OLD POINT FINANCIAL CORP
Form 10-Q
August 10, 2016
UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)
QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended June 30, 2016

or

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

For the transition period from____________ to___________

Commission File Number: 000-12896

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

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

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

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

Not Applicable
(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

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

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

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

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

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

4,959,009 shares of common stock ($5.00 par value) outstanding as of July 29, 2016

OLD POINT FINANCIAL CORPORATION

FORM 10-Q

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PART I – FINANCIAL INFORMATION

Item 1. Financial Statements.

Old Point Financial Corporation and Subsidiaries
Consolidated Balance Sheets

	June 30, 2016	December 31, 2015
	(dollars in thousands except per share data)	
	(unaudited)	
Assets		
Cash and due from banks	$28,974	$33,514
Interest-bearing due from banks	1,722	1,064
Federal funds sold	1,520	2,412
Cash and cash equivalents	32,216	36,990
Securities available-for-sale, at fair value	166,216	214,192
Restricted securities	2,882	2,016
Loans, net of allowance for loan losses of $7,934 and $7,738	590,227	560,737
Premises and equipment, net	40,285	41,282
Bank-owned life insurance	24,843	24,411
Other real estate owned, net of valuation allowance of $2,046 and $2,549	1,887	2,741
Other assets	39,117	14,418
Total assets	$897,673	$896,787
Liabilities & Stockholders' Equity		
Deposits:		
Noninterest-bearing deposits	$206,815	$215,090
Savings deposits	311,932	321,370
Time deposits	208,254	210,011
Total deposits	727,001	746,471
Overnight repurchase agreements	23,865	25,950
Federal Home Loan Bank advances	45,000	25,000
Accrued expenses and other liabilities	5,874	6,190
Total liabilities	801,740	803,611
Commitments and contingencies		
Stockholders' equity:		
Common stock, $5/share par value, 10,000,000 shares authorized; 4,959,009 shares issued and outstanding	24,795	24,795
Additional paid-in capital	16,392	16,392
Retained earnings	55,732	55,151
Accumulated other comprehensive loss, net	(986)	(3,162)
Total stockholders' equity	95,933	93,176
Total liabilities and stockholders' equity	$897,673	$896,787

See Notes to Consolidated Financial Statements.

Old Point Financial Corporation and Subsidiaries
Consolidated Statements of Income

	Three Months Ended June 30,		Six Months Ended June 30,	
	2016	2015	2016	2015
	(unaudited, dollars in thousands except per share data)			
Interest and Dividend Income:				
Interest and fees on loans	$6,560	$6,485	$12,973	$12,840
Interest on due from banks	1	3	5	10
Interest on federal funds sold	1	1	2	1
Interest on securities:				
Taxable	471	615	1,019	1,301
Tax-exempt	376	415	760	838
Dividends and interest on all other securities	26	31	41	64
Total interest and dividend income	7,435	7,550	14,800	15,054
Interest Expense:				
Interest on savings deposits	54	57	109	109
Interest on time deposits	517	544	1,034	1,072
Interest on federal funds purchased, securities sold under agreements to repurchase and other borrowings	8	8	14	16
Interest on Federal Home Loan Bank advances	3	309	144	614
Total interest expense	582	918	1,301	1,811
Net interest income	6,853	6,632	13,499	13,243
Provision for loan losses	1,250	25	1,400	300
Net interest income, after provision for loan losses	5,603	6,607	12,099	12,943
Noninterest Income:				
Income from fiduciary activities	877	914	1,778	1,894
Service charges on deposit accounts	1,021	994	1,996	1,976
Other service charges, commissions and fees	1,033	1,058	2,051	2,063
Income from bank-owned life insurance	217	222	432	443
Income from Old Point Mortgage	80	125	89	158
Gain on sale of available-for-sale securities, net	6	0	515	0
Other operating income	52	46	90	102
Total noninterest income	3,286	3,359	6,951	6,636
Noninterest Expense:				
Salaries and employee benefits	4,890	5,057	10,044	10,106
Occupancy and equipment	1,390	1,304	2,748	2,631
Data processing	435	407	857	765
FDIC insurance	156	153	321	300
Customer development	154	161	304	315
Legal and audit expenses	295	160	497	274
Other outside service fees	178	195	361	309
Employee professional development	179	162	327	293
Capital stock tax	127	111	262	225
ATM and check losses	83	142	170	279

Prepayment fee on Federal Home Loan Bank advance	0	0	391	0
Loss on write-down/sale of other real estate owned	9	3	108	72
Other operating expenses	589	639	1,186	1,212
Total noninterest expense	8,485	8,494	17,576	16,781
Income before income taxes	404	1,472	1,474	2,798
Income tax expense (benefit)	(148)	193	(99)	314
Net income	$552	$1,279	$1,573	$2,484
Basic earnings per share				
Weighted average shares outstanding	4,959,009	4,959,009	4,959,009	4,959,009
Net income per share of common stock	$0.11	$0.26	$0.32	$0.50
Diluted earnings per share				
Weighted average shares outstanding	4,959,009	4,959,009	4,959,009	4,959,009
Net income per share of common stock	$0.11	$0.26	$0.32	$0.50

See Notes to Consolidated Financial Statements.

Old Point Financial Corporation and Subsidiaries
Consolidated Statements of Comprehensive Income

	Three Months Ended June 30,		Six Months Ended June 30,	
	2016	2015	2016	2015
	(unaudited, dollars in thousands)			
Net income	$552	$1,279	$1,573	$2,484
Other comprehensive income (loss), net of tax				
Net unrealized gain (loss) on available-for-sale securities	1,661	(1,002)	2,176	(911)
Amortization of unrealized losses on securities transferred to held-to-maturity	0	170	0	311
Other comprehensive income (loss), net of tax	1,661	(832)	2,176	(600)
Comprehensive income	$2,213	$447	$3,749	$1,884

See Notes to Consolidated Financial Statements.

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

	Shares of Common Stock	Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total
	(unaudited, dollars in thousands except per share data)					
SIX MONTHS ENDED JUNE 30, 2016						
Balance at beginning of period	4,959,009	$ 24,795	$ 16,392	$ 55,151	$ (3,162)	$ 93,176
Net income	0	0	0	1,573	0	1,573
Other comprehensive income, net of tax	0	0	0	0	2,176	2,176
Cash dividends ($0.20 per share)	0	0	0	(992)	0	(992)
Balance at end of period	4,959,009	$ 24,795	$ 16,392	$ 55,732	$ (986)	$ 95,933
SIX MONTHS ENDED JUNE 30, 2015						
Balance at beginning of period	4,959,009	$ 24,795	$ 16,392	$ 53,203	$ (5,893)	$ 88,497
Net income	0	0	0	2,484	0	2,484
Other comprehensive loss, net of tax	0	0	0	0	(600)	(600)
Cash dividends ($0.16 per share)	0	0	0	(793)	0	(793)
Balance at end of period	4,959,009	$ 24,795	$ 16,392	$ 54,894	$ (6,493)	$ 89,588

See Notes to Consolidated Financial Statements.

Old Point Financial Corporation and Subsidiaries
Consolidated Statements of Cash Flows

	Six Months Ended June 30, 2016	2015
	(unaudited, dollars in thousands)	
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	$1,573	$2,484
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	1,349	1,257
Provision for loan losses	1,400	300
Net gain on sale of available-for-sale securities	(515)	0
Net amortization of securities	1,060	1,111
Net (gain) loss on disposal of premises and equipment	(3)	1
Net loss on write-down/sale of other real estate owned	108	72
Income from bank owned life insurance	(432)	(443)
Deferred tax expense	122	138
Increase in other assets	(1,459)	(5,034)
Increase (decrease) in other liabilities	(316)	4,061
Net cash provided by operating activities	2,887	3,947
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchases of available-for-sale securities	(83,098)	(42,381)
Cash used in purchases of restricted securities	(866)	(573)
Proceeds from maturities and calls of available-for-sale securities	41,765	40,690
Proceeds from maturities and calls of held-to-maturity securities	0	300
Proceeds from sales of available-for-sale securities	61,680	2,055
Paydowns on available-for-sale securities	5,899	4,918
Paydowns on held-to-maturity securities	0	4,021
Purchases of government-guaranteed student loans	0	(14,315)
Net increase in all other loans (including repayments on student loans)	(30,890)	(21,662)
Proceeds from sales of other real estate owned	924	522
Payments for improvements to other real estate owned	(52)	0
Purchases of premises and equipment	(476)	(1,048)
Net cash used in investing activities	(5,114)	(27,473)
CASH FLOWS FROM FINANCING ACTIVITIES		
Decrease in noninterest-bearing deposits	(8,275)	(1,315)
Increase (decrease) in savings deposits	(9,438)	9,975
Decrease in time deposits	(1,757)	(1,654)
Decrease in federal funds purchased, repurchase agreements and other borrowings, net	(2,085)	(9,936)
Increase in Federal Home Loan Bank advances	55,000	20,000
Repayment of Federal Home Loan Bank advances	(35,000)	(5,000)
Cash dividends paid on common stock	(992)	(793)
Net cash provided by (used in) financing activities	(2,547)	11,277
Net decrease in cash and cash equivalents	(4,774)	(12,249)
Cash and cash equivalents at beginning of period	36,990	33,305

