AMERICAN NATIONAL BANKSHARES INC.
Form 10-Q
May 12, 2014

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 10-Q

x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE QUARTERLY PERIOD ENDED March 31, 2014.

o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE TRANSITION PERIOD FROM _____ TO_____ .

Commission file number: 0-12820

AMERICAN NATIONAL BANKSHARES INC.
(Exact name of registrant as specified in its charter)

VIRGINIA	54-1284688
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
628 Main Street	
Danville, Virginia	24541
(Address of principal executive offices)	(Zip Code)

(434) 792-5111
(Registrant's telephone number, including area code)

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.

YesxNoo

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.

YesxNoo

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

Large accelerated filer o Accelerated filer x Non-accelerated filer o
Smaller reporting company -

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

YesoNox

At April 30, 2014, the Company had 7,905,243 shares of Common Stock outstanding, $1 par value.

AMERICAN NATIONAL BANKSHARES INC.

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Part I. Financial Information
Item 1. Financial Statements

American National Bankshares Inc. and Subsidiaries
Consolidated Balance Sheets
(Dollars in thousands, except share data)

	(Unaudited) March 31, 2014	(Audited) December 31, 2013
Assets		
Cash and due from banks	$ 25,880	$ 19,808
Interest-bearing deposits in other banks	45,466	47,873
Securities available for sale, at fair value	349,123	346,124
Restricted stock, at cost	4,529	4,889
Loans held for sale	1,389	2,760
Loans, net of unearned income	783,369	794,671
Less allowance for loan losses	(12,614)	(12,600)
Net loans	770,755	782,071
Premises and equipment, net	23,359	23,674
Other real estate owned, net	3,233	3,422
Goodwill	39,043	39,043
Core deposit intangibles, net	2,828	3,159
Bank owned life insurance	14,845	14,746
Accrued interest receivable and other assets	19,352	19,943
Total assets	$ 1,299,802	$ 1,307,512
Liabilities		
Liabilities:		
Demand deposits -- noninterest bearing	$ 218,795	$ 229,347
Demand deposits -- interest bearing	170,894	167,736
Money market deposits	194,528	185,270
Savings deposits	89,024	85,724
Time deposits	378,008	389,598
Total deposits	1,051,249	1,057,675
Customer repurchase agreements	34,153	39,478
Long-term borrowings	9,919	9,951
Trust preferred capital notes	27,444	27,419
Accrued interest payable and other liabilities	6,538	5,438
Total liabilities	1,129,303	1,139,961
Shareholders' equity		
Preferred stock, $5 par, 2,000,000 shares authorized, none outstanding	-	-
Common stock, $1 par, 20,000,000 shares authorized, 7,905,243 shares outstanding at March 31, 2014 and 7,890,697 shares outstanding at December 31, 2013	7,905	7,891
Capital in excess of par value	58,202	58,050
Retained earnings	100,721	99,090

Accumulated other comprehensive income, net	3,671	2,520
Total shareholders' equity	170,499	167,551
Total liabilities and shareholders' equity	$ 1,299,802	$ 1,307,512

The accompanying notes are an integral part of the consolidated financial statements.

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American National Bankshares Inc. and Subsidiaries
Consolidated Statements of Income
(Dollars in thousands, except share and per share data) (Unaudited)

	Three Months Ended March 31	
	2014	2013
Interest and Dividend Income:		
Interest and fees on loans	$9,847	$11,395
Interest and dividends on securities:		
Taxable	964	878
Tax-exempt	1,035	1,052
Dividends	75	55
Other interest income	33	29
Total interest and dividend income	11,954	13,409
Interest Expense:		
Interest on deposits	1,229	1,436
Interest on short-term borrowings	2	21
Interest on long-term borrowings	80	82
Interest on trust preferred capital notes	184	188
Total interest expense	1,495	1,727
Net Interest Income	10,459	11,682
Provision for Loan Losses	-	294
Net Interest Income After Provision for Loan Losses	10,459	11,388
Noninterest Income:		
Trust fees	1,122	588
Service charges on deposit accounts	413	409
Other fees and commissions	444	459
Mortgage banking income	263	718
Securities gains, net	39	198
Other	422	398
Total noninterest income	2,703	2,770
Noninterest Expense:		
Salaries	3,538	3,439
Employee benefits	975	899
Occupancy and equipment	936	916
FDIC assessment	164	161
Bank franchise tax	222	187
Core deposit intangible amortization	331	420
Data processing	348	277
Software	262	212
Foreclosed real estate, net	16	243

