stems from an agreement between the creditor and the debtor or is imposed by law or a court. Troubled debt restructurings include modification of the terms of a debt, such as a reduction of the stated interest rate for the remaining original life of the debt, an extension of the maturity date or dates at a stated interest rate lower than the current market rate for new debt with similar risk, a reduction of the face amount or maturity amount of the debt as stated in the instrument or other agreement, or a reduction of accrued interest.

Management reviews all restructured loans that occur during the year for identification as troubled debt restructurings. Management identified as troubled debt restructurings certain loans for which the allowance for loan losses had previously been measured under a general allowance for loan losses methodology (ASC 450-20). Upon identifying the reviewed loans as troubled debt restructurings, management also identified them as impaired under the guidance in ASC 310-10-35.

Modification Categories. The Bank offers a variety of modifications to borrowers. The modification categories offered can generally be described in the following categories:

Rate Modification – A modification in which the interest rate is changed.

Term Modification – A modification in which the maturity date, timing of payments, or frequency of payments is changed.

Interest Only Modification – A modification in which the loan is converted to interest only payments for a period of time.

Payment Modification – A modification in which the dollar amount of the payment is changed, other than an interest only modification as described above.

Combination Modification – Any other type of modification, including the use of multiple categories above.

(In thousands, except share and per-share data)

Note 5 – Troubled Debt Restructurings (continued)

The following tables present troubled debt restructurings as of December 31, 2015 and 2014:

	December 31, 2015			
	Number of Contracts	Accrual Status	Non-Accrual Status	Total Modifications
Real estate mortgage loans:				
Commercial mortgages	1	$ 57	$ -	$ 57
1-4 Family residential mortgages	9	591	15	606
Home equity lines of credit	-	-	-	-
Other mortgages	-	-	-	-
Real estate construction loans	-	-	-	-
Commercial loans	1	14	-	14
Consumer loans	25	215	-	215
Total	36	$ 877	$ 15	$ 892

	December 31, 2014			
	Number of Contracts	Accrual Status	Non-Accrual Status	Total Modifications
Real estate mortgage loans:				
Commercial mortgages	2	$ 79	$ -	$ 79
1-4 Family residential mortgages	9	603	-	603
Home equity lines of credit	-	-	-	-
Other mortgages	-	-	-	-
Real estate construction loans	-	-	-	-
Commercial loans	2	127	-	127
Consumer loans	21	157	1	158
Total	34	$ 966	$ 1	$ 967

(In thousands, except share and per-share data)

Note 5 – Troubled Debt Restructurings (continued)

The following tables present newly restructured loans, broken down by type of modification that occurred during the years ended December 31, 2015 and 2014:

Year Ended December 31, 2015

		Type of Modification					
Pre-Modification Outstanding Recorded Investment	No. of contracts	Rate	Term	Interest Only	Payment	Combination	Total
Real estate mortgage loans:							
Commercial mortgages	-	$ -	$ -	$ -	$ -	$ -	$ -
1-4 Family residential mortgages	1	-	-	-	-	58	58
Home equity lines of credit	-	-	-	-	-	-	-
Other mortgages	-	-	-	-	-	-	-
Real estate construction loans	-	-	-	-	-	-	-
Commercial loans	-	-	-	-	-	-	-
Consumer loans	8	-	4	-	-	100	104
Total	9	$ -	$ 4	$ -	$ -	$ 158	$ 162
Post-Modification Outstanding Recorded Investment							
Real estate mortgage loans:							
Commercial mortgages	-	$ -	$ -	$ -	$ -	$ -	$ -
1-4 Family residential mortgages	1	-	-	-	-	67	67
Home equity lines of credit	-	-	-	-	-	-	-
Other mortgages	-	-	-	-	-	-	-
Real estate construction loans	-	-	-	-	-	-	-
Commercial loans	-	-	-	-	-	-	-
Consumer loans	8	-	3	-	-	96	99
Total	9	$ -	$ 3	$ -	$ -	$ 163	$ 166

(In thousands, except share and per-share data)

Note 5 – Troubled Debt Restructurings (continued)

Year Ended December 31, 2014

		Type of Modification					
Pre-Modification Outstanding Recorded Investment	No. of contracts	Rate	Term	Interest Only	Payment	Combination	Total
Real estate mortgage loans:							
Commercial mortgages	-	$ -	$ -	$ -	$ -	$ -	$ -
1-4 Family residential mortgages	2	-	35	-	-	39	74
Home equity lines of credit	-	-	-	-	-	-	-
Other mortgages	-	-	-	-	-	-	-
Real estate construction loans	-	-	-	-	-	-	-
Commercial loans	1	-	-	-	-	96	96
Consumer loans	10	3	6	-	-	93	102
Total	13	$ 3	$ 41	$ -	$ -	$ 228	$ 272
Post-Modification Outstanding Recorded Investment							
Real estate mortgage loans:							
Commercial mortgages	-	$ -	$ -	$ -	$ -	$ -	$ -
1-4 Family residential mortgages	2	-	35	-	-	57	92
Home equity lines of credit	-	-	-	-	-	-	-
Other mortgages	-	-	-	-	-	-	-
Real estate construction loans	-	-	-	-	-	-	-
Commercial loans	1	-	-	-	-	96	96
Consumer loans	10	3	6	-	-	92	101
Total	13	$ 3	$ 41	$ -	$ -	$ 245	$ 289