Cash and cash equivalents at end of period	$32,216	$21,056
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION		
Cash payments for:		
Interest	$1,322	$1,815
Income tax	$0	$200
SUPPLEMENTAL SCHEDULE OF NONCASH TRANSACTIONS		
Unrealized gain (loss) on securities available-for-sale	$3,297	$(1,381)
Loans transferred to other real estate owned	$0	$454
Former bank building transferred from fixed assets to other real estate owned	$127	$0
Amortization of unrealized loss on securities transferred to held-to-maturity	$0	$471
Securities sold but not settled	$24,483	$0

See Notes to Consolidated Financial Statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

Note 1. General

The accompanying unaudited consolidated financial statements of Old Point Financial Corporation (the Company) and its subsidiaries have been prepared in accordance with U.S. generally accepted accounting principles (GAAP) for interim financial information. All significant intercompany balances and transactions have been eliminated. In the opinion of management, the accompanying unaudited consolidated financial statements contain all adjustments and reclassifications of a normal and recurring nature considered necessary to present fairly the financial position at June 30, 2016 and December 31, 2015, the statements of income and comprehensive income for the three and six months ended June 30, 2016 and 2015, and the statements of changes in stockholders' equity and cash flows for the six months ended June 30, 2016 and 2015. The results of operations for the interim periods are not necessarily indicative of the results that may be expected for the full year.

These consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company's 2015 annual report on Form 10-K. Certain previously reported amounts have been reclassified to conform to current period presentation, none of which were material in nature.

PRINCIPLES OF CONSOLIDATION

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries, The Old Point National Bank of Phoebus (the Bank) and Old Point Trust & Financial Services N.A. (Trust). All significant intercompany balances and transactions have been eliminated in consolidation. The Company consolidates subsidiaries in which it holds, directly or indirectly, more than 50 percent of the voting rights or where it exercises control. Entities where the Company holds 20 to 50 percent of the voting rights, or has the ability to exercise significant influence, or both, are accounted for under the equity method. As discussed below, the Company consolidates entities deemed to be variable interest entities (VIEs) when it is determined to be the primary beneficiary.

NATURE OF OPERATIONS

Old Point Financial Corporation is a holding company that conducts substantially all of its operations through two subsidiaries, The Old Point National Bank of Phoebus and Old Point Trust & Financial Services, N.A. The Bank serves individual and commercial customers, the majority of which are in Hampton Roads, Virginia. As of June 30, 2016, the Bank had 18 branch offices. The Bank offers a full range of deposit and loan products to its retail and commercial customers. Trust offers a full range of services for individuals and businesses. Products and services include retirement planning, estate planning, financial planning, estate and trust administration, retirement plan administration, tax services and investment management services.

VARIABLE INTEREST ENTITIES

A legal entity is referred to as a VIE if any of the following conditions exist, which are outlined in the Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) variable interest accounting guidance (FASB ASC 810-10-15-14): (1) the total equity investment at risk is insufficient to permit the legal entity to finance its activities without additional subordinated financial support from other parties, or (2) the entity has equity investors that cannot make significant decisions about the entity's operations or that do not absorb their proportionate share of the expected losses or receive the expected returns of the entity.

Note 2. Securities

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

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(in thousands)			
June 30, 2016				
Obligations of U.S. Government agencies	$24,270	$ 5	$ 0	$24,275
Obligations of state and political subdivisions	70,669	2,065	0	72,734
Mortgage-backed securities	64,533	339	(15)	64,857
Money market investments	621	0	0	621
Corporate bonds and other securities	3,598	27	(1)	3,624
Other marketable equity securities	100	5	0	105
Total	$163,791	$ 2,441	$ (16)	$166,216
December 31, 2015				
Obligations of U.S. Government agencies	$24,353	$ 1	$ (114)	$24,240
Obligations of state and political subdivisions	77,223	1,323	(113)	78,433
Mortgage-backed securities	109,360	0	(1,964)	107,396
Money market investments	631	0	0	631
Corporate bonds and other securities	3,397	4	(8)	3,393
Other marketable equity securities	100	0	(1)	99
Total	$215,064	$ 1,328	$ (2,200)	$214,192

The following table summarizes realized gains and losses on the sale of investment securities during the periods indicated:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2016	2015	2016	2015
Securities Available-for-sale				
Realized gains on sales of securities	$6	$ 0	$554	$ 0
Realized losses on sales of securities	0	0	(39)	0
Net realized gain	$6	$ 0	$515	$ 0

OTHER-THAN-TEMPORARILY IMPAIRED SECURITIES

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

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

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

The Company has not recorded impairment charges through income on securities for the three or six months ended June 30, 2016 or 2015.

TEMPORARILY IMPAIRED SECURITIES

The following table shows the number of securities with unrealized losses, and the gross unrealized losses and fair value of the Company's investments with unrealized losses that are deemed to be temporarily impaired, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position as of the dates indicated:

	June 30, 2016						
	Less Than Twelve Months		More Than Twelve Months		Total		
	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Number of Securities
	(dollars in thousands)						
Securities Available-for-Sale							
Mortgage-backed securities	$ 15	4,062	$ 0	$ 0	$ 15	$ 4,062	1
Corporate bonds	0	0	1	99	1	99	1
Total securities available-for-sale	$ 15	$ 4,062	$ 1	$ 99	$ 16	$ 4,161	2

	December 31, 2015						
	Less Than Twelve Months		More Than Twelve Months		Total		
	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Number of Securities
	(dollars in thousands)						
Securities Available-for-Sale							
Obligations of U.S. Government agencies	$ 0	$ 0	$ 114	$ 3,940	$ 114	$ 3,940	2
Obligations of state and political subdivisions	42	4,177	71	3,545	113	7,722	13
Mortgage-backed securities	848	62,698	1,116	44,698	1,964	107,396	13
Corporate bonds	6	2,091	2	198	8	2,289	16
Other marketable equity securities	1	99	0	0	1	99	1
Total securities available-for-sale	$ 897	$ 69,065	$ 1,303	$ 52,381	$ 2,200	$ 121,446	45

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Certain investments within the Company's portfolio had unrealized losses at June 30, 2016 and December 31, 2015, as shown in the tables above. The unrealized losses were caused by increases in market interest rates. Because the Company does not intend to sell the investments and management believes it is unlikely that the Company will be required to sell the investments before recovery of their amortized cost basis, which may be maturity, the Company does not consider the investments to be other-than-temporarily impaired at June 30, 2016 or December 31, 2015.

Restricted Securities
The restricted security category is comprised of stock in the Federal Home Loan Bank of Atlanta (FHLB) and the Federal Reserve Bank (FRB). These stocks are classified as restricted securities because their ownership is restricted to certain types of entities and the securities lack a market. Therefore, FHLB and FRB stock is carried at cost and evaluated for impairment. When evaluating these stocks for impairment, their value is determined based on the ultimate recoverability of the par value rather than by recognizing temporary declines in value. Restricted stock is viewed as a long-term investment and management believes that the Company has the ability and the intent to hold this stock until its value is recovered.

Note 3. Loans and the Allowance for Loan Losses

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

	June 30, 2016	December 31, 2015
	(in thousands)	
Mortgage loans on real estate:		
Residential 1-4 family	$96,892	$96,997
Commercial	281,323	277,758
Construction	26,286	19,685
Second mortgages	16,673	15,148
Equity lines of credit	46,669	47,256
Total mortgage loans on real estate	467,843	456,844
Commercial loans	54,996	43,197
Consumer loans	44,112	50,427
Other	31,210	18,007
Total loans, net of deferred fees (1)	598,161	568,475
Less: Allowance for loan losses	(7,934)	(7,738)
Loans, net of allowance and deferred fees (1)	$590,227	$560,737

(1) Deferred loan fees totaled $443 thousand and $407 thousand at June 30, 2016 and December 31, 2015, respectively.

Overdrawn deposit accounts are reclassified as loans and included in the Other category in the table above. Overdrawn deposit accounts totaled $617 thousand and $648 thousand at June 30, 2016 and December 31, 2015, respectively.