Other	1,631	1,564
Total noninterest expense	8,423	8,318
Income Before Income Taxes	4,739	5,840
Income Taxes	1,289	1,689
Net Income	$3,450	$4,151
Net Income Per Common Share:		
Basic	$0.44	$0.53
Diluted	$0.44	$0.53
Average Common Shares Outstanding:		
Basic	7,904,759	7,861,991
Diluted	7,917,601	7,871,508

The accompanying notes are an integral part of the consolidated financial statements.

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American National Bankshares Inc. and Subsidiaries
Consolidated Statements of Comprehensive Income
(Dollars in thousands) (Unaudited)

	Three Months Ended March 31	
	2014	2013
Net income	$3,450	$4,151
Other comprehensive income (loss):		
Unrealized gains (losses) on securities available for sale	1,809	(882)
Income tax (expense) benefit	(633)	309
Reclassification adjustment for gains on securities	(39)	(198)
Income tax expense	14	69
Other comprehensive income (loss)	1,151	(702)
Comprehensive income	$4,601	$3,449

The accompanying notes are an integral part of the consolidated financial statements.

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American National Bankshares Inc. and Subsidiaries
Consolidated Statements of Changes in Shareholders' Equity
Three Months Ended March 31, 2014 and 2013
(Dollars in thousands except per share data) (Unaudited)

	Common Stock	Capital in Excess of Par Value	Retained Earnings	Accumulated Other Comprehensive Income	Total Shareholders' Equity
Balance, December 31, 2012	$ 7,847	$ 57,211	$ 90,591	$ 7,597	$ 163,246
Net income	-	-	4,151	-	4,151
Other comprehensive loss	-	-	-	(702)	(702)
Equity based compensation	16	130	-	-	146
Cash dividends declared, $0.23 per share	-	-	(1,809)	-	(1,809)
Balance, March 31, 2013	$ 7,863	$ 57,341	$ 92,933	$ 6,895	$ 165,032
Balance, December 31, 2013	$ 7,891	$ 58,050	$ 99,090	$ 2,520	$ 167,551
Net income	-	-	3,450	-	3,450
Other comprehensive income	-	-	-	1,151	1,151
Equity based compensation	14	152	-	-	166
Cash dividends declared, $0.23 per share	-	-	(1,819)	-	(1,819)
Balance, March 31, 2014	$ 7,905	$ 58,202	$ 100,721	$ 3,671	$ 170,499

The accompanying notes are an integral part of the consolidated financial statements.

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American National Bankshares Inc. and Subsidiaries
Consolidated Statements of Cash Flows
Three Months Ended March 31, 2014 and 2013
(Dollars in thousands) (Unaudited)

	2014			2013		
Cash Flows from Operating Activities:						
Net income	$	3,450		$	4,151	
Adjustments to reconcile net income to net cash provided by operating activities:						
Provision for loan losses		-			294	
Depreciation		434			424	
Net accretion of purchase accounting adjustments		(896	)		(1,983	)
Core deposit intangible amortization		331			420	
Net amortization (accretion) of securities		668			788	
Net gain on sale or call of securities		(39	)		(198	)
Gain on sale of loans held for sale		(215	)		(650	)
Proceeds from sales of loans held for sale		13,745			33,782	
Originations of loans held for sale		(12,159	)		(23,675	)
Net gain on foreclosed real estate		(49	)		(14	)
Valuation allowance on foreclosed real estate		24			70	
Equity based compensation expense		166			146	
Deferred income tax expense (benefit)		94			(43	)
Net change in interest receivable		344			175	
		(565	)		(1,504	)