The following table presents restructured loans with a payment default which occurred within 12 months of the restructuring date, and during the years ended December 31, 2015 and 2014:

	Year Ended December 31, 2015		Year Ended December 31, 2014	
Type of Loan	Number of contracts	Recorded Investment	Number of contracts	Recorded Investment
Real estate mortgage loans:				
Commercial mortgages	-	$ -	-	$ -
1 – 4 Family residential mortgage	1	67	1	35
Real estate construction loans	-	-	-	-
Commercial loans	-	-	-	-
Consumer loans	1	1	-	-
Total	2	$ 68	1	$ 35

(In thousands, except share and per-share data)

Note 6 - Bank premises and equipment

A summary of bank premises and equipment stated at cost, less accumulated depreciation, follows:

	December 31	
	2015	2014
Land	$ 465	$ 465
Buildings and improvements	3,436	3,282
Equipment, furniture and fixtures	2,134	2,084
	6,035	5,831
Less accumulated depreciation	(3,481)	(3,295)
Net bank premises and equipment	$ 2,554	$ 2,536

Note 7 – Bank-owned life insurance

During 2012, the Bank purchased life insurance on key employees in the face amount of $15,397. Generally accepted accounting standards require that these policies are recorded at the cash surrender value, net of surrender charges and/or early termination charges. As of December 31, 2015 and 2014, the BOLI cash surrender value was $5,549 and $5,386, respectively, resulting in other income of $163 and $171 in 2015 and 2014, respectively. The increases in the cash surrender values resulted in an annualized net yield of 2.88% (4.80% on a pre-tax equivalent basis) in 2015 and 3.05% (5.08% on a pre-tax equivalent basis) in 2014.

Note 8 - Pension plans

Effective January 1, 2012, the Bank amended its defined benefit pension plan (the "Plan"), converting it to a cash-balance pension plan whereby benefits earned by participants under the plan through December 31, 2011 were converted to an opening account balance for each participant. The opening balance was calculated based on IRS-mandated assumptions for lump-sum payouts. Eligibility under the cash-balance plan is the same as the previous defined benefit pension plan except the vesting period was shortened from five years to three years. Benefits under the cash-balance plan are computed based on graduated earnings rates determined by employees' years of credited service as of December 31, 2011, plus interest at rates pre-set by management and the cash-balance plan administrators. As with the previous defined benefit pension plan, assets are invested in a balanced fund, fixed income fund and equity fund administered by the Virginia Bankers Association. As of December 31, 2011, no new entrants will be allowed into the Plan.

The Bank complies with ASC 715, *Compensation – Retirement Benefits,* which requires management to present in the statement of financial position the funded status of the plan as an asset (overfunded) or liability (underfunded) with any unrecognized actuarial gain (loss), prior service costs, or transition amount from the adoption of ASC 715, shown as an adjustment to the accumulated other comprehensive income.

(In thousands, except share and per-share data)

Note 8 - Pension plans (continued)

Amounts recognized in accumulated other comprehensive income consist of an unrecognized net actuarial loss and an unrecognized prior service cost, both net of deferred income tax. The unrecognized net actuarial loss decreased $45 during the year ended December 31, 2015 compared to an increase of $764 during the year ended December 31, 2014, while the unrecognized prior service cost decreased $75 during both the years ended December 31, 2015 and 2014. These transactions were net of deferred income tax benefits of $10 and $285 during the years ended December 31, 2015 and December 31, 2014.

Because plan assets are held in a qualified trust, anticipated returns are not reduced for taxes. Further, solely for this purpose, the plan is assumed to continue in force and not terminate during the period during which assets are invested. However, consideration is given to the potential impact of current and future investment policy, cash flow into and out of the trust, and expenses (both investment and non-investment) typically paid from plan assets (to the extent such expenses are not explicitly estimated within periodic cost).

Asset Allocation

The plan's weighted-average asset allocations at December 31, 2015 and 2014, by asset category, are as follows:

	December 31,	
	2015	2014
Mutual Funds - Fixed Income	60%	58%
Mutual Funds - Equity	40%	42%
Total	100%	100%

The trust fund is sufficiently diversified to maintain a reasonable level of risk without imprudently sacrificing return, with a targeted asset allocation of 50% fixed income and 50% equities. The Investment Manager selects investment fund managers with demonstrated experience and expertise, and funds with demonstrated historical performance, for the implementation of the Plan's investment strategy. The Investment Manager will consider both actively and passively managed investment strategies and will allocate funds across the asset classes to develop an efficient investment structure.