CREDIT QUALITY INFORMATION

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

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

- Pass: Loans are of acceptable risk.
- Other Assets Especially Mentioned (OAEM): Loans have potential weaknesses that deserve management's close attention.
- Substandard: Loans reflect significant deficiencies due to several adverse trends of a financial, economic or managerial nature.
- Doubtful: Loans have all the weaknesses inherent in a substandard loan with added characteristics that make collection or liquidation in full based on currently existing facts, conditions and values highly questionable or improbable.
- Loss: Loans have been charged off because they are considered uncollectible and of such little value that their continuance as bankable assets is not warranted.

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

Credit Quality Information As of June 30, 2016 (in thousands)				
	Pass	OAEM	Substandard	Total
Mortgage loans on real estate:				
Residential 1-4 family	$94,796	$0	$ 2,096	$96,892
Commercial	262,291	10,627	8,405	281,323
Construction	25,375	164	747	26,286
Second mortgages	16,346	0	327	16,673
Equity lines of credit	46,575	0	94	46,669
Total mortgage loans on real estate	445,383	10,791	11,669	467,843
Commercial loans	52,485	1,483	1,028	54,996
Consumer loans	44,035	0	77	44,112
Other	31,210	0	0	31,210
Total	$573,113	$12,274	$ 12,774	$598,161

Credit Quality Information As of December 31, 2015 (in thousands)				
	Pass	OAEM	Substandard	Total
Mortgage loans on real estate:				
Residential 1-4 family	$94,576	$0	$ 2,421	$96,997
Commercial	261,749	7,394	8,615	277,758
Construction	18,931	0	754	19,685
Second mortgages	14,835	0	313	15,148
Equity lines of credit	47,161	0	95	47,256
Total mortgage loans on real estate	437,252	7,394	12,198	456,844
Commercial loans	40,268	467	2,462	43,197
Consumer loans	50,327	0	100	50,427
Other	18,007	0	0	18,007
Total	$545,854	$7,861	$ 14,760	$568,475

As of June 30, 2016 and December 31, 2015, the Company did not have any loans internally classified as Loss or Doubtful.

AGE ANALYSIS OF PAST DUE LOANS BY CLASS

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

Age Analysis of Past Due Loans as of June 30, 2016

	30 - 59 Days Past Due	60 - 89 Days Past Due	90 or More Days Past Due	Total Past Due	Total Current Loans (1)	Total Loans	Recorded Investment > 90 Days Past Due and Accruing
	(in thousands)						
Mortgage loans on real estate:							
Residential 1-4 family	$505	$309	$810	$1,624	$95,268	$96,892	$ 520
Commercial	1,582	0	129	1,711	279,612	281,323	17
Construction	0	0	0	0	26,286	26,286	0
Second mortgages	144	0	214	358	16,315	16,673	60
Equity lines of credit	28	0	51	79	46,590	46,669	51
Total mortgage loans on real estate	2,259	309	1,204	3,772	464,071	467,843	648
Commercial loans	2	16	86	104	54,892	54,996	0
Consumer loans	1,191	971	2,570	4,732	39,380	44,112	2,570
Other	49	9	4	62	31,148	31,210	4
Total	$3,501	$1,305	$3,864	$8,670	$589,491	$598,161	$ 3,222

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

In the table above, the consumer category includes student loans with principal and interest amounts that are 97 - 98% guaranteed by the federal government. The past due principal portion of these guaranteed loans totaled $4.5 million at June 30, 2016.

Age Analysis of Past Due Loans as of December 31, 2015

	30 - 59 Days Past Due	60 - 89 Days Past Due	90 or More Days Past Due	Total Past Due	Total Current Loans (1)	Total Loans	Recorded Investment > 90 Days Past Due and Accruing
	(in thousands)						
Mortgage loans on real estate:							
Residential 1-4 family	$309	$1,042	$275	$1,626	$95,371	$96,997	$ 0
Commercial	1,266	31	23	1,320	276,438	277,758	23
Construction	161	0	0	161	19,524	19,685	0
Second mortgages	21	39	165	225	14,923	15,148	0
Equity lines of credit	170	0	0	170	47,086	47,256	0
Total mortgage loans on real estate	1,927	1,112	463	3,502	453,342	456,844	23

Commercial loans	500	88	232	820	42,377	43,197	164
Consumer loans	1,673	1,350	3,163	6,186	44,241	50,427	3,163
Other	64	3	6	73	17,934	18,007	6
Total	$4,164	$2,553	$3,864	$10,581	$557,894	$568,475	$ 3,356

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

In the table above, the consumer category includes student loans with principal and interest amounts that are 97 - 98% guaranteed by the federal government. The past due principal portion of these guaranteed loans totaled $5.7 million at December 31, 2015.

Although the portion of the student loan portfolio that is 90 days or more past due would normally be considered impaired, the Company does not include these loans in its impairment analysis. Because the federal government has provided guarantees of repayment of these student loans in an amount ranging from 97% to 98% of the total principal and interest of the loans, management does not expect significant increases in past due student loans to have a material effect on the Company.

NONACCRUAL LOANS

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

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

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

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

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

Nonaccrual Loans by Class

	June 30, 2016	December 31, 2015
	(in thousands)	
Mortgage loans on real estate		
Residential 1-4 family	$1,058	$ 1,457
Commercial	2,501	2,623
Second mortgages	154	226
Total mortgage loans on real estate	3,713	4,306
Commercial loans	197	276

Total	$3,910	$ 4,582

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

	Six Months Ended June 30,	
	2016	2015
	(in thousands)	
Interest income that would have been recorded under original loan terms	$101	$110
Actual interest income recorded for the period	85	97
Reduction in interest income on nonaccrual loans	$16	$13

TROUBLED DEBT RESTRUCTURINGS

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

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

The following table presents TDRs during the period indicated, by class of loan. There were no troubled debts restructured in the first six months of 2015 or in the second quarter of 2016.

Troubled Debt Restructurings by Class
For the Six Months Ended June 30, 2016
(dollars in thousands)

	Number of Modifications	Recorded Investment Prior to Modification	Recorded Investment After Modification	Current Investment on June 30, 2016
Commercial loans	1	$ 152	$ 152	$ 110

The loan restructured in the first six months of 2016 was given a below-market rate for debt with similar risk characteristics. At June 30, 2016 and December 31, 2015, the Company had no outstanding commitments to disburse additional funds on any TDR. At December 31, 2015, the Company had $53 thousand in loans secured by residential 1 - 4 family real estate that were in the process of foreclosure. There were no loans loans secured by residential 1 - 4 family real estate in the process of foreclosure at June 30, 2016.

In the three and six months ended June 30, 2016 and 2015, there were no defaulting TDRs where the default occurred within twelve months of restructuring. The Company considers a TDR in default when any of the following occurs: the loan, as restructured, becomes 90 days or more past due; the loan is moved to nonaccrual status following the restructure; the loan is restructured again under terms that would qualify it as a TDR if it were not already so classified; or any portion of the loan is charged off.

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

IMPAIRED LOANS

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

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

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

Impaired Loans by Class
(in thousands)

	As of June 30, 2016				For the six months ended June 30, 2016	
	Unpaid Principal Balance	Recorded Investment Without Valuation Allowance	With Valuation Allowance	Associated Allowance	Average Recorded Investment	Interest Income Recognized
Mortgage loans on real estate:						
Residential 1-4 family	$2,721	$1,735	$ 640	$ 124	$2,642	$ 51
Commercial	10,183	6,188	3,168	463	9,353	232
Construction	633	536	97	35	366	21
Second mortgages	526	482	0	0	517	14
Total mortgage loans on real estate	$14,063	$8,941	$ 3,905	$ 622	$12,878	$ 318
Commercial loans	1,145	197	824	137	664	41
Consumer loans	0	0	0	0	6	0
Total	$15,208	$9,138	$ 4,729	$ 759	$13,548	$ 359

Impaired Loans by Class
(in thousands)

	As of December 31, 2015				For the Year Ended December 31, 2015	
	Unpaid Principal Balance	Recorded Investment Without Valuation Allowance	With Valuation Allowance	Associated Allowance	Average Recorded Investment	Interest Income Recognized
Mortgage loans on real estate:						
Residential 1-4 family	$2,994	$1,530	$ 1,261	$ 146	$2,267	$ 132
Commercial	10,203	6,166	3,208	608	9,305	473
Construction	99	0	99	36	465	5
Second mortgages	535	499	0	0	571	21
Total mortgage loans on real estate	$13,831	$8,195	$ 4,568	$ 790	$12,608	$ 631
Commercial loans	330	207	68	8	952	28
Consumer loans	12	12	0	0	13	1
Total	$14,173	$8,414	$ 4,636	$ 798	$13,573	$ 660

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

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

ALLOWANCE FOR LOAN LOSSES

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

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

Each portfolio segment has risk characteristics as follows:

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

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

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

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

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

Each segment of the portfolio is pooled by risk grade or by days past due. Consumer loans not secured by real estate and made to individuals for household, family and other personal expenditures are segmented into pools based on days past due, while all other loans, including loans to consumers that are secured by real estate, are segmented by risk grades. A historical loss percentage is then calculated by migration analysis and applied to each pool. The migration analysis applied to all pools is able to track the risk grading and historical performance of individual loans throughout a number of periods set by management, which provides management with information regarding trends (or migrations) in a particular loan segment. At December 31, 2015 and June 30, 2016, management used twelve-quarter migration periods.