Net change in other assets				
Net change in interest payable	(43	)	(23	)
Net change in other liabilities	1,143		1,813	
Net cash provided by operating activities	6,433		13,973	
Cash Flows from Investing Activities:				
Proceeds from sales of securities available for sale	2,061		2,627	
Proceeds from maturities, calls and paydowns of securities available for sale	22,540		9,329	
Purchases of securities available for sale	(26,459	)	(19,555	)
Net change in restricted stock	360		411	
Net decrease (increase) in loans	12,225		(2,112	)
Purchases of premises and equipment	(119	)	(178	)
Proceeds from sales of foreclosed real estate	232		645	
Net cash provided by (used in) investing activities	10,840		(8,833	)
Cash Flows from Financing Activities:				
Net change in demand, money market, and savings deposits	5,164		4,199	
Net change in time deposits	(11,590	)	5,986	
Net change in customer repurchase agreements	(5,325	)	(3,276	)
Net change in long-term borrowings	(38	)	(37	)
Common stock dividends paid	(1,819	)	(1,809	)
	(13,608	)	5,063	

Net cash (used in) provided by financing activities				
Net Increase in Cash and Cash Equivalents		3,665		10,203
Cash and Cash Equivalents at Beginning of Period		67,681		47,442
Cash and Cash Equivalents at End of Period	$	71,346	$	57,645

The accompanying notes are an integral part of the consolidated financial statements.

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AMERICAN NATIONAL BANKSHARES INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 1 – Basis of Presentation

The consolidated financial statements include the accounts of American National Bankshares Inc. (the "Company") and its wholly owned subsidiary, American National Bank and Trust Company (the "Bank"). The Bank offers a wide variety of retail, commercial, secondary market mortgage lending, and trust and investment services which also include non-deposit products such as mutual funds and insurance policies.

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America ("GAAP") requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses, the valuation of foreclosed real estate, goodwill and intangible assets, the valuation of deferred tax assets, other-than-temporary impairments of securities, and acquired loans with specific credit-related deterioration.

All significant inter-company transactions and accounts are eliminated in consolidation, with the exception of the AMNB Trust and the MidCarolina Trusts, as detailed in Note 9.

In the opinion of management, the accompanying unaudited consolidated financial statements contain all adjustments (consisting of normal recurring accruals) necessary to present fairly the results of the interim periods. The results of operations for the interim periods are not necessarily indicative of the results that may occur for the year ending December 31, 2014. Certain reclassifications have been made to prior period balances to conform to the current period presentation. These statements should be read in conjunction with the Notes to Consolidated Financial Statements included in the Company's Annual Report on Form 10-K for the year ended December 31, 2013.

Note 2 – Recent Accounting Pronouncements

In January 2014, the Financial Accounting Standards Board (the"FASB") issued Accounting Standards Update ("ASU") 2014-01, "Investments—Equity Method and Joint Ventures (Topic 323): Accounting for Investments in Qualified Affordable Housing Projects (a consensus of the FASB Emerging Issues Task Force)." The amendments in this ASU permit reporting entities to make an accounting policy election to account for their investments in qualified affordable housing projects using the proportional amortization method if certain conditions are met. Under the proportional amortization method, an entity amortizes the initial cost of the investment in proportion to the tax credits and other tax benefits received and recognizes the net investment performance in the income statement as a component of income tax expense (benefit). The amendments in this ASU should be applied retrospectively to all periods presented. A reporting entity that uses the effective yield method to account for its investments in qualified affordable housing projects before the date of adoption may continue to apply the effective yield method for those preexisting investments. The amendments in this ASU are effective for public business entities for annual periods and interim reporting periods within those annual periods, beginning after December 15, 2014. Early adoption is permitted. The Company does not expect the adoption of ASU 2014-01 to have a material impact on its consolidated financial statements.