It is the responsibility of the Trustee to administer the investments of the trust within reasonable costs, being careful to avoid sacrificing quality. These costs include, but are not limited to, management and custodial fees, consulting fees, transaction costs and other administrative costs chargeable to the trust.

The investment strategy for plan assets is to provide allocation models with varying degrees of investment return and risk consistent with sound funding objectives and participant demographics utilizing various types of assets such as large-cap stocks, S&P 500 index fund, small and mid-cap stocks, cash equivalents and short-term bonds. The performance goal for the investments of the plan is to exceed the investment benchmarks over the most recent 3- and 5-year periods while taking less risk than the market.

(In thousands, except share and per-share data)

Note 8 – Pension plans (continued)

Plan investments are stated at fair value, which is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (an exit price). The following table presents the fair value of the net assets, by asset category, at December 31, 2015 and 2014:

Description of Assets:		2015		2014
Mutual Funds / Equity	$	1,778	$	1,709
Mutual Funds / Fixed Income		2,616		2,339
Total plan assets	$	4,394	$	4,048

All of the plan's assets are considered to be Level 1 assets, within the fair value hierarchy, as of December 31, 2015 and 2014. Level 1 assets are those with quoted prices in active markets for identical assets or liabilities.

Other disclosures for the year ended December 31, 2015 and 2014:

Change in benefit obligation

		2015		2014
Projected benefit obligation – beginning of year	$	4,148	$	3,071
Service cost		135		125
Interest cost		156		158
Actuarial (gain) / loss		(142)		814
Benefits paid		(44)		(20)
Projected benefit obligation – end of year	$	4,253	$	4,148

Change in plan assets

		2015		2014
Fair value of assets – beginning of the year	$	4,048	$	3,463
Actual return on plan assets		(10)		155
Employer contribution		400		450
Benefits paid		(44)		(20)
Fair value of assets – end of the year	$	4,394	$	4,048
Deferred asset loss	$	275	$	78

(In thousands, except share and per-share data)

Note 8 – Pension plans (continued)

Funded status

		2015		2014
Projected benefit obligation – end of year	$	(4,253)	$	(4,148)
Fair value of assets – end of year		4,394		4,048
Funded status at the end of the year	$	141	$	(100)

Other changes in plan assets and benefit obligations recognized in other comprehensive income:

		2015		2014
Net (gain) loss	$	(45)	$	764
Amortization of prior service cost		75		75
Total amount recognized	$	30	$	839

The following tables set forth the disclosures regarding the defined benefit plan:

Components of net periodic benefit costs

		2015		2014
Service cost	$	135	$	125
Interest cost		156		158
Expected return on plan assets		(265)		(233)
Net amortization of prior service cost		(75)		(75)
Recognized net actuarial loss		177		128
Net periodic benefit cost	$	128	$	103

(In thousands, except share and per-share data)

Note 8 – Pension plans (continued)

The end of year weighted-average assumptions are:

	2015	2014
Discount rate used for net periodic pension cost	4.00%	5.00%
Discount rate used for disclosure	4.25%	4.00%
Expected return on plan assets	7.00%	7.00%
Rate of compensation increase	3.00%	3.00%
Rate of compensation increase for net periodic pension cost	3.00%	3.00%
Expected future interest crediting rate	3.00%	3.00%

Additional disclosure information

Accumulated benefit obligation, December 31, 2015	$ 4,253
Vested benefit obligation, December 31, 2015	$ 4,053

The projected benefit payments for the next ten years are as follows:

Year	Amount
2016	$ 599
2017	393
2018	103
2019	472
2020	309
2021 – 2025	2,200

401(k) plan

In addition to the defined benefit plan described above, the Bank also sponsors a 401(k) defined contribution plan. The Bank makes a matching contribution to the plan in the amount of 100% of the first 3% and 50% of the next 3% of the elective contributions made by the participants. Participants have the right to contribute up to the maximum allowed under section 401(g) of the Internal Revenue Code.

Effective January 1, 2012, the Bank made supplemental contributions to the 401(k) accounts of salaried employees with a minimum of 14 years of credited service as of December 31, 2011. These supplemental contributions were made to help compensate for the projected loss of pension benefits for these employees due to the transition to the cash-balance defined benefit plan. The supplemental contribution will be paid at the end of each year from 2012 through 2018 in which the employee remains in a salaried status with a minimum of 1,000 hours of credited service for that year.

(In thousands, except share and per-share data)

Note 8 – Pension plans (continued)

The Bank also made supplemental contributions to the 401(k) accounts of employees hired January 1, 2012 or later who were not eligible for participation in the cash-balance defined benefit plan. The supplemental contribution was equal to 2.0% of the employee salary and will be paid at the end of each year, beginning December 31, 2012. The Bank's expense for all 401(k) contributions totaled $210 and $204 for 2015 and 2014, respectively.

