SUMMIT FINANCIAL GROUP INC
Form 10-K
March 01, 2019
UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-K

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

For the fiscal year ended December 31, 2018

Commission File Number 0-16587
Summit Financial Group, Inc.
(Exact name of registrant as specified in its charter)

West Virginia (State or other jurisdiction of incorporation or organization)	55-0672148 (I.R.S. Employer Identification No.)
300 N. Main Street Moorefield, West Virginia (Address of principal executive offices)	26836 (Zip Code)

(304) 530-1000
(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

Common
(Title of Class)

The NASDAQ Capital Market
(Name of Exchange on which registered)

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.
Yes ¨ No þ

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.
Yes ¨ No þ

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 þ No ¨

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted 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 such files). Yes þ No ¨

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) is not contained herein and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendments to this Form 10-K. ¨

Indicate by check mark whether the registrant is large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company or an emerging growth company. See definitions of “large accelerated filer”, “accelerated filer”, “smaller reporting company” and "emerging growth company" in Rule 12b-2 of the Exchange Act.
Large accelerated filer o   Accelerated filer þ
Non-accelerated filer o   Smaller reporting company o
Emerging growth company o

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. o
Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).
Yes o No þ

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

The aggregate market value of the voting common equity held by non-affiliates of the registrant at June 30, 2018, was approximately $290,798,000. Registrant has assumed that all of its executive officers and directors are affiliates. Such assumption shall not be deemed to be conclusive for any other purpose.

The number of shares of the Registrant’s Common Stock outstanding on February 28, 2019 was 12,803,918.

Documents Incorporated by Reference

The following lists the documents which are incorporated by reference in the Annual Report Form 10-K and the Parts and Items of the Form 10-K into which the documents are incorporated.

Document	Part of Form 10-K into which document is incorporated
Portions of the Registrant's Proxy Statement for the Annual Meeting of Shareholders to be held May 21, 2019	Part III - Items 10, 11, 12, 13 and 14

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PART I.

Item 1. Business

Summit Financial Group, Inc. (“Company” or “Summit”) is a $2.20 billion financial holding company headquartered in Moorefield, West Virginia incorporated on March 5, 1987. We provide community banking services primarily in the Eastern Panhandle and Southern regions of West Virginia and the Northern, Shenandoah Valley and Southwestern regions of Virginia. We provide these services through our community bank subsidiary, Summit Community Bank (“Summit Community” or “Bank”). We also operate Summit Insurance Services, LLC in Moorefield, West Virginia and Leesburg, Virginia, which provides insurance brokerage services to individuals and businesses covering corporate and personal property and casualty insurance products, as well as group health and life insurance products and consulting services.

Community Banking

We provide a wide range of community banking services, including demand, savings and time deposits; commercial, real estate and consumer loans; trust and wealth management services; and cash management services. The deposits of Summit Community are insured by the Federal Deposit Insurance Corporation ("FDIC").

In order to compete with other financial service providers, we principally rely upon personal relationships established by our officers, directors and employees with our clients and specialized services tailored to meet our clients’ needs. We have maintained a strong community orientation by, among other things, supporting the active participation of staff members in local charitable, civic, school, religious and community development activities. We also have a marketing program that primarily utilizes local radio and newspapers to advertise. Banking, like most industries, is becoming more dependent on technology as a means of marketing to customers, including the Internet, which we also utilize. This approach, coupled with continuity of service by the same staff members, enables Summit Community to develop long-term customer relationships, maintain high quality service and respond quickly to customer needs. We believe that our emphasis on local relationship banking, together with a prudent approach to lending, are important factors in our success and growth.

All operational and support functions that are transparent to clients are centralized in order to achieve consistency and cost efficiencies in the delivery of products and services by each banking office. The central office provides services such as data processing, deposit operations, accounting, treasury management, loan administration, loan review, compliance, risk management and internal auditing to enhance our delivery of quality service. We also provide overall direction in the areas of credit policy and administration, strategic planning, marketing, investment portfolio management, human resources administration and other financial and administrative services. The banking offices work closely with us to develop new products and services needed by their customers and to introduce enhancements to existing products and services.

Lending

Our primary lending focus is providing commercial loans to local businesses with annual sales generally up to $75 million and providing owner-occupied real estate loans to individuals. We typically do not seek credit relationships of more than $25 million but will consider larger lending relationships exhibiting above-average credit quality. Under our commercial banking strategy, we focus on offering a broad line of financial products and services to small and medium-sized businesses through full service banking offices. Summit Community Bank has senior management with extensive lending experience. These managers exercise substantial authority over credit and pricing decisions, subject to loan committee approval for larger credits.

We segment our loan portfolio in to the following major lending categories: commercial, commercial real estate, construction and land development, residential real estate, consumer and mortgage warehouse lines of credit. Commercial loans are loans made to commercial borrowers that are not secured by real estate. These encompass loans secured by accounts receivable, inventory and equipment, as well as unsecured loans. Commercial real estate loans consist of commercial mortgages, which generally are secured by nonresidential and multi-family residential properties. Commercial real estate loans are made to many of the same customers and carry similar industry risks as the commercial loan portfolio. Construction and development loans are loans made for the purpose of financing construction or development projects. This portfolio includes commercial and residential land development loans, one-to-four family housing construction, both pre-sold and speculative in nature, multi-family housing construction, non-residential building construction and undeveloped land. Residential real estate loans are mortgage loans to consumers and are secured primarily by a first lien deed of trust. These loans are traditional one-to-four family residential mortgages. Also included in this category of loans are second liens on one-to-four family properties, commercial loans secured by one-to-four family residence and home equity loans. Consumer loans are loans that establish consumer credit that is granted for the consumer’s personal use. These loans include automobile loans and recreational vehicle loans, as well as personal secured and unsecured loans. Our mortgage warehouse lines of credit result solely from a

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participation arrangement with a regional bank to fund residential mortgage warehouse lines of medium- and large-sized mortgage originators located throughout the United States.

Our loan underwriting guidelines and standards are consistent with the prudent banking practices applicable to the relevant exposure and are updated periodically and presented to the Board of Directors for approval. The purpose of these standards and guidelines are: to grant loans on a sound and collectible basis; to invest available funds in a safe and profitable manner; to serve the legitimate credit needs of our primary market area; and to ensure that all loan applicants receive fair and equal treatment in the lending process. It is the intent of the underwriting guidelines and standards to: minimize losses by carefully investigating the credit history of each applicant; verify the source of repayment and the ability of the applicant to repay; collateralize those loans in which collateral is deemed to be required; exercise care in the documentation of the application, review, approval and origination process; and administer a comprehensive loan collection program.

Our real estate underwriting loan-to-value (“LTV”) policy limits are at or below current bank regulatory guidelines, as follows:

	Regulatory LTV Guideline	Summit LTV Policy Limit
Undeveloped land	65%	65%
Land development	75%	70%
Land development - Finished building lots	85%	85%
Construction:		
Commercial, multifamily and other non-residential	80%	80%
1-4 family residential, consumer borrower	85%	85%
1-4 family residential, pre-sold commercial borrower	80%	80%
1-4 family residential, spec, commercial borrower	80%	70%
Improved property:		
Residential real estate - nonowner occupied	85%	85%
Commercial real estate - owner occupied	85%	85%
Commercial real estate - nonowner occupied	85%	85%
Owner occupied 1-4 family	90%	90%
Home equity	90%	90%

Exceptions are permitted to these regulatory guidelines as long as such exceptions are identified, monitored and reported to the Board of Directors at least quarterly and the total of such exceptions do not exceed 100% of Summit Community’s total regulatory capital, which totaled $227.0 million as of December 31, 2018. As of this date, we had loans approximating $94.5 million which exceeded the above regulatory LTV guidelines, as follows:

Undeveloped land	$4.5	million
Land development	$4.8	million
Land development - Finished building lots	$3.4	million
Construction:		
Commercial, multifamily and other non-residential	$4.3	million
1-4 family residential, consumer borrower	$—	
1-4 family residential, pre-sold, commercial borrower	$0.3	million
1-4 family residential, spec, commercial borrower	$3.5	million
Improved property:		
Residential real estate - nonowner occupied	$13.5	million
Commercial real estate - owner occupied	$13.8	million
Commercial real estate - nonowner occupied	$31.5	million
Owner occupied 1-4 family	$14.1	million

Home equity	$0.8 million

Our underwriting standards and practice are designed to originate both fixed and variable rate loan products, consistent with the underwriting guidelines discussed above. Adjustable rate and variable rate loans are underwritten, giving consideration both to the loan's initial rate and to higher assumed rates, commensurate with reasonably anticipated market conditions. Accordingly, we want to insure that adequate primary repayment capacity exists to address both future increases in interest rates and fluctuations in the underlying cash flows available for repayment. Historically, we have not offered "payment option ARM"

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loans. Further, we have had no loan portfolio products which were specifically designed for “sub-prime” borrowers (defined as consumers with a credit score of less than 599).

Supervision and Regulation

General

We are subject to regulation by the Board of Governors of the Federal Reserve System (“FRB”), the West Virginia Division of Financial Institutions, the Securities and Exchange Commission (the “SEC”) and other federal and state regulators. As a financial holding company, we are subject to the restrictions of the Bank Holding Company Act of 1956, as amended (“BHCA”), are registered pursuant to its provisions and are subject to examination by the FRB. As a financial holding company doing business in West Virginia, we are also subject to regulation by and must submit annual reports to the West Virginia Division of Financial Institutions.

The BHCA prohibits the acquisition by a financial holding company of direct or indirect ownership of more than five percent (5%) of the voting shares of any bank within the United States without prior approval of the FRB. With certain exceptions, a financial holding company is prohibited from acquiring direct or indirect ownership or control of more than five percent (5%) of the voting shares of any company that is not a bank and from engaging directly or indirectly in business unrelated to the business of banking or managing or controlling banks.

The FRB, in its Regulation Y, permits financial holding companies to engage in non-banking activities closely related to banking or managing or controlling banks. Approval of the FRB is necessary to engage in these activities or to make acquisitions of corporations engaging in these activities as the FRB determines whether these acquisitions or activities are in the public interest. In addition, by order, and on a case by case basis, the FRB may approve other non-banking activities.

The BHCA permits us to purchase or redeem our own securities. However, Regulation Y provides that prior notice must be given to the FRB if the total consideration for such purchase or consideration, when aggregated with the net consideration paid by us for all such purchases or redemptions during the preceding 12 months is equal to ten percent (10%) or more of our consolidated net worth. Prior notice is not required if (i) both before and immediately after the redemption, the financial holding company is well capitalized; (ii) the financial holding company is well managed and (iii) the financial holding company is not the subject of any unresolved supervisory issues.

The FRB has broad authority to prohibit activities of bank holding companies and their non-banking subsidiaries that represent unsafe and unsound banking practices or which constitute violations of laws or regulations. The FRB also can assess civil money penalties for certain activities conducted on a knowing and reckless basis, if those activities caused a substantial loss to a depository institution. The penalties can be as high as $1 million for each day the activity continues.

Summit Community, our only bank subsidiary, is subject to West Virginia banking statutes and regulations, and is primarily regulated by the West Virginia Division of Financial Institutions and the FDIC. The Bank is also subject to regulations promulgated by the FRB. As a member of the FDIC, Summit Community’s deposits are insured as required by federal law. Bank regulatory authorities regularly examine revenues, loans, investments, management practices and other aspects of Summit Community. These examinations are conducted primarily to protect depositors and not shareholders. In addition to these regular examinations, the Bank must furnish to regulatory authorities quarterly reports containing full and accurate statements of its affairs.

Because we are a public company, we are subject to regulation by the SEC. SEC regulations require us to disclose certain types of business and financial data on a regular basis to the SEC and to our shareholders. We are required to file annual, quarterly and current reports with the SEC. We prepare and file an annual report on Form 10-K with the

SEC that contains detailed financial and operating information, as well as a management response to specific questions about our operations. SEC regulations require that our annual reports to shareholders contain certified financial statements and other specific items such as management's discussion and analysis of our financial condition and results of operations. We must also file quarterly reports with the SEC on Form 10-Q that contain detailed financial and operating information for the prior quarter and we must file current reports on Form 8-K to provide the pubic with information on recent material events.

In addition to periodic reporting to the SEC, we are subject to proxy rules and tender offer rules issued by the SEC. Our officers, directors and principal shareholders (holding 10% or more of our stock) must also submit reports to the SEC regarding their holdings of our stock and any changes to such holdings and they are subject to short-swing profit liability. Because we are traded on the NASDAQ, we are also subject to the listing standards of NASDAQ.

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Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010

The "Dodd-Frank Wall Street Reform and Consumer Protection Act" (the "Dodd-Frank Act"), which is complex and broad in scope, established the Bureau of Consumer Financial Protection (the "CFPB"), which has extensive regulatory and enforcement powers over consumer financial products and services, and the Financial Stability Oversight Council, which has oversight authority for monitoring systemic risk. We will be required to comply with the Consumer Financial Protection Act and the CFPB's rules; however, these rules will be enforced by our primary regulator, the FRB, not the CFPB. In addition, the Dodd-Frank Act alters the authority and duties of the federal banking and securities regulatory agencies, implements certain corporate governance requirements for all public companies, including financial institutions with regard to executive compensation, proxy access by shareholders and certain whistleblower provisions and restricts certain proprietary trading and hedge fund and private equity activities of banks and their affiliates. Although the regulations that directly affect our business have been adopted, many of the provisions of the Dodd-Frank Act are subject to final rulemaking by the U.S. financial regulatory agencies and the implications of the Dodd-Frank Act for our business will depend to some extent on how such rules are adopted and implemented by the primary U.S. financial regulatory agencies.

Bank Holding Company Activities

In general, the BHC Act limits the business of bank holding companies to banking, managing or controlling banks and other activities that the FRB has determined to be so closely related to banking as to be a proper incident thereto. In addition, bank holding companies that qualify and elect to be financial holding companies may engage in any activity, or acquire and retain the shares of a company engaged in any activity, that is either (i) financial in nature or incidental to such financial activity (as determined by the FRB in consultation with the Secretary of the Treasury) or (ii) complementary to a financial activity and does not pose a substantial risk to the safety and soundness of depository institutions or the financial system generally (as solely determined by the FRB), without prior approval of the FRB.

Activities that are financial in nature include securities underwriting and dealing, insurance underwriting and making merchant banking investments. Some examples of non-banking activities which presently may be performed by a financial holding company are: making or acquiring, for its own account or the account of others, loans and other extensions of credit; operating as an industrial bank, or industrial loan company, in the manner authorized by state law; servicing loans and other extensions of credit; performing or carrying on any one or more of the functions or activities that may be performed or carried on by a trust company in the manner authorized by federal or state law; acting as an investment or financial advisor; leasing real or personal property; making equity or debt investments in corporations or projects designed primarily to promote community welfare, such as the economic rehabilitation and the development of low income areas; providing bookkeeping services or financially oriented data processing services for the holding company and its subsidiaries; acting as an insurance agent or a broker; acting as an underwriter for credit life insurance, which is directly related to extensions of credit by the financial holding company system; providing courier services for certain financial documents; providing management consulting advice to non-affiliated banks; selling retail money orders having a face value of not more than $1,000, traveler's checks and U.S. savings bonds; performing appraisals of real estate; arranging commercial real estate equity financing under certain limited circumstances; providing securities brokerage services related to securities credit activities; underwriting and dealing in government obligations and money market instruments; providing foreign exchange advisory and transactional services; and acting, under certain circumstances, as futures commission merchant for non-affiliated persons in the execution and clearance on major commodity exchanges of futures contracts and options.

To maintain financial holding company status, a financial holding company and all of its depository institution subsidiaries must be "well capitalized" and "well managed." A depository institution subsidiary is considered to be "well capitalized" if it satisfies the requirements for this status discussed in the section captioned "Capital Requirements" included elsewhere in this item. A depository institution subsidiary is considered "well managed" if it received a composite rating and management rating of at least "satisfactory" in its most recent examination. A financial holding company's status will also depend upon it maintaining its status as "well capitalized" and "well managed' under applicable FRB regulations. If a financial holding company ceases to meet these capital and management requirements, the FRB's regulations provide that the financial holding company must enter into an agreement with the FRB to comply with all applicable capital and management requirements. Until the financial holding company returns to compliance, the FRB may impose limitations or conditions on the conduct of its activities and the company may not commence any of the broader financial activities permissible for financial holding companies or acquire a company engaged in such financial activities without prior approval of the FRB. If the company does not return to compliance within 180 days, the FRB may require divestiture of the holding company's depository institutions. Bank holding companies and banks must also be both well capitalized and well managed in order to acquire banks located outside their home state.

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In order for a financial holding company to commence any new activity permitted by the BHC Act or to acquire a company engaged in any new activity permitted by the BHC Act, each insured depository institution subsidiary of the financial holding company must have received a rating of at least “satisfactory” in its most recent examination under the Community Reinvestment Act. See the section captioned “Community Reinvestment Act” included elsewhere in this item.

The FRB has the power to order any bank holding company or its subsidiaries to terminate any activity or to terminate its ownership or control of any subsidiary when the FRB has reasonable grounds to believe that continuation of such activity or such ownership or control constitutes a serious risk to the financial soundness, safety or stability of any bank subsidiary of the bank holding company.

The Dodd-Frank Act amends the BHC Act to require the federal financial regulatory agencies to adopt rules that prohibit banks and their affiliates from engaging in proprietary trading and investing in and sponsoring certain unregistered investment companies (defined as hedge funds and private equity funds). The statutory provision is commonly called the “Volcker Rule”. The Volcker Rule has not had a material impact on our operations as we do not generally engage in activities prohibited by the Volcker Rule.

The BHC Act, the Bank Merger Act, the West Virginia Banking Code and other federal and state statutes regulate acquisitions of commercial banks. The BHC Act requires the prior approval of the FRB for the direct or indirect acquisition by a bank holding company of more than 5.0% of the voting shares of a commercial bank or its parent holding company. Under the Bank Merger Act, the prior approval of the FRB or other appropriate bank regulatory authority is required for a member bank to merge with another bank or purchase the assets or assume the deposits of another bank. In reviewing applications seeking approval of merger and acquisition transactions, the bank regulatory authorities will consider, among other things, the competitive effect and public benefits of the transactions, the capital position of the combined organization, the risks to the stability of the U.S. banking or financial system, the applicant’s performance record under the Community Reinvestment Act (see the section captioned “Community Reinvestment Act” included elsewhere in this item) and its compliance with fair housing and other consumer protection laws and the effectiveness of the subject organizations in combating money laundering activities.

Dividends

The principal source of our liquidity is dividends from Summit Community. The prior approval of the Federal Reserve is required if the total of all dividends declared by a state-chartered member bank in any calendar year would exceed the sum of the bank’s net profits for that year and its retained net profits for the preceding two calendar years, less any required transfers to surplus or to fund the retirement of preferred stock. Federal law also prohibits a state-chartered, member bank from paying dividends that would be greater than the bank’s undivided profits. Summit Community is also subject to limitations under West Virginia state law regarding the level of dividends that may be paid.