In January 2014, the FASB issued ASU 2014-04, "Receivables—Troubled Debt Restructurings by Creditors (Subtopic 310-40): Reclassification of Residential Real Estate Collateralized Consumer Mortgage Loans upon Foreclosure (a consensus of the FASB Emerging Issues Task Force)." The amendments in this ASU clarify that an in substance repossession or foreclosure occurs, and a creditor is considered to have received physical possession of residential real estate property collateralizing a consumer mortgage loan, upon either (1) the creditor obtaining legal title to the residential real estate property upon completion of a foreclosure or (2) the borrower conveying all interest in the residential real estate property to the creditor to satisfy that loan through completion of a deed in lieu of foreclosure or through a similar legal agreement. Additionally, the amendments require interim and annual disclosure of both (1) the amount of foreclosed residential real estate property held by the creditor and (2) the recorded investment in consumer mortgage loans collateralized by residential real estate property that are in the process of foreclosure according to local requirements of the applicable jurisdiction. The amendments in this ASU are effective for public business entities for annual periods, and interim periods within those annual periods, beginning after December 15, 2014. The Company is currently assessing the impact that ASU 2014-04 will have on its consolidated financial statements.

In April 2014, the FASB issued ASU 2014-08, "Presentation of Financial Statements (Topic 205) and Property, Plant, and Equipment (Topic 360): Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity." The amendments in this ASU change the criteria for reporting discontinued operations while enhancing disclosures in this area. Under the new guidance, only disposals representing a strategic shift in operations should be presented as discontinued operations. Those strategic shifts should have a major effect on the organization's operations and financial results and include disposals of a major geographic area, a major line of business, or a major equity method investment. The new guidance requires expanded disclosures about discontinued operations that will provide financial statement users with more information about the assets, liabilities, income, and expenses of discontinued operations. Additionally, the new guidance requires disclosure of the pre-tax income attributable to a disposal of a significant part of an organization that does not qualify for discontinued operations reporting. The amendments in the ASU are effective for public business entities for annual periods, and interim periods within those annual periods, beginning after December 15, 2014. Early adoption is permitted. The Company does not expect the adoption of ASU 2014-08 to have a material impact on its consolidated financial statements.

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Note 3 – Securities

The amortized cost and estimated fair value of investments in debt and equity securities at March 31, 2014 and December 31, 2013 were as follows:

	March 31, 2014			
(in thousands)	Amortized Cost	Unrealized Gains	Unrealized Losses	Estimated Fair Value
Securities available for sale:				
Federal agencies and GSEs	$72,872	$ 107	$ 394	$72,585
Mortgage-backed and CMOs	64,129	940	398	64,671
State and municipal	194,114	7,178	287	201,005
Corporate	9,733	13	115	9,631
Equity securities	1,000	231	-	1,231
Total securities available for sale	$341,848	$ 8,469	$ 1,194	$349,123

	December 31, 2013			
(in thousands)	Amortized Cost	Unrealized Gains	Unrealized Losses	Estimated Fair Value
Securities available for sale:				
Federal agencies and GSE	$66,241	$ 126	$ 486	$65,881
Mortgage-backed and CMOs	69,168	1,085	645	69,608
State and municipal	193,251	5,999	517	198,733
Corporate	10,959	4	164	10,799
Equity securities	1,000	103	-	1,103
Total securities available for sale	$340,619	$ 7,317	$ 1,812	$346,124

Restricted Stock

Due to restrictions placed upon the Bank's common stock investment in the Federal Reserve Bank of Richmond ("FRB") and Federal Home Loan Bank of Atlanta ("FHLB"), these securities have been classified as restricted equity securities and carried at cost. The restricted securities are not subject to the investment security classification and are included as a separate line item on the Company's balance sheet. The Federal Reserve Bank of Richmond requires the Bank to maintain stock with a par value equal to 4.5% of its outstanding capital. The FHLB requires the Bank to maintain stock in an amount equal to 6% of outstanding borrowings and a specific percentage of the Bank's total assets. The Bank also owns common stock in CBB Financial Corporation, a Community Bankers Bank located in Richmond, Virginia which provides services to community banks that was inherited from the merger with Community First Financial Corporation in 2006 and common stock in Danville Community Development Corporation, a corporation formed by local banks in the Danville, Virginia area that restores dilapidated properties for resale. The cost of restricted stock at March 31, 2014 and December 31, 2013 were as follows:

(in thousands)	March 31, 2014	December 31, 2013
FRB stock	$2,727	$ 2,722
FHLB stock	1,635	2,000
CBB Financial Corporation stock	101	101
Danville Community Development Corporation stock	66	66

Total restricted stock	$4,529	$ 4,889

Temporarily Impaired Securities

The following table shows estimated fair value and gross unrealized losses, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position, at March 31, 2014. The reference point for determining when securities are in an unrealized loss position is month-end. Therefore, it is possible that a security's market value exceeded its amortized cost on other days during the past twelve-month period.

