

Village Bank & Trust Financial Corp.
Form 10-Q
May 15, 2013

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q
x QUARTERLY REPORT UNDER SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended March 31, 2013

.. TRANSITION REPORT UNDER SECTION 13 OR 15(d)
OF THE EXCHANGE ACT

For the transition period from _____ to _____

Commission file number: 0-50765

VILLAGE BANK AND TRUST FINANCIAL CORP.
(Exact name of registrant as specified in its charter)

Virginia
(State or other jurisdiction of
incorporation or organization)

16-1694602
(I.R.S. Employer
Identification No.)

15521 Midlothian Turnpike, Midlothian, Virginia
(Address of principal executive offices)

23113
(Zip code)

804-897-3900
(Registrant's telephone number, including area code)

Indicate by check whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act 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 x No .

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

Edgar Filing: Village Bank & Trust Financial Corp. - Form 10-Q

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

Large Accelerated Filer Accelerated Filer
Non-Accelerated Filer (Do not check if smaller reporting company) Smaller Reporting Company

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

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

4,251,795 shares of common stock, \$4.00 par value, outstanding as of May 8, 2013

Village Bank and Trust Financial Corp.
Form 10-Q

TABLE OF CONTENTS

Part I – Financial Information

Item 1. Financial Statements	
Consolidated Balance Sheets March 31, 2013 (unaudited) and December 31, 2012	3
Consolidated Statements of Operations For the Three Months Ended March 31, 2013 and 2012 (unaudited)	4
Consolidated Statements of Comprehensive Income (Loss) For the Three Months Ended March 31, 2013 and 2012 (unaudited)	5
Consolidated Statements of Stockholders' Equity For the Three Months Ended March 31, 2013 and 2012 (unaudited)	6
Consolidated Statements of Cash Flows For the Three Months Ended March 31, 2013 and 2012 (unaudited)	7
Notes to Condensed Consolidated Financial Statements (unaudited)	8
Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations	35
Item 3. Quantitative and Qualitative Disclosures About Market Risk	55
Item 4. Controls and Procedures	55

Part II – Other Information

Item 1. Legal Proceedings	56
Item 1A. Risk Factors	56
Item 2. Unregistered Sales of Equity Securities and Use of Proceeds	56

Item 3. Defaults Upon Senior Securities	56
Item 4. Mine Safety Disclosures	56
Item 5. Other Information	56
Item 6. Exhibits	56
Signatures	57

PART I – FINANCIAL INFORMATION

ITEM 1 – FINANCIAL STATEMENTS

Village Bank and Trust Financial Corp. and Subsidiary
Consolidated Balance Sheets
March 31, 2013 (Unaudited) and December 31, 2012

	March 31, 2013	December 31, 2012
Assets		
Cash and due from banks	\$ 12,340,643	\$ 13,945,105
Federal funds sold	56,796,937	39,185,837
Total cash and cash equivalents	69,137,580	53,130,942
Investment securities available for sale	29,635,046	25,154,046
Loans held for sale	16,377,826	24,188,384
Loans		
Outstandings	324,004,492	354,910,266
Allowance for loan losses	(10,319,965)	(10,807,827)
Deferred fees and costs	783,137	787,823
	314,467,664	344,890,262
Premises and equipment, net	23,992,037	25,815,342
Accrued interest receivable	1,580,147	1,676,518
Bank owned life insurance	6,625,325	6,575,018
Other real estate owned	21,382,831	20,203,691
Other assets	7,855,987	8,453,169
	\$491,054,443	\$510,087,372
Liabilities and Stockholders' Equity		
Liabilities		
Deposits		
Noninterest bearing demand	\$62,301,743	\$57,049,348
Interest bearing	359,117,502	379,273,614
Total deposits	421,419,245	436,322,962
Federal Home Loan Bank advances	27,000,000	28,000,000
Long-term debt - trust preferred securities	8,764,000	8,764,000
Other borrowings	1,882,346	4,851,811
Accrued interest payable	981,527	911,635
Other liabilities	6,780,872	6,272,163
Total liabilities	466,827,990	485,122,571
Stockholders' equity		
Preferred stock, \$4 par value, \$1,000 liquidation preference, 1,000,000 shares authorized, 14,738 shares issued and outstanding	58,952	58,952
Common stock, \$4 par value - 10,000,000 shares authorized; 4,251,795 shares issued and outstanding at March 31, 2013 4,251,795 shares issued and outstanding at December 31, 2012	17,007,180	17,007,180