In addition, the Company and Summit Community are subject to other regulatory policies and requirements relating to the payment of dividends, including requirements to maintain adequate capital above regulatory minimums. The appropriate federal regulatory authority is authorized to determine under certain circumstances relating to the financial condition of a bank holding company or a bank that the payment of dividends would be an unsafe or unsound practice and to prohibit payment thereof. The appropriate federal regulatory authorities have stated that paying dividends that deplete a bank’s capital base to an inadequate level would be an unsafe and unsound banking practice and that banking organizations should generally pay dividends only out of current operating earnings.

Credit and Monetary Policies and Related Matters

Summit Community is affected by the fiscal and monetary policies of the federal government and its agencies, including the FRB. An important function of these policies is to curb inflation and control recessions through control of the supply of money and credit. The operations of Summit Community are affected by the policies of government regulatory authorities, including the FRB, which regulates money and credit conditions through open-market operations in United States Government and Federal agency securities, adjustments in the discount rate on member bank borrowings and requirements against deposits and regulation of interest rates payable by member banks on time and savings deposits. These policies have a significant influence on the growth and distribution of loans, investments and deposits, and interest rates charged on loans, or paid for time and savings deposits, as well as yields on investments. The FRB has had a significant effect on the operating results of commercial banks in the past and is expected to continue to do so in the future. Future policies of the FRB and other authorities and their effect on future earnings cannot be predicted.

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The FRB has a policy that a financial holding company is expected to act as a source of financial and managerial strength to each of its subsidiary banks and to commit resources to support each such subsidiary bank. Under the source of strength doctrine, the FRB may require a financial holding company to contribute capital to a troubled subsidiary bank and may charge the financial holding company with engaging in unsafe and unsound practices for failure to commit resources to such a subsidiary bank. This capital injection may be required at times when Summit may not have the resources to provide it. Any capital loans by a holding company to any subsidiary bank are subordinate in right of payment to deposits and to certain other indebtedness of such subsidiary bank. In addition, the Crime Control Act of 1990 provides that in the event of a financial holding company's bankruptcy, any commitment by such holding company to a Federal bank or thrift regulatory agency to maintain the capital of a subsidiary bank will be assumed by the bankruptcy trustee and entitled to a priority of payment.

Capital Requirements

Our bank subsidiary, Summit Community, is subject to various regulatory capital requirements administered by the banking regulatory agencies. Under the capital adequacy guidelines and the regulatory framework for prompt corrective action, Summit Community must meet specific capital guidelines that involve quantitative measures of its assets, liabilities and certain off-balance sheet items as calculated under regulatory accounting practices. Summit Community’s capital amounts and classifications are also subject to qualitative judgments by the regulators about components, risk weightings and other factors. Quantitative measures established by regulation to ensure capital adequacy require Summit Community to maintain minimum amounts and ratios of Common Equity Tier 1("CET1"), Total capital and Tier I capital (as defined in the regulations) to risk-weighted assets (as defined), and of Tier I capital (as defined) to average assets (as defined). Summit Community’s regulatory capital ratios as of December 31, 2018 are set forth in the table in Note 18 of the notes to the consolidated financial statements beginning on page 85. We believe, as of December 31, 2018, that our bank subsidiary met all capital adequacy requirements to which it was subject.

The most recent notifications from the banking regulatory agencies categorized Summit Community as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized, Summit Community must maintain minimum CET1, Total risk-based, Tier I risk-based, and Tier I leverage ratios as set forth in the table below.

The Basel III Capital Rules became effective for us on January 1, 2015, with full compliance with all of the final rule's requirements phased-in over a multi-year schedule, to be fully phased-in by January 1, 2019. As of December 31, 2018, Summit Community’s capital levels remained characterized as "well-capitalized" under the new rules.

On August 28, 2018, the FRB issued an interim final rule expanding the applicability of the FRB's small bank holding company policy statement, as required by the Economic Growth, Regulatory Relief, and Consumer Protection Act of 2018. The interim final rule raises the small bank holding company policy statement's asset threshold from $1 billion to $3 billion in total consolidated assets, and as a result, the Company was exempted from all regulatory capital guidelines, to which it previously had been subject, until such time as its consolidated assets exceed $3 billion.

Prompt Corrective Action. The Federal Deposit Insurance Corporation Improvement Act of 1991 ("FDICIA") establishes a new regulatory scheme, which ties the level of supervisory intervention by bank regulatory authorities primarily to a depository institution's capital category. Among other things, FDICIA authorizes regulatory authorities to take "prompt corrective action" with respect to depository institutions that do not meet minimum capital requirements. FDICIA establishes five capital tiers: well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized and critically undercapitalized. The relevant capital measures, which reflect changes under the Basel III Capital Rules, are the total capital ratio, the CET1 capital ratio, the Tier 1 capital ratio and the leverage ratio.

A bank will be (i) “well capitalized” if the institution has a total risk-based capital ratio of 10.0% or greater, a CET1 capital ratio of 6.5% or greater, a Tier 1 risk-based capital ratio of 8.0% or greater and a leverage ratio of 5.0% or greater and is not subject to any order or written directive by any such regulatory authority to meet and maintain a specific capital level for any capital measure; (ii) “adequately capitalized” if the institution has a total risk-based capital ratio of 8.0% or greater, a CET1 capital ratio of 4.5% or greater, a Tier 1 risk-based capital ratio of 6.0% or greater and a leverage ratio of 4.0% or greater and is not “well capitalized”; (iii) “undercapitalized” if the institution has a total risk-based capital ratio that is less than 8.0%, a CET1 capital ratio less than 4.5%, a Tier 1 risk-based capital ratio of less than 6.0% or a leverage ratio of less than 4.0%; (iv) “significantly undercapitalized” if the institution has a total risk-based capital ratio of less than 6.0%, a CET1 capital ratio less than 3.0%, a Tier 1 risk-based capital ratio of less than 4.0% or a leverage ratio of less than 3.0%; and (v) “critically undercapitalized” if the institution’s tangible equity is equal to or less than 2.0% of average quarterly tangible assets. An institution may be downgraded to, or deemed to be in, a capital category that is lower than indicated by its capital ratios if it is determined to be in an unsafe or unsound condition or if it receives an unsatisfactory examination rating with respect to certain matters. A bank’s capital category is determined solely for the purpose of applying prompt corrective action regulations and the capital category may not constitute an accurate representation of the bank's overall financial condition or prospects for other purposes."

Community Reinvestment Act

Financial holding companies and their subsidiary banks are also subject to the provisions of the Community Reinvestment Act of 1977 ("CRA"). Under the CRA, the FRB (or other appropriate bank regulatory agency) is required, in connection with its examination of a bank, to assess such bank's record in meeting the credit needs of the communities served by that bank, including low and moderate income neighborhoods. Further, such assessment is also required of any financial holding company that has applied to (i) charter a national bank, (ii) obtain deposit insurance coverage for a newly chartered institution, (iii) establish a new branch office that will accept deposits, (iv) relocate an office, or (v) merge or consolidate with, or acquire the assets or assume the liabilities of a federally-regulated financial institution. In the case of a financial holding company applying for approval to acquire a bank or other financial holding company, the FRB will assess the record of each subsidiary of the applicant financial holding company and such records may be the basis for denying the application or imposing conditions in connection with approval of the application.

In the most recent CRA examination by the bank regulatory authorities, Summit Community was given a "satisfactory" CRA rating.

Graham-Leach-Bliley Act of 1999

The enactment of the Graham-Leach-Bliley Act of 1999 (the "GLB Act") represents a pivotal point in the history of the financial services industry. The GLB Act swept away large parts of a regulatory framework that had its origins in the Depression Era of the 1930s. New opportunities were available for banks, other depository institutions, insurance companies and securities firms to enter into combinations that permit a single financial services organization to offer customers a more complete array of financial products and services. The GLB Act provides a new regulatory framework through the financial holding company, which has as its "umbrella regulator" the FRB. Functional regulation of the financial holding company's separately regulated subsidiaries is conducted by their primary functional regulators. The GLB Act makes a CRA rating of satisfactory or above necessary for insured depository institutions and their financial holding companies to engage in new financial activities. The GLB Act specifically gives the FRB the authority, by regulation or order, to expand the list of "financial" or "incidental" activities, but requires consultation with the U.S. Treasury Department, and gives the FRB authority to allow a financial holding company to engage in any activity that is "complementary" to a financial activity and does not "pose a substantial risk to the safety and soundness of depository institutions or the financial system generally."

Under the GLB Act, all financial institutions are required to adopt privacy policies, restrict the sharing of nonpublic customer data with nonaffiliated parties at the customer's request and establish procedures and practices to protect customer data from unauthorized access. We have established policies and procedures to assure our compliance with all privacy provisions of the GLB Act. Pursuant to Title V of the GLB Act, we, like all other financial institutions, are required to:

- provide notice to our customers regarding privacy policies and practices,
- inform our customers regarding the conditions under which their non-public personal information may be disclosed to non-affiliated third parties and
- give our customers an option to prevent certain disclosure of such information to non-affiliated third parties.

Deposit Acquisition Limitation

Under West Virginia banking law, an acquisition or merger is not permitted if the resulting depository institution or its holding company, including its affiliated depository institutions, would assume additional deposits to cause it to control deposits in the State of West Virginia in excess of twenty five percent (25%) of such total amount of all deposits held by insured depository institutions in West Virginia. This limitation may be waived by the Commissioner of Banking by showing good cause.

Consumer Laws and Regulations

In addition to the banking laws and regulations discussed above, bank subsidiaries are also subject to certain consumer laws and regulations that are designed to protect consumers in transactions with banks. Among the more prominent of such laws and regulations are the Truth in Lending Act, the Home Mortgage Disclosure Act and Regulation C, the Electronic Funds Transfer Act, the Expedited Funds Availability Act, the Equal Credit Opportunity Act, the Fair Credit Reporting Act, the Fair Debt Collection Act, the Right to Financial Privacy Act and the Fair Housing Act. These laws and regulations mandate certain

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disclosure requirements and regulate the manner in which financial institutions must deal with customers when taking deposits or making loans to such customers. Bank subsidiaries must comply with the applicable provisions of these consumer protection laws and regulations as part of their ongoing customer relations.

Dodd-Frank centralized responsibility for consumer financial protection by creating the CFPB and giving it responsibility for implementing, examining and enforcing compliance with federal consumer protection laws. The CFPB has broad rulemaking, supervisory and enforcement authority over consumer financial products and services, including deposit products, residential mortgages, home-equity loans and credit cards. The CFPB’s functions include investigating consumer complaints, rulemaking, supervising and examining banks’ consumer transactions and enforcing rules related to consumer financial products and services including mortgage lending and servicing, fair lending requirements, and automotive finance. Summit Community Bank, as a bank with less than $10 billion in assets, is subject to these federal consumer financial laws, but continues to be examined for compliance by the FDIC, its primary federal banking regulator.

The CFPB has issued final regulations implementing provisions of the Dodd-Frank Act that require all creditors to determine a consumer’s ability to repay a mortgage loan before making a loan. The final rule, referred to as the Ability-to Repay (ATR)/Qualified Mortgage (QM) standards, provide that a lender making a special type of loan, known as a Qualified Mortgage, is entitled to presume that the loan complies with the ATR safe harbor requirements. The rule establishes different types of Qualified Mortgages that are generally identified as loans with restrictions on loan features, limits on fees being charged and underwriting requirements.

USA Patriot Act of 2001

The USA Patriot Act of 2001 and its related regulations require insured depository institutions, broker-dealers and certain other financial institutions to have policies, procedures and controls to detect, prevent and report money laundering and terrorist financing. The statute and its regulations also provide for information sharing, subject to conditions, between federal law enforcement agencies and financial institutions, as well as among financial institutions, for counter-terrorism purposes. Federal banking regulators are required, when reviewing bank holding company acquisition and bank merger applications, to take into account the effectiveness of the anti-money laundering activities of the applicants. Summit expects to continue to devote significant resources to its Bank Secrecy Act/anti-money laundering program, particularly as risks persistently emerge and evolve and as regulatory expectations escalate.

Sarbanes-Oxley Act of 2002

The Sarbanes-Oxley Act of 2002 (“SOA”) addresses, among other issues, corporate governance, auditing and accounting, executive compensation and enhanced and timely disclosure of corporate information. SOA requires our Chief Executive Officer and Chief Financial Officer each to certify that Summit’s Quarterly and Annual Reports do not contain any untrue statement of a material fact. The rules have several requirements, including requiring these officers certify that: they are responsible for establishing, maintaining and regularly evaluating the effectiveness of our internal controls; they have made certain disclosures to our auditors and the audit committee of the Board of Directors about our internal controls; and they have included information in Summit’s Quarterly and Annual Reports about their evaluation and whether there have been significant changes in our internal controls or in other factors that could significantly affect internal controls subsequent to the evaluation.

Furthermore, in response to the directives of the SOA, NASDAQ adopted substantially expanded corporate governance criteria for the issuers of securities quoted on the NASDAQ Capital Market (the market on which our common stock is listed for trading). The new NASDAQ rules govern, among other things, the enhancement and regulation of corporate disclosure and internal governance of listed companies and of the authority, role and responsibilities of their boards of directors and, in particular, of “independent” members of such boards of directors, in the areas of nominations, corporate governance, compensation and the monitoring of the audit and internal financial control processes.

Cybersecurity

In 2015, federal regulators issued two related statements regarding cybersecurity. One statement indicates that financial institutions should design multiple layers of security controls to establish lines of defense and to ensure that their risk management processes also address the risk posed by compromised customer credentials, including security measures to reliably authenticate customers accessing internet-based services of the financial institution. The other statement indicates that a financial institution's management is expected to maintain sufficient business continuity planning processes to ensure the rapid recovery, resumption and maintenance of the institution's operations after a cyber-attack involving destructive malware. A financial institution is also expected to develop appropriate processes to enable recovery of data and business operations and address rebuilding network capabilities and restoring data if the institution or its critical service providers fall victim to this type of cyber-attack. If we fail to observe the regulatory guidance, we could be subject to various regulatory sanctions, including financial penalties.

In the ordinary course of business, we rely on electronic communications and information systems to conduct our operations and to store sensitive data. We employ an in-depth, layered, defensive approach that leverages people, processes and technology to manage and maintain cybersecurity controls. We employ a variety of preventative and detective tools to monitor, block and provide alerts regarding suspicious activity, as well as to report on any suspected advanced persistent threats. Notwithstanding the strength of our defensive measures, the threat from cyber attacks is severe, attacks are sophisticated and increasing in volume and attackers respond rapidly to changes in defensive measures. While to date, we have not experienced a significant compromise, significant data loss or any material financial losses related to cybersecurity attacks, our systems and those of our customers and third-party service providers are under constant threat and it is possible that we could experience a significant event in the future. Risks and exposures related to cybersecurity attacks are expected to remain high for the foreseeable future due to the rapidly evolving nature and sophistication of these threats, as well as due to the expanding use of Internet banking, mobile banking and other technology-based products and services by us and our customers. See Item 1A. Risk Factors for a further discussion of risks related to cybersecurity.

Transactions with Affiliates

Federal law restricts subsidiary banks of a financial holding company from making certain extensions of credit to the parent financial holding company or to any of its subsidiaries; from investing in the holding company stock; and limits the ability of a subsidiary bank to take its parent company stock as collateral for the loans of any borrower. Additionally, federal law prohibits a financial holding company and its subsidiaries from engaging in certain tie-in arrangements in conjunction with the extension of credit or furnishing of services.

There are various statutory and regulatory limitations, including those set forth in sections 23A and 23B of the Federal Reserve Act and the related Federal Reserve Regulation W, governing the extent to which the bank will be able to purchase assets from or securities of or otherwise finance or transfer funds to us or our non-banking affiliates. Among other restrictions, such transactions between the bank and any one affiliate (including Summit) generally will be limited to ten percent (10%) of the bank’s capital and surplus and transactions between the bank and all affiliates will be limited to twenty percent (20%) of the bank’s capital and surplus. Furthermore, loans and extensions of credit are required to be secured in specified amounts and are required to be on terms and conditions consistent with safe and sound banking practices.

In addition, any transaction by a bank with an affiliate and any sale of assets or provisions of services to an affiliate generally must be on terms that are substantially the same, or at least as favorable, to the bank as those prevailing at the time for comparable transactions with non-affiliated companies.

Incentive Compensation

The Federal Reserve Board reviews, as part of its regular, risk-focused examination process, the incentive compensation arrangements of banking organizations, such as Summit, that are not “large, complex banking organizations.” These reviews are tailored to each organization based on the scope and complexity of the organization’s activities and the prevalence of incentive compensation arrangements. The scope and content of the U.S. banking regulators’ policies on incentive compensation are continuing to develop.
The federal bank regulatory agencies have issued joint guidance on incentive compensation policies intended to ensure that the incentive compensation policies of banking organizations do not undermine the safety and soundness of such organizations by encouraging excessive risk-taking. In addition, the Dodd-Frank Act requires the federal bank regulatory agencies and the SEC to issue regulations or guidelines requiring covered financial institutions, including the Company and Summit Community, to prohibit incentive-based payment arrangements that encourage

inappropriate risks by providing compensation that is excessive or that could lead to material financial loss to the institution. A proposed rule was issued in 2016. Also, pursuant to the Dodd-Frank Act, in 2015, the SEC proposed rules that would direct stock exchanges to require listed companies to implement clawback policies to recover incentive-based compensation from current or former executive officers in the event of certain financial restatements and would also require companies to disclose their clawback policies and their actions under those policies. The Company continues to evaluate the proposed rules, both of which are subject to further rulemaking procedures.

Competition

We engage in highly competitive activities. Each activity and market served involves competition with other banks and savings institutions, as well as with non-banking and non-financial enterprises that offer financial products and services that compete directly with our products and services. We actively compete with other banks, mortgage companies and other financial service companies in our efforts to obtain deposits and make loans, in the scope and types of services offered, in interest rates paid on time deposits and charged on loans and in other aspects of banking.

Of particular note, banking laws limit the total amount we can lend to any one borrower generally to 15 percent of Summit Community's Tier 1 capital plus its allowance for loan losses. Summit Community evaluated the risks and rewards of lending up to this legal lending limit and established a self-imposed lending limit equal to 85 percent of its legal lending limit. Accordingly, institutions larger than Summit Community have a natural competitive advantage to serve the loan needs of larger clients as their legal lending limits are proportionally greater than ours.

In addition to competing with other banks and mortgage companies, we compete with other financial institutions engaged in the business of making loans or accepting deposits, such as savings and loan associations, credit unions, industrial loan associations, insurance companies, small loan companies, finance companies, real estate investment trusts, certain governmental agencies, credit card organizations and other enterprises. In addition, competition for money market accounts from securities brokers has also intensified. Additional competition for deposits comes from government and private issues of debt obligations and other investment alternatives for depositors, such as money market funds. We take an aggressive competitive posture and intend to continue vigorously competing for market share within our service areas by offering competitive rates and terms on both loans and deposits.

Employees

At February 28, 2019, we employed 371 full-time equivalent employees.