	Total		Less than 12 Months		12 Months or More	
	Estimated		Estimated		Estimated	
	Fair	Unrealized	Fair	Unrealized	Fair	Unrealized
(in thousands)	Value	Loss	Value	Loss	Value	Loss
Federal agencies and GSEs	$52,841	$ 394	$52,841	$ 394	$-	$ -
Mortgage-backed and CMOs	21,655	398	19,001	354	2,654	44
State and municipal	25,232	287	20,672	215	4,560	72
Corporate	6,212	115	6,212	115	-	-
Total	$105,940	$ 1,194	$98,726	$ 1,078	$7,214	$ 116

GSE debt securities: The unrealized losses on the Company's investment in 26 government sponsored entities ("GSE") were caused by interest rate increases. The contractual terms of those investments do not permit the issuer to settle the securities at a price less than the amortized cost basis of the investments. Because the Company does not intend to sell the investments and it is not more likely than not 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 those investments to be other-than-temporarily impaired at March 31, 2014.

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Mortgage-backed securities and CMOs: The unrealized losses on the Company's investment in 16 GSE mortgage-backed securities and collateralized mortgage obligations ("CMOs") were caused by interest rate increases. The contractual cash flows of those investments are guaranteed by an agency of the U.S. Government. Accordingly, it is expected that the securities would not be settled at a price less than the amortized cost basis of the Company's investments. Because the decline in market value is attributable to changes in interest rates and not credit quality, and because the Company does not intend to sell the investments and it is not more likely than not 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 those investments to be other-than-temporarily impaired at March 31, 2014.

State and municipal securities: The unrealized losses on 28 state and municipal securities were caused by interest rate increases. The contractual terms of those investments do not permit the issuer to settle the securities at a price less than the amortized cost basis of the investments. Because the Company does not intend to sell the investments and it is not more likely than not 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 those investments to be other-than-temporarily impaired at March 31, 2014.

Corporate securities: The unrealized losses on six investments in corporate securities were caused by interest rate increases. The contractual terms of those investments do not permit the issuer to settle the securities at a price less than the amortized cost basis of the investments. Because the Company does not intend to sell the investments and it is not more likely than not 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 those investments to be other-than-temporarily impaired at March 31, 2014.

Restricted stock: When evaluating restricted stock for impairment, its value is based on the ultimate recoverablity of the par value rather than by recognizing temporary declines is value. The company does not consider restricted stock to be other-than-temorailly impaired at March 31, 2014, and no impairment has been recognized.

The table below shows gross unrealized losses and fair value, aggregated by investment category and length of time that individual securities had been in a continuous unrealized loss position, at December 31, 2013.

	Total		Less than 12 Months		12 Months or More	
(in thousands)	Estimated Fair Value	Unrealized Loss	Estimated Fair Value	Unrealized Loss	Estimated Fair Value	Unrealized Loss
Federal agencies and GSEs	$41,586	$ 486	$41,586	$ 486	$-	$ -
Mortgage-backed and CMOs	23,916	645	19,042	577	4,874	68
State and municipal	33,192	517	29,732	462	3,460	55
Corporate	7,347	164	7,347	164	-	-
Total	$106,041	$ 1,812	$97,707	$ 1,689	$8,334	$ 123

Other-Than-Temporary-Impaired Securities

As of March 31, 2014 and December 31, 2013, there were securities classified as having other-than-temporary impairment.