Edgar Filing: Village Bank & Trust Financial Corp. - Form 10-Q

Additional paid-in capital	40,705,498	40,705,257
Retained earnings (deficit)	(33,905,887)	(33,173,525)
Common stock warrant	732,479	732,479
Discount on preferred stock	(161,887)	(198,993)
Accumulated other comprehensive loss	(209,882)	(166,549)
Total stockholders' equity	24,226,453	24,964,801
	\$491,054,443	\$510,087,372

See accompanying notes to consolidated financial statements.

Village Bank and Trust Financial Corp. and Subsidiary
Consolidated Statements of Operations
Three Months Ended March 31, 2013 and 2012
(Unaudited)

	Three Months Ended March 31,	
	2013	2012
Interest income		
Loans	\$5,142,951	\$5,899,208
Investment securities	188,099	150,349
Federal funds sold	25,115	20,932
Total interest income	5,356,165	6,070,489
Interest expense		
Deposits	1,042,384	1,358,238
Borrowed funds	224,392	290,986
Total interest expense	1,266,776	1,649,224
Net interest income	4,089,389	4,421,265
Provision for loan losses	823,000	1,735,000
Net interest income after provision for loan losses	3,266,389	2,686,265
Noninterest income		
Service charges and fees	511,504	507,643
Gain on sale of loans	1,955,717	1,750,663
Gain (loss) on sale of assets	598,182	-
Gain (loss) on sale of investment securities	90,067	164,207
Rental income	264,697	176,496
Other	186,305	89,644
Total noninterest income	3,606,472	2,688,653
Noninterest expense		
Salaries and benefits	3,439,408	3,098,224
Occupancy	556,930	546,367
Equipment	177,855	205,364
Supplies	105,272	91,902
Professional and outside services	686,360	635,382
Advertising and marketing	63,301	76,063
OREO expense	1,574,700	1,118,775
Other operating expenses	780,069	1,003,221
Total noninterest expense	7,383,895	6,775,298
Net income (loss) before income taxes	(511,034)	(1,400,380)
Income tax expense (benefit)	-	-

Edgar Filing: Village Bank & Trust Financial Corp. - Form 10-Q

Net income (loss)	(511,034)	(1,400,380)
Preferred stock dividends and amortization of discount	221,328	220,448
Net income (loss) available to common shareholders	\$(732,362)	\$(1,620,828)
Earnings (loss) per share, basic	\$(0.17)	\$(0.38)
Earnings (loss) per share, diluted	\$(0.17)	\$(0.38)

See accompanying notes to consolidated financial statements.

Village Bank and Trust Financial Corp. and Subsidiary
 Consolidated Statements of Changes in Comprehensive Income (Loss)
 Three Months Ended March 31, 2013 and 2012
 (Unaudited)

	Three Months Ended March 31,					
	Amount	2013 Tax Expense (Benefit)	Total	Amount	2012 Tax Expense (Benefit)	Total
Net loss	\$(511,034)	\$-	\$(511,034)	\$(1,400,380)	\$-	\$(1,400,380)
Other comprehensive income (loss)						
Unrealized holding gains (losses)						
arising during the period	21,161	7,195	13,966	(377,355)	(128,301)	(249,054)
Reclassification adjustment for losses realized in income	(90,067)	(30,623)	(59,444)	(164,207)	(55,830)	(108,377)
Minimum pension adjustment	3,250	1,105	2,145	3,250	1,105	2,145
Total other comprehensive loss	(65,656)	(22,323)	(43,333)	(538,312)	(183,026)	(355,286)
Total comprehensive loss	\$(576,690)	\$(22,323)	\$(554,367)	\$(1,938,692)	\$(183,026)	\$(1,755,666)

See accompanying notes to consolidated financial statements.