Available Information

Our Internet website address is www.summitfgi.com and our Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, current reports on Form 8-K and amendments to such filed reports with the SEC are accessible through this website free of charge as soon as reasonably practicable after we electronically file such reports with the SEC. The information on our website is not and shall not be deemed to be, a part of this report or incorporated into any other filing with the SEC.

These reports are available at the SEC's website at www.sec.gov that contains reports, proxy and information statements and other information regarding issuers that file electronically with the SEC.

Statistical Information

The information noted below is provided pursuant to Guide 3 – Statistical Disclosure by Bank Holding Companies.

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Item 1A. Risk Factors

We, like other financial holding companies, are subject to a number of risks that may adversely affect our financial condition or results of operation, many of which are outside of our direct control, though efforts are made to manage those risks while optimizing returns. Among the risks assumed are: (i) credit risk, which is the risk of loss due to loan clients or other counterparties not being able to meet their financial obligations under agreed upon terms, (ii) market risk, which is the risk of loss due to changes in the market value of assets and liabilities due to changes in market interest rates, equity prices and credit spreads, (iii) liquidity risk, which is the risk of loss due to the possibility that funds may not be available to satisfy current or future commitments based on external market issues, investor and customer perception of financial strength and events unrelated to the Company such as war, terrorism, or financial institution market specific issues and (iv) operational risk, which is the risk of loss due to human error, inadequate or failed internal systems and controls, violations of, or noncompliance with, laws, rules, regulations, prescribed practices, or ethical standards and external influences such as market conditions, fraudulent activities, disasters and security risks.

In addition to the other information included or incorporated by reference into this report, readers should carefully consider that the following important factors, among others, could materially impact our business, future results of operations and future cash flows.

RISKS RELATING TO THE ECONOMIC ENVIRONMENT

Our business may be adversely affected by conditions in financial markets and economic conditions generally.

Our business is concentrated in West Virginia and the Northern, Shenandoah Valley and Southwestern regions of Virginia. As a result, our financial condition, results of operations and cash flows are subject to changes if there are changes in the economic conditions in these areas. A prolonged period of economic recession or other adverse economic conditions in these areas could have a negative impact on Summit. A significant decline in general economic conditions nationally, caused by inflation, recession, acts of terrorism, outbreak of hostilities or other international or domestic occurrences, unemployment, changes in securities markets, declines in the housing market, a tightening credit environment or other factors could impact these local economic conditions and, in turn, have a material adverse effect on our financial condition and results of operations.

The soundness of other financial institutions could adversely affect us.

Financial services institutions are interrelated as a result of trading, clearing, counterparty or other relationships. We have exposure to many different industries and counterparties and routinely execute transactions with counterparties in the financial services industry, including brokers and dealers, commercial banks, or other institutional firms. Defaults by financial services institutions and even rumors or questions about a financial institution or the financial services industry in general, have led to market wide liquidity problems and could lead to losses or defaults by us or other institutions. Any such losses could adversely affect our financial condition or results of operations.

The value of certain investment securities is volatile and future declines or other-than-temporary impairments could have a materially adverse effect on future earnings and regulatory capital.

Volatility in the fair value for certain investment securities, whether caused by changes in market conditions, interest rates, credit risk of the issuer, the expected yield of the security, or actual defaults in the portfolio could result in significant fluctuations in the value of the securities as well as any regulatory rulemaking which could exclude or limit the holdings of certain investment securities. This could have a material adverse impact on our accumulated other comprehensive income and shareholders’ equity depending on the direction of the fluctuations. Furthermore, future downgrades, defaults or prepayments, including the liquidation of the underlying collateral in certain securities, could result in future classifications as other-than-temporarily impaired. This could have a material impact on our future earnings, although the impact on shareholders' equity will be offset by any amount already included in other comprehensive income for securities that were temporarily impaired.

RISKS RELATING TO OUR BUSINESS

We are subject to extensive government regulation and supervision.

The Company and Summit Community are subject to extensive federal and state regulation and supervision, which vests a significant amount of discretion in the various regulatory authorities. Banking regulations are primarily intended to protect depositors and customers, the Federal Deposit Insurance fund and the banking system as a whole, not security holders. These regulations and supervisory guidance affect our lending practices, capital structure, investment practices, dividend policy and growth, among other things. Congress and federal regulatory agencies continually review banking laws, regulations and policies for possible changes. The Dodd-Frank Act instituted major changes to the banking and financial institutions regulatory regimes. Other changes to statutes, regulations or regulatory policies or supervisory guidance, including changes in interpretation or implementation of statutes, regulations, policies or supervisory guidance, could affect us in substantial and unpredictable ways. Such changes could subject us to additional costs, limit the types of financial services and products we may offer and/or increase the ability of non-banks to offer competing financial services and products, among other things. Failure to comply with laws, regulations, policies or supervisory guidance could result in enforcement and other legal actions by Federal or state authorities, including criminal and civil penalties, the loss of FDIC insurance, the revocation of a banking charter, other sanctions by regulatory agencies, civil money penalties and/or reputation damage. In this regard, government authorities, including the bank regulatory agencies, are pursuing aggressive enforcement actions with respect to compliance and other legal matters involving financial activities, which heightens the risks associated with actual and perceived compliance failures. Any of the foregoing could have a material adverse effect on our business, financial condition and results of operations.

See the section captioned "Supervision and Regulation" included in Item 1. Business on page 1.

We may become subject to additional regulatory restrictions in the event that our regulatory capital levels decline.

Although the Bank is qualified as "well capitalized" under the regulatory framework for prompt corrective action as of December 31, 2018, there is no guarantee that we will not have a decline in our capital category in the future. In the event of such a capital category decline, we would be subject to increased regulatory restrictions that could have a material adverse effect on our business, financial condition, results of operations, cash flows and/or future prospects.

If a bank is classified as undercapitalized, the bank is required to submit a capital restoration plan to the FDIC. Pursuant to FDICIA, an undercapitalized bank is prohibited from increasing its assets, engaging in a new line of business, acquiring any interest in any company or insured depository institution, or opening or acquiring a new branch office, except under certain circumstances, including the acceptance by the FDIC of a capital restoration plan for the bank. Furthermore, if a state non-member bank is classified as undercapitalized, the FDIC may take certain actions to correct the capital position of the bank; if a bank is classified as significantly undercapitalized or critically undercapitalized, the FDIC would be required to take one or more prompt corrective actions. These actions would include, among other things, requiring sales of new securities to bolster capital; improvements in management; limits on interest rates paid; prohibitions on transactions with affiliates; termination of certain risky activities and restrictions on compensation paid to executive officers. If a bank is classified as critically undercapitalized, FDICIA requires the bank to be placed into conservatorship or receivership within ninety (90) days, unless the Federal Reserve determines that other action would better achieve the purposes of FDICIA regarding prompt corrective action with respect to undercapitalized banks.

Under FDICIA, banks may be restricted in their ability to accept brokered deposits, depending on their capital classification. "Well capitalized" banks are permitted to accept brokered deposits, but all banks that are not well capitalized could be restricted from accepting such deposits. The FDIC may, on a case-by-case basis, permit banks that are adequately capitalized to accept brokered deposits if the FDIC determines that acceptance of such deposits would not constitute an unsafe or unsound banking practice with respect to the bank. These restrictions could materially and adversely affect our ability to access lower costs funds and thereby decrease our future earnings capacity.

Our financial flexibility could be severely constrained if we are unable to renew our wholesale funding or if adequate financing is not available in the future at acceptable rates of interest. We may not have sufficient liquidity to continue to fund new loan originations and we may need to liquidate loans or other assets unexpectedly in order to repay obligations as they mature. Our inability to obtain regulatory consent to accept or renew brokered deposits could have a material adverse effect on our business, financial condition, results of operations, cash flows and/or future prospects

and our ability to continue as a going concern.
Finally, the capital classification of a bank affects the frequency of examinations of the bank, the deposit insurance premiums paid by such bank and the ability of the bank to engage in certain activities, all of which could have a material adverse effect on our business, financial condition, results of operations, cash flows and/or future prospects. Under FDICIA, the FDIC is required to conduct a full-scope, on-site examination of every bank at least once every twelve (12) months.

Our decisions regarding credit risk could be inaccurate and our allowance for loan losses may be inadequate, which could materially and adversely affect our business, financial condition, results of operations, cash flows and/or future prospects.

Our loan portfolio subjects us to credit risk. Inherent risks in lending also include fluctuations in collateral values and economic downturns. Making loans is an essential element of our business and there is a risk that our loans will not be repaid.

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We attempt to maintain an appropriate allowance for loan losses to provide for estimated probable credit losses inherent in our loan portfolio. As of December 31, 2018, our allowance for loan losses totaled $13.0 million, which represents approximately 0.77% of our total loans. There is no precise method of predicting loan losses and therefore, we always face the risk that losses in future periods will exceed our allowance for loan losses and that we would need to make additional provisions to our allowance for loan losses. Our methodology for the determination of the adequacy of the allowance for loan losses is set forth in Note 8 of the accompanying consolidated financial statements.

The FDIC and the West Virginia Division of Financial Institutions review our allowance for loan and lease losses and may require us to establish additional allowances. Additions to the allowance for loan and lease losses will result in a decrease in our net earnings and capital and could hinder our ability to grow our assets.

We do business with other financial institutions that could experience financial difficulty.

We do business through check clearing and the purchase and sale of loan participations with other financial institutions. Because these financial institutions have many risks, as do we, we could be adversely affected should one of these financial institutions experience significant financial difficulties or fail to comply with our agreements with them.

We may elect or be compelled to seek additional capital in the future, but capital may not be available when it is needed.

We are required by federal and state regulatory authorities to maintain adequate levels of capital to support our operations. In addition, we may elect to raise additional capital to support our business or to finance acquisitions, if any, or we may otherwise elect to raise additional capital. Our ability to raise additional capital, if needed, will depend on conditions in the capital markets, economic conditions and a number of other factors, many of which are outside our control and on our financial performance. Accordingly, we cannot be assured of our ability to raise additional capital, if needed or on terms acceptable to us. If we cannot raise additional capital when needed, it may have a material adverse effect on our financial condition, results of operations and prospects.

We rely on funding sources to meet our liquidity needs, such as brokered deposits and FHLB borrowings, which are generally more sensitive to changes in interest rates and can be adversely affected by general economic conditions.

We have frequently utilized, as a source of funds, certificates of deposit obtained through third parties that solicit funds from their customers for deposit with us, or brokered deposits. Brokered deposits, when compared to retail deposits attracted through a branch network, are generally more sensitive to changes in interest rates and volatility in the capital markets and could reduce our net interest spread and net interest margin. In addition, brokered deposit funding sources may be more sensitive to significant changes in our financial condition. As of December 31, 2018, brokered deposits totaled $220.5 million, or approximately 13.5% of our total deposits, compared to brokered deposits in the amount of $216.9 million or approximately 13.6% of our total deposits at December 31, 2017. As of December 31, 2018, approximately $73.0 million in brokered deposits, or approximately 33.1% of our total brokered deposits, mature within one year. Our ability to continue to acquire brokered deposits is subject to our ability to price these deposits at competitive levels, which may increase our funding costs and the confidence of the market. In addition, if our capital ratios fall below the levels necessary to be considered “well capitalized” under current regulatory guidelines, we could be restricted from using brokered deposits as a funding source.

We also have borrowings with the Federal Home Loan Bank of Pittsburgh, or the FHLB. As of December 31, 2018, our FHLB borrowings maturing within one year totaled $304.0 million. If we were unable to borrow from the FHLB in the future, we may be required to seek higher cost funding sources, which could materially and adversely affect our net interest income.

One aspect of our liquidity management process is establishing contingent liquidity funding plans under various scenarios in order to prepare for unexpected liquidity shortages or events. Page 40 of Management's Discussion and Analysis of Financial Condition and Results of Operations shows three "stressed" liquidity circumstances and our related contingency plans with respect to each.

We pursue a strategy of supplementing internal growth by acquiring other financial companies or their assets and liabilities that we believe will help us fulfill our strategic objectives and enhance our earnings. There are risks associated with this strategy.

As part of our general growth strategy, we have partially expanded our business through acquisitions. We completed the acquisition of Peoples Bankshares, Inc. ("Peoples") on January 1, 2019, the First Century Bankshares, Inc. ("FCB") acquisition in April 2017 and the acquisition of Highland County Bankshares, Inc. ("HCB") in October 2016. Although our business strategy emphasizes organic expansion, we continue, from time to time in the ordinary course of business, to engage in preliminary discussions with potential acquisition targets. There can be no assurance that, in the future, we will successfully identify suitable acquisition candidates, complete acquisitions and successfully integrate acquired operations into our existing operations or expand into new markets. The consummation of any future acquisitions may dilute shareholder value or may have an adverse effect upon our operating results while the operations of the acquired business are being integrated into our operations. In addition, once integrated, acquired operations may not achieve levels of profitability comparable to those achieved by our existing operations, or otherwise perform as expected. Further, transaction-related expenses may adversely affect our earnings. These adverse effects on our earnings and results of operations may have a negative impact on the value of our common stock. Acquiring banks, bank branches or other businesses involves risks commonly associated with acquisitions, including:

- We may be exposed to potential asset quality issues or unknown or contingent liabilities of the banks, businesses, assets, and liabilities we acquire. If these issues or liabilities exceed our estimates, our results of operations and financial condition may be materially negatively affected;
- Prices at which acquisitions can be made fluctuate with market conditions. We have experienced times during which acquisitions could not be made in specific markets at prices we considered acceptable and expect that we will experience this condition in the future;
- The acquisition of other entities generally requires integration of systems, procedures and personnel of the acquired entity into our company to make the transaction economically successful. This integration process is complicated and time consuming and can also be disruptive to the customers of the acquired business. If the integration process is not conducted successfully and with minimal effect on the acquired business and its customers, we may not realize the anticipated economic benefits of particular acquisitions within the expected time frame, and we may lose customers or employees of the acquired business. We may also experience greater than anticipated customer losses even if the integration process is successful.
- To the extent our costs of an acquisition exceed the fair value of the net assets acquired, the acquisition will generate goodwill. As discussed below, we are required to assess our goodwill for impairment at least annually, and any goodwill impairment charge could have a material adverse effect on our results of operations and financial condition; and
- To finance an acquisition, we may borrow funds, thereby increasing our leverage and diminishing our liquidity, or issue additional shares, which could dilute the interests of our existing stockholders.

The value of our goodwill and other intangible assets may decline.

Goodwill and other intangible assets are subject to a decline, perhaps even significantly, for several reasons including if there is a significant decline in our expected future cash flows, change in the business environment, or a material and sustained decline in the market value of our stock, which may require us to take future charges related to the impairment of that goodwill and other intangible assets in the future, which could have a material adverse effect on our financial condition and results of our operations.

We operate in a very competitive industry and market.

We face aggressive competition not only from banks, but also from other financial services companies, including finance companies and credit unions and, to a limited degree, from other providers of financial services, such as money market mutual funds, brokerage firms and consumer finance companies. A number of competitors in our market areas are larger than we are and have substantially greater access to capital and other resources, as well as larger lending limits and branch systems and offer a wider array of banking services. Many of our non-bank competitors are not subject to the same extensive regulations that govern us. As a result, these non-bank competitors have advantages over us in providing certain services. Our profitability depends upon our ability to attract loans and deposits. There is a risk that aggressive competition could result in our controlling a smaller share of our markets. A decline in market share could adversely affect our results of operations and financial condition.

We are subject to environmental liability risk associated with lending activities.

A significant portion of our loan portfolio is secured by real property. During the ordinary course of business, we may foreclose on and take title to properties securing certain loans. In doing so, there is a risk that hazardous or toxic substances could be found on those properties. If hazardous or toxic substances are found, we may be liable for remediation costs, as well as for personal injury and property damage. Environmental laws may require us to incur substantial expenses and may materially reduce the affected property's value or limit our ability to use or sell the affected property. In addition, future laws or more stringent interpretations or enforcement policies with respect to existing laws may increase our exposure to environmental liability. The remediation costs and any other financial liabilities associated with an environmental hazard could have a material adverse effect on our financial condition and results of operations.

Changes in interest rates could negatively impact our future earnings.

Changes in interest rates could reduce income and cash flow. Our income and cash flow depend primarily on the difference between the interest earned on loans and investment securities and the interest paid on deposits and other borrowings. Interest rates are beyond our control and they fluctuate in response to general economic conditions and the policies of various governmental and regulatory agencies, in particular, the FRB. Changes in monetary policy, including changes in interest rates, will influence loan originations, purchases of investments, volumes of deposits and rates received on loans and investment securities and paid on deposits. Our results of operations may be adversely affected by increases or decreases in interest rates or by the shape of the yield curve.

The repeal of Federal prohibitions on payment of interest on demand deposits could increase our interest expense as interest rates rise.

All federal prohibitions on the ability of financial institutions to pay interest on demand deposit accounts were repealed as part of the Dodd-Frank Act. We do not yet know what interest rates other institutions may offer as market interest rates begin to increase. Our interest expense will increase and our net interest margin will decrease if we begin offering interest on demand deposits to attract additional customers or maintain current customers, which could have a material adverse effect on our business, financial condition and results of operations.

We rely heavily on our management team and the unexpected loss of key officers could adversely affect our business, financial condition, results of operations, cash flows and/or future prospects.

Our success has been and will continue to be greatly influenced by our ability to retain the services of existing senior management and, as we expand, to attract and retain qualified additional senior and middle management. Our senior executive officers have been instrumental in the development and management of our business. The loss of the services of any of our senior executive officers could have an adverse effect on our business, financial condition, results of operations, cash flows and/or future prospects.

Our business may be adversely affected by increasing prevalence of fraud and other financial crimes.

As a financial institution, we are subject to risk of loss due to fraud and other financial crimes. Nationally, reported incidents of fraud and other financial crimes have increased. We believe we have controls in place to detect and prevent such losses but in some cases multi-party collusion or other sophisticated methods of hiding fraud, may not be readily detected or detectable, and could result in losses that affect our financial condition and results of our operations.

Financial crime is not limited to the financial services industry. Our customers could experience fraud in their businesses, which could materially impact their ability to repay their loans, and deposit customers in all financial institutions are constantly and unwittingly solicited by others in fraud schemes that vary from easily detectable and obvious attempts to high-level and very complex international schemes that could drain an account of a significant amount and require detailed financial forensics to unravel. While we have controls in place, contractual agreements with our customers partitioning liability, and insurance to help mitigate the risk, none of these are guarantees that we will not experience a loss, potentially a loss that could have a material adverse effect on our financial condition, reputation and results of our operations.

Our information systems may experience failure, interruption or breach in security.