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Note 4 - Loans

Segments

Loans, excluding loans held for sale, were comprised of the following:

(in thousands)	March 31, 2014	December 31, 2013
Commercial	$119,042	$122,553
Commercial real estate:		
Construction and land development	40,458	41,822
Commercial real estate	358,362	364,616
Residential real estate:		
Residential	170,517	171,917
Home equity	89,081	87,797
Consumer	5,909	5,966
Total loans	$783,369	$794,671

Acquired Loans

Interest income, including accretion, on loans acquired from MidCarolina Financial Corporation ("MidCarolina") in connection with the Company's acquisition of MidCarolina for the three months ended March 31, 2014 was approximately $3.4 million. This included $1.1 million in accretion income of which $88,000 was related to loan payoffs and renewals and $410,000 related to recoveries of loans charged off prior to the merger. The outstanding principal balance and the carrying amount of these loans included in the consolidated balance sheets at March 31, 2014 and December 31, 2013 are as follows:

(in thousands)	March 31, 2014	December 31, 2013
Outstanding principal balance	$110,702	$134,099
Carrying amount	102,133	124,828

The outstanding principal balance and related carrying amount of acquired impaired loans, for which the Company applies Accounting Standards Codification ("ASC") 310-30 (formerly Statement of Position ("SOP") 03-3), to account for interest earned, at March 31, 2014 and December 31, 2013 are as follows:

(in thousands)	March 31, 2014	December 31, 2013
Outstanding principal balance	$19,958	$ 21,014
Carrying amount	15,909	16,644

The following table presents changes in the accretable discount on acquired impaired loans, for which the Company applies ASC 310-30 (formerly SOP 03-3), for the three months ended March 31, 2014. The accretion reflected below includes $88,000 related to loan payoffs.

(in thousands)	Accretable Discount

Balance at December 31, 2013	$ 2,046
Accretion	(440)
Reclassification from nonaccretable difference	236
Balance at March 31, 2014	$ 1,842

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Past Due Loans

The following table shows an analysis by portfolio segment of the Company's past due loans at March 31, 2014.

(in thousands)	30-59 Days Past Due	60-89 Days Past Due	90 Days + Past Due and Still Accruing	Non-Accrual Loans	Total Past Due	Current	Total Loans
Commercial	$ 69	$ -	$ -	$ 9	$ 78	$ 118,964	$ 119,042
Commercial real estate:							
Construction and land development	-	-	-	909	909	39,549	40,458
Commercial real estate	-	312	-	3,296	3,608	354,754	358,362
Residential:							
Residential	201	147	-	931	1,279	169,238	170,517
Home equity	109	432	-	409	950	88,131	89,081
Consumer	3	-	-	3	6	5,903	5,909
Total	$ 382	$ 891	$ -	$ 5,557	$ 6,830	$ 776,539	$ 783,369

The following table shows an analysis by portfolio segment of the Company's past due loans at December 31, 2013.

(in thousands)	30- 59 Days Past Due	60-89 Days Past Due	90 Days + Past Due and Still Accruing	Non-Accrual Loans	Total Past Due	Current	Total Loans
Commercial	$ 27	$ -	$ -	$ 11	$ 38	$ 122,515	$ 122,553
Commercial real estate:							
Construction and land development	-	51	-	877	928	40,894	41,822
Commercial real estate	667	-	-	2,879	3,546	361,070	364,616
Residential:							
Residential	642	202	-	880	1,724	170,193	171,917
Home equity	109	18	-	424	551	87,246	87,797
Consumer	21	1	-	-	22	5,944	5,966
Total	$ 1,466	$ 272	$ -	$ 5,071	$ 6,809	$ 787,862	$ 794,671

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Impaired Loans

The following table presents the Company's impaired loan balances by portfolio segment, excluding loans acquired with deteriorated credit quality, at March 31, 2014.

(in thousands)	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
With no related allowance recorded:					
Commercial	$ 16	$ 16	$ -	$ 14	$ -
Commercial real estate:					
Construction and land development	63	63	-	64	-
Commercial real estate	1,942	1,955	-	2,063	1
Residential:					
Residential	932	936	-	956	-
Home equity	409	409	-	413	-
Consumer	3	3	-	3	-
	$ 3,365	$ 3,382	$ -	$ 3,513	$ 1
With a related allowance recorded:					
Commercial	-	-	-	-	-
Commercial real estate:					
Construction and land development	1,453	1,496	88	1,456	8
Commercial real estate	2,231	2,239	483	2,246	2
Residential					
Residential	4	-	-	-	-
Home equity	-	-	-	-	-
Consumer	17	17	3	18	-
	$ 3,705	$ 3,752	$ 574	$ 3,720	$ 10
Total:					
Commercial	$ 16	$ 16	$ -	$ 14	$ -
Commercial real estate:					
Construction and land development	1,516	1,559	88	1,520	8
Commercial real estate	4,173	4,194	483	4,309	3
Residential:					
Residential	936	936	-	956	-
Home equity	409	409	-	413	-
Consumer	20	20	3	21	-
	$ 7,070	$ 7,134	$ 574	$ 7,233	$ 11

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The following table presents the Company's impaired loan balances by portfolio segment, excluding loans acquired with deteriorated credit quality, at December 31, 2013.