Note 9 - Income taxes

Income tax expense attributable to income before income tax expense is summarized as follows:

	December 31, 2015	December 31, 2014
Current federal income tax expense	$ 490	$ 462
Deferred federal income tax expense	181	50
Total	$ 671	$ 512

Income tax expense differed from amounts computed by applying the U.S. Federal income tax rate of 34% to income before income tax expense as a result of the following:

	December 31, 2015	December 31, 2014
Income tax expense at the statutory rate	$ 985	$ 859
Increase (reduction) in income tax expense resulting from		
Tax-exempt interest	(382)	(342)
Disallowance of interest expense	10	10
Bank-owned life insurance	(55)	(58)
Other	113	43
Total	$ 671	$ 512

(In thousands, except share and per-share data)

Note 9 - Income taxes (continued)

The tax effects of temporary differences that give rise to significant portions of the deferred tax assets and deferred tax liabilities are as follows:

	December 31	
	2015	2014
Deferred tax assets		
Loans, due to allowance for loan losses and net unearned fees	$ 101	$ 141
Other real estate, due to valuation allowances	20	54
Pension valuation adjustment	572	562
Other	150	153
Total gross deferred tax assets	843	910
Deferred tax liabilities		
Bank premises and equipment due to differences in depreciation	103	102
Prepaid pension, due to actual pension contribution in excess of accrual for financial reporting purposes	620	528
Net unrealized gain on available-for-sale securities	465	540
Loan costs	117	106
Total gross deferred tax liabilities	1,305	1,276
Net deferred tax (liability) asset	$ (462)	$ (366)

The Bank did not recognize any interest or penalties related to income tax during the years ended December 31, 2015 and 2014, and did not accrue interest or penalties as of December 31, 2015 and 2014. The Bank does not have an accrual for uncertain tax positions as of December 31, 2015 and 2014, as deductions taken and benefits accrued are based on widely understood administrative practices and procedures and are based on clear and unambiguous tax law. Tax returns for all years 2012 and thereafter are subject to future examination by tax authorities.

(In thousands, except share and per-share data)

Note 10 - Securities sold under repurchase agreements and time deposits

The Bank offers to its larger commercial customers a cash management service known as securities sold under repurchase agreements. These cash management accounts are administered by the Bank and pay a set interest rate determined by management. These accounts are secured by a pledge of the Bank's investments, which remain under management's control. The Bank had $1,418 and $1,080 outstanding in cash management accounts as of December 31, 2015 and 2014, respectively. The maximum month-end outstanding balances were $1,929 and $3,539 during 2015 and 2014, respectively, and the average outstanding balances were $1,273 and $2,265 during these periods.

At December 31, 2015, maturities of time deposits are scheduled as follows:

Year Ending	Amount
2016	$ 37,359
2017	12,199
2018	7,760
2019	4,722
2020	7,455
	$ 69,495

In the ordinary course of business, certain directors, executive officers, and their affiliates (collectively referred to as "related parties") of the Bank have maintained deposit accounts with the Bank. These deposits were opened on substantially the same terms, including interest rates for interest-bearing accounts, as those prevailing at the time for comparable transactions with other unaffiliated persons. Balances for these deposits as of December 31, 2015 were $1,771.

Note 11 - Dividend restrictions and capital requirements

The Bank is subject to certain regulatory restrictions pertaining to the amount of dividends that it may pay. The Federal Reserve restricts, without prior approval, the total dividend payments of a member bank in any calendar year to the bank's net income of that year, as defined, combined with its retained net income of the preceding two calendar years, less any required transfers to surplus. At December 31, 2015, retained earnings which are free of such restrictions amounted to approximately $3,930.

The Bank is subject to various regulatory capital requirements administered by the federal and state banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory and possibly additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the Bank's consolidated financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Bank must meet specific capital guidelines that involve quantitative measures of the Bank's assets, liabilities and certain off-balance-sheet items as calculated under regulatory accounting practices. The Bank's capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings and other factors.

(In thousands, except share and per-share data)

Note 11 - Dividend restrictions and capital requirements (continued)

Quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain minimum amounts and ratios (set forth in the table below) of total and Tier 1 risk-based capital (as defined in the regulations), to risk-weighted assets (as defined), and of Tier 1 capital (as defined) to average assets (as defined). Effective January 1, 2015, new capital rules implemented revisions to the risk-based regulatory capital framework for banks. These revisions included the establishment of the measure of common equity Tier 1 risk-based capital (as defined in the regulations) to risk-weighted assets (as defined). Management believes, as of December 31, 2015, that the Bank meets all capital adequacy requirements to which it is subject.