In the ordinary course of business, we rely on electronic communications and information systems to conduct our operations and to store sensitive data. Any failure, interruption or breach in security of these systems could result in significant disruption to our operations. Information security breaches and cybersecurity-related incidents may include, but are not limited to, attempts to access information, including customer and company information, malicious code, computer viruses and denial of service attacks that could result in unauthorized access, misuse, loss or destruction of data (including confidential customer information), account takeovers, unavailability of service or other events. These types of threats may derive from human error, fraud or malice on the part of external or internal parties, or may result from accidental technological failure. Further, to access our products and services our customers may use computers and mobile devices that are beyond our security control systems. Our technologies, systems, networks and software and those of other financial institutions have been and are likely to continue to be, the target of cybersecurity threats and attacks, which may range from uncoordinated individual attempts to sophisticated and targeted measures directed at us. The risk of a security breach or disruption, particularly through cyber attack or cyber intrusion, has increased as the number, intensity and sophistication of attempted attacks and intrusions from around the world have increased.

Our business requires the collection and retention of large volumes of customer data, including personally identifiable information in various information systems that we maintain and in those maintained by third parties with whom we contract to provide data services. We also maintain important internal company data such as personally identifiable information about our employees and information relating to our operations. The integrity and protection of that customer and company data is important to us. Our collection of such customer and company data is subject to extensive regulation and oversight.

Our customers and employees have been and will continue to be, targeted by parties using fraudulent e-mails and other communications in attempts to misappropriate passwords, bank account information or other personal information or to introduce viruses or other malware through "Trojan horse" programs to our information systems and/or our customers' computers. Though we endeavor to mitigate these threats through product improvements, use of encryption and authentication technology and customer and employee education, such cyber attacks against us or our merchants and our third party service providers remain a serious issue. The pervasiveness of cybersecurity incidents in general and the risks of cyber crime are complex and continue to evolve. More generally, publicized information concerning security and cyber-related problems could inhibit the use or growth of electronic or web-based applications or solutions as a means of conducting commercial transactions.

Although we make significant efforts to maintain the security and integrity of our information systems and have implemented various measures to manage the risk of a security breach or disruption, there can be no assurance that our security efforts and measures will be effective or that attempted security breaches or disruptions would not be successful or damaging. Even the most well protected information, networks, systems and facilities remain potentially vulnerable because attempted security breaches, particularly cyber attacks and intrusions, or disruptions will occur in the future and because the techniques used in such attempts are constantly evolving and generally are not recognized until launched against a target and in some cases are designed not to be detected and, in fact, may not be detected. Accordingly, we may be unable to anticipate these techniques or to implement adequate security barriers or other preventative measures and thus it is virtually impossible for us to entirely mitigate this risk. While we maintain specific “cyber” insurance coverage, which would apply in the event of various breach scenarios, the amount of coverage may not be adequate in any particular case. Furthermore, because cyber threat scenarios are inherently difficult to predict and can take many forms, some breaches may not be covered under our cyber insurance coverage.

A security breach or other significant disruption of our information systems or those related to our customers, merchants and our third party vendors, including as a result of cyber attacks, could (i) disrupt the proper functioning of our networks and systems and therefore our operations and/or those of certain of our customers; (ii) result in the unauthorized access to and destruction, loss, theft, misappropriation or release of confidential, sensitive or otherwise valuable information of ours or our customers; (iii) result in a violation of applicable privacy, data breach and other laws, subjecting us to additional regulatory scrutiny and expose the us to civil litigation, governmental fines and possible financial liability; (iv) require significant management attention and resources to remedy the damages that result; or (v) harm our reputation or cause a decrease in the number of customers that choose to do business with us. The occurrence of any of the foregoing could have a material adverse effect on our business, financial condition and results of operations.

The negative economic effects caused by terrorist attacks, including cyber attacks, potential attacks and other destabilizing events, would likely contribute to the deterioration of the quality of our loan portfolio and could reduce our customer base, level of deposits and demand for our financial products, such as loans.

High inflation, natural disasters, acts of terrorism, including cyber attacks, an escalation of hostilities or other international or domestic occurrences and other factors could have a negative impact on the economy of the Mid-Atlantic regions in which we operate. An additional economic downturn in our markets would likely contribute to the deterioration of the quality of our loan portfolio by impacting the ability of our customers to repay loans, the value of the collateral securing loans and may reduce the level of deposits in our bank and the stability of our deposit funding sources. An additional economic downturn could also have a significant impact on the demand for our products and services. The cumulative effect of these matters on our results of operations and financial condition could be adverse and material.

We are dependent upon third parties for certain information system, data management and processing services and to provide key components of our business infrastructure.

We outsource certain information system and data management and processing functions to third party providers. These third party service providers are sources of operational and informational security risk to us, including risks associated with operational errors, information system interruptions or breaches and unauthorized disclosures of sensitive or confidential client or customer information. If third party service providers encounter any of these issues, or if we have difficulty communicating with them, we could be exposed to disruption of operations, loss of service or connectivity to customers, reputational damage and litigation risk that could have a material adverse effect on our results of operations or our business.

Third party vendors provide key components of our business infrastructure such as internet connections, network access and core application processing. While we have selected these third party vendors carefully, we do not control their actions.
These services must be available on a continuous and timely basis and be in compliance with any regulatory requirements. Failure to do so could substantially harm our business.
We often purchase services from vendors under agreements that typically can be terminated on a periodic basis. There can be no assurance, however, that vendors will be able to meet their obligations under these agreements or that we will be able to compel them to do so. Risks of relying on vendors include the following:

- If an existing agreement expires or a certain service is discontinued by a vendor, then we may not be able to continue to offer our customers the same breadth of products and our operating results would likely suffer unless we are able to find an alternate supply of a similar service.
- Agreements we may negotiate in the future may commit us to certain minimum spending obligations. It is possible that we will not be able to create the market demand to meet such obligations.
- If market demand for our products increases suddenly, our current vendors might not be able to fulfill our commercial needs, which would require us to seek new arrangements or new sources of supply and may result in substantial delays in meeting market demand.
- We may not be able to control or adequately monitor the quality of services we receive from our vendors. Poor quality services could damage our reputation with our customers.

Potential problems with vendors such as those discussed above could have a significant adverse effect on our business, lead to higher costs and damage our reputation with our customers and, in turn, have a material adverse effect on our financial condition and results of operations.
Changes in accounting standards could impact reported earnings.

The accounting standard setting bodies, including the Financial Accounting Standards Board and other regulatory bodies, periodically change the financial accounting and reporting standards affecting the preparation of financial statements. These changes are not within our control and could materially impact our financial statements.

Our business is dependent on technology and our inability to invest in technological improvements may adversely affect our results of operations, financial condition and cash flows.

The financial services industry is undergoing rapid technological changes with frequent introductions of new technology-driven products and services. In addition to better serving customers, the effective use of technology increases efficiency and enables financial institutions to reduce costs. Our future success depends in part upon our ability to address the needs of our customers by using technology to provide products and services that will satisfy customer demands for convenience, as well as create additional efficiencies in its operations. Many of our competitors have substantially greater resources to invest in technological improvements. We may not be able to effectively implement new technology-driven products and services or be successful in marketing these products and services to our customers, which may negatively affect our results of operations, financial condition and cash flows.

Our potential inability to integrate companies we may acquire in the future could have a negative effect on our expenses and results of operations.

On occasion, we may engage in a strategic acquisition when we believe there is an opportunity to strengthen and expand our business. To fully benefit from such acquisition, however, we must integrate the administrative, financial, sales, lending, collections and marketing functions of the acquired company. If we are unable to successfully integrate an acquired company, we may not realize the benefits of the acquisition and our financial results may be negatively affected. A completed acquisition may adversely affect our financial condition and results of operations, including our capital requirements and the accounting treatment of the acquisition. Completed acquisitions may also lead to significant unexpected liabilities after the consummation of these acquisitions.

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RISKS RELATING TO AN INVESTMENT IN OUR SECURITIES

Our ability to pay dividends is limited.

We are a separate and distinct legal entity from our subsidiaries. We receive substantially all of our revenue from dividends from our subsidiary bank, Summit Community. These dividends are the principal source of funds to pay dividends on our common stock and interest and principal on our debt. Various federal and/or state laws and regulations limit the amount of dividends that Summit Community may pay to Summit. Also, Summit's right to participate in a distribution of assets upon a subsidiary's liquidation or reorganization is subject to the prior claims of the subsidiary's creditors. In the event Summit Community is unable to pay dividends to us, we may not be able to service debt, pay obligations or pay dividends on our common stock. The inability to receive dividends from Summit Community could have a material adverse effect on our business, financial condition and results of operations.

Our stock price can be volatile.

Stock price volatility may make it more difficult for our shareholders to resell their common stock when they want and at prices they find attractive. Our stock price can fluctuate significantly in response to a variety of factors, including, but not limited to, general market fluctuations, industry factors and general economic and political conditions and events, interest rate changes, credit loss trends, or changes in government regulations.

The trading volume in our common stock is less than that of larger financial services companies.
Although our common stock is listed for trading on the NASDAQ, the trading volume in our common stock is less than that of larger financial services companies. A public trading market having the desired characteristics of depth, liquidity and orderliness depends on the presence in the marketplace of willing buyers and sellers of our common stock at any given time. This presence depends on the individual decisions of investors over which we have no control. Given the lower trading volume of our common stock, significant sales of our common stock, or the expectation of these sales, could cause our stock price to fluctuate.

Our executive officers and directors own shares of our common stock, allowing management to have an impact on our corporate affairs.

As of February 25, 2019 our executive officers and directors beneficially own 12.48% (computed in accordance with Exchange Act Rule 13d-3) of the outstanding shares of our common stock. Accordingly, these executive officers and directors will be able to impact the outcome of all matters required to be submitted to our shareholders for approval, including decisions relating to the election of directors, the determination of our day-to-day corporate and management policies and other significant corporate transactions.

There may be future sales of additional common stock or preferred stock or other dilution of our equity, which may adversely affect the market price of our common stock.

Our board of directors is authorized to cause us to issue additional classes or series of preferred shares without any action on the part of the shareholders. The board of directors also has the power, without shareholder approval, to set the terms of any such classes or series of preferred shares that may be issued, including voting rights, dividend rights and preferences over the common stock with respect to dividends or upon the liquidation, dissolution or winding-up of our business and other terms. If we issue preferred shares in the future that have a preference over the common stock with respect to the payment of dividends or upon liquidation, dissolution or winding-up, or if we issue preferred shares with voting rights that dilute the voting power of the common stock, the rights of holders of the common stock or the market price of the common stock could be adversely affected.

The market price of our common stock could decline as a result of sales of a large number of shares of common stock or preferred stock or similar securities in the market or the perception that such sales could occur.

Holders of our junior subordinated debentures have rights that are senior to those of our shareholders.

We have three statutory business trusts that were formed for the purpose of issuing mandatorily redeemable securities (the "capital securities") for which we are obligated to third-party investors and investing the proceeds from the sale of the capital securities in our junior subordinated debentures (the "debentures"). The debentures held by the trusts are their sole assets. Our subordinated debentures of these unconsolidated statutory trusts totaled approximately $19.6 million at December 31, 2018 and 2017.

Distributions on the capital securities issued by the trusts are payable quarterly, at the variable interest rates specified in those certain securities. The capital securities are subject to mandatory redemption, in whole or in part, upon repayment of the debentures.

Payments of the principal and interest on the trust preferred securities of the statutory trusts are conditionally guaranteed by us. The junior subordinated debentures are senior to our shares of common stock. As a result, we must make payments on the junior subordinated debentures before any dividends can be paid on our common stock and, in the event of our bankruptcy, dissolution or liquidation, the holders of the junior subordinated debentures must be satisfied before any distributions can be made on our common stock. We have the right to defer distributions on the junior subordinated debentures (and the related trust preferred securities) for up to five (5) years, during which time no dividends may be paid on our common stock. In 2018, our total interest payments on these junior subordinated debentures approximated $875,000. Based on current rates, our quarterly interest payment obligation on our junior subordinated debentures is approximately $244,000.

The capital securities held by our three trust subsidiaries qualify as Tier 1 capital under FRB guidelines. In accordance with these guidelines, trust preferred securities generally are limited to twenty-five percent (25%) of Tier 1 capital elements, net of goodwill. The amount of trust preferred securities and certain other elements in excess of the limit can be included in Tier 2 capital.

Provisions of our amended and restated articles of incorporation could delay or prevent a takeover of us by a third party.

Our amended and restated articles of incorporation could delay, defer or prevent a third party from acquiring us, despite the possible benefit to our shareholders, or could otherwise adversely affect the price of our common stock. For example, our amended and restated articles of incorporation contain advance notice requirements for nominations for election to our Board of Directors. We also have a staggered board of directors, which means that only one-third (1/3) of our Board of Directors can be replaced by shareholders at any annual meeting.

OTHER RISKS

Additional factors could have a negative effect on our financial performance and the value of our common stock. These factors include, but are not limited to, general economic and financial market conditions, continuing consolidation in the financial services industry, new litigation or changes in existing litigation, regulatory actions and losses.

Item 1B. Unresolved Staff Comments

Not applicable.

Item 2. Properties

Our principal executive office is located at 300 North Main Street, Moorefield, West Virginia, in a building owned by Summit Community. Summit Community's headquarters and branch locations occupy offices which are either owned or operated under lease arrangements. At December 31, 2018, Summit Community operated 30 banking offices. Summit Insurance Services, LLC operates out of the Moorefield, West Virginia and Leesburg, Virginia, offices of Summit Community.

	Number of Offices		
Office Location	Owned	Leased	Total
Summit Community Bank			
Moorefield, West Virginia	1	—	1
Mathias, West Virginia	1	—	1
Franklin, West Virginia	1	—	1
Petersburg, West Virginia	1	—	1
Charleston, West Virginia	2	—	2
Rainelle, West Virginia	1	—	1
Rupert, West Virginia	1	—	1
Winchester, Virginia	1	1	2
Leesburg, Virginia	1	—	1
Harrisonburg, Virginia	1	1	2
Warrenton, Virginia	—	1	1
Martinsburg, West Virginia	1	—	1
Monterey, Virginia	1	—	1
Hot Springs, Virginia	1	—	1
Churchville, Virginia	—	1	1
Bluefield, West Virginia	2	—	2
Princeton, West Virginia	2	—	2
Oceana, West Virginia	1	—	1
Pineville, West Virginia	1	—	1
Bluefield, Virginia	1	—	1
Wytheville, Virginia	1	—	1
Max Meadows, Virginia	1	—	1
Hinton, West Virginia	1	—	1
Beckley, West Virginia	1	—	1
Christiansburg, Virginia	—	1	1

We believe that the premises occupied by us and our subsidiaries generally are well located and suitably equipped to serve as financial services facilities. See Notes 9 and 10 of our consolidated financial statements beginning on page 75.

Item 3. Legal Proceedings

Information required by this item is set forth under the caption "Legal Contingencies" in Note 17 of our consolidated financial statements beginning on page 84.

Item 4. Mine Safety Disclosures

Not applicable.

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PART II.

Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

Common Stock Dividend and Market Price Information: Our stock trades on the NASDAQ Capital Market under the symbol “SMMF.”

As of February 22, 2019, there were approximately 1,184 shareholders of record of Summit’s common stock.

Purchases of Summit Equity Securities: We have an Employee Stock Ownership Plan (“ESOP”), which enables eligible employees to acquire shares of our common stock. The cost of the ESOP is borne by us through annual contributions to an Employee Stock Ownership Trust in amounts determined by the Board of Directors.

In September 2018, the Board of Directors authorized the open market repurchase of up to 500,000 shares of the issued and outstanding shares of Summit's common stock ("September 2018 Repurchase Plan"). The timing and quantity of purchases under this stock repurchase plan are at the discretion of management. The plan will expire December 31, 2019, but may be discontinued, suspended, or restarted at any time at the Company's discretion.

The following table sets forth certain information regarding Summit’s purchase of its common stock under the Repurchase Plan for the quarter ended December 31, 2018.

Period	Total Number of Shares Purchased (a)	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares that May Yet be Purchased Under the Plans or Programs
October 1, 2018 - October 31, 2018	—	$ ——		—
November 1, 2018 - November 30, 2018	41,423	20.80	41,423	458,577
December 1, 2018 - December 31, 2018	41,000	20.00	41,000	417,577

(a) Shares purchased under the September 2018 Repurchase Plan.

Performance Graph: Set forth below is a line graph comparing the cumulative total return of Summit's common stock assuming reinvestment of dividends, with that of the NASDAQ Composite Index ("NASDAQ Composite"), and the SNL Small Cap U.S. Bank Index for the five year period ending December 31, 2018.

The cumulative total shareholder return assumes a $100 investment on December 31, 2013 in the common stock of Summit and each index and the cumulative return is measured as of each subsequent fiscal year-end. There is no assurance that Summit's common stock performance will continue in the future with the same or similar trends as depicted in the graph.

	For the Year Ended					
Index	12/31/2013	12/31/2014	12/31/2015	12/31/2016	12/31/2017	12/31/2018
Summit Financial Group, Inc.	100.00	120.08	123.23	291.79	284.34	213.35
NASDAQ Composite	100.00	114.75	122.74	133.62	173.22	168.30
SNL Small Cap U.S. Bank	100.00	105.40	115.43	163.66	171.65	153.83

The Stock Performance Graph and related information shall not be deemed "soliciting material" or to be "filed" with the Securities and Exchange Commission, nor shall such information be incorporated by reference into any future filing under the Securities Act of 1933 or Securities Exchange Act of 1934, each as amended, except to the extent that Summit specifically incorporates it by reference into such filing.

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Item 6. Selected Financial Data

The following consolidated selected financial data is derived from our audited financial statements as of and for each of the five (5) years ended December 31, 2018. The selected financial data should be read in conjunction with Management's Discussion and Analysis of Financial Condition and Results of Operations and the Consolidated Financial Statements and related notes contained elsewhere in this report.

	For the Year Ended (unless otherwise noted)				
Dollars in thousands, except per share amounts	2018	2017	2016	2015	2014
Summary of Operations					
Interest income	$95,409	$84,527	$64,091	$58,883	$57,626
Interest expense	25,612	18,380	15,084	12,867	15,241
Net interest income	69,797	66,147	49,007	46,016	42,385
Provision for loan losses	2,250	1,250	500	1,250	2,250
Net interest income after provision for loan losses	67,547	64,897	48,507	44,766	40,135
Noninterest income	17,422	14,427	11,600	11,861	11,223
Noninterest expense	49,873	57,745	34,802	33,632	35,324
Income before income taxes	35,096	21,579	25,305	22,995	16,034
Income tax expense	7,024	9,664	8,008	6,893	4,678
Net income	28,072	11,915	17,297	16,102	11,356
Dividends on preferred shares	—	—	—	—	771
Net income applicable to common shares	$28,072	$11,915	$17,297	$16,102	$10,585
Balance Sheet Data (at year end)					
Assets	$2,200,586	$2,134,240	$1,758,647	$1,492,429	$1,443,568
Debt securities available for sale	293,147	328,586	266,405	280,715	282,827
Loans, net	1,682,005	1,593,744	1,307,862	1,079,331	1,019,842
Deposits	1,634,826	1,600,601	1,295,519	1,066,709	1,061,314
Short-term borrowings	309,084	250,499	224,461	171,394	123,633
Long-term borrowings	735	45,751	46,670	75,581	77,490
Shareholders' equity	219,830	201,505	155,360	143,744	131,644
Credit Quality					
Net loan charge-offs	$1,768	$359	$298	$945	$3,742
Nonperforming assets	36,462	36,861	39,090	41,340	50,244
Allowance for loan losses	13,047	12,565	11,674	11,472	11,167
Per Share Data					
Earnings per share					
Basic earnings	$2.27	$1.00	$1.62	$1.56	$1.40
Diluted earnings	2.26	1.00	1.61	1.50	1.17
Book value per common share (at year end) (A)	17.85	16.30	14.47	13.48	12.60
Tangible book value per common share (at year end) (A)	15.75	14.08	13.20	12.78	11.86
Cash dividends	$0.53	$0.44	$0.40	$0.32	$—
Performance Ratios					
Return on average equity	13.43 %	6.40 %	11.53 %	11.62 %	9.54 %
Return on average tangible equity	16.09 %	8.01 %	12.38 %	12.39 %	10.37 %
Return on average assets	1.32 %	0.59 %	1.08 %	1.10 %	0.80 %

Equity to assets	10.0 %	9.4 %	8.8 %	9.6 %	9.1 %
Tangible equity to tangible assets	8.9 %	8.3 %	8.1 %	9.2 %	8.6 %
Tangible common equity to tangible assets	8.9 %	8.3 %	8.1 %	9.2 %	8.0 %
Dividend payout ratio	23.3 %	44.0 %	24.7 %	21.1 %	— %

(A)- Assumes conversion of outstanding convertible preferred stock in 2014.