Village Bank and Trust Financial Corp. and Subsidiary
Consolidated Statements of Stockholders' Equity
Three Months Ended March 31, 2013 and 2012
(Unaudited)

	Preferred Stock	Common Stock	Additional Paid-in Capital	Retained Earnings (Deficit)	Warrant	Discount on Preferred Stock	Accumulated Other Comprehensive Income (loss)	Total
Balance, December 31, 2012	\$58,952	\$17,007,180	\$40,705,257	\$(33,173,525)	\$732,479	\$(198,993)	\$(166,549)	\$24,964,801
Amortization of preferred stock discount	-	-	-	(37,106)	-	37,106	-	-
Preferred stock dividend	-	-	-	(184,222)	-	-	-	(184,222)
Issuance of common stock	-	-	-	-	-	-	-	-
Stock based compensation	-	-	241	-	-	-	-	241
Minimum pension adjustment (net of income taxes of \$2,917)	-	-	-	-	-	-	2,145	2,145
Net loss	-	-	-	(511,034)	-	-	-	(511,034)
Change in unrealized gain on investment securities available-for-sale, net of reclassification and tax effect	-	-	-	-	-	-	(45,478)	(45,478)
Balance, March 31, 2013	\$58,952	\$17,007,180	\$40,705,498	\$(33,905,887)	\$732,479	\$(161,887)	\$(209,882)	\$24,226,453
Balance, December 31, 2011	\$58,952	\$16,973,512	\$40,732,178	\$(21,895,557)	\$732,479	\$(346,473)	\$(7,449)	\$36,247,642
Amortization of preferred stock	-	-	-	-	-	-	-	-

Edgar Filing: Village Bank & Trust Financial Corp. - Form 10-Q

discount	-		(36,729)	-	36,729			-
Preferred stock dividend	-	-	(183,719)	-	-	-		(183,719)
Issuance of common stock	-	33,668	(33,668)	-	-	-		-
Stock based compensation			1,589					1,589
Minimum pension adjustment (net of income taxes of \$2,917)	-	-	-	-	-	-	2,145	2,145
Net loss	-	-	-	(1,400,380)	-	-	-	(1,400,380)
Change in unrealized gain on investment securities available-for-sale, net of reclassification and tax effect	-	-	-	-	-	-	(357,431)	(357,431)
Balance, March 31, 2012	\$58,952	\$17,007,180	\$40,700,099	\$(23,516,385)	\$732,479	\$(309,744)	\$(362,735)	\$34,309,846

See accompanying notes to consolidated financial statements.

Village Bank and Trust Financial Corp. and Subsidiary
Consolidated Statements of Cash Flows
Three Months Ended March 31, 2013 and 2012
(Unaudited)