(in thousands)	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
With no related allowance recorded:					
Commercial	$ 19	$ 19	$ -	$ 20	$ 1
Commercial real estate:					
Construction and land development	18	18	-	261	4
Commercial real estate	936	936	-	950	13
Residential:					
Residential	880	888	-	1,200	11
Home equity	424	424	-	433	-
Consumer	-	-	-	-	-
	$ 2,277	$ 2,285	$ -	$ 2,864	$ 29
With a related allowance recorded:					
Commercial	$ -	$ -	$ -	$ -	$ -
Commercial real estate:					
Construction and land development	1,468	1,507	68	1,551	33
Commercial real estate	2,266	2,264	488	1,198	7
Residential:					
Residential	1,198	-	-	-	-
Home equity	-	-	-	-	-
Consumer	18	18	3	19	1
	$ 3,752	$ 3,789	$ 559	$ 2,768	$ 41
Total:					
Commercial	$ 19	$ 19	$ -	$ 20	$ 1
Commercial real estate:					
Construction and land development	1,486	1,525	68	1,812	37
Commercial real estate	3,202	3,200	488	2,148	20
Residential:					
Residential	880	888	-	1,200	11
Home equity	424	424	-	433	-
Consumer	18	18	3	19	1
	$ 6,029	$ 6,074	$ 559	$ 5,632	$ 70

There were no loans modified as a troubled debt restructuring ("TDR") for the three months ended March 31, 2014 and 2013.

None of the loans modified as a TDR within the previous twelve months have subsequently defaulted during the three month periods ending March 31, 2014 and 2013.

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Risk Grades

The following table shows the Company's loan portfolio broken down by internal risk grading as of March 31, 2014.

(in thousands)

Commercial and Consumer Credit Exposure

Credit Risk Profile by Internally Assigned Grade

	Commercial	Commercial Real Estate Construction	Commercial Real Estate Other	Residential	Home Equity
Pass	$ 117,576	$ 33,911	$ 347,780	$ 158,722	$ 86,519
Special Mention	1,450	887	5,345	8,265	1,788
Substandard	16	5,660	5,237	3,530	774
Doubtful	-	-	-	-	-
Total	$ 119,042	$ 40,458	$ 358,362	$ 170,517	$ 89,081

Consumer Credit Exposure

Credit Risk Profile Based on Payment Activity

	Consumer
Performing	$ 5,906
Nonperforming	3
Total	$ 5,909

The following table shows the Company's loan portfolio broken down by internal risk grading as of December 31, 2013.

(in thousands)

Commercial and Consumer Credit Exposure

Credit Risk Profile by Internally Assigned Grade

	Commercial	Commercial Real Estate Construction	Commercial Real Estate Other	Residential	Home Equity
Pass	$ 121,033	$ 35,563	$ 351,801	$ 158,478	$ 85,163
Special Mention	1,500	1,005	6,795	8,242	1,650
Substandard	20	5,254	6,020	5,197	984
Doubtful	-	-	-	-	-
Total	$ 122,553	$ 41,822	$ 364,616	$ 171,917	$ 87,797

Consumer Credit Exposure

Credit Risk Profile Based on Payment Activity

	Consumer
Performing	$ 5,966

Nonperforming	-
Total	$ 5,966

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Loans classified in the Pass category typically are fundamentally sound and risk factors are reasonable and acceptable.

Loans classified in the Special Mention category typically have been criticized internally, by loan review or the loan officer, or by external regulators under the current credit policy regarding risk grades.