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

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

ALLOWANCE FOR LOAN LOSSES BY SEGMENT

The total allowance reflects management's estimate of losses inherent in the loan portfolio at the balance sheet date. The Company considers the allowance for loan losses of $7.9 million adequate to cover loan losses inherent in the loan portfolio at June 30, 2016.

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

ALLOWANCE FOR LOAN LOSSES AND RECORDED INVESTMENT IN LOANS
(in thousands)

For the Six Months Ended June 30, 2016	Commercial	Real Estate - Construction	Real Estate - Mortgage (1)	Consumer	Other	Total
Allowance for Loan Losses:						
Balance at the beginning of period	$ 633	$ 985	$ 5,628	$ 279	$ 213	$ 7,738
Charge-offs	(858)	0	(268)	(99)	(62)	(1,287)
Recoveries	24	3	17	22	17	83
Provision for loan losses	1,287	297	(496)	198	114	1,400
Ending balance	$ 1,086	$ 1,285	$ 4,881	$ 400	$ 282	$ 7,934
Ending balance individually evaluated for impairment	$ 137	$ 35	$ 587	$ 0	$ 0	$ 759
Ending balance collectively evaluated for impairment	949	1,250	4,294	400	282	7,175
Ending balance	$ 1,086	$ 1,285	$ 4,881	$ 400	$ 282	$ 7,934
Loan Balances:						
Ending balance individually evaluated for impairment	$ 1,021	$ 633	$ 12,213	$ 0	$ 0	$ 13,867
Ending balance collectively evaluated for impairment	53,975	25,653	429,344	44,112	31,210	584,294
Ending balance	$ 54,996	$ 26,286	$ 441,557	$ 44,112	$ 31,210	$ 598,161

For the Year Ended December 31, 2015	Commercial	Real Estate - Construction	Real Estate - Mortgage (1)	Consumer	Other	Total
Allowance for Loan Losses:						
Balance at the beginning of period	$ 595	$ 703	$ 5,347	$ 219	$ 211	$ 7,075
Charge-offs	(293)	0	(321)	(92)	(191)	(897)
Recoveries	50	1	393	39	52	535
Provision for loan losses	281	281	209	113	141	1,025
Ending balance	$ 633	$ 985	$ 5,628	$ 279	$ 213	$ 7,738
Ending balance individually evaluated for impairment	$ 8	$ 36	$ 754	$ 0	$ 0	$ 798
Ending balance collectively evaluated for impairment	625	949	4,874	279	213	6,940
Ending balance	$ 633	$ 985	$ 5,628	$ 279	$ 213	$ 7,738
Loan Balances:						
Ending balance individually evaluated for impairment	$ 275	$ 99	$ 12,664	$ 12	$ 0	$ 13,050
Ending balance collectively evaluated for impairment	42,922	19,586	424,495	50,415	18,007	555,425
Ending balance	$ 43,197	$ 19,685	$ 437,159	$ 50,427	$ 18,007	$ 568,475

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

CHANGES IN ACCOUNTING METHODOLOGY

There were no changes in the Company's accounting methodology for the allowance for loan losses in the first six months of 2016.

Note 4. Low-Income Housing Tax Credits

The Company was invested in 4 separate housing equity funds at both June 30, 2016 and December 31, 2015. The general purpose of these funds is to encourage and assist participants in investing in low-income residential rental properties located in the Commonwealth of Virginia; develop and implement strategies to maintain projects as low-income housing; deliver Federal Low Income Housing Credits to investors; allocate tax losses and other possible tax benefits to investors; and preserve and protect project assets.

The investments in these funds were recorded as other assets on the consolidated balance sheets and were $4.0 million and $4.2 million at June 30, 2016 and December 31, 2015, respectively. The expected terms of these investments and the related tax benefits run through 2032. Total projected tax credits to be received for 2016 are $399 thousand, which is based on the most recent quarterly estimates received from the funds. Additional capital calls expected for the funds totaled $3.0 million at both June 30, 2016 and December 31, 2015, and are recorded in accrued expenses and other liabilities on the corresponding consolidated balance sheet.

The table below summarizes the tax credits and other tax benefits recognized by the Company and related to these investments, as of the periods indicated:

Three Months Ended June 30,		Six Months Ended June 30,	
2016	2015	2016	2015
$96	$102	$222	$221

Note 5. Share-Based Compensation

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

Historically, the Company has only granted share-based compensation in the form of stock options. There were no options granted in the first six months of 2016.

The Company's 1998 Stock Option Plan, pursuant to which stock options could be granted to key employees and non-employee directors, expired on March 9, 2008. Stock options that were outstanding on March 9, 2008 remained outstanding in accordance with their terms, but no new awards could be granted under the plan after March 9, 2008. Options to purchase 68,730 shares of common stock were outstanding under the Company's 1998 Stock Option Plan at June 30, 2016. The exercise price of each option equals the market price of the Company's common stock on the date of the grant and each option's maximum term is ten years.

Stock option activity for the six months ended June 30, 2016 is summarized below:

	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life	Aggregate Intrinsic Value (in thousands)

			(in years)	
Options outstanding, January 1, 2016	74,960	$ 20.05		
Granted	0	0		
Exercised	0	0		
Canceled or expired	(6,230)	20.05		
Options outstanding, June 30, 2016	68,730	$ 20.05	1.29	$ 0
Options exercisable, June 30, 2016	68,730	$ 20.05	1.29	$ 0

The aggregate intrinsic value of a stock option in the table above represents the total pre-tax intrinsic value (the amount by which the current fair value of the underlying stock exceeds the exercise price of the option) that would have been received by the option holders had all option holders exercised their options on June 30, 2016. This amount changes based on changes in the fair value of the Company's common stock. As of June 30, 2016, the outstanding options had no intrinsic value because the exercise prices of all outstanding options were above the fair value of a share of the Company's common stock.

No options were exercised during the six months ended June 30, 2016.

As of June 30, 2016, all outstanding stock options were fully vested and there was no unrecognized stock-based compensation expense.

At the Company's 2016 Annual Meeting of Stockholders held on May 24, 2016, stockholders approved the Old Point Financial Corporation 2016 Incentive Stock Plan (Incentive Stock Plan). The Incentive Stock Plan provides for the grant to key employees and non-employee directors of awards that may include one or more of the following: stock options, restricted stock, restricted stock units, stock appreciation rights, stock awards, and performance units (collectively, the awards). No awards may be granted under the Incentive Stock Plan after May 23, 2026. Complete details of the Incentive Stock Plan are contained in Appendix A of the Proxy Statement for the Company's 2016 Annual Meeting of Stockholders. As of June 30, 2016, there were no awards outstanding under the plan.

Also at the Company's 2016 Annual Meeting of Stockholders held on May 24, 2016, stockholders approved an Employee Stock Purchase Plan (ESPP). The ESPP provides a means for employees of the Company and employees of the Company's subsidiaries to authorize payroll deductions on a voluntary basis to be used for the periodic purchase of shares of the Company's common stock. Under the ESPP, eligible employees will be able to purchase shares of the Company's common stock at a price equal to at least 85% of the fair market value of the common stock at the end of the applicable offering period. The maximum number of shares that may be purchased under the ESPP is 250,000 shares. Complete details of the ESPP are contained in Appendix B of the Proxy Statement for the Company's 2016 Annual Meeting of Stockholders. The first offering period will begin on September 1, 2016; accordingly, as of June 30, 2016, no shares have been issued under the plan.

Note 6. Pension Plan

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

Three months ended June 30,	2016	2015
	(in thousands)	
Interest cost	$70	$65
Expected return on plan assets	(98)	(90)
Amortization of net loss	140	98
Net periodic pension plan cost	$112	$73

Six months ended June 30,	2016	2015
	(in thousands)	
Interest cost	$140	$131
Expected return on plan assets	(196)	(179)
Amortization of net loss	280	197
Net periodic pension plan cost	$224	$149

At June 30, 2016, management had not yet determined the amount, if any, that the Company will contribute to the plan in the year ending December 31, 2016.