	Three Months Ended March 31,	
	2013	2012
Cash Flows from Operating Activities		
Net loss	\$(511,034)	\$(1,400,380)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:		
Depreciation and amortization	258,649	344,244
Deferred income taxes	(108,145)	1,104
Valuation allowance	-	476,129
Provision for loan losses	823,000	1,735,000
Write-down of other real estate owned	397,053	670,023
Gain on securities sold	(90,067)	(164,207)
Gain on loans sold	(1,955,717)	(1,750,663)
Gain on sale of premises and equipment	(598,182)	-
(Gain) loss on sale of other real estate owned	129,821	4,355
Stock compensation expense	241	1,589
Proceeds from sale of mortgage loans	67,727,357	64,848,047
Origination of mortgage loans for sale	(57,961,082)	(64,120,807)
Amortization of premiums and accretion of discounts on securities, net	86,934	39,306
Decrease in interest receivable	96,371	146,743
Increase in bank owned life insurance	(50,307)	(50,392)
(Increase) decrease in other assets	730,900	2,899,037
Increase (decrease) in interest payable	69,892	74,487
Increase (decrease) in other liabilities	324,488	(2,959,078)
Net cash provided by operating activities	9,370,172	794,537
Cash Flows from Investing Activities		
Purchases of available for sale securities	(12,791,077)	(20,764,694)
Proceeds from the sale or calls of available for sale securities	8,244,304	14,277,005
Proceeds from maturities and principal payments of available for sale securities	-	874,715
Net decrease (increase) in loans	26,731,220	5,847,047
Proceeds from sale of other real estate owned	1,162,364	526,370
Purchases of premises and equipment	481,213	(44,839)
Proceeds from sale of premises and equipment	1,681,624	-
Net cash provided by investing activities	25,509,648	715,604
Cash Flows from Financing Activities		
Net increase (decrease) in deposits	(14,903,717)	(20,127,993)
Net increase (decrease) in Federal Home Loan Bank Advances	(1,000,000)	(1,000,000)
Net increase (decrease) in other borrowings	(2,969,465)	(571,092)
Net cash used in financing activities	(18,873,182)	(21,699,085)

Edgar Filing: Village Bank & Trust Financial Corp. - Form 10-Q

Net increase (decrease) in cash and cash equivalents	16,006,638	(20,188,944)
Cash and cash equivalents, beginning of period	53,130,942	62,786,016
Cash and cash equivalents, end of period	\$69,137,580	\$42,597,072
Supplemental Schedule of Non Cash Activities		
Real estate owned assets acquired in settlement of loans	\$2,868,378	\$6,614,046
Dividends on preferred stock accrued	\$184,224	\$183,719

See accompanying notes to consolidated financial statements.

Village Bank and Trust Financial Corp. and Subsidiary
Notes to Condensed Consolidated Financial Statements
Three Months Ended March 31, 2013 and 2012
(Unaudited)

Note 1 - Principles of presentation

Village Bank and Trust Financial Corp. (the “Company”) is the holding company of Village Bank (the “Bank”). The consolidated financial statements include the accounts of the Company, the Bank and the Bank’s subsidiaries. All material intercompany balances and transactions have been eliminated in consolidation.

In the opinion of management, the accompanying condensed consolidated financial statements of the Company have been prepared on the accrual basis in accordance with generally accepted accounting principles for interim financial information. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. However, all adjustments that are, in the opinion of management, necessary for a fair presentation have been included. The results of operations for the three month period ended March 31, 2013 are not necessarily indicative of the results to be expected for the full year ending December 31, 2013. The unaudited interim financial statements should be read in conjunction with the audited financial statements and notes to financial statements that are presented in the Company’s Annual Report on Form 10-K for the year ended December 31, 2012 as filed with the Securities and Exchange Commission.

Note 2 - Use of estimates

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the date of the statements of financial condition and revenues and expenses during the reporting period. Actual results could differ significantly from those estimates. A material estimate that is particularly susceptible to significant change in the near term relates to the determination of the allowance for loan losses and the related provision.

Note 3 – Earnings (loss) per common share

The following table presents the basic and diluted earnings per share computations:

	Three Months Ended March 31,	
	2013	2012
Numerator		
Net income (loss) - basic and diluted	\$ (511,034)	\$ (1,400,380)
Preferred stock dividend and accretion	221,328	220,448
Net income (loss) available to common shareholders	\$ (732,362)	\$ (1,620,828)
Denominator		
Weighted average shares outstanding - basic	4,253,932	4,249,336
Dilutive effect of common stock options and restricted stock awards	-	-
Weighted average shares outstanding - diluted	4,253,932	4,249,336
Earnings (loss) per share - basic and diluted		
Earnings (loss) per share - basic	\$ (0.17)	\$ (0.38)
Effect of dilutive common stock options	-	-
Earnings (loss) per share - diluted	\$ (0.17)	\$ (0.38)

Outstanding options and warrants to purchase common stock were considered in the computation of diluted earnings per share for the periods presented. Stock options for 254,630 and 264,530 shares of common stock were not included in computing diluted earnings per share for the three months ended March 31, 2013 and 2012, respectively, because their effects were anti-dilutive. Warrants for 499,029 shares of common stock were not included in computing earnings per share in 2013 and 2012 because their effects were also anti-dilutive.