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Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

FORWARD LOOKING STATEMENTS

This annual report contains comments or information that constitute forward looking statements (within the meaning of the Private Securities Litigation Act of 1995) that are based on current expectations that involve a number of risks and uncertainties. Words such as “expects”, “anticipates”, “believes”, “estimates” and other similar expressions or future or conditional verbs such as “will”, “should”, “would” and “could” are intended to identify such forward-looking statements. The Private Securities Litigation Act of 1995 indicates that the disclosure of forward-looking information is desirable for investors and encourages such disclosure by providing a safe harbor for forward-looking statements by us. In order to comply with the terms of the safe harbor, we note that a variety of factors could cause our actual results and experience to differ materially from the anticipated results or other expectations expressed in those forward-looking statements.

Although we believe the expectations reflected in such forward looking statements are reasonable, actual results may differ materially. Factors that might cause such a difference include changes in interest rates and interest rate relationships; demand for products and services; the degree of competition by traditional and non-traditional competitors; changes in banking laws and regulations; changes in tax laws; the impact of technological advances; the outcomes of contingencies; trends in customer behavior as well as their ability to repay loans; and changes in the national and local economy.

DESCRIPTION OF BUSINESS

We are a $2.20 billion community-based financial services company providing a full range of banking and other financial services to individuals and businesses through our three operating segments: community banking, trust and wealth management and insurance. Our community bank, Summit Community Bank, Inc. has a total of 33 banking offices located in West Virginia and Virginia. Our trust and wealth management division offers trust services and other non-bank financial products principally within our community bank's market area. In addition, we also operate Summit Insurance Services, LLC in Moorefield, West Virginia and Leesburg, Virginia, which provides insurance brokerage services to individuals and businesses covering corporate and personal property and casualty insurance products, as well as group health and life insurance products and consulting services. See Note 19 of the accompanying consolidated financial statements for our segment information. Summit Financial Group, Inc. employs approximately 371 full time equivalent employees.

OVERVIEW

Our primary source of income is net interest income from loans and deposits. Business volumes tend to be influenced by the overall economic factors including market interest rates, business spending and consumer confidence, as well as competitive conditions within the marketplace.

Key Items in 2018

- Our earnings per diluted share increased from $1.00 in 2017 to $2.26 in 2018.
- Our return on average equity and return on average tangible equity increased from 6.40% to 13.43% and 8.01% to 16.09%, respectively.
- 2018 net income was $28.07 million ($2.26 per diluted share) compared to $11.92 million ($1.00 per diluted share) in 2017. 2017 earnings were negatively impacted by a $9.9 million (or $6.2 million after-tax or $0.52 per diluted share) litigation settlement charge and a $3.5 million ($0.29 per diluted share) tax charge due to enactment of the Tax Cuts and Jobs Act ("TCJA").
- Net interest margin decreased 10 basis points in 2018, principally due to a 37 basis point increase in funding costs compared to a 21 basis point increase in our yield on interest earning assets.

- Net revenues increased $6.6 million, or 8.2 percent during 2018 primarily as result of the First Century Bankshares, Inc. ("FCB") acquisition.
- We achieved loan growth, excluding mortgage warehouse lines of credit, of 5.1 percent, or $80.4 million during 2018.
- Nonperforming assets declined to their lowest level since 2008, representing 1.66 percent of total assets at year end 2018 compared to 1.73 percent at the prior year end.
- During 2018, provisions for loan losses increased by $1.0 million, primarily due to higher levels of loan net charge-offs during 2018 and loan growth.

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- Cash dividends paid on our common stock in 2018 totaled $0.53 per share compared to $0.44 paid per share in 2017.
- On July 24, 2018, we entered into a Definitive Merger Agreement with Mullens, West Virginia-based Peoples Bankshares, Inc. ("Peoples") and its subsidiary, First Peoples Bank. The transaction closed on January 1, 2019. At consummation, Peoples had total assets of $133.1 million, loans of $42.3 million and deposits of $112.9 million.

OUTLOOK

The year just concluded represents another significant milestone relative to Summit's goal to be a consistent growth, high-performing community banking institution. Our solid lending activity and strong core operating performance of the past year offer significant evidence of our progress. In addition, our acquisition strategy continued to present us with significant opportunities for ongoing performance enhancement. Looking forward to 2019, while we could be challenged by a variety of potential economic uncertainties, we anticipate sustaining our recent positive trends with respect to: revenue growth, loan portfolio growth, a relatively stable net interest margin, low overhead, and reductions in overall levels of problem assets.

CRITICAL ACCOUNTING POLICIES

Our consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States of America and follow general practices within the financial services industry. Application of these principles requires us to make estimates, assumptions and judgments that affect the amounts reported in our financial statements and accompanying notes. These estimates, assumptions and judgments are based on information available as of the date of the financial statements; accordingly, as this information changes, the financial statements could reflect different estimates, assumptions and judgments. Certain policies inherently have a greater reliance on the use of estimates, assumptions and judgments and as such have a greater possibility of producing results that could be materially different than originally reported.

Our most significant accounting policies are presented in the notes to the accompanying consolidated financial statements. These policies, along with the other disclosures presented in the financial statement notes and in this financial review, provide information on how significant assets and liabilities are valued in the financial statements and how those values are determined.

Based on the valuation techniques used and the sensitivity of financial statement amounts to the methods, assumptions and estimates underlying those amounts, we have identified the determination of the allowance for loan losses, the valuation of goodwill, fair value measurements, accounting for acquired loans and deferred tax assets to be the accounting areas that require the most subjective or complex judgments and as such could be most subject to revision as new information becomes available.

Allowance for Loan Losses: The allowance for loan losses represents our estimate of probable credit losses inherent in the loan portfolio. Determining the amount of the allowance for loan losses is considered a critical accounting estimate because it requires significant judgment and the use of estimates related to the amount and timing of expected future cash flows on impaired loans, estimated losses on pools of homogeneous loans based on historical loss experience and consideration of current economic trends and conditions, all of which may be susceptible to significant change. The loan portfolio also represents the largest asset type on our consolidated balance sheet. To the extent actual outcomes differ from our estimates, additional provisions for loan losses may be required that would negatively impact earnings in future periods. Note 8 to the accompanying consolidated financial statements describes the methodology used to determine the allowance for loan losses and a discussion of the factors driving changes in the amount of the allowance for loan losses is included in the Asset Quality section of this financial review.

Goodwill: Goodwill is subject to an analysis by reporting unit at least annually by comparing the fair value of a reporting unit with its carrying amount to determine whether write-downs of the recorded balances are necessary. An entity still has the option to perform a qualitative assessment for a reporting unit to determine if a quantitative impairment test is necessary. If the fair value is less than the carrying value, an expense may be required on our books to write down the goodwill to the proper carrying value.

We cannot assure you that future goodwill impairment tests will not result in a charge to earnings. See Note 11 of the accompanying consolidated financial statements for further discussion of our intangible assets, which include goodwill.

Fair Value Measurements: Fair value is based upon the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants, including, but not limited to, property held for sale, impaired loans and derivatives. Based on the observability of the inputs used in the valuation techniques, we classify our financial assets and liabilities measured and disclosed at fair value in accordance with a three-level hierarchy (e.g., Level 1, Level 2 and Level 3) . Fair value determination requires that we make a number of significant judgments. In determining the fair value of financial instruments, we use market prices of the same or similar instruments whenever such prices are available. We do not use prices involving distressed sellers in determining fair value. If observable market prices are unavailable or impracticable to obtain, then fair value is estimated using modeling techniques such as discounted cash flow analyses. These modeling techniques incorporate our assessments regarding assumptions that market participants would use in pricing the asset or the liability, including assumptions about the risks inherent in a particular valuation technique and the risk of nonperformance.

Fair value is used on a recurring basis for certain assets and liabilities in which fair value is the primary basis of accounting. Additionally, fair value is used on a non-recurring basis to evaluate assets or liabilities for impairment or for disclosure purposes.

Accounting for Acquired Loans: Loans acquired are initially recorded at their acquisition date fair values. The fair value of the acquired loans are based on the present value of the expected cash flows, including principal, interest and prepayments. Periodic principal and interest cash flows are adjusted for expected losses and prepayments, then discounted to determine the present value and summed to arrive at the estimated fair value. Fair value estimates involve assumptions and judgments as to credit risk, interest rate risk, prepayment risk, liquidity risk, default rates, loss severity, payment speeds, collateral values and discount rate.

Acquired loans are divided into loans with evidence of credit quality deterioration (acquired impaired) and loans that do not meet this criteria (acquired performing). Acquired impaired loans have experienced a deterioration of credit quality from origination to acquisition for which it is probable that we will be unable to collect all contractually required payments receivable, including both principal and interest. In the assessment of credit quality, numerous assumptions, interpretations and judgments must be made, based on internal and third-party credit quality information and ultimately the determination as to the probability that all contractual cash flows will not be able to be collected. This is a point in time assessment and inherently subjective due to the nature of the available information and judgment involved.

Subsequent to the acquisition date, we continue to estimate the amount and timing of cash flows expected to be collected on acquired impaired loans. Increases in expected cash flows will generally result in a recovery of any previously recorded allowance for loan losses, to the extent applicable, and/or a reclassification from the nonaccretable difference to accretable yield, which will be recognized prospectively. The present value of any decreases in expected cash flows after the acquisition date will generally result in an impairment charge recorded as a provision for loan losses, resulting in an increase to the allowance for loan losses.

For acquired performing loans, the difference between the acquisition date fair value and the contractual amounts due at the acquisition date represents the fair value adjustment. Fair value adjustments may be discounts (or premiums) to a loan’s cost basis and are accreted (or amortized) to interest income over the loan’s remaining life using the level yield method. Subsequent to the acquisition date, the methods utilized to estimate the required allowance for loan losses for these loans is similar to originated loans.

See Note 3 and Note 7 of the accompanying consolidated financial statements for additional information regarding our acquired loans.

BUSINESS SEGMENT RESULTS

We are organized and managed along three major business segments, as described in Note 19 of the accompanying consolidated financial statements. The results of each business segment are intended to reflect each segment as if it were a stand alone business. Net income by segment follows:

Dollars in thousands	2018	2017	2016

Community banking	$28,701	$12,365	$18,314
Trust and wealth management	417	95	21
Insurance services	461	514	169
Parent	(1,507)	(1,059)	(1,207)
Consolidated net income	$28,072	$11,915	$17,297

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RESULTS OF OPERATIONS

Earnings Summary

Net income increased 135.6% during 2018 to $28.1 million, compared to $11.9 million in 2017, which was 31.1% less than 2016's $17.3 million. Net income was $2.26, $1.00 and $1.61 per diluted share for 2018, 2017 and 2016, respectively, representing a 126.0% increase in 2018 and a 37.9% decrease in 2017. Return on average equity was 13.43% in 2018 compared to 6.40% in 2017 and 11.53% in 2016. Return on average assets for the year ended December 31, 2018 was 1.32% compared to 0.59% in 2017 and 1.08% in 2016.

Included in 2017's net income were a $9.9 million pre-tax ($6.2 million after-tax or $0.52 per diluted share) litigation settlement charge, $3.5 million ($0.29 per diluted share) preliminary income tax charge due to enactment of the TCJA, and $1.6 million ($0.08 per diluted share) of merger related expenses. A summary of the significant factors influencing our results of operations and related ratios is included in the following discussion.

2018 net income was positively impacted by higher net interest income of $3.7 million (or $0.29 per diluted share), $790,000 growth in trust and wealth management fees ($0.06 per diluted share), $522,000 increased deposit account-related fees ($0.08 per diluted share) and $2.6 million ($0.25 per diluted share) in lower income tax expense as result of TCJA's lower income tax rates. Excluding 2017's litigation charge, higher total noninterest expense of $2.0 million ($0.16 per diluted share) partially offset these positive impacts.

Net Interest Income

The major component of our net earnings is net interest income, which is the excess of interest earned on earning assets over the interest expense incurred on interest bearing sources of funds. Net interest income is affected by changes in volume, resulting from growth and alterations of the balance sheet's composition, fluctuations in interest rates and maturities of sources and uses of funds. We seek to maximize net interest income through management of our balance sheet components. This is accomplished by determining the optimal product mix with respect to yields on assets and costs of funds in light of projected economic conditions, while maintaining portfolio risk at an acceptable level.

Net interest income on a fully tax equivalent basis, average balance sheet amounts and corresponding average yields on interest earning assets and costs of interest bearing liabilities for the years 2014 through 2018 are presented in Table I. Table II presents, for the periods indicated, the changes in interest income and expense attributable to (a) changes in volume (changes in volume multiplied by prior period rate) and (b) changes in rate (change in rate multiplied by prior period volume). Changes in interest income and expense attributable to both rate and volume have been allocated between the factors in proportion to the relationship of the absolute dollar amounts of the change in each.

Net interest income on a fully tax equivalent basis totaled $71.1 million, $68.6 million and $50.6 million for the years ended December 31, 2018, 2017 and 2016, respectively, representing an increase of 3.7% in 2018 and 35.5% in 2017. During 2018, 2017 and 2016, the volumes of both interest earning assets and interest bearing liabilities increased.

During 2018, our earnings on interest earning assets increased $9.7 million due to both higher volumes and higher yields, while the cost of interest bearing liabilities increased $7.2 million due to higher cost of funds.

During 2017, our earnings on interest earning assets increased $21.3 million due to both higher volumes and higher yields, while the cost of interest bearing liabilities increased $3.3 million due to higher volumes of interest bearing deposits.

During 2016, our earnings on interest earning assets increased $5.3 million as the increase in earnings due to higher volumes, primarily loans, more than offset reductions in yield, while the cost of interest bearing liabilities increased $2.2 million primarily due to both higher cost of funds, principally on short-term borrowings, and higher volumes of interest bearing deposits.

Total average earning assets increased 6.4% to $1.99 billion for 2018 from $1.87 billion in 2017. Total average interest bearing liabilities increased 5.2% to $1.69 billion at December 31, 2018, compared to $1.60 billion at December 31, 2017.

Our net interest margin was 3.57% for 2018 compared to 3.67% and 3.39% for 2017 and 2016, respectively. Our net interest margin decreased 10 basis points during 2018 as the cost of funds increased 37 basis points while yields on interest earning assets increased 21 basis points. The 2018 increase in yields on interest earning assets was negatively impacted by lower taxable equivalent adjustments to interest earned on tax-exempt securities and loans as a result of enactment of the TCJA in late

2017, which lowered our statutory corporate Federal income tax rate effective January 1, 2018, from 35% to 21%. Our net interest margin increased 28 basis points in 2017 primarily due to the 25 basis point increase in yield on interest earning assets. See Tables I and II for further details regarding changes in volumes and rates of average assets and liabilities and how those changes affect our net interest income.

Assuming no significant unanticipated changes in market interest rates, we expect growth in our net interest income to continue over the near term primarily due to continuing expected growth in earning assets, primarily loans. We continue to monitor the net interest margin through net interest income simulation to minimize the potential for any significant negative impact.
See the "Market Risk Management" section for discussion of the impact changes in market interest rates could have on us. Further analysis of our yields on interest earning assets and interest bearing liabilities are presented in Tables I and II below.

Table I - Average Balances - Assets, Liabilities and Shareholders' Equity,
Interest Earnings & Expenses and Average Yields/Rates

	Average Balances				
Dollars in thousands	2018	2017	2016	2015	2014
ASSETS					
Interest earning assets					
Loans, net of unearned interest (1)					
Taxable	$1,626,725	$1,480,601	$1,177,445	$1,049,172	$984,723
Tax-exempt (2)	15,776	14,899	14,628	13,706	7,823
Securities					
Taxable	170,912	200,596	202,795	209,316	211,700
Tax-exempt (2)	136,913	129,342	79,571	77,280	81,549
Interest bearing deposits with other banks	38,148	43,400	19,211	8,878	9,325
	1,988,474	1,868,838	1,493,650	1,358,352	1,295,120
Noninterest earning assets					
Cash and due from banks	9,517	8,492	3,968	3,839	3,756
Premises and equipment	36,025	31,750	21,858	20,707	20,346
Other assets	107,856	109,456	90,957	94,996	112,504
Allowance for loan losses	(12,830)	(12,196)	(10,836)	(11,307)	(11,724)
Total assets	$2,129,042	$2,006,340	$1,599,597	$1,466,587	$1,420,002
LIABILITIES AND SHAREHOLDERS' EQUITY					
Liabilities					
Interest bearing liabilities					
Interest bearing demand deposits	$471,725	$358,225	$220,708	$208,160	$192,190
Savings deposits	320,184	363,949	306,312	255,186	238,340
Time deposits	621,659	609,156	491,652	481,732	513,110
Short-term borrowings	228,142	205,743	190,876	151,102	100,786
Long-term borrowings and subordinated debentures	44,132	65,629	92,343	99,805	142,213
	1,685,842	1,602,702	1,301,891	1,195,985	1,186,639
Noninterest bearing liabilities					
Demand deposits	218,541	200,707	128,894	116,995	104,262
Other liabilities	15,574	16,669	18,795	15,024	10,119
Total liabilities	1,919,957	1,820,078	1,449,580	1,328,004	1,301,020
Shareholders' equity - preferred	—	—	—	1,786	9,276
Shareholders' equity - common	209,085	186,262	150,017	136,797	109,706
Total shareholders' equity	209,085	186,262	150,017	138,583	118,982
Total liabilities and shareholders' equity	$2,129,042	$2,006,340	$1,599,597	$1,466,587	$1,420,002
Net Interest Earnings					
Net Interest Margin					

(1) For purposes of this table, nonaccrual loans are included in average loan balances. Included in interest and fees on loans are loan fees of $839,000, $998,000 and $528,000 for the years ended December 31, 2018, 2017 and 2016, respectively.