As of December 31, 2015, the most recent notification from the Federal Reserve Bank of Richmond categorized the Bank as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized, the Bank must maintain minimum total risk-based, common equity Tier 1 risk-based, Tier 1 risk-based and Tier 1 leverage ratios as set forth in the following table. There are no conditions or events since that notification that management believes have changed the Bank's category.

The Bank's actual regulatory capital amounts and ratios are also presented in the table below.

	Actual		For Capital Adequacy Purposes		To Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
December 31, 2015						
Total capital						
(to risk-weighted assets)	$ 28,743	19.7%	$ 11,674	8.0%	$ 14,592	>10.0%
Tier 1 capital						
(to risk-weighted assets)	$ 28,122	19.3%	$ 8,755	6.0%	$ 11,674	>8.0%
Common equity Tier 1 capital						
(to risk-weighted assets)	$ 28,122	19.3%	$ 6,566	4.5%	$ 9,489	>6.5%
Tier 1 capital (leverage)						
(to average assets)	$ 28,122	12.6%	$ 8,907	4.0%	$ 11,134	>5.0%
December 31, 2014						
Total capital						
(to risk-weighted assets)	$ 27,345	20.7%	$ 10,579	8.0%	$ 13,223	>10.0%
Tier 1 capital						
(to risk-weighted assets)	$ 26,655	20.2%	$ 5,289	4.0%	$ 7,934	>6.0%
Tier 1 capital (leverage)						
(to average assets)	$ 26,655	12.5%	$ 8,547	4.0%	$ 10,684	>5.0%

(In thousands, except share and per-share data)

Note 12 – Noninterest expense - Other operating expenses

Major items included in the other operating expenses component of noninterest expense are as follows:

	2015	2014
Office supplies	$ 96	$ 86
Data processing	558	504
Virginia franchise tax	185	174
Audit fees	84	84
Board expense	98	94
FDIC assessments	116	110
Marketing and advertising costs	29	22
Other	904	834
	$ 2,070	$ 1,908

Note 13 - Financial instruments with off-balance-sheet risk

The Bank is not a party to derivative financial instruments with off-balance-sheet risks such as futures, forwards, swaps and options. The Bank is a party to financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of its customers. These instruments may involve, to varying degrees, elements of credit risk in excess of the amount recognized in the balance sheets. The contract amounts of these instruments reflect the extent of involvement the Bank has in particular classes of financial instruments.

Credit risk is defined as the possibility of sustaining a loss because the other party to a financial instrument fails to perform in accordance with the terms of the contract. The Bank's maximum exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit and standby letters of credit is represented by the contractual amount of the instruments. The Bank uses the same credit policies in making commitments and conditional obligations as it does for on-balance-sheet instruments.

The Bank requires collateral or other security to support financial instruments when it is deemed necessary. The Bank evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Bank upon extension of credit, is based on management's credit evaluation of the counterparty and the Bank's access to the collateral. Types of collateral may include marketable securities, real estate and business equipment.

(In thousands, except share and per-share data)

Note 13 - Financial instruments with off-balance-sheet risk (continued)

Financial instruments whose contract amounts represent credit risk are as follows:

	Contract Amounts at December 31	
	2015	2014
Commitments to extend credit	$ 19,366	$ 18,729
Standby letters of credit	$ 481	$ 437

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since some of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements.

Standby letters of credit are conditional commitments issued by the Bank to guarantee the performance of a customer to a third party. Those guarantees are primarily issued to support private borrowing arrangements. The credit risk involved in issuing standby letters of credit is generally less than that involved in extending loans to customers because the Bank generally holds deposits equal to the commitment. Management does not anticipate any material losses as a result of these transactions.

The Bank's business activity is with customers located in the Counties of Appomattox, Buckingham, Campbell, and Prince Edward, Virginia. Accordingly, operating results are closely correlated with the economic trends within the counties and influenced by the significant industries within the region, including agriculture, timber and logging, and light manufacturing. In addition, the ultimate collectability of the Bank's loan portfolio is susceptible to changes in the market conditions within the region.

Note 14 - Disclosures about fair values of financial instruments

ASC 825, *Financial Instruments*, requires the Bank to disclose estimated fair values of its financial instruments.

The following methods and assumptions were used to estimate the approximate fair value of each class of financial instrument for which it is practicable to estimate fair value.

Cash and due from banks and federal funds sold

The carrying amount is a reasonable estimate of fair value due to the short investment duration.

Securities

The fair value of securities, except certain state and municipal instruments, is estimated based on bid prices published in financial newspapers or bid quotations received from securities dealers. The fair value of certain state and municipal securities is not readily available through market sources other than dealer quotations, so fair value estimates are based on quoted market prices of similar instruments, adjusted for differences between the quoted instruments and the instruments being valued.

Note 14 - Disclosures about fair values of financial instruments (continued)

Loans

Fair values are estimated for portfolios of loans with similar financial characteristics. Loans are segregated by two types, namely residential real estate (variable rate) and other loans (predominantly fixed rate consumer and commercial).