Note 4 – Investment securities

At March 31, 2013 and December 31, 2012, all of our securities were classified as available for sale. The following table presents the composition of our investment portfolio at the dates indicated (dollars in thousands).

Edgar Filing: Village Bank & Trust Financial Corp. - Form 10-Q

	Par Value	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value	Average Yield	
March 31, 2013							
US Government Agencies							
Five to ten years	\$3,500	\$4,375	\$-	\$(33)	\$4,342	1.97	%
More than ten years	12,000	11,715	40	-	11,755	2.91	%
Total	15,500	16,090	40	(33)	16,097	2.65	%
Mortgage-backed securities							
More than ten years	1,445	1,513	2	(2)	1,513	0.97	%
Total	1,445	1,513	2	(2)	1,513	0.97	%
Municipals							
Five to ten years	3,700	4,226	2	(26)	4,202	2.16	%
More than ten years	6,280	7,984	3	(164)	7,823	2.27	%
Total	9,980	12,210	5	(190)	12,025	2.23	%
Total investment securities	\$26,925	\$29,813	\$47	\$(225)	\$29,635	2.40	%
December 31, 2012							
US Government Agencies							
More than ten years	\$10,500	\$11,394	\$8	\$(15)	\$11,387	2.27	%
Total	10,500	11,394	8	(15)	11,387	2.27	%
Mortgage-backed securities							
More than ten years	1,744	1,830	1	(2)	1,829	0.97	%
Total	1,744	1,830	1	(2)	1,829	0.97	%
Municipals							
One to five years	1,000	1,100	-	(22)	1,078	3.25	%
Five to ten years	3,500	4,031	-	(47)	3,984	2.29	%
More than ten years	5,280	6,908	10	(42)	6,876	2.70	%
Total	9,780	12,039	10	(111)	11,938	2.61	%
Total investment securities	\$22,024	\$25,263	\$19	\$(128)	\$25,154	2.34	%

Investment securities available for sale that have an unrealized loss position at March 31, 2013 and December 31, 2012 are detailed below (in thousands):

	Securities in a loss Position for less than 12 Months		Securities in a loss Position for more than 12 Months		Total	
	Fair Value	Unrealized Losses	Fair Value (Loss)	Unrealized Losses	Fair Value	Unrealized Losses
March 31, 2013						
Investment Securities available for sale						
US Treasuries	\$6,241	\$(33)	\$-	\$-	\$6,241	\$(33)
Municipals	8,797	(190)	-	-	8,797	(190)
Mortgage-backed securities	162	(2)	-	-	162	(2)
Total	\$15,200	\$(225)	\$-	\$-	\$15,200	\$(225)
December 31, 2012						
Investment Securities available for sale						
US Treasuries	\$4,378	\$(15)	\$-	\$-	\$4,378	\$(15)
Municipals	8,064	(111)	-	-	8,064	(111)
Mortgage-backed securities	167	(2)	-	-	167	(2)
Total	\$12,609	\$(128)	\$-	\$-	\$12,609	\$(128)

Management does not believe that any individual unrealized loss as of March 31, 2013 and December 31, 2012 is other than a temporary impairment. These unrealized losses are primarily attributable to changes in interest rates. As of March 31, 2013, management does not have the intent to sell any of the securities classified as available for sale and management believes that it is more likely than not that the Company will not have to sell any such securities before a recovery of cost.