(2) For purposes of this table, interest income on tax-exempt securities and loans has been adjusted assuming a Federal tax rate of 21% for 2018 , 35% for 2017 and 34% for all other years presented. The taxable equivalent adjustment results in an increase in interest income of $1,280,000, $2,413,000, $1,589,000, $1,542,000 and $1,465,000 for the years ended December 31, 2018, 2017, 2016, 2015 and 2014 respectively.

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	Interest Earnings/Expense					Average Yield/Rate				
Dollars in thousands	2018	2017	2016	2015	2014	2018	2017	2016	2015	2014
ASSETS										
Interest earning assets										
Loans, net of unearned interest (1)										
Taxable	$84,716	$74,365	$56,439	$51,554	$50,078	5.21%	5.02%	4.79%	4.91%	5.09%
Tax-exempt (2)	718	835	820	779	533	4.55%	5.60%	5.61%	5.68%	6.81%
Securities										
Taxable	5,341	5,071	4,395	4,328	4,692	3.13%	2.53%	2.17%	2.07%	2.22%
Tax-exempt (2)	5,375	6,060	3,853	3,756	3,780	3.93%	4.69%	4.84%	4.86%	4.64%
Interest bearing deposits with other banks	539	609	173	8	8	1.41%	1.40%	0.90%	0.09%	0.09%
Total assets	96,689	86,940	65,680	60,425	59,091	4.86%	4.65%	4.40%	4.45%	4.56%
LIABILITIES AND SHAREHOLDERS' EQUITY										
Liabilities										
Interest bearing liabilities										
Interest bearing demand deposits	$4,205	$1,169	$376	$251	$222	0.89%	0.33%	0.17%	0.12%	0.12%
Savings deposits	3,233	2,563	2,296	1,781	1,580	1.01%	0.70%	0.75%	0.70%	0.66%
Time deposits	10,237	7,478	6,292	6,304	7,193	1.65%	1.23%	1.28%	1.31%	1.40%
Short-term borrowings	5,993	4,473	2,288	525	306	2.63%	2.17%	1.20%	0.35%	0.30%
Long-term borrowings subordinated debentures	1,944	2,697	3,832	4,007	5,940	4.40%	4.11%	4.15%	4.01%	4.18%
Total interest bearing liabilities	25,612	18,380	15,084	12,868	15,241	1.52%	1.15%	1.16%	1.08%	1.28%
Net Interest Earnings	$71,077	$68,560	$50,596	$47,557	$43,850					
Net Interest Margin						3.57%	3.67%	3.39%	3.50%	3.39%

Table II - Changes in Interest Margin Attributable to Rate and Volume

	2018 Versus 2017 Increase (Decrease) Due to Change in:			2017 Versus 2016 Increase (Decrease) Due to Change in:		
Dollars in thousands	Volume	Rate	Net	Volume	Rate	Net
Interest earned on						
Loans						
Taxable	$7,536	$2,815	$10,351	$15,117	$2,809	$17,926
Tax-exempt	47	(164)	(117)	15	—	15
Securities						
Taxable	(818)	1,088	270	(48)	724	676
Tax-exempt	340	(1,025)	(685)	2,336	(129)	2,207
Interest bearing deposits with other banks	(74)	4	(70)	302	134	436
Total interest earned on interest earning assets	7,031	2,718	9,749	17,722	3,538	21,260
Interest paid on						
Interest bearing demand deposits	469	2,567	3,036	321	472	793
Savings deposits	(337)	1,007	670	412	(145)	267
Time deposits	156	2,603	2,759	1,452	(266)	1,186
Short-term borrowings	522	998	1,520	191	1,994	2,185
Long-term borrowings and subordinated debentures	(935)	182	(753)	(1,099)	(36)	(1,135)
Total interest paid on interest bearing liabilities	(125)	7,357	7,232	1,277	2,019	3,296
Net interest income	$7,156	$(4,639)	$2,517	$16,445	$1,519	$17,964

Noninterest Income

Noninterest income totaled 0.82%, 0.72% and 0.73%, of average assets in 2018, 2017 and 2016, respectively. Noninterest income totaled $17.4 million in 2018 compared to $14.4 million in 2017 and $11.6 million in 2016. The 2018 and 2017 increases are principally due to higher trust and wealth management fees and service fees related to deposit accounts as a result of the FCB acquisition in Q2 2017. Further detail regarding noninterest income is reflected in the following table.

Table III - Noninterest Income

Dollars in thousands	2018	2017	2016
Insurance commissions	$4,320	$4,005	$4,022
Trust and wealth management fees	2,653	1,863	449
Service charges on deposit accounts	4,631	4,109	2,656
Bank card revenue	3,152	2,697	1,869
Realized securities gains (losses), net	622	(14)	1,127
Bank owned life insurance income	1,022	1,017	1,054
Other	1,022	750	423
Total	$17,422	$14,427	$11,600

Noninterest Expense

Noninterest expense totaled $49.9 million, $57.7 million and $34.8 million, or 2.3%, 2.9% and 2.2% of average assets for each of the years ended December 31, 2018, 2017 and 2016. Total noninterest expense decreased $7.9 million in 2018 compared to 2017 and increased $22.9 million in 2017 compared to 2016. Our most notable changes in noninterest expense during 2018 were increased salaries, commissions and employee benefits and decreases in merger related expenses and the litigation settlement charge. Table IV below presents a summary of our noninterest expenses for the past 3 years and the related year-over-year changes in each such expense.

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Table IV - Noninterest Expense

Dollars in thousands	2018	Change $	%	2017	Change $	%	2016
Salaries, commissions and employee benefits	$27,478	$2,403	9.6 %	$25,075	$5,502	28.1 %	$19,573
Net occupancy expense	3,364	353	11.7 %	3,011	913	43.5 %	2,098
Equipment expense	4,411	457	11.6 %	3,954	1,195	43.3 %	2,759
Professional fees	1,607	240	17.6 %	1,367	(148)	(9.8)%	1,515
Advertising and public relations	654	76	13.1 %	578	133	29.9 %	445
Amortization of intangibles	1,671	261	18.5 %	1,410	1,163	470.9 %	247
FDIC premiums	830	(235)	(22.1)%	1,065	190	21.7 %	875
Bank card expense	1,475	43	3.0 %	1,432	190	15.3 %	1,242
Foreclosed properties expense, net of gains/losses	1,350	11	0.8 %	1,339	1,173	706.6 %	166
Litigation settlement	—	(9,900)	(100.0)%	9,900	9,900	n/a	—
Merger-related expense	144	(1,445)	(90.9)%	1,589	656	70.3 %	933
Other	6,889	(136)	(1.9)%	7,025	2,076	41.9 %	4,949
Total	$49,873	$(7,872)	(13.6)%	$57,745	$22,943	65.9 %	$34,802

Salaries, commissions and employee benefits: These expenses are 10% higher in 2018 compared to 2017 primarily due to general merit increases and the increased average number of annual full-time equivalent employees related to the FCB acquisition in Q2 2017. These expenses are 28% higher in 2017 compared to 2016 primarily due to general merit increases and an increase in our average annual full-time equivalent employees, primarily those in conjunction with the FCB and HCB acquisitions.

Net occupancy expense: The 43.5% increase in 2017 is primarily due to the acquired FCB locations.

Equipment: The 2017 increase in equipment expense is primarily increased depreciation and amortization related to various technological upgrades, both hardware and software, made during the past two years and also the FCB acquisition.

Amortization of intangibles: Amortization of intangibles increased during 2018 and 2017 as a result of the additional amortization of the core deposit intangibles associated with the FCB and HCB acquisitions.

FDIC premiums: FDIC premiums decreased 22% during 2018 primarily due to improvement in earnings and performance. FDIC premiums increased 21.7% during 2017 as a result of the significant increase in our balance sheet due to recent acquisitions, partially offset by lower premium rates caused by the FDIC's change in the factors used to compute its deposit insurance rates, effective the second half of 2016. These lower effective premium rates are expected to continue.

Merger-related expense: These 2017 and 2016 expenses are comprised of data processing conversion costs, employee severance costs, write-downs of equipment and legal fees related to the FCB and HCB acquisitions. Such costs are expected to approximate $500,000 in 2019 relative to the Peoples acquisition.

Foreclosed properties expense, net of gains/losses: Foreclosed properties expense, net of gains/losses increased for 2017 as a result of higher repairs and maintenance of foreclosed properties, as well as the expenses attributable to the properties acquired in conjunction with the FCB acquisition and 2016 also included gains of $1.1 million related to sales of lots in two foreclosed residential subdivisions.

Litigation settlement: During 2017, we recorded a $9.9 million pre-tax charge as full resolution of the ResCap Litigation which had been pending since 2014. See the Legal Contingencies section of Note 17 Commitments and Contingencies in the accompanying notes to consolidated financial statements.

Other: Other expenses increased $2.1 million during 2017 primarily due to increased general operating costs due to the acquisitions of FCB and HCB.

Income Tax Expense

Income tax expense for the years ended December 31, 2018, 2017 and 2016 totaled $7.0 million, $9.7 million and $8.0 million, respectively. Our effective tax rate (income tax expense as a percentage of income before taxes) for 2018, 2017 and 2016 were 20.0%, 44.8% and 31.6%, respectively. The 2018 decreased effective tax rate is due to the lower corporate income tax rates enacted late 2017 in conjunction with the Tax Cuts and Jobs Act ("TCJA"), which permanently lowered the federal corporate income tax rate to 21% from the prior maximum rate of 35%, effective January 1, 2018. As a result of the reduction of the federal corporate income tax rate, U.S. generally accepted accounting principles required companies to remeasure their deferred tax assets and deferred tax liabilities, including those accounted for in accumulated other comprehensive income, as of the date of TCJA's enactment and record the effects as income tax expense in the reporting period of enactment. We remeasured our deferred tax assets and deferred tax liabilities as of December 22, 2017, at the new federal corporate income tax rate of 21%, and recorded additional income tax expense of $3.5 million to reduce our net deferred tax assets, thus causing a higher effective tax rate for 2017. Refer to Note 15 of the accompanying consolidated financial statements for further information and additional discussion of the significant components influencing our effective income tax rates.

CHANGES IN FINANCIAL POSITION

Our average assets increased during 2018 to $2.13 billion, an increase of 6.1% above 2017's average of $2.01 billion, and our year end December 31, 2018 assets were $66.3 million more than December 31, 2017. Average assets increased 25.4% in 2017, from $1.60 billion in 2016. Significant changes in the components of our balance sheet in 2018 and 2017 are discussed below.

Table V - Summary of Significant Changes in Financial Position 2018 versus 2017

Dollars in thousands	Balance December 31, 2017	Increase (Decrease)	Balance December 31, 2018
Assets			
Cash and cash equivalents	$52,631	$ 6,909	$59,540
Debt securities available for sale	328,586	(35,439)	293,147
Other investments	15,071	1,564	16,635
Loans, net	1,593,744	88,261	1,682,005
Property held for sale	21,470	(38)	21,432
Premises and equipment	34,209	3,344	37,553
Goodwill and other intangibles	27,513	(1,671)	25,842
Cash surrender value of life insurance policies	41,358	1,028	42,386
Other assets	19,658	2,354	22,012
Total Assets	$2,134,240	$ 66,312	$2,200,552
Liabilities			
Deposits	$1,600,601	$ 34,225	$1,634,826
Short-term borrowings	250,499	58,585	309,084
Long-term borrowings	45,751	(45,016)	735
Subordinated debentures owed to unconsolidated subsidiary trusts	19,589	—	19,589
Other liabilities	16,295	227	16,522
Shareholders' Equity	201,505	18,325	219,830
Total liabilities and shareholders' equity	$2,134,240	$ 66,346	$2,200,586

Table VI - Summary of Significant Changes in Financial Position 2017 versus 2016

		Increase (Decrease)		
Dollars in thousands	Balance December 31, 2016	Impact of FCB Acquisition	Other Changes	Balance December 31, 2017
Assets				
Cash and cash equivalents	$46,616	$39,053	$(33,038)	$52,631
Debt securities available for sale	266,405	100,735	(38,554)	328,586
Other investments	13,079	582	1,410	15,071
Loans, net	1,307,862	225,743	60,139	1,593,744
Property held for sale	24,504	2,377	(5,411)	21,470
Premises and equipment	23,737	6,174	4,298	34,209
Goodwill and other intangibles	13,652	15,056	(1,195)	27,513
Cash surrender value of life insurance policies	39,143	1,509	706	41,358
Other assets	23,649	3,593	(7,584)	19,658
Total Assets	$1,758,647	$394,822	$(19,229)	$2,134,240
Liabilities				
Deposits	$1,295,519	$350,533	$(45,451)	$1,600,601
Short-term borrowings	224,461	7,309	18,729	250,499
Long-term borrowings	46,670	—	(919)	45,751
Subordinated debentures owed to unconsolidated subsidiary trusts	19,589	—	—	19,589
Other liabilities	17,048	3,853	(4,606)	16,295
Shareholders' Equity	155,360	33,127	13,018	201,505
Total liabilities and shareholders' equity	$1,758,647	$394,822	$(19,229)	$2,134,240

Cash and Cash Equivalents

Included in the $33.0 million decrease in cash and cash equivalents during 2017 was the cash consideration of $15.0 million paid in conjunction with the FCB acquisition.

Loan Portfolio

Table VII depicts gross loan balances by type and the respective percentage of each to total loans at December 31, as follows:

Table VII - Loans by Type

	2018		2017		2016		2015		2014	
Dollars in thousands	Amount	Percent of Total	Amount	Percent of Total	Amount	Percent of Total	Amount	Percent of Total	Amount	Percent of Total
Commercial	$194,527	11.5 %	$190,270	11.8 %	$119,256	9.0 %	$97,324	8.9 %	$88,688	8.6 %
Commercial real estate	833,392	49.1 %	737,961	45.8 %	586,014	44.3 %	541,388	49.6 %	475,343	46.0 %
Construction and development	94,155	5.5 %	101,022	6.3 %	89,069	6.7 %	75,648	6.9 %	96,630	9.4 %
	491,441	28.9 %	500,720	31.1 %	406,293	30.7 %	346,380	31.7 %	340,269	33.0 %

Residential mortgage										
Mortgage warehouse lines	39,140	2.3 %	30,757	1.9 %	85,963	6.5 %	—	— %	—	— %
Consumer	32,569	1.9 %	36,302	2.3 %	25,524	1.9 %	19,297	1.8 %	19,500	1.9 %
Other	12,903	0.8 %	13,245	0.8 %	9,499	0.7 %	11,683	1.1 %	11,522	1.1 %
Total loans	$1,698,127	100.0%	$1,610,277	100.0%	$1,321,618	100.0%	$1,091,720	100.0%	$1,031,952	100.0%

Total net loans averaged $1.6 billion in 2018, which represented 77% of total average assets compared to $1.5 billion in 2017, or 75% of total average assets. A continued improving economic environment in our market area contributed to 5.1% organic

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loan growth, excluding mortgage warehouse lines, which increased $8.4 million in 2018, primarily in the commercial real estate portfolio, following 2017's growth of 9.6% and 2016's growth of 7.9%.

Refer to Note 7 of the accompanying consolidated financial statements for our loan maturities and a discussion of our adjustable rate loans as of December 31, 2018.

In the normal course of business, we make various commitments and incur certain contingent liabilities, which are disclosed in Note 17 of the accompanying consolidated financial statements but not reflected in the accompanying consolidated financial statements. There have been no significant changes in these types of commitments and contingent liabilities and we do not anticipate any material losses as a result of these commitments.

Securities

Securities comprised approximately 13.3% of total assets at December 31, 2018 compared to 15.4% at December 31, 2017. Average securities approximated $307.8 million for 2018 or 6.7% less than 2017's average of $329.9 million. The $38.6 million decrease in securities during 2018 was used to fund loan growth. In 2017, we obtained $100.7 million of available for sale securities in the FCB acquisition; the portfolio was restructured by selling $94 million of those securities and only $54 million of the proceeds were reinvested. Refer to Note 5 of the accompanying consolidated financial statements for details of amortized cost, the estimated fair values, unrealized gains and losses as well as the security classifications by type.

The following table presents the fair value of our securities portfolio by type at December 31, 2018, 2017 and 2016.

Table VIII - Fair Value of Securities	December 31		
Dollars in thousands	2018	2017	2016
Available for Sale			
Taxable debt securities			
U.S. Government and agencies and corporations	$26,140	$31,613	$15,174
Residential mortgage-backed securities:			
Government-sponsored agencies	80,309	121,321	138,846
Nongovernment-sponsored entities	614	2,077	4,653
State and political subdivisions	19,243	17,677	—
Corporate debt securities	14,512	16,245	18,170
Asset-backed securities	25,175	—	—
Total taxable debt securities	165,993	188,933	176,843
Tax-exempt debt securities			
State and political subdivisions	127,154	139,653	89,562
Total tax-exempt debt securities	127,154	139,653	89,562
Total available for sale securities	$293,147	$328,586	$266,405

All of our securities are classified as available for sale to provide us with flexibility to better manage our balance sheet structure and react to asset/liability management issues as they arise. Anytime that we carry a security with an unrealized loss that has been determined to be “other-than-temporary”, we must recognize that loss in income in the period of such determination.

At December 31, 2018, we did not own securities of any one issuer that were not issued by the U.S. Treasury or a U.S. Government agency that exceeded ten percent of shareholders’ equity. The maturity distribution of the securities portfolio at December 31, 2018, together with the weighted average yields for each range of maturity, is summarized in Table VI. The stated average yields are stated on a tax equivalent basis.

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Table IX - Securities Maturity Analysis

(At amortized cost, dollars in thousands)	Within one year Amount	Yield	After one but within five years Amount	Yield	After five but within ten years Amount	Yield	After ten years Amount	Yield
U. S. Government agencies and corporations	$2,361	6.2%	$4,550	3.6%	$10,209	2.9%	$9,183	2.8%
Residential mortgage backed securities:								
Government sponsored agencies	24,279	3.5%	48,128	3.4%	6,853	3.0%	1,623	2.7%
Nongovernment sponsored entities	279	3.8%	303	4.3%	29	5.3%	—	— %
State and political subdivisions	760	3.3%	3,736	3.5%	23,340	3.1%	118,523	3.6%
Corporate debt securities	—	—	1,000	4.5%	7,654	4.2%	6,153	5.9%
Asset-backed securities	4,682	3.2%	12,196	3.0%	8,410	3.0%	—	— %
Total	$32,361	3.7%	$69,913	3.4%	$56,495	3.2%	$135,482	3.6%

Deposits

Total deposits at December 31, 2018 increased $34.2 million or 2.1% compared to December 31, 2017. Total deposits at December 31, 2017 increased $305.1 million or 23.5% compared to December 31, 2016. Deposits acquired in conjunction with the purchase of FCB totaled $350.0 million. We have strengthened our focus on growing core transaction accounts. During 2018, core transaction accounts grew $118.5 million or 18.8% while our internet-only high yielding savings product declined $38.1 million and direct CDs decreased $30.1 million as we were less aggressive on the pricing of these funds as there was more than ample funding and liquidity as result of the FCB acquisition.