Loans classified in the Substandard category typically have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt; they are typically characterized by the possibility that the Bank will sustain some loss if the deficiencies are not corrected.

Loans classified in the Doubtful category typically have all the weaknesses inherent in loans classified as substandard, plus the added characteristic that the weaknesses make collection or liquidation in full on the basis of currently existing facts, conditions, and values highly questionable and improbable. However, these loans are not yet rated as loss because certain events may occur that may salvage the debt.

Consumer loans are classified as performing or nonperforming. A loan is nonperforming when payments of interest and principal are past due 90 days or more, or payments are less than 90 days past due, but there are other good reasons to doubt that payment will be made in full.

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Note 5 – Allowance for Loan Losses and Reserve for Unfunded Lending Commitments

Changes in the allowance for loan losses and the reserve for unfunded lending commitments as of the indicated dates and periods are presented below:

The reserve for unfunded loan commitments is included in other liabilities.

(in thousands)	Three Months Ended March 31, 2014	Year Ended December 31, 2013	Three Months Ended March 31, 2013
Allowance for Loan Losses			
Balance, beginning of period	$12,600	$ 12,118	$12,118
Provision for loan losses	-	294	294
Charge-offs	(73)	(837)	(287)
Recoveries	87	1,025	403
Balance, end of period	$12,614	$ 12,600	$12,528
Reserve for Unfunded Lending Commitments			
Balance, beginning of period	$210	$ 201	$201
Provision for loan losses	7	9	10
Charge-offs	-	-	-
Balance, end of period	$217	$ 210	$211

The following table presents the Company's allowance for loan losses by portfolio segment and the related loan balance total by segment at March 31, 2014.

(in thousands)	Commercial	Commercial Real Estate	Residential Real Estate	Consumer	Unallocated	Total
Allowance for Loan Losses						
Balance as of December 31, 2013	$ 1,810	$ 6,819	$ 3,690	$ 99	$ 182	$12,600
Charge-offs	-	-	(53)	(20)	-	(73)
Recoveries	8	14	43	22	-	87
Provision for loan losses	(30)	113	126	(27)	(182)	-
Balance as of March 31, 2014	$ 1,788	$ 6,946	$ 3,806	$ 74	$ -	$12,614
Balance as of March 31, 2014:						
Allowance for Loan Losses						
Individually evaluated for impairment	$ -	$ 571	$ -	$ 3	$ -	$574
Collectively evaluated for impairment	1,785	6,110	3,615	71	-	11,581
Loans acquired with deteriorated credit quality	3	265	191	-	-	459

Total	$ 1,788	$ 6,946	$ 3,806	$ 74	$ -	$ 12,614
Loans						
Individually evaluated for impairment	$ 16	$ 5,689	$ 1,345	$ 20	$ -	$ 7,070
Collectively evaluated for impairment	118,906	384,693	250,902	5,889	-	760,390
Loans acquired with deteriorated credit quality	120	8,438	7,351	-	-	15,909
Total	$ 119,042	$ 398,820	$ 259,598	$ 5,909	$ -	$ 783,369

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The following table presents the Company's allowance for loan losses by portfolio segment and the related loan balance total by segment at December 31, 2013.

(in thousands)	Commercial	Commercial Real Estate	Residential Real Estate	Consumer	Unallocated	Total
Allowance for Loan Losses						
Balance as of December 31, 2012	$ 1,450	$ 6,822	$ 3,638	$ 208	$ -	$ 12,118
Charge-offs	(129)	(164)	(369)	(175)	-	(837)
Recoveries	335	323	244	123	-	1,025
Provision for loan losses	154	(162)	177	(57)	182	294
Balance as of December 31, 2013	$ 1,810	$ 6,819	$ 3,690	$ 99	$ 182	$ 12,600
Balance as of December 31, 2013:						
Allowance for Loan Losses						
Individually evaluated for impairment	$ -	$ 556	$ -	$ 3	$ -	$ 559
Collectively evaluated for impairment	1,810	6,039	3,483	96	182	11,610
Loans acquired with deteriorated credit quality	-	224	207	-	-	431
Total	$ 1,810	$ 6,819	$ 3,690	$ 99	$ 182	$ 12,600

Loans