The fair value of loans is calculated by discounting scheduled cash flows for loans maturing after one year and through the estimated maturity using the average loan yield for the most recent quarter. The carrying amount of loans maturing within one year approximates their fair value. The estimate of maturity is based on actual loan maturity schedules for all types of loans.

Investment in bank-owned life insurance

Fair values of insurance policies owned are based on the insurance contract's cash surrender value.

Deposits

The fair values of noninterest-bearing demand deposits, interest-bearing demand deposits and savings deposits are equal to their carrying amounts since the amounts are payable on demand. The fair value of fixed maturity time deposits and certificates of deposit is estimated by discounting scheduled cash flows through maturity using the average time deposit yield for the most recent quarter.

Accrued interest receivable and accrued interest payable

The carrying amount of accrued interest receivable on the Bank's investment securities and loans is assumed to approximate fair value. Likewise, the carrying amount of accrued interest payable on the Bank's interest-bearing deposits is assumed to approximate fair value.

Securities sold under repurchase agreements

The carrying amount is a reasonable estimate of fair value.

Commitments to extend credit and standby letters of credit

The only amounts recorded for commitments to extend credit and standby letters of credit are the fees arising from these unrecognized financial instruments. These fees were minimal at December 31, 2015 and 2014, and as such, the related fair values have not been estimated.

(In thousands, except share and per-share data)

Note 14 - Disclosures about fair values of financial instruments (continued)

The carrying amounts and approximate fair values of the Bank's financial instruments are summarized as follows:

	December 31, 2015		December 31, 2014	
	Carrying Amounts	Approximate Fair Values	Carrying Amounts	Approximate Fair Values
Financial assets				
Cash and due from banks	$ 4,338	$ 4,338	$ 3,776	$ 3,776
Federal funds sold	3,169	3,169	3,064	3,064
Securities				
Available-for-sale	59,595	59,595	65,040	65,040
Held to maturity	18,447	18,958	11,209	11,930
Loans, net	126,559	117,371	120,417	112,338
Accrued interest receivable	1,155	1,155	1,157	1,157
Investment in bank-owned life insurance	5,549	5,549	5,386	5,386
Total financial assets	$ 218,812	$ 210,135	$ 210,049	$ 202,691
Financial liabilities				
Deposits	$ 192,680	$ 192,038	$ 185,420	$ 184,760
Securities sold under repurchase agreements	1,418	1,418	1,058	1,058
Accrued interest payable	100	100	114	114
Total financial liabilities	$ 194,198	$ 193,556	$ 186,592	$ 185,932

Fair value estimates are made at a specific point in time, based on relevant market information and information about the financial instrument. These estimates do not reflect any premium or discount that could result from offering for sale at one time the Bank's entire holdings of a particular financial instrument. Because no market exists for a significant portion of the Bank's financial instruments, fair value estimates are based on judgments regarding future expected loss experience, current economic conditions, risk characteristics of various financial instruments and other factors. These estimates are subjective in nature and involve uncertainties and matters of significant judgment, and therefore cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

Fair value estimates are based on existing on-balance-sheet and off-balance-sheet financial instruments without attempting to estimate the value of anticipated future business and the value of assets and liabilities that are not considered financial instruments. Significant assets that are not considered financial instruments include bank premises and equipment, and intangible assets; significant liabilities that are not considered financial instruments are accrued pension expense and the deferred income tax liability. In addition, the tax ramifications related to the realization of the unrealized gains and losses can have a significant effect on fair value estimates and have not been considered in the estimates.

Note 15 – Fair Value Measurements

ASC 820, *Fair Value Measurements and Disclosures*, provides a framework for measuring fair value under generally accepted accounting principles (GAAP) and enhances disclosures about fair value measurements. ASC 820 defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. When measuring fair value, valuation techniques should be appropriate in the circumstances and consistently applied. A hierarchy is used to prioritize valuation inputs into the following three levels to determine fair value:

- Level 1 – quoted prices (unadjusted) in active markets for identical assets or liabilities.
- Level 2 – observable inputs other than the quoted prices included in Level 1.
- Level 3 – unobservable inputs.

Assets measured at fair value on a recurring basis, including financial instruments for which the Bank has elected the fair value option, are summarized below. The Bank has not elected the fair value option to value liabilities.

Investment Securities Available-for-Sale
Investment securities available-for-sale are recorded at fair value on a recurring basis. Fair value measurement is based upon quoted prices, if available. If quoted prices are not available, fair values are measured using independent pricing models or other model-based valuation techniques. Level 1 securities include those traded on an active exchange, such as the New York Stock Exchange, U.S. Treasury securities that are traded by dealers or brokers in active over-the-counter markets and money market funds. Level 2 securities include mortgage-backed securities issued by government-sponsored entities, municipal bonds and corporate debt securities. Securities classified as Level 3 include asset-backed securities in less liquid markets.