Note 7. Stockholders' Equity and Earnings per Share

STOCKHOLDERS' EQUITY – ACCUMULATED OTHER COMPREHENSIVE LOSS

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

	Three Months Ended June 30, 2016	Three Months Ended June 30, 2015	Six Months Ended June 30, 2016	Six Months Ended June 30, 2015	Affected Line Item on Consolidated Statements of Income
	(in thousands)				
Available-for-sale securities					
Realized gains (losses) on sales of securities	$$6	$$0	$$515	$$0	Gain on sale of available-for-sale securities, net
Tax effect	2	0	175	0	Income tax expense
	$$4	$$0	$$340	$$0	

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

	Unrealized Gains (Losses) on Securities	Unrealized Losses on Securities Transferred to Held-to-Maturity	Defined Benefit Pension Plans	Accumulated Other Comprehensive Loss
	(in thousands)			
Six Months Ended June 30, 2016				
Balance at beginning of period	$(576)	$ 0	$(2,586)	$ (3,162)
Net change for the period	2,176	0	0	2,176
Balance at end of period	$1,600	$ 0	$(2,586)	$ (986)
Six Months Ended June 30, 2015				
Balance at beginning of period	$(78)	$ (3,386)	$(2,429)	$ (5,893)
Net change for the period	(911)	311	0	(600)
Balance at end of period	$(989)	$ (3,075)	$(2,429)	$ (6,493)

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

	Six Months Ended June 30, 2016		
	Pretax	Tax	Net-of-Tax
	(in thousands)		
Unrealized gains on available-for-sale securities:			
Unrealized holding gains arising during the period	$3,812	$1,296	$ 2,516
Reclassification adjustment for gains recognized in income	(515)	(175)	(340)
Net unrealized gains on securities	3,297	1,121	2,176
Total change in accumulated other comprehensive loss	$3,297	$1,121	$ 2,176

	Six Months Ended June 30, 2015		
	Pretax	Tax	Net-of-Tax
	(in thousands)		
Unrealized losses on available-for-sale securities:			
Unrealized holding losses arising during the period	$(1,381)	$(470)	$ (911)
Unrealized losses on securities transferred from available-for-sale to held-to-maturity:			
Amortization	471	160	311
Net change	$(910)	$(310)	$ (600)

EARNINGS PER COMMON SHARE

Basic earnings per share is computed by dividing net income by the weighted average number of common shares outstanding during the period. Diluted earnings per share is computed using the weighted average number of common shares outstanding during the period, including the effect of dilutive potential common shares attributable to outstanding stock options. The Company did not include an average of 69 thousand and 77 thousand potential common shares attributable to outstanding stock options in the diluted earnings per share calculation for the first six months of 2016 and 2015, respectively, because they were antidilutive. Antidilutive shares were 69 thousand and 76 thousand for the second quarters of 2016 and 2015, respectively.

Note 8. Recent Accounting Pronouncements

In August 2014, the FASB issued ASU No. 2014-15, "Presentation of Financial Statements – Going Concern (Subtopic 205-40): Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern". This update is intended to provide guidance about management's responsibility to evaluate whether there is substantial doubt about an entity's ability to continue as a going concern and to provide related footnote disclosures. Management is required under the new guidance to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about the entity's ability to continue as a going concern within one year after the date the financial statements are issued when preparing financial statements for each interim and annual reporting period. If conditions or events are identified, the ASU specifies the process that must be followed by management and also clarifies the timing and content of going concern footnote disclosures in order to reduce diversity in practice. The amendments in this ASU are effective for annual periods and interim periods within those annual periods beginning after December

15, 2016. Early adoption is permitted. The Company does not expect the adoption of ASU 2014-15 to have a material impact on its consolidated financial statements.

In January 2016, the FASB issued ASU 2016-01, "Financial Instruments – Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities". The amendments in ASU 2016-01, among other things: 1) Requires equity investments (except those accounted for under the equity method of accounting, or those that result in consolidation of the investee) to be measured at fair value with changes in fair value recognized in net income. 2) Requires public business entities to use the exit price notion when measuring the fair value of financial instruments for disclosure purposes. 3) Requires separate presentation of financial assets and financial liabilities by measurement category and form of financial asset (i.e., securities or loans and receivables). 4) Eliminates the requirement for public business entities to disclose the method(s) and significant assumptions used to estimate the fair value that is required to be disclosed for financial instruments measured at amortized cost. The amendments in this ASU are effective for public companies for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. The Company is currently assessing the impact that ASU 2016-01 will have on its consolidated financial statements.

In February 2016, the FASB issued ASU No. 2016-02, "Leases (Topic 842)". Among other things, in the amendments in ASU 2016-02, lessees will be required to recognize the following for all leases (with the exception of short-term leases) at the commencement date: (1) A lease liability, which is a lessee's obligation to make lease payments arising from a lease, measured on a discounted basis; and (2) A right-of-use asset, which is an asset that represents the lessee's right to use, or control the use of, a specified asset for the lease term. Under the new guidance, lessor accounting is largely unchanged. Certain targeted improvements were made to align, where necessary, lessor accounting with the lessee accounting model and Topic 606, Revenue from Contracts with Customers. The amendments in this ASU are effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. Early application is permitted upon issuance. Lessees (for capital and operating leases) and lessors (for sales-type, direct financing, and operating leases) must apply a modified retrospective transition approach for leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements. The modified retrospective approach would not require any transition accounting for leases that expired before the earliest comparative period presented. Lessees and lessors may not apply a full retrospective transition approach. The Company is currently assessing the impact that ASU 2016-02 will have on its consolidated financial statements.

During March 2016, the FASB issued ASU No. 2016-05, "Derivatives and Hedging (Topic 815): Effect of Derivative Contract Novations on Existing Hedge Accounting Relationships". The amendments in this ASU clarify that a change in the counterparty to a derivative instrument that has been designated as the hedging instrument does not, in and of itself, require dedesignation of that hedging relationship provided that all other hedge accounting criteria remain intact. The amendments are effective for public business entities for financial statements issued for fiscal years beginning after December 15, 2016, and interim periods within those fiscal years. Early adoption is permitted, including adoption in an interim period. The Company does not expect the adoption of ASU 2016-05 to have a material impact on its consolidated financial statements.

In March 2016, the FASB issued ASU No. 2016-07, "Investments – Equity Method and Joint Ventures (Topic 323): Simplifying the Transition to the Equity Method of Accounting". The amendments in this ASU eliminate the requirement that when an investment qualifies for use of the equity method as a result of an increase in the level of ownership interest or degree of influence, an investor must adjust the investment, results of operations, and retained earnings retroactively on a step-by-step basis as if the equity method had been in effect during all previous periods that the investment had been held. The amendments require that the equity method investor add the cost of acquiring the additional interest in the investee to the current basis of the investor's previously held interest and adopt the equity method of accounting as of the date the investment becomes qualified for equity method accounting. Therefore, upon qualifying for the equity method of accounting, no retroactive adjustment of the investment is required. In addition, the amendments in this ASU require that an entity that has an available-for-sale equity security that becomes qualified for the equity method of accounting recognize through earnings the unrealized holding gain or loss in accumulated other comprehensive income at the date the investment becomes qualified for use of the equity method. The amendments are effective for all entities for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2016. The amendments should be applied prospectively upon their effective date to increases in the level of ownership interest or degree of influence that result in the adoption of the equity method. Early Adoption is permitted. The Company does not expect the adoption of ASU 2016-07 to have a material impact on its consolidated financial statements.

During March 2016, the FASB issued ASU No. 2016-09, "Compensation – Stock Compensation (Topic 718): Improvements to Employee Shares-Based Payment Accounting". The amendments in this ASU simplify several aspects of the accounting for share-based payment award transactions including: (a) income tax consequences; (b) classification of awards as either equity or liabilities; and (c) classification on the statement of cash flows. The amendments are effective for public companies for annual periods beginning after December 15, 2016, and interim periods within those annual periods. The Company is currently assessing the impact that ASU 2016-09 will have on its consolidated financial statements.

During June 2016, the FASB issued ASU No. 2016-13, "Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments". The amendments in this ASU, among other things, require the measurement of all expected credit losses for financial assets held at the reporting date based on historical experience, current conditions, and reasonable and supportable forecasts. Financial institutions and other organizations will now use forward-looking information to better inform their credit loss estimates. Many of the loss estimation techniques applied today will still be permitted, although the inputs to those techniques will change to reflect the full amount of expected credit losses. In addition, the ASU amends the accounting for credit losses on available-for-sale debt securities and purchased financial assets with credit deterioration. The amendments in this ASU are effective for Securities and Exchange Commission (SEC) filers for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2019. For public companies that are not SEC filers, the amendments in this ASU are effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2020. The Company is currently assessing the impact that ASU 2016-13 will have on its consolidated financial statements.