Note 5 – Loans and allowance for loan losses

The following table presents the composition of our loan portfolio (excluding mortgage loans held for sale) at the dates indicated (dollars in thousands).

Edgar Filing: Village Bank & Trust Financial Corp. - Form 10-Q

	March 31, 2013		December 31, 2012		
	Amount	%	Amount	%	
Construction and land development					
Residential	\$3,002	0.93	% \$2,845	0.80	%
Commercial	36,209	11.18	% 41,210	11.61	%
Total construction and land development	39,211	12.11	% 44,055	12.41	%
Commercial real estate					
Farmland	2,571	0.79	% 2,581	0.73	%
Commercial real estate - owner occupied	81,459	25.14	% 92,773	26.14	%
Commercial real estate - non-owner occupied	47,470	14.65	% 54,551	15.37	%
Multifamily	8,908	2.75	% 7,979	2.25	%
Total commercial real estate	140,408	43.33	% 157,884	44.49	%
Consumer real estate					
Home equity lines	24,614	7.60	% 25,521	7.19	%
Secured by 1-4 family residential, secured by first deeds of trust	78,796	24.32	% 80,788	22.76	%
Secured by 1-4 family residential, secured by second deeds of trust	8,668	2.67	% 9,517	2.68	%
Total consumer real estate	112,078	34.59	% 115,827	32.63	%
Commercial and industrial loans (except those secured by real estate)	29,647	9.15	% 34,384	9.69	%
Consumer and other	2,660	0.82	% 2,761	0.78	%
Total Loans	324,004	100.0	% 354,910	100.0	%
Deferred loan cost (unearned income), net	783		788		
Less: Allowance for loan losses	(10,320)		(10,808)		
	\$314,467		\$344,890		

The Company assigns risk rating classifications to its loans. These risk ratings are divided into the following groups:

- Risk rated 1 to 4 loans are considered of sufficient quality to preclude an adverse rating. 1-4 assets generally are well protected by the current net worth and paying capacity of the obligor or by the value of the asset or underlying collateral;
 - Risk rated 5 loans are defined as having potential weaknesses that deserve management's close attention;
- Risk rated 6 loans are inadequately protected by the current sound worth and paying capacity of the obligor or of the collateral pledged, if any, and;
- Risk rated 7 loans have all the weaknesses inherent in substandard loans, with the added characteristics that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions and values, highly questionable and improbable.

Edgar Filing: Village Bank & Trust Financial Corp. - Form 10-Q

The following tables provide information on the risk rating of loans at the dates indicated:

	March 31, 2013				Total Loans
	Risk Rated 1-4	Risk Rated 5	Risk Rated 6	Risk Rated 7	
Construction and land development					
Residential	\$2,794,616	\$207,597	\$-	\$-	\$3,002,213
Commercial	14,490,031	7,441,270	14,277,551	-	36,208,852
Total construction and land development	17,284,647	7,648,867	14,277,551	-	39,211,065
Commercial real estate					
Farmland	1,521,465		1,049,489	-	2,570,954
Commercial real estate - owner occupied	54,565,411	13,111,802	13,781,322	-	81,458,535
Commercial real estate - non-owner occupied	17,545,150	17,237,400	12,431,518	256,067	47,470,135
Multifamily	5,426,270	1,072,501	2,409,185	-	8,907,956
Total commercial real estate	79,058,296	31,421,703	29,671,514	256,067	140,407,580
Consumer real estate					
Home equity lines	19,225,118	1,533,770	3,855,576	-	24,614,464
Secured by 1-4 family residential, secured by first deeds of trust	48,349,677	12,472,929	17,973,830	-	78,796,436
Secured by 1-4 family residential, secured by second deeds of trust	6,756,458	205,169	1,706,021	-	8,667,648
Total consumer real estate	74,331,253	14,211,868	23,535,427	-	112,078,548
Commercial and industrial loans (except those secured by real estate)	21,795,862	2,987,775	4,863,410	-	29,647,047
Consumer and other	2,316,604	172,908	170,740	-	2,660,252
Total loans	\$194,786,662	\$56,443,121	\$72,518,642	\$256,067	\$324,004,492