Table X - Deposits

Dollars in thousands	2018	2017	2016	2015	2014
Noninterest bearing demand	$222,120	$217,493	$149,737	$119,010	$115,427
Interest bearing demand	523,257	410,606	262,591	215,721	204,030
Savings	284,173	358,168	337,348	266,825	253,578
Time deposits	605,276	614,334	545,843	465,153	488,279
Total deposits	$1,634,826	$1,600,601	$1,295,519	$1,066,709	$1,061,314

See Table I for average deposit balance and rate information by deposit type for the past five years and Note 12 of the accompanying consolidated financial statements for a maturity distribution of time deposits as of December 31, 2018.

Borrowings

Lines of Credit: We have a remaining available line of credit from the Federal Home Loan Bank of Pittsburgh ("FHLB") totaling $462.8 million at December 31, 2018. We use this line primarily to fund loans to customers. Funds acquired through this program are reflected on the consolidated balance sheet in short-term borrowings or long-term borrowings, depending on the repayment terms of the debt agreement. We also had $159.3 million available on a short term line of credit with the Federal Reserve Bank at December 31, 2018, which is primarily secured by consumer loans, construction loans and commercial and industrial loans and a $6 million available line of credit with a correspondent bank.

Short-term Borrowings: Total short-term borrowings consisting primarily of advances from the FHLB having original maturities of 30 days or less increased $58.6 million from $250.5 million at December 31, 2017 to $309.1 million at December 31, 2018. See Note 13 of the accompanying consolidated financial statements for additional disclosures regarding our short-term borrowings.

Long-term Borrowings: Long-term borrowings historically have been used to fund our loan growth, however, as a result of prolonged low short-term interest rates following the economic downturn of 2008, long-term borrowings have been reduced significantly as we have replaced maturing long-term borrowings with short-term funding. Total long-term borrowings of $735,000 at December 31, 2018 consisted of a long-term FHLB advance and the $45.8 million at December 31, 2017 consisted primarily of structured repurchase agreements with unaffiliated institutions, which matured in 2018. Long-term borrowings from the FHLB totaled $751,000 at December 31, 2017. During 2007, we entered into $110 million of structured repurchase agreements, with terms ranging from 5 to 10 years and call features ranging from 2 to 3.5 years in which they are callable by

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the purchaser. These structured repurchase agreements totaled $45.0 million at December 31, 2017 and matured during 2018. Refer to Note 13 of the accompanying consolidated financial statements for additional information regarding our long-term borrowings.

ASSET QUALITY

For purposes of this discussion, we define nonperforming assets to include foreclosed properties, other repossessed assets and nonperforming loans, which is comprised of loans 90 days or more past due and still accruing interest and nonaccrual loans. Performing troubled debt restructurings ("TDRs") are excluded from nonperforming loans.

Table XI presents a summary of nonperforming assets at December 31, as follows:

Table XI - Nonperforming Assets

Dollars in thousands	2018	2017	2016	2015	2014
Accruing loans past due 90 days or more					
Commercial	$—	$—	$—	$—	$—
Commercial real estate	—	237	—	—	—
Residential construction & development	—	—	—	—	—
Residential real estate	—	—	—	—	—
Consumer	36	37	—	9	—
Other	—	—	—	—	—
Total accruing loans 90+ days past due	36	274	—	9	—
Nonaccrual loans					
Commercial	935	696	298	853	392
Commercial real estate	3,238	2,927	4,845	5,955	1,844
Commercial construction & development	—	—	—	—	—
Residential construction & development	3,198	3,569	4,465	5,623	4,619
Residential real estate	7,506	7,656	4,815	3,245	5,556
Consumer	112	201	151	83	83
Total nonaccrual loans	14,989	15,049	14,574	15,759	12,494
Foreclosed properties					
Commercial	—	—	—	—	110
Commercial real estate	1,762	1,789	1,749	1,300	5,204
Commercial construction & development	6,479	7,392	8,610	8,717	10,179
Residential construction & development	11,543	11,182	13,265	14,069	19,267
Residential real estate	1,648	1,107	880	1,481	2,769
Total foreclosed properties	21,432	21,470	24,504	25,567	37,529
Repossessed assets	5	68	12	5	221
Total nonperforming assets	$36,462	$36,861	$39,090	$41,340	$50,244
Total nonperforming loans as a percentage of total loans	0.89 %	0.95 %	1.10 %	1.45 %	1.21 %
Total nonperforming assets as a percentage of total assets	1.66 %	1.73 %	2.22 %	2.77 %	3.48 %
Allowance for loan losses as a percentage of nonperforming loans	86.84 %	82.00 %	80.10 %	72.75 %	89.38 %
Allowance for loan losses as a percentage of period end loans	0.77 %	0.78 %	0.88 %	1.05 %	1.08 %

Refer to Note 7 for information regarding our past due loans, impaired loans, nonaccrual loans and troubled debt restructurings.

We monitor our concentrations in higher-risk lending areas in accordance with the Interagency Guidance for Concentrations in Commercial Real Estate Lending issued in 2006. This guidance establishes concentration guidelines of 100% of Tier 1 Capital plus the allowance for loan and lease loss for lending in construction, land development and other land loans. It further establishes a guideline of 300% of Tier 1 Capital plus the allowance for loan and lease loss for lending in construction, land development and other land loans plus loans secured by non-owner occupied non-farm non-residential properties. As of December 31, 2018, Summit Community Bank was within the recommended limits of 100% and 300%, respectively.

We maintain the allowance for loan losses at a level considered adequate to provide for estimated probable credit losses inherent in the loan portfolio. The allowance is comprised of three distinct reserve components: (1) specific reserves related to loans individually evaluated, (2) quantitative reserves related to loans collectively evaluated and (3) qualitative reserves related to loans collectively evaluated. A summary of the methodology we employ on a quarterly basis with respect to each of these components in order to evaluate the overall adequacy of our allowance for loan losses is provided in Note 8 of the accompanying financial statements.

Relationship between Allowance for Loan Losses, Net Charge-offs and Nonperforming Loans

In analyzing the relationship among the allowance for loan losses, net loan charge-offs and nonperforming loans, it is helpful to understand the process of how loans are treated as the probability of collection changes over time. Allowances are established at origination through the quantitative and qualitative assessment process discussed above based upon credit quality.

Charge-offs, if necessary, are typically recognized in a period after the allowances were established. If the previously established allowance exceeds that needed to satisfactorily resolve the problem credit, a reduction in the overall level of the allowance could be recognized. In summary, if loan quality deteriorates, the typical credit sequence consists of periods of expense recognition, followed by periods of charge-offs.

Consumer loans are generally charged to the allowance for loan losses upon reaching specified stages of delinquency, in accordance with the Federal Financial Institutions Examination Council policy. For example, credit card loans are charged off by the end of the month in which the account becomes 180 days past due or within 60 days from receiving notification about a specified event (e.g., bankruptcy of the borrower), whichever is earlier. Residential mortgage loans are generally charged off to net realizable value no later than when the account becomes 180 days past due. Other consumer loans, if collateralized, are generally charged off to net realizable value at 120 days past due.

Commercial-related loans (which are risk-rated) are charged to the allowance for loan losses when the loss has been confirmed. This determination includes many factors, including among others, the prioritization of our claim in bankruptcy, expectations of the workout/restructuring of the loan and valuation of the borrower's equity.

Substantially all of our nonperforming loans are secured by real estate. The majority of these loans were underwritten in accordance with our loan-to-value policy guidelines which range from 70-85% at the time of origination. Although $8.0 million of our nonperforming loans have a related allowance of $1.5 million, the fair values of the underlying collateral value or the discounted cash flows remain in excess of the recorded investment in many of our nonperforming loans and therefore, no specific allocation of the allowance is required.

At December 31, 2018 and 2017, our allowance for loan losses totaled $13.0 million, or 0.77% of total loans and $12.6 million, or 0.78% of total loans, respectively. If the acquired FCB and HCB loans are excluded, the allowance for loan losses to total loans ratio at December 31, 2018 and 2017 would have been 0.84% and 0.91%, respectively. The allowance for loan losses is considered adequate to cover our estimate of probable credit losses inherent in our loan portfolio.

Table XII presents an allocation of the allowance for loan losses by loan type at each respective year end date, as follows:

Table XII - Allocation of the Allowance for Loan Losses

	2018		2017		2016		2015		2014	
Dollars in thousands	Amount	% of loans in each category to total	Amount	% of loans in each category to total	Amount	% of loans in each category to total	Amount	% of loans in each category to total	Amount	% of loans in each category to total

		loans			loans			loans			loans			loans	
Commercial	$1,705	11.5	%	$1,303	11.8	%	$934	9.0	%	$781	8.9	%	$1,204	8.6	%
Commercial real estate	7,956	49.1	%	7,374	45.8	%	5,547	44.4	%	4,566	49.6	%	2,244	46.0	%
Construction and development	403	5.5	%	794	6.3	%	2,287	6.7	%	2,867	6.9	%	3,844	9.4	%
Residential real estate	2,636	28.9	%	2,621	31.1	%	2,682	30.8	%	3,099	31.7	%	3,547	33.0	%
Mortgage warehouse lines	—	2.3	%	—	1.9	%	—	6.5	%	—	—	%	—	—	%
Consumer	79	1.9	%	210	2.3	%	121	1.9	%	59	1.8	%	97	1.9	%
Other	268	0.8	%	263	0.8	%	103	0.7	%	100	1.1	%	231	1.1	%
Total	$13,047	100.0	%	$12,565	100.0	%	$11,674	100.0	%	$11,472	100.0	%	$11,167	100.0	%

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A reconciliation of the activity in the allowance for loan losses follows:

Table XIII - Allowance for Loan Losses

Dollars in thousands	2018	2017	2016	2015	2014
Balance, beginning of year	$12,565	$11,674	$11,472	$11,167	$12,659
Losses					
Commercial	248	23	489	77	390
Commercial real estate	657	70	303	737	11
Construction and development	259	36	136	457	3,535
Residential real estate	913	519	344	701	514
Mortgage warehouse lines	—	—	—	—	—
Consumer	244	389	98	69	265
Other	282	251	185	110	118
Total	2,603	1,288	1,555	2,151	4,833
Recoveries					
Commercial	16	124	73	10	34
Commercial real estate	23	180	48	303	358
Construction and development	270	278	840	456	298
Residential real estate	263	164	145	206	254
Mortgage warehouse lines	—	—	—	—	—
Consumer	141	82	76	105	74
Other	122	101	75	126	73
Total	835	929	1,257	1,206	1,091
Net losses	1,768	359	298	945	3,742
Provision for loan losses	2,250	1,250	500	1,250	2,250
Balance, end of year	$13,047	$12,565	$11,674	$11,472	$11,167
Net losses as a % of average loans	0.11 %	0.02 %	0.02 %	0.09 %	0.38 %

At December 31, 2018 and 2017, we had approximately $21.4 million and $21.5 million, respectively, in property held for sale which was obtained as the result of foreclosure proceedings. Although foreclosed property is recorded at the lower of investment in the real estate or fair value less estimated costs to sell, the prices ultimately realized upon their sale may or may not result in us recognizing additional loss.

LIQUIDITY AND CAPITAL RESOURCES

Bank Liquidity: Liquidity reflects our ability to ensure the availability of adequate funds to meet loan commitments and deposit withdrawals, as well as provide for other transactional requirements. Liquidity is provided primarily by excess funds at correspondent banks, non-pledged securities and available lines of credit with the FHLB, Federal Reserve Bank of Richmond and correspondent banks, which totaled approximately $871.4 million or 39.6% of total consolidated assets at December 31, 2018.

Our liquidity strategy is to fund loan growth with deposits and other borrowed funds while maintaining an adequate level of short- and medium-term investments to meet normal daily loan and deposit activity.   As a member of the FHLB, we have access to borrow approximately $767.5 million. At December 31, 2018, we had available borrowing capacity of $462.8 million on our FHLB line. We also maintain a credit line with the Federal Reserve Bank of Richmond as a contingency liquidity vehicle. The amount available on this line at December 31, 2018 was approximately $159 million, which is secured by a pledge of our consumer loans, construction loans and commercial and industrial loan portfolios. We have a $6 million unsecured line of credit with a correspondent bank. Also, we classify all of our securities as available for sale to enable us to liquidate them if the need arises. During 2018, our loan growth was funded primarily by mortgage backed securities paydowns and deposits as our loans increased approximately $88.7 million, while securities decreased $35.4 million and total deposits increased $34.2 million.

Liquidity risk represents the risk of loss due to the possibility that funds may not be available to satisfy current or future commitments based on external market issues, customer or creditor perception of financial strength and events unrelated to Summit such as war, terrorism, or financial institution market specific issues. The Asset/Liability Management Committee ("ALCO"), comprised of members of senior management and certain members of the Board of Directors, oversees our liquidity risk management process. The ALCO develops and recommends policies and limits governing our liquidity to the Board of

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Directors for approval with the objective of ensuring that we can obtain cost-effective funding to meet current and future obligations, as well as maintain sufficient levels of on-hand liquidity, under both normal and "stressed" circumstances.

One aspect of our liquidity management process is establishing contingent liquidity funding plans under various scenarios in order to prepare for unexpected liquidity shortages or events. The following represents three "stressed" liquidity circumstances and our related contingency plans with respect to each.

Scenario 1 – Summit Community's capital status becomes less than "well capitalized". Banks which are less than "well capitalized" in accordance with regulatory capital guidelines are prohibited from issuing new brokered deposits without first obtaining a waiver from the FDIC to do so. In the event Summit Community's capital status were to fall below well capitalized and was not successful in obtaining the FDIC's waiver to issue new brokered deposits, Summit Community:

- Would have limited amounts of maturing brokered deposits to replace in the short-term, as we have limited our brokered deposits maturing in any one quarter to no more than $50 million.
- Presently has $871 million in available sources of liquid funds which could be drawn upon to fund maturing brokered deposits until Summit Community had restored its capital to well capitalized status.
- Would first seek to restore its capital to well capitalized status through capital contributions from Summit, its parent holding company.
- Would generally have no more than $100 million in brokered deposits maturing in any one year time frame, which is well within its presently available sources of liquid funds, if in the event Summit does not have the capital resources to restore Summit Community's capital to well capitalized status. One year would give Summit Community ample time to raise alternative funds either through retail deposits or the sale of assets and obtain capital resources to restore it to well capitalized status.

Scenario 2 – Summit Community's credit quality deteriorates such that the FHLB restricts further advances. If in the event that the Bank's credit quality deteriorated to the point that further advances under its line with the FHLB were restricted, Summit Community:

- Would severely curtail lending and other growth activities until such time as access to this line could be restored, thus eliminating the need for net new advances.
- Would still have available current liquid funding sources secured by unemcumbered loans and securities totaling $468 million aside from its FHLB line, which would result in a funding source of approximately $366 million.

Scenario 3 – A competitive financial institution offers a retail deposit program at interest rates significantly above current market rates in Summit Community's market areas. If a competitive financial institution offered a retail deposit program at rates well in excess of current market rates in Summit Community's market area, the Bank:

- Presently has $871 million in available sources of liquid funds which could be drawn upon immediately to fund any "net run off" of deposits from this activity.
- Would severely curtail lending and other growth activities so as to preserve the availability of as much contingency funds as possible.
- Would begin offering its own competitive deposit program when deemed prudent so as to restore the retail deposits lost to the competition.

We continuously monitor our liquidity position to ensure that day-to-day as well as anticipated funding needs are met. We are not aware of any trends, commitments, events or uncertainties that have resulted in or are reasonably likely to result in a material change to our liquidity. Refer to page 13 of Item 1A. Risk Factors for further discussion of our liquidity risk.

Growth and Expansion: During 2018, we spent approximately $5.5 million on capital expenditures for premises and equipment. We expect our capital expenditures to approximate $7 - $8 million in 2019, primarily for new branch sites and construction and equipment and technological upgrades.

Absent an acquisition, management anticipates 5-6% organic asset growth in 2019.

Capital Compliance: Our capital position is strong. Stated as a percentage of total assets, our equity ratio was 10.0% at December 31, 2018 compared to 9.4% at December 31, 2017. Our subsidiary bank, Summit Community Bank, had Tier 1 risk-based, Total risk-based and Tier 1 leverage capital in excess of the minimum "well capitalized" levels of $71.3 million, $49.7 million and $107.0 million, respectively. We intend to maintain both Summit's and its subsidiary bank's capital ratios at levels that would be considered to be “well capitalized” in accordance with regulatory capital guidelines. See Note 18 of the accompanying consolidated financial statements for further discussion of our regulatory capital.

During 2018, we retained $21.5 million of earnings and the net change in accumulated other comprehensive income was $2.7 million, principally resulting from $3.7 million unrealized net losses on securities available for sale and $1.2 million in net gains on cash flow hedges.

On July 30, 2015, our Employee Stock Ownership Plan ("ESOP") purchased 225,000 shares of Summit Financial Group Inc. common stock, which is shown as a reduction of shareholders' equity, similar to a purchase of treasury stock. When the shares are committed to be released and become available for allocation to plan participants, the then fair value of such shares will be charged to compensation expense. Unallocated shares owned by the Company’s ESOP are not considered to be outstanding for the purpose of computing earnings per share.

Dividends: Cash dividends per share totaled $0.53 and $0.44 during 2018 and 2017, respectively, representing dividend payout ratios of 23.3% and 44.0%, respectively. It is our intention to continue to pay dividends on a quarterly basis during 2019. Future dividend amounts will depend on the earnings and financial condition of our subsidiary bank as well as general economic conditions.

The primary source of funds for the dividends paid to our shareholders is dividends received from our subsidiary bank. Dividends paid by our subsidiary bank are subject to restrictions by banking law and regulations and require approval by the bank’s regulatory agency if dividends declared in any year exceed the bank’s current year's net income, as defined, plus its retained net profits of the two preceding years. In addition, cash dividends depend on the earnings and financial condition of our subsidiary bank and our capital adequacy as well as general economic conditions. During 2019, the net retained profits available for distribution to Summit as dividends without regulatory approval are approximately $25.6 million.

Contractual Cash Obligations: During our normal course of business, we incur contractual cash obligations. The following table summarizes our contractual cash obligations at December 31, 2018.

Table XIV - Contractual Cash Obligations

Dollars in thousands	Long Term Debt and Subordinated Debentures	Operating Leases
2019	$ 18	$ 244
2020	18	97
2021	19	76
2022	21	78
2023	22	78
Thereafter	20,226	74
Total	$ 20,324	$ 647

Off-Balance Sheet Arrangements: We are involved with some off-balance sheet arrangements that have or are reasonably likely to have an effect on our financial condition, liquidity, or capital. These arrangements at December 31, 2018 are presented in the following table. Refer to Note 17 of the accompanying consolidated financial statements for further discussion of our off-balance sheet arrangements.