Note 9. Fair Value Measurements

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

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

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

In accordance with ASC 820, "Fair Value Measurements and Disclosures," the Company groups its financial assets and financial liabilities generally measured at fair value into three levels, based on the markets in which the assets and liabilities are traded and the reliability of the assumptions used to determine fair value.

Level 1 –	Valuation is based on quoted prices in active markets for identical assets or liabilities that the reporting entity has the ability to access at the measurement date. Level 1 assets and liabilities generally include debt and equity securities that are traded in an active exchange market. Valuations are obtained from readily available pricing sources for market transactions involving identical assets or liabilities.
Level 2 –	Valuation is based on inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. The valuation may be based on quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the asset or liability.
Level 3 –	Valuation is based on unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. Level 3 assets and liabilities include financial instruments whose value is determined using pricing models, discounted cash flow methodologies, or similar techniques, as well as instruments for which determination of fair value requires significant management judgment or estimation.

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

ASSETS MEASURED AT FAIR VALUE ON A RECURRING BASIS

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

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

		Fair Value Measurements at June 30, 2016 Using		
	Balance	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
	(in thousands)			
Available-for-sale securities				
Obligations of U.S. Government agencies	$24,275	$0	$24,275	$ 0
Obligations of state and political subdivisions	72,734	0	72,734	0
Mortgage-backed securities	64,857	0	64,857	0
Money market investments	621	0	621	0
Corporate bonds	3,624	0	3,624	0
Other marketable equity securities	105	0	105	0
Total available-for-sale securities	$166,216	$0	$166,216	$ 0

		Fair Value Measurements at December 31, 2015 Using		
	Balance	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
	(in thousands)			
Available-for-sale securities				
Obligations of U.S. Government agencies	$24,240	$0	$24,240	$ 0
Obligations of state and political subdivisions	78,433	0	78,433	0
Mortgage-backed securities	107,396	0	107,396	0
Money market investments	631	0	631	0
Corporate bonds	3,393	0	3,393	0
Other marketable equity securities	99	0	99	0
Total available-for-sale securities	$214,192	$0	$214,192	$ 0

ASSETS MEASURED AT FAIR VALUE ON A NONRECURRING BASIS

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

Impaired loans

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

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

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

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

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

		Carrying Value at June 30, 2016 Using		
	Fair Value	Quoted Prices in Active Markets	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)

	for Identical Assets (Level 1)			
	(in thousands)			
Impaired loans				
Mortgage loans on real estate:				
Residential 1-4 family	$353	$0	$ 0	$ 353
Commercial	278	0	0	278
Construction	63	0	0	63
Total mortgage loans on real estate	694	0	0	694
Commercial loans	687	0	0	687
Total	$1,381	$0	$ 0	$ 1,381
Other real estate owned				
Residential 1-4 family	$299	$0	$ 0	$ 299
Commercial	371	0	0	371
Construction	1,090	0	0	1,090
Total	$1,760	$0	$ 0	$ 1,760

	Carrying Value at December 31, 2015 Using			
	Fair Value (in thousands)	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Impaired loans				
Mortgage loans on real estate:				
Residential 1-4 family	$952	$ 0	$ 0	$ 952
Commercial	267	0	0	267
Construction	62	0	0	62
Total	$1,281	$ 0	$ 0	$ 1,281
Other real estate owned				
Residential 1-4 family	$724	$ 0	$ 0	$ 724
Commercial	927	0	0	927
Construction	1,090	0	0	1,090
Total	$2,741	$ 0	$ 0	$ 2,741

The following table displays quantitative information about Level 3 Fair Value Measurements as of the dates indicated:

	Quantitative Information About Level 3 Fair Value Measurements			
	Fair Value at June 30, 2016 (dollars in thousands)	Valuation Techniques	Unobservable Input	Range (Weighted Average)
Impaired loans				
Residential 1-4 family real estate	$ 353	Market comparables	Selling costs	0.00% - 7.25% (4.92 %)
			Liquidation discount	4.00% - 42.20% (16.30 %)
Commercial real estate	$ 278	Market comparables	Selling costs	7.25 %
			Liquidation discount	4.00 %
Construction	$ 63	Market comparables	Selling costs	7.25 %
			Liquidation discount	4.00 %
Commercial not secured by real estate	687	Market comparables	Liquidation discount	32.71 %
Other real estate owned				
Residential 1-4 family	$ 299	Market comparables	Selling costs	7.25 %

			Liquidation discount	4.00	%
Commercial	$	371	Market comparables	Selling costs	7.25	%
			Liquidation discount	0.00	%
Construction	$	1,090	Market comparables	Selling costs	6.72	%
			Liquidation discount	33.05	%

	Quantitative Information About Level 3 Fair Value Measurements			
	Fair Value at December 31, 2015 (dollars in thousands)	Valuation Techniques	Unobservable Input	Range (Weighted Average)
Impaired loans				
Residential 1-4 family real estate	$ 952	Market comparables	Selling costs	7.25 %
			Liquidation discount	0.00% - 4.00% (3.75 %)
Commercial real estate	$ 267	Market comparables	Selling costs	7.25 %
			Liquidation discount	4.00 %
Construction	$ 62	Market comparables	Selling costs	7.25 %
			Liquidation discount	4.00 %
Other real estate owned				
Residential 1-4 family	$ 724	Market comparables	Selling costs	7.25 %
			Liquidation discount	4.00% - 7.17% (4.79 %)
Commercial	$ 927	Market comparables	Selling costs	7.25 %
			Liquidation discount	4.00% - 24.70% (11.77 %)
Construction	$ 1,090	Market comparables	Selling costs	6.72 %
			Liquidation discount	33.05 %

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

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

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

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

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

Level 3 in the fair value hierarchy. Fair values for non-performing loans are estimated as described above.

BANK-OWNED LIFE INSURANCE

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

DEPOSIT LIABILITIES

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

SHORT-TERM BORROWINGS

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

LONG-TERM BORROWINGS

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

ACCRUED INTEREST

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

COMMITMENTS TO EXTEND CREDIT AND IRREVOCABLE LETTERS OF CREDIT

The fair value of commitments is estimated using the fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the present credit-worthiness of the counterparties. For fixed-rate loan commitments, fair value also considers the difference between current levels of interest rates and the committed rates. The fair value of letters of credit is based on fees currently charged for similar agreements or on the estimated cost to terminate them or otherwise settle the obligations with the counterparties at the reporting date. At June 30, 2016 and December 31, 2015, the fair value of fees charged for loan commitments and irrevocable letters of credit was immaterial.

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

		Fair Value Measurements at June 30, 2016 Using		
	Carrying Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
	(in thousands)			
Assets				
Cash and cash equivalents	$32,216	$32,216	$ 0	$ 0
Securities available-for-sale	166,216	0	166,216	0
Restricted securities	2,882	0	2,882	0
Loans, net of allowances for loan losses	590,227	0	0	594,046
Bank-owned life insurance	24,843	0	24,843	0
Accrued interest receivable	3,090	0	3,090	0
Liabilities				
Deposits	$727,001	$0	$ 727,603	$ 0
Overnight repurchase agreements	23,865	0	23,865	0
Federal Home Loan Bank advances	45,000	0	45,003	0
Accrued interest payable	220	0	220	0

		Fair Value Measurements at December 31, 2015 Using		
	Carrying Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
	(in thousands)			
Assets				
Cash and cash equivalents	$36,990	$36,990	$ 0	$ 0
Securities available-for-sale	214,192	0	214,192	0
Restricted securities	2,016	0	2,016	0
Loans, net of allowances for loan losses	560,737	0	0	559,488
Bank-owned life insurance	24,411	0	24,411	0
Accrued interest receivable	3,059	0	3,059	0

Liabilities				
Deposits	$746,471	$0	$746,740	$ 0
Overnight repurchase agreements	25,950	0	25,950	0
Federal Home Loan Bank advances	25,000	0	25,501	0
Accrued interest payable	241	0	241	0

Note 10. Segment Reporting

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

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

Information about reportable segments, and reconciliation of such information to the consolidated financial statements as of and for the three and six months ended June 30, 2016 and 2015 follows:

	Three Months Ended June 30, 2016				
	Bank	Trust	Parent	Eliminations	Consolidated
	(in thousands)				
Revenues					
Interest and dividend income	$7,420	$15	$725	$ (725)	$ 7,435
Income from fiduciary activities	0	877	0	0	877
Other income	2,174	250	50	(65)	2,409
Total operating income	9,594	1,142	775	(790)	10,721
Expenses					
Interest expense	582	0	0	0	582
Provision for loan losses	1,250	0	0	0	1,250
Salaries and employee benefits	4,124	679	87	0	4,890
Other expenses	3,183	251	226	(65)	3,595
Total operating expenses	9,139	930	313	(65)	10,317
Income before taxes	455	212	462	(725)	404
Income tax expense (benefit)	(131)	72	(89)	0	(148)
Net income	$586	$140	$551	$ (725)	$ 552
Capital expenditures	$105	$0	$0	$ 0	$ 105
Total assets	$891,786	$5,814	$95,933	$ (95,860)	$ 897,673

	Three Months Ended June 30, 2015				
	Bank	Trust	Parent	Eliminations	Consolidated
	(in thousands)				
Revenues					
Interest and dividend income	$7,537	$13	$1,375	$ (1,375)	$ 7,550
Income from fiduciary activities	0	914	0	0	914
Other income	2,211	250	50	(66)	2,445
Total operating income	9,748	1,177	1,425	(1,441)	10,909
Expenses					
Interest expense	918	0	0	0	918
Provision for loan losses	25	0	0	0	25
Salaries and employee benefits	4,275	671	111	0	5,057
Other expenses	3,163	256	84	(66)	3,437
Total operating expenses	8,381	927	195	(66)	9,437
Income before taxes	1,367	250	1,230	(1,375)	1,472

Income tax expense (benefit)	157	85	(49)	0	193
Net income	$1,210	$165	$1,279	$ (1,375)	$ 1,279
Capital expenditures	$73	$2	$0	$ 0	$ 75
Total assets	$888,344	$5,815	$89,599	$ (90,256)	$ 893,502

	Six Months Ended June 30, 2016				
	Bank	Trust	Parent	Eliminations	Consolidated
	(in thousands)				
Revenues					
Interest and dividend income	$14,771	$29	$1,871	$ (1,871)	$ 14,800
Income from fiduciary activities	0	1,778	0	0	1,778
Other income	4,677	526	100	(130)	5,173
Total operating income	19,448	2,333	1,971	(2,001)	21,751
Expenses					
Interest expense	1,301	0	0	0	1,301
Provision for loan losses	1,400	0	0	0	1,400
Salaries and employee benefits	8,486	1,357	201	0	10,044
Other expenses	6,798	512	352	(130)	7,532
Total operating expenses	17,985	1,869	553	(130)	20,277
Income before taxes	1,463	464	1,418	(1,871)	1,474
Income tax expense (benefit)	(103)	158	(154)	0	(99)
Net income	$1,566	$306	$1,572	$ (1,871)	$ 1,573
Capital expenditures	$472	$4	$0	$ 0	$ 476
Total assets	$891,786	$5,814	$95,933	$ (95,860)	$ 897,673

	Six Months Ended June 30, 2015				
	Bank	Trust	Parent	Eliminations	Consolidated
	(in thousands)				
Revenues					
Interest and dividend income	$15,028	$26	$2,643	$ (2,643)	$ 15,054
Income from fiduciary activities	0	1,894	0	0	1,894
Other income	4,262	511	100	(131)	4,742
Total operating income	19,290	2,431	2,743	(2,774)	21,690
Expenses					
Interest expense	1,811	0	0	0	1,811
Provision for loan losses	300	0	0	0	300
Salaries and employee benefits	8,583	1,298	225	0	10,106
Other expenses	6,198	492	116	(131)	6,675
Total operating expenses	16,892	1,790	341	(131)	18,892
Income before taxes	2,398	641	2,402	(2,643)	2,798
Income tax expense (benefit)	178	218	(82)	0	314
Net income	$2,220	$423	$2,484	$ (2,643)	$ 2,484
Capital expenditures	$1,028	$20	$0	$ 0	$ 1,048

Total assets	$888,344	$5,815	$89,599	$ (90,256)	$ 893,502

The accounting policies of the segments are the same as those described in the summary of significant accounting policies reported in the Company's 2015 annual report on Form 10-K. The Company evaluates performance based on profit or loss from operations before income taxes, not including nonrecurring gains or losses.

Both the Parent and the Trust companies maintain deposit accounts with the Bank, on terms substantially similar to those available to other customers. These transactions are eliminated to reach consolidated totals.

Note 11. Commitments and Contingencies

There have been no material changes in the Company's commitments and contingencies from those disclosed in the Company's 2015 annual report on Form 10-K.

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

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

The following discussion is intended to assist readers in understanding and evaluating the financial condition, changes in financial condition and the results of operations of the Company. The Company consists of the parent company and its wholly-owned subsidiaries, The Old Point National Bank of Phoebus (the Bank) and Old Point Trust & Financial Services, N. A. (Trust), collectively referred to as the Company. This discussion should be read in conjunction with the consolidated financial statements and other financial information contained elsewhere in this report.

Caution About Forward-Looking Statements
In addition to historical information, this report may contain forward-looking statements. For this purpose, any statement that is not a statement of historical fact may be deemed to be a forward-looking statement. These forward-looking statements may include, but are not limited to, statements regarding profitability and future financial performance; the net interest margin; strategies for managing the net interest margin and the expected impact of such efforts; levels and sources of liquidity; the loan portfolio and expected trends in the quality of the loan portfolio; the allowance and provision for loan losses; the effect of a sustained increase in nonperforming assets; the securities portfolio; use of proceeds from the sale of securities; the effect of increases in past due loans in the Company's purchased student loan portfolio; interest rate sensitivity; asset quality; levels of net loan charge-offs or recoveries and nonperforming assets; levels of interest expense; levels and components of noninterest income and noninterest expense; income taxes; low-income housing tax credits and additional capital calls related to the Company's investment in housing equity funds; expected impact of efforts to restructure the balance sheet; expected yields on the loan and securities portfolios; expected monetary policy actions by the Federal Open Market Committee; expected rates on interest-bearing liabilities; expected interest savings resulting from the prepayment of the Company's FHLB advance; market risk; business and growth strategies; investment strategy; and financial and other goals. Forward-looking statements often use words such as "believes," "expects," "plans," "may," "will," "should," "projects," "contemplates," "anticipates," "forecasts," "intends" or other words of similar meaning. These statements can also be identified by the fact that they do not relate strictly to historical or current facts. Forward-looking statements are subject to numerous assumptions, risks and uncertainties, and actual results could differ materially from historical results or those anticipated by such statements.

There are many factors that could have a material adverse effect on the operations and future prospects of the Company including, but not limited to, changes in interest rates and yields; general economic and general business conditions, including unemployment levels; uncertainty over future federal spending or the effects of federal budget cuts, particularly to the Department of Defense, on the Company's service area; changes associated with the new leadership of the Bank; effects of the transfer of the securities portfolio from held-to-maturity securities to available-for-sale securities; the quality or composition of the loan or securities portfolios; changes in the volume and mix of interest-earning assets and interest-bearing liabilities; the effects of management's investment strategy and strategy to manage the net interest margin; the adequacy of the Company's credit quality review processes; the level of nonperforming assets and related charge-offs and recoveries; turnover times experienced by the mortgage companies to which the Company has extended warehouse lines of credit; the federal government's guarantee of repayment of student loans purchased by the Company; the ability of the Company to diversify its sources of noninterest income; the effect of the Company's sales training efforts for branch staff; the local real estate market; volatility and disruption in national and international financial markets; government intervention in the U.S. financial system; application of the Basel III capital standards to the Company and its subsidiaries; FDIC premiums and/or assessments; demand for loan and other banking products and financial services in the Company's primary service area; levels of noninterest income and expense; deposit flows; competition; the use of inaccurate assumptions in management's modeling systems; technology; any interruption or breach of security in the Company's information systems or those of the Company's third party vendors or other service providers; reliance on third parties for key services; adequacy of the allowance for loan losses; and changes in accounting principles, policies and guidelines. The Company could also be adversely affected by monetary and fiscal policies of the U.S. Government, as well as any regulations or programs implemented pursuant to the Dodd-Frank Act or other legislation and policies of the Office of the Comptroller of the Currency, U.S. Treasury and the Federal Reserve Board.

These risks and uncertainties, in addition to the risks and uncertainties identified in the Company's 2015 annual report on Form 10-K, should be considered in evaluating the forward-looking statements contained herein, and readers are cautioned not to place undue reliance on such statements. Any forward-looking statement speaks only as of the date on which it is made, and the Company undertakes no obligation to update any forward-looking statement to reflect events or circumstances after the date on which it is made. In addition, past results of operations are not necessarily indicative of future results.