	December 31, 2012				Total Loans
	Risk Rated 1-4	Risk Rated 5	Risk Rated 6	Risk Rated 7	
Construction and land development:					
Residential	\$2,173,885	\$671,709	\$-	\$-	\$2,845,594
Commercial	17,638,646	7,496,950	16,074,235	-	41,209,831
Total construction and land development	19,812,531	8,168,659	16,074,235	-	44,055,425
Commercial real estate:					
Farmland	1,531,808	-	1,049,489	-	2,581,297
Commercial real estate - owner occupied	63,772,277	19,273,229	9,727,026	-	92,772,532
Commercial real estate - non-owner occupied	24,199,053	15,671,633	14,170,546	509,585	54,550,817
Multifamily	5,438,427	1,739,283	800,679	-	7,978,389
Total commercial real estate	94,941,565	36,684,145	25,747,740	509,585	157,883,035

Edgar Filing: Village Bank & Trust Financial Corp. - Form 10-Q

Consumer real estate:					
Home equity lines	20,180,206	2,015,248	3,325,943	-	25,521,397
Secured by 1-4 family residential, secured by first deeds of trust	49,659,724	11,235,261	19,893,440	-	80,788,425
Secured by 1-4 family residential, secured by second deeds of trust	7,385,394	342,770	1,789,081	-	9,517,245
Total consumer real estate	77,225,324	13,593,279	25,008,464	-	115,827,067
Commercial and industrial loans (except those secured by real estate)	26,712,028	2,590,735	5,081,354	-	34,384,117
Consumer and other	2,446,304	261,140	53,178	-	2,760,622
 Total Loans	 \$221,137,752	 \$61,297,958	 \$71,964,971	 \$509,585	 \$354,910,266

Edgar Filing: Village Bank & Trust Financial Corp. - Form 10-Q

The following table presents the aging of the recorded investment in past due loans and leases as of the dates indicated:

	March 31, 2013						Recorded Investment > 90 Days and Accruing
	30-59 Days Past Due	60-89 Days Past Due	Greater Than 90 Days	Total Past Due	Current	Total Loans	
Construction and land development							
Residential	\$ -	\$ -	\$ -	\$ -	\$ 3,002,213	\$ 3,002,213	\$ -
Commercial	86,941	6,051	120,489	213,481	35,995,371	36,208,852	120,489
Total construction and land development	86,941	6,051	120,489	213,481	38,997,584	39,211,065	120,489
Commercial real estate							
Farmland	-	-	-	-	2,570,954	2,570,954	-
Commercial real estate - owner occupied	1,576,739	376,707	-	1,953,446	79,505,089	81,458,535	-
Commercial real estate - non-owner occupied	1,186,292	-	-	1,186,292	46,283,843	47,470,135	-
Multifamily	-	-	-	-	8,907,956	8,907,956	-
Total commercial real estate	2,763,031	376,707	-	3,139,738	137,267,842	140,407,580	-
Consumer real estate							
Home equity lines Secured by 1-4 family residential, secured by first deeds of trust	168,713	-	-	168,713	24,445,751	24,614,464	-
Secured by 1-4 family residential, secured by second deeds of trust	1,121,751	60,778	-	1,182,529	77,613,907	78,796,436	-
Total consumer real estate	1,805,507	60,778	-	1,866,285	110,212,263	112,078,548	-
Commercial and industrial loans							

Edgar Filing: Village Bank & Trust Financial Corp. - Form 10-Q

(except those secured by real estate)	246,611	-	-	246,611	29,400,436	29,647,047	-
Consumer and other	11,535	13,962	-	25,497	2,634,755	2,660,252	-
Total loans	\$ 4,913,625	\$ 457,498	\$ 120,489	\$ 5,491,612	\$ 318,512,880	\$ 324,004,492	\$ 120,489