Loans
The Bank does not record loans at fair value on a recurring basis. However, from time to time, a loan is considered impaired and an allowance for loan losses is established. Loans for which it is probable that payment of interest and principal will not be made in accordance with the contractual terms of the loan agreement are considered impaired. Once a loan is identified as individually impaired, management measures impairment in accordance with ASC 310, *Receivables*. The fair value of impaired loans is estimated using one of several methods, including collateral value, market value of similar debt, enterprise value, liquidation value and discounted cash flows. Those impaired loans not requiring an allowance represent loans for which the fair value of the expected repayments or collateral exceeds the recorded investments in such loans.

At December 31, 2015, substantially all of the total impaired loans were evaluated based on the fair value of the collateral. In accordance with ASC 820, impaired loans where an allowance is established based on the fair value of collateral require classification in the fair value hierarchy. When the fair value of the collateral is based on an observable market price or a current appraised value, the Bank records the impaired loan as nonrecurring Level 2. When an appraised value is not available or management determines the fair value of the collateral is further impaired below the appraised value and there is no observable market price, the Bank records the impaired loan as nonrecurring Level 3. Appraised values may be discounted to reflect current market conditions and ultimate collectability. These discounts typically ranged from 0% to 10% for each of the respective periods.

(In thousands, except share and per-share data)

Note 15 – Fair Value Measurements (continued)

Other Real Estate Owned
Real estate acquired primarily through foreclosure is transferred to other real estate owned ("OREO"). The measurement of loss associated with OREO is based on the fair value of the collateral compared to the unpaid loan balance and anticipated costs to sell the property. The value of OREO collateral is determined utilizing an income or market valuation approach based on an appraisal conducted by an independent, licensed appraiser outside of the Bank using observable market data (Level 2). However, if the collateral is a house or building in the process of construction or if an appraisal of the real estate is over one year old, then the fair value is considered Level 3. Any fair value adjustments are recorded in the period incurred and expensed against current earnings. Appraised values may be discounted to reflect current market conditions and ultimate collectability. These discounts typically ranged from 0% to 10% for each of the respective periods.

The following table summarizes quantitative disclosures about the fair value measurement for each category of assets carried at fair value as of December 31, 2015 and 2014, on a recurring or nonrecurring basis:

Description	Fair Value of Asset	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Recurring Basis:				
December 31, 2015				
Securities, Available-for-sale	$ 59,595	$ 10,705	$ 48,890	$ -
December 31, 2014				
Securities, Available-for-sale	$ 65,040	$ 11,724	$ 53,316	$ -
Nonrecurring Basis:				
December 31, 2015				
Impaired loans	$ 259	$ -	$ -	$ 259
Other real estate owned	$ 175	$ -	$ -	$ 175
December 31, 2014				
Impaired loans	$ 76	$ -	$ -	$ 76
Other real estate owned	$ 592	$ -	$ -	$ 592

Note 16 – Subsequent Events

Management has evaluated subsequent events for potential recognition and/or disclosure in the December 31, 2015 consolidated financial statements. This evaluation was through March 18, 2016, the date the consolidated financial statements were available to be issued. Management noted that on February 9, 2016, the Board of Directors declared a dividend of $0.40 per share payable March 3, 2016 to shareholders of record as of February 22, 2016.

BOARD OF DIRECTORS

L-R standing: Thomas D. Evans, Jr., R. Kinckle Robinson, John R. Caldwell, Douglas M. Webb, Alfred L. Jones, III, Luther C. Thomas, Benjamin H. Johnson

L-R seated: Alison F. Gobble, Floyd E. Williams, Ronald C. Spiggle, Watkins M. Abbitt, Jr., Laurie S.Harris

EXECUTIVE OFFICERS

L-R: Jane H. Kelly, Bruce S. Drinkard, Dawn S. Tolley, John R. Caldwell, Michael F. Ledin

FB

FARMERS BANK MANAGEMENT

Executive Officers:

John R. Caldwell	President & Chief Executive Officer
Bruce S. Drinkard	Senior Vice President & Chief Lending Officer
Jane H. Kelly	Senior Vice President, Chief Operations Officer, Cashier & Corporate Secretary
Michael F. Ledin	Senior Vice President & Chief Compliance Officer
Dawn S. Tolley	Senior Vice President & Chief Financial Officer

Officers:

Betty G. Craft	Vice President, Branch Administrator & Human Resource Officer
Sandra L. Clapp	Vice President & Accounting Officer II
Kenneth A. Shorter	Vice President & Data Processing Officer
Thomas L. Rasey, Jr.	Vice President & Loan Administration Officer
Thomas R. Cobb	Vice President & Main Office Branch Manager
Brian D. Wilkerson	Vice President & Concord Branch Manager
Stephanie L. Oliver	Vice President & Buckingham Branch Manager
Dianne Rudder	Vice President & Triangle Plaza Branch Manager
Anabelle Rodriquez-Milligan	Vice President & Longwood Village Branch Manager
Kris McFadden	Vice President & Mortgage Loan Officer
Leila A. Paulette	Vice President & Assistant Compliance Officer
Robin B. Harvey	Assistant Vice President & Assistant Operations Officer
Katherine Kraince	Assistant Vice President, Payroll & Benefits Officer
Jane Thomas	Assistant Vice President, Assistant Operations Officer & Assistant Branch Manager, Main
Lisa Warner	Assistant Vice President & Assistant Branch Manager, Buckingham
Judy Bolt	Bank Officer, Assistant Branch Manager & CSR, Farmville
Christopher Lewis	Bank Officer & Assistant Branch Manager, Concord
Sarah Overstreet	Bank Officer & Assistant Branch Manager, Triangle
Linda Sears	Bank Officer & Loan Support Supervisor
Kelly Smith	Bank Officer, Operations Specialist & Bank Security Officer
Jessica Hall	Bank Officer – Loan Officer
Jodi E. Simpson	Bank Officer – Loan Officer

EMPLOYEES

MAIN OFFICE

Tara Almond
Janet Baker
James Bollinger
Candy Burrell
Whitney Drew
Dorothy Evans
Wanda Evans
Penny Franklin
Sue Fulcher
Aubrey Hall, IV
Curtis Hancock
Kaitlyn Hopkins
Michael Inglett
Joan Jamerson
Uwana Litchford
Barbara Moore
Marty Moore
Gwen Phelps
Sue Ranson
Cassandra Reed
Sonny Smith
Mary Sue Stanley
Tommy Stanley
Mary Staples
Dela Trejo
Taylor Webster
Zach Williams
Lynn Wilmoth

TRIANGLE PLAZA BRANCH

Del Chambers
Rachel Franklin
Cindy Mayberry
Keelyn Wheeler
Betty Wingfield

CONCORD BRANCH

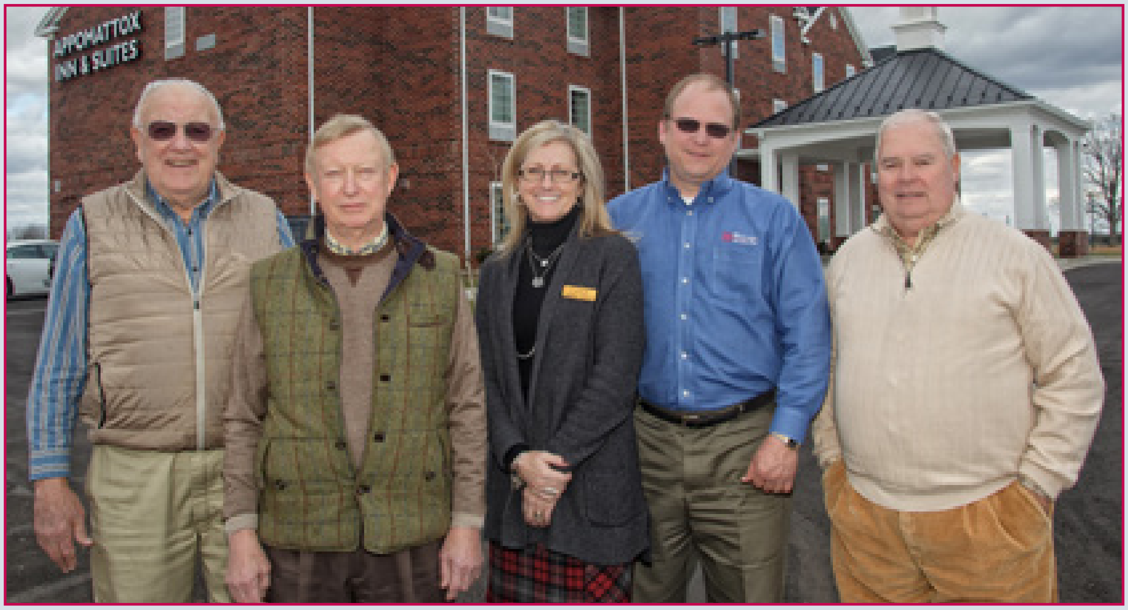
Hope Bondurant
Sue Doss
Connie French
Sarah Glover
Scottie Tyree
Lisa Vitalis

BUCKINGHAM BRANCH

Beverly Jo Devore
Kara Kitchen
Sherri Martin
Jackie Murphy
Stacy Perkins

FARMVILLE BRANCH

Ellen McGarry
Rachel Overstreet
Danielle Scruggs
Samantha Williams



Helping Local Businesses Grow

Our Experienced and Dedicated Lending Officers Stand Ready to Serve You

Breast Cancer Awareness “Pink Day” 2015

Volunteerism - Making a Difference in Our Communities