General
The Company is the parent company of the Bank and Trust. The Bank is a locally managed community bank serving the Hampton Roads localities of Chesapeake, Hampton, Isle of Wight County, Newport News, Norfolk, Virginia Beach, Williamsburg/James City County and York County. The Bank currently has 18 branch offices. Trust is a wealth management services provider.

Critical Accounting Policies and Estimates
As of June 30, 2016, there have been no significant changes with regard to the critical accounting policies and estimates disclosed in the Company's 2015 annual report on Form 10-K. The accounting policy that required management's most difficult, subjective or complex judgments is the Company's allowance for loan losses. The Company's policies for calculating the allowance for loan losses are discussed in this Item 2 and in Note 3 of the Notes to the Consolidated Financial Statements included in this quarterly report on Form 10-Q, and are discussed in further detail in the Company's 2015 annual report on Form 10-K.

Earnings Summary
Beginning in the fourth quarter of 2015, the Company re-evaluated its strategy to ensure it was positioned for possible future interest rate changes. This strategy was implemented in the first quarter of 2016 and included restructuring the investment portfolio through the sale and purchase of certain investments. While implementing its strategy, the Company took advantage of the opportunity to recognize gains which would offset losses on other real estate owned incurred in the sale of the properties, as well as a fee paid to unwind one of the Company's FHLB advances (discussed in greater detail below).

Net income for the first six months of 2016 was $1.6 million, or $0.32 per diluted share, compared to net income of $2.5 million, or $0.50 per diluted share, for the first six months of 2015. This 36.67% decrease is primarily attributable to reduced interest income, primarily on the securities portfolio; a higher provision for loan losses due to a charge-off on a single borrowing relationship; and higher noninterest expense, in particular legal and audit expenses and the prepayment fee on the Company's FHLB advance. These factors were partially offset by net gains on the sales of investment securities.

In the second quarter of 2016, net income decreased $727 thousand, or 56.84% when compared to the second quarter of 2015. As in the six month period ended June 30, 2016, the decrease in quarterly net income was mainly due to an increased provision for loan losses, slightly offset by higher net interest income. In the second quarter of 2016, noninterest income and noninterest expense were both lower than in the comparable period in 2015.

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

The Company experienced moderate loan growth, with average total loans increasing $20.8 million when comparing the first half of 2016 and 2015. While loan yields declined when comparing the same periods, the increase in average balances increased interest income on loans by $131 thousand when comparing the six months ended June 30, 2016 to the same period in 2015. This growth in loans was funded through sales from the securities portfolio and excess liquidity held in cash and due from banks and interest-bearing due from banks. As seen in the table below, loans bear higher yields than securities and significantly higher yields than funds due from banks. Shifting funds from investments to loans increased the Company's return on average earning assets to 4.02% for the first six months of 2016, compared to 4.01% for the first six months of 2015, despite overall declines in market rates.

Excess liquidity and the sales of securities also funded the early payoff of one of the Company's advance from the FHLB, an advance which would have matured in June of 2016. The rate on this advance was significantly higher than other available funding sources in the current rate environment and would have cost the Company $597 thousand in interest expense during 2016. By paying off the advance in February of 2016, the Company paid only $141 thousand, thus saving $456 thousand in interest expense for 2016. As a result of this reduction in interest expense, the Company's weighted-average cost of total interest-bearing liabilities decreased from 0.60% in the first half of 2015 to 0.47% in the first half of 2016 and its net interest margin improved from 3.55% to 3.67% over the same periods.

Although the Company took out additional borrowings in June of 2016, these borrowings would have been necessary even had the Company not prepaid the $25.0 million advance in February, as the additional funding was needed at the end of the quarter, after the maturity date of the advance. In addition, the advances taken out in June of 2016 cost the Company only $3 thousand for that month, less than the amount saved by prepaying the advance.

Net interest income, on a fully tax-equivalent basis, was $14.0 million for the six months ended June 30, 2016, compared to $13.7 million for the six months ended June 30, 2015, an increase of $213 thousand or 1.55%. Tax-equivalent interest income decreased $297 thousand between these two periods due to a decrease in average earning assets, partially offset by a slight increase in the average yield. Interest income on the securities portfolio decreased $401 thousand, or 15.60%, for the first six months of 2016 compared to the first six months of 2015, primarily as a result of the sale of investment securities during the first six months of 2016. Interest expense decreased $510 thousand, or 28.16%, when comparing those six month periods as average interest-bearing liabilities and the rate paid on these accounts both declined, due to the payoff of the FHLB advance discussed above.

For the second quarter of 2016, tax-equivalent net interest income was $7.1 million, an increase of $199 thousand, or 2.89%, from the second quarter of 2015, due to a decrease in interest expense of $336 thousand. Both the average balances on interest-bearing liabilities and the average rate paid on these liabilities decreased when comparing the second quarters of 2016 and 2015. The rates on average interest-bearing liabilities decreased primarily due to the payoff of the FHLB advance. As in the six months ended June 30, 2016, average earning assets decreased when comparing the second quarter of 2016 to the same period in 2015. The yield on earning assets increased between the three months ended June 30, 2016 and 2015 despite decreases in yields on both loans and investment securities, as the yield on other investments increased.

Management expects that the Company's loan yields will continue to decline, due to intense competition for quality loans and rate reductions on loans currently held in the portfolio. Management expects that the reduction in loan yields will likely continue in 2016 at approximately the same pace seen in 2015, depending on monetary policy actions taken by the Federal Open Market Committee (FOMC). Although the FOMC did raise the target range for the federal funds rate in December of 2015, predictions for future rate increases are varied. Barring additional rate increases by the FOMC in 2016, management expects continued declines in loan yields. To partially offset this anticipated decline, management has placed an increased focus on managing the mix of the liabilities in order to increase low cost funds and reduce high cost funds when possible. If the FOMC does increase the target rate in 2016, management expects that the decline in loan yields will slow or stop. Based on management's evaluation of current predictions of the FOMC's likely actions with regards to the target range, management does not expect loan yields to increase in 2016.

The following table shows an analysis of average earning assets, interest-bearing liabilities and rates and yields for the periods indicated. Nonaccrual loans are included in loans outstanding.

AVERAGE BALANCE SHEETS, NET INTEREST INCOME* AND RATES*

	For the quarter ended June 30,					
	2016			2015		
	Average Balance	Interest Income/ Expense	Yield/ Rate**	Average Balance	Interest Income/ Expense	Yield/ Rate**
	(dollars in thousands)					
ASSETS						
Loans*	$581,281	$6,593	4.54 %	$568,137	$6,519	4.59 %
Investment securities:						
Taxable	109,300	471	1.72 %	132,853	615	1.85 %
Tax-exempt*	65,432	568	3.47 %	71,824	628	3.50 %
Total investment securities	174,732	1,039	2.38 %	204,677	1,243	2.43 %
Interest-bearing due from banks	1,097	1	0.36 %	6,089	3	0.20 %
Federal funds sold	1,415	1	0.28 %	1,745	1	0.23 %
Other investments	1,086	26	9.58 %	2,598	31	4.77 %
Total earning assets	759,611	$7,660	4.03 %	783,246	$7,797	3.98 %
Allowance for loan losses	(7,794)			(7,511)		
Other non-earning assets	107,155			114,296		
Total assets	$858,972			$890,031		
LIABILITIES AND STOCKHOLDERS' EQUITY						
Time and savings deposits:						
Interest-bearing transaction accounts	$14,150	$1	0.03 %	$11,257	$1	0.04 %
Money market deposit accounts	223,561	43	0.08 %	231,377	47	0.08 %
Savings accounts	77,903	10	0.05 %	74,711	9	0.05 %
Time deposits, $100,000 or more	109,224	281	1.03 %	115,829	293	1.01 %
Other time deposits	98,684	236	0.96 %	108,383	251	0.93 %
Total time and savings deposits	523,522	571	0.44 %	541,557	601	0.44 %
Federal funds purchased, repurchase agreements and other borrowings	26,582	8	0.12 %	33,931	8	0.09 %
Federal Home Loan Bank advances	2,747	3	0.44 %	29,725	309	4.16 %
Total interest-bearing liabilities	552,851	582	0.42 %	605,213	918	0.61 %
Demand deposits	204,623			190,515		
Other liabilities	6,603			4,251		
Stockholders' equity	94,895			90,052		
Total liabilities and stockholders' equity	$858,972			$890,031		
Net interest margin		$7,078	3.73 %		$6,879	3.51 %

*Computed on a fully tax-equivalent basis using a 34% rate
**Annualized