Table XV - Off-Balance Sheet Arrangements

Dollars in thousands	
Commitments to extend credit	
Revolving home equity and credit card lines	$69,893

Construction loans	85,392
Other loans	161,619
Standby letters of credit	6,366
Total	$323,270

QUARTERLY FINANCIAL DATA

A summary of our selected quarterly financial data is as follows:

	2018			
Dollars in thousands, except per share amounts	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Interest income	$22,897	$23,399	$23,800	$25,313
Net interest income	17,257	17,275	17,213	18,052
Net income	7,443	6,280	6,899	7,450
Basic earnings per share	$0.60	$0.51	$0.56	$0.60
Diluted earnings per share	$0.60	$0.51	$0.55	$0.60

	2017			
Dollars in thousands, except per share amounts	First Quarter (A)	Second Quarter	Third Quarter	Fourth Quarter (B)
Interest income	$17,674	$22,231	$22,036	$22,587
Net interest income	13,630	17,848	17,232	17,438
Net income	(1,616)	5,278	5,930	2,323
Basic earnings per share	$(0.15)	$0.43	$0.48	$0.19
Diluted earnings per share	$(0.15)	$0.43	$0.48	$0.19

(A) Includes $6.2 million or $0.52 per diluted share after-tax charge related to litigation settlement.
(B) Includes $3.5 million or $0.29 per diluted share preliminary charge to income taxes due to enactment of TCJA.

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Item 7A. Quantitative and Qualitative Disclosures about Market Risk

MARKET RISK MANAGEMENT

Market risk is the risk of loss arising from adverse changes in the fair value of financial instruments due to changes in interest rates, exchange rates and equity prices. Interest rate risk is our primary market risk and results from timing differences in the repricing of assets, liabilities and off-balance sheet instruments, changes in relationships between rate indices and the potential exercise of embedded options. The principal objective of asset/liability management is to minimize interest rate risk and our actions in this regard are taken under the guidance of our Asset/Liability Management Committee ("ALCO"). The ALCO is comprised of members of the Board of Directors and of members of senior management. The ALCO actively formulates the economic assumptions that we use in our financial planning and budgeting process and establishes policies which control and monitor our sources, uses and prices of funds.

Some amount of interest rate risk is inherent and appropriate to the banking business. Our net income is affected by changes in the absolute level of interest rates. Our interest rate risk position at December 31, 2018 is slightly liability sensitive over the next twelve months, however we are asset sensitive thereafter. The nature of our lending and funding activities tends to drive our interest rate risk position to being liability sensitive. That is, liabilities are likely to reprice faster than assets, resulting in a decrease in net interest income in a rising rate environment, while a falling interest rate environment would produce an increase in net interest income. Net interest income is also subject to changes in the shape of the yield curve. In general, a flat yield curve results in a decline in our earnings due to the compression of earning asset yields and funding rates, while a steepening would result in increased earnings as margins widen.

Several techniques are available to monitor and control the level of interest rate risk. We primarily use earnings simulations modeling to monitor interest rate risk. The earnings simulation model forecasts the effects on net interest income under a variety of interest rate scenarios that incorporate changes in the absolute level of interest rates and changes in the shape of the yield curve. Each increase or decrease in rates is assumed to gradually take place over a 12 month period and then remain stable, except for the up 400 scenario, which assumes a gradual increase in rates over 24 months. Assumptions used to project yields and rates for new loans and deposits are derived from historical analysis. Securities portfolio maturities and prepayments are reinvested in like instruments. Mortgage loan prepayment assumptions are developed from industry estimates of prepayment speeds. Noncontractual deposit repricings are modeled on historical patterns.

The following table presents the estimated sensitivity of our net interest income to changes in interest rates, as measured by our earnings simulation model as of December 31, 2018. The sensitivity is measured as a percentage change in net interest income given the stated changes in interest rates (gradual change over 12 months, stable thereafter) compared to net interest income with rates unchanged in the same period. The estimated changes set forth below are dependent on the assumptions discussed above.

	Estimated % Change in Net Interest Income over:	
Change in Interest Rates	0 - 12 Months	13 - 24 Months
Down 100 basis points (1)	1.05 %	2.99 %
Up 100 basis points (1)	-1.00 %	1.27 %
Up 200 basis points (1)	-1.48 %	-0.29 %

(1) assumes a parallel shift in the yield curve
over 12 months

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REPORT OF MANAGEMENT'S ASSESSMENT OF INTERNAL CONTROL OVER FINANCIAL REPORTING

Summit Financial Group, Inc. is responsible for the preparation, integrity and fair presentation of the consolidated financial statements included in this annual report. The consolidated financial statements and notes included in this annual report have been prepared in conformity with United States generally accepted accounting principles and necessarily include some amounts that are based on management's best estimates and judgments.

We, as management of Summit Financial Group, Inc., are responsible for establishing and maintaining effective internal control over financial reporting that is designed to produce reliable financial statements in conformity with United States generally accepted accounting principles and in conformity with the Federal Financial Institutions Examination Council instructions for consolidated Reports of Condition and Income (call report instructions). The system of internal control over financial reporting as it relates to the financial statements is evaluated for effectiveness by management and tested for reliability through a program of internal audits. Actions are taken to correct potential deficiencies as they are identified. Any system of internal control, no matter how well designed, has inherent limitations, including the possibility that a control can be circumvented or overridden and misstatements due to error or fraud may occur and not be detected. Also, because of changes in conditions, internal control effectiveness may vary over time. Accordingly, even an effective system of internal control will provide only reasonable assurance with respect to financial statement preparation.

The Audit Committee, consisting entirely of independent directors, meets regularly with management, internal auditors and the independent registered public accounting firm and reviews audit plans and results, as well as management's actions taken in discharging responsibilities for accounting, financial reporting and internal control. Yount, Hyde & Barbour, P.C., independent registered public accounting firm and the internal auditors have direct and confidential access to the Audit Committee at all times to discuss the results of their examinations.

Management assessed the Corporation's system of internal control over financial reporting as of December 31, 2018. In making this assessment, we used the criteria for effective internal control over financial reporting set forth in Internal Control-Integrated Framework, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in 2013. Based on this assessment, management concludes that, as of December 31, 2018, its system of internal control over financial reporting is effective and meets the criteria of the Internal Control-Integrated Framework. Yount, Hyde & Barbour, P.C., independent registered public accounting firm, has issued an attestation report on the Corporation's internal control over financial reporting.

Management is also responsible for compliance with the federal and state laws and regulations concerning dividend restrictions and federal laws and regulations concerning loans to insiders designated by the FDIC as safety and soundness laws and regulations.

/s/ H. Charles Maddy, III	/s/ Robert S. Tissue	/s/ Julie R. Markwood
President and Chief Executive Officer	Senior Vice President and Chief Financial Officer	Vice President and Chief Accounting Officer

Moorefield, West Virginia
March 1, 2019

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Shareholders
Summit Financial Group, Inc.
Moorefield, West Virginia

Opinion on the Internal Control over Financial Reporting
We have audited Summit Financial Group, Inc. and subsidiaries' (the Company) internal control over financial reporting as of December 31, 2018, based on criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission in 2013. In our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2018, based on criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission in 2013.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (PCAOB), the consolidated balance sheets as of December 31, 2018 and 2017, and the related consolidated statements of income, comprehensive income, shareholders’ equity and cash flows for each of the three years in the period ended December 31, 2018 of the Company and our report dated March 1, 2019 expressed an unqualified opinion.

Basis for Opinion
The Company’s management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting in the accompanying Report of Management’s Assessment of Internal Control over Financial Reporting. Our responsibility is to express an opinion on the Company’s internal control over financial reporting based on our audit. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audit in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audit also included performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

Definition and Limitations of Internal Control over Financial Reporting
A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

/s/ YOUNT, HYDE & BARBOUR, P.C.
Winchester, Virginia
March 1, 2019

Item 8. Financial Statements and Supplementary Data

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Shareholders
Summit Financial Group, Inc.
Moorefield, West Virginia

Opinion on the Financial Statements
We have audited the accompanying consolidated balance sheets of Summit Financial Group, Inc. and subsidiaries (the Company) as of December 31, 2018 and 2017, the related consolidated statements of income, comprehensive income, shareholders' equity and cash flows for each of the three years in the period ended December 31, 2018, and the related notes to the consolidated financial statements (collectively, the financial statements). In our opinion, the financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2018 and 2017, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2018, in conformity with accounting principles generally accepted in the United States of America.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (PCAOB), the Company's internal control over financial reporting as of December 31, 2018, based on criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission in 2013, and our report dated March 1, 2019 expressed an unqualified opinion on the effectiveness of the Company's internal control over financial reporting.

Basis for Opinion
These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on the Company's financial statements based on our audits. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

/s/ YOUNT, HYDE & BARBOUR, P.C.

We have served as the Company's auditor since 2016.

Winchester, Virginia
March 1, 2019

Consolidated Balance Sheets

	December 31,	
Dollars in thousands	2018	2017
ASSETS		
Cash and due from banks	$23,061	$9,641
Interest bearing deposits with other banks	36,479	42,990
Cash and cash equivalents	59,540	52,631
Debt securities available for sale	293,147	328,586
Other investments	16,635	15,071
Loans held for sale	400	—
Loans net of unearned income	1,695,052	1,606,309
Less: allowance for loan losses	(13,047)	(12,565)
Loans, net	1,682,005	1,593,744
Property held for sale	21,432	21,470
Premises and equipment, net	37,553	34,209
Accrued interest receivable	8,708	8,329
Goodwill and other intangible assets	25,842	27,513
Cash surrender value of life insurance policies	42,386	41,358
Other assets	12,938	11,329
Total assets	$2,200,586	$2,134,240
LIABILITIES AND SHAREHOLDERS' EQUITY		
Liabilities		
Deposits		
Non-interest bearing	$222,120	$217,493
Interest bearing	1,412,706	1,383,108
Total deposits	1,634,826	1,600,601
Short-term borrowings	309,084	250,499
Long-term borrowings	735	45,751
Subordinated debentures owed to unconsolidated subsidiary trusts	19,589	19,589
Other liabilities	16,522	16,295
Total liabilities	1,980,756	1,932,735
Commitments and Contingencies		
Shareholders' Equity		
Preferred stock, $1.00 par value, authorized 250,000 shares	—	—
Common stock and related surplus, $2.50 par value; authorized 20,000,000 shares; issued: 2018 - 12,399,887 shares, 2017 - 12,465,296 shares; outstanding: 2018 - 12,312,933 shares, 2017 - 12,358,562 shares	80,431	81,098
Unallocated common stock held by Employee Stock Ownership Plan - 2018 - 86,954 shares, 2017 - 106,734 shares	(939)	(1,152)
Retained earnings	141,354	119,827
Accumulated other comprehensive (loss) income	(1,016)	1,732
Total shareholders' equity	219,830	201,505
Total liabilities and shareholders' equity	$2,200,586	$2,134,240

See Notes to Consolidated Financial Statements

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Consolidated Statements of Income

	For the Year Ended December 31,		
Dollars in thousands (except per share amounts)	2018	2017	2016
Interest income			
Interest and fees on loans			
Taxable	$84,716	$74,365	$56,439
Tax-exempt	567	543	541
Interest and dividends on securities			
Taxable	5,341	5,071	4,395
Tax-exempt	4,246	3,939	2,543
Interest on interest bearing deposits with other banks	539	609	173
Total interest income	95,409	84,527	64,091
Interest expense			
Interest on deposits	17,675	11,210	8,964
Interest on short-term borrowings	5,993	4,473	2,288
Interest on long-term borrowings and subordinated debentures	1,944	2,697	3,832
Total interest expense	25,612	18,380	15,084
Net interest income	69,797	66,147	49,007
Provision for loan losses	2,250	1,250	500
Net interest income after provision for loan losses	67,547	64,897	48,507
Noninterest income			
Insurance commissions	4,320	4,005	4,022
Trust and wealth management fees	2,653	1,863	449
Service fees related to deposit accounts	4,631	4,109	2,656
Bank card revenue	3,152	2,697	1,869
Realized securities gains (losses), net	622	(14)	1,127
Bank owned life insurance income	1,022	1,017	1,054
Other	1,022	750	423
Total noninterest income	17,422	14,427	11,600
Noninterest expenses			
Salaries, commissions and employee benefits	27,478	25,075	19,573
Net occupancy expense	3,364	3,011	2,098
Equipment expense	4,411	3,954	2,759
Professional fees	1,607	1,367	1,515
Advertising and public relations	654	578	445
Amortization of intangibles	1,671	1,410	247
FDIC premiums	830	1,065	875
Bank card expense	1,475	1,432	1,242
Foreclosed properties expense, net of losses	1,350	1,339	166
Litigation settlement	—	9,900	—
Merger-related expenses	144	1,589	933
Other	6,889	7,025	4,949
Total noninterest expenses	49,873	57,745	34,802
Income before income tax expense	35,096	21,579	25,305
Income tax expense	7,024	9,664	8,008
Net income	$28,072	$11,915	$17,297
Basic earnings per common share	$2.27	$1.00	$1.62

Diluted earnings per common share	$2.26	$1.00	$1.61

See Notes to Consolidated Financial Statements

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Consolidated Statements of Comprehensive Income

	For the Year Ended December 31,		
Dollars in thousands	2018	2017	2016
Net income	$28,072	$11,915	$17,297
Other comprehensive (loss) income:			
Net unrealized gain on cashflow hedges of:			
2018 - $1,645, net of deferred taxes of $395; 2017 - $2,556, net of deferred taxes of $946; 2016 - $459, net of deferred taxes of $170	1,250	1,610	289
Net unrealized (loss) gain on securities available for sale of:			
2018 - ($4,920), net of deferred taxes of ($1,181) and reclassification adjustment for net realized gains included in net income of $622, net of tax of $149	(3,739)		
2017 - $4,378 net of deferred taxes of $1,620 and reclassification adjustment for net realized losses included in net income of ($14), net of tax of ($5)		2,758	
2016 - ($4,913), net of deferred taxes of ($1,818) and reclassification adjustment for net realized gains included in net income of $1,127, net of tax of $417			(3,095)
Net unrealized (loss) gain on other post-retirement benefits of:			
2018 - ($341), net of deferred taxes of ($82); 2017- $521, net of deferred taxes of $193	(259)	328	—
Total other comprehensive (loss) income	(2,748)	4,696	(2,806)
Total comprehensive income	$25,324	$16,611	$14,491

See Notes to Consolidated Financial Statements

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Consolidated Statements of Shareholders' Equity
For the Years Ended December 31, 2018, 2017 and 2016

Dollars in thousands (except per share amounts)	Common Stock and Related Surplus	Unallocated Common Stock Held by ESOP	Retained Earnings	Accumulated Other Compre- hensive (Loss) Income	Total Share- holders' Equity
Balance, December 31, 2015	$45,741	$ (1,964)	$100,423	$ (456)	$143,744
Net income	—	—	17,297	—	17,297
Other comprehensive loss				(2,806)	(2,806)
Exercise of stock options - 24,740 shares	447	—	—	—	447
Share-based compensation expense	200	—	—	—	200
Unallocated ESOP shares committed to be released - 35,283 shares	268	381	—	—	649
Common stock issuances from reinvested dividends - 5,203 shares	101	—	—	—	101
Common stock cash dividends declared ($0.40 per share)	—	—	(4,272)	—	(4,272)
Balance, December 31, 2016	46,757	(1,583)	113,448	(3,262)	155,360
Net income	—	—	11,915	—	11,915
Other comprehensive income				4,696	4,696
Reclassification of tax effects due to change in U.S. corporate tax rate	—	—	(298)	298	—
Exercise of stock options and SARs - 36,925 shares	304	—	—	—	304
Share-based compensation expense	385	—	—	—	385
Unallocated ESOP shares committed to be released - 39,805 shares	515	431	—	—	946
Acquisition of First Century Bankshares, Inc. - 1,537,912 shares, net of issuance costs	32,968	—	—	—	32,968
Common stock issuances from reinvested dividends - 6,950 shares	169	—	—	—	169
Common stock cash dividends declared ($0.44 per share)	—	—	(5,238)	—	(5,238)
Balance, December 31, 2017	81,098	(1,152)	119,827	1,732	201,505
Net income	—	—	28,072	—	28,072
Other comprehensive loss				(2,748)	(2,748)
Exercise of stock options - 6,800 shares	122	—	—	—	122
Share-based compensation expense	391	—	—	—	391
Unallocated ESOP shares committed to be released - 19,780 shares	272	213	—	—	485
Purchase and retirement of 82,423 shares of common stock	(1,689)	—	—	—	(1,689)
Common stock issuances from reinvested dividends - 10,214 shares	237	—	—	—	237
Common stock cash dividends declared ($0.53 per share)	—	—	(6,545)	—	(6,545)
Balance, December 31, 2018	$80,431	$ (939)	$141,354	$ (1,016)	$219,830

See Notes to Consolidated Financial Statements

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Consolidated Statements of Cash Flows

	For the Year Ended December 31,		
Dollars in thousands	2018	2017	2016
CASH FLOWS FROM OPERATING ACTIVITIES			
Net income	$28,072	$11,915	$17,297
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation	2,168	1,887	1,224
Provision for loan losses	2,250	1,250	500
Share-based compensation expense	391	385	200
Deferred income tax (benefit) expense	(349)	4,076	(357)
Loans originated for sale	(15,939)	(16,248)	(10,593)
Proceeds from sale of loans	15,834	16,747	11,425
Gains on loans held for sale	(295)	(323)	(229)
Realized securities (gains) losses, net	(622)	14	(1,127)
Loss (gain) on disposal of assets	74	(133)	(946)
Write-downs of foreclosed properties	776	885	668
Amortization of securities premiums, net	3,412	4,190	4,325
Accretion related to acquisitions, net	(580)	(1,051)	(44)
Amortization of intangibles	1,671	1,410	247
Earnings on bank owned life insurance	(1,028)	(707)	(1,059)
Increase in accrued interest receivable	(378)	(1,102)	(254)
(Increase) decrease in other assets	(320)	668	(894)
Increase in other liabilities	3,384	510	2,827
Net cash provided by operating activities	38,521	24,373	23,210
CASH FLOWS FROM INVESTING ACTIVITIES			
Proceeds from maturities and calls of securities available for sale	1,145	2,700	3,235
Proceeds from sales of securities available for sale	107,559	152,882	72,453
Principal payments received on securities available for sale	24,814	31,902	35,881
Purchases of securities available for sale	(105,789)	(148,174)	(99,497)
Purchases of other investments	(14,550)	(18,604)	(18,273)
Proceeds from redemptions of other investments	11,717	15,932	14,066
Net loan originations	(92,189)	(61,104)	(170,716)
Purchases of premises and equipment	(5,545)	(6,185)	(1,857)
Proceeds from disposal of premises and equipment	42	—	43
Improvements to property held for sale	(1,304)	(316)	(463)
Proceeds from sale of repossessed assets & property held for sale	2,365	5,883	5,168
Cash and cash equivalents acquired in acquisition, net of $14,989 cash consideration paid - 2017, net of $21,826 cash consideration paid - 2016			