December 31, 2012

	30-59 Days Past Due	60-89 Days Past Due	Greater Than 90 Days	Total Past Due	Current	Total Loans	Recorded Investment > 90 Days and Accruing
Construction and land development:							
Residential	\$ -	\$ -	\$ -	\$ -	\$ 2,845,594	\$ 2,845,594	\$ -
Commercial	76,351	10,709	-	87,060	41,122,771	41,209,831	-
Total construction and land development	76,351	10,709	-	87,060	43,968,365	44,055,425	-
Commercial real estate:							
Farmland	-	-	-	-	2,581,297	2,581,297	-
Commercial real estate - owner occupied	708,278	377,563	-	1,085,841	91,686,691	92,772,532	-
Commercial real estate - non-owner occupied	1,094,906	714,655	-	1,809,561	52,741,256	54,550,817	-
Multifamily	-	-	-	-	7,978,389	7,978,389	-
Total commercial real estate	1,803,184	1,092,218	-	2,895,402	154,987,633	157,883,035	-
Consumer real estate:							
Home equity lines	110,614	24,746	16,130	151,490	25,369,907	25,521,397	16,130
Secured by 1-4 family residential, secured by first deeds of trust	645,807	1,507,073	-	2,152,880	78,635,545	80,788,425	-

Secured by 1-4 family residential, secured by second deeds of trust	157,816	50,016	50,000	257,832	9,259,413	9,517,245	50,000
Total consumer real estate	914,237	1,581,835	66,130	2,562,202	113,264,865	115,827,067	66,130
Commercial and industrial loans (except those secured by real estate)	40,171	31,057	49,139	120,367	34,263,750	34,384,117	49,139
Consumer and other	4,286	36,030	-	40,316	2,720,306	2,760,622	-
Total Loans	\$ 2,838,229	\$ 2,751,849	\$ 115,269	\$ 5,705,347	\$ 349,204,919	\$ 354,910,266	\$ 115,269

Loans are considered impaired when, based on current information and events it is probable the Company will be unable to collect all amounts due in accordance with the original contractual terms of the loan agreement, including scheduled principal and interest payments. Loans evaluated individually for impairment include non-performing loans, such as loans on non-accrual, loans past due by 90 days or more, restructured loans and other loans selected by management. The evaluations are based upon discounted expected cash flows or collateral valuations. If the evaluation shows that a loan is individually impaired, then a specific reserve is established for the amount of impairment. Impairment is evaluated in total for smaller-balance loans of a similar nature and on an individual loan basis for other loans. If a loan is impaired, a specific valuation allowance is allocated, if necessary, so that the loan is reported net, at the present value of estimated future cash flows using the loan's existing rate or at the fair value of collateral if repayment is expected solely from the collateral. Interest payments on impaired loans are typically applied to principal unless collectability of the principal amount is reasonably assured, in which case interest is recognized on a cash basis. Impaired loans, or portions thereof, are charged off when deemed uncollectible. Impaired loans are set forth in the following table as of the dates indicated.

Edgar Filing: Village Bank & Trust Financial Corp. - Form 10-Q

March 31, 2013

	Recorded Investment	Unpaid Principal Balance	Related Allowance
With no related allowance recorded			
Construction and land development			
Residential	\$ 140,000	\$-	\$-
Commercial	7,083,847	10,655,937	-
Total construction and land development	7,223,847	10,655,937	-
Commercial real estate			
Farmland	-	-	-
Commercial real estate - owner occupied	7,221,916	7,267,500	-
Commercial real estate - non-owner occupied	14,521,050	14,719,050	-
Multifamily	3,035,772	3,035,772	-
Total commercial real estate	24,778,738	25,022,322	-
Consumer real estate			
Home equity lines	1,801,054	1,813,711	-
Secured by 1-4 family residential, secured by first deeds of trust	12,471,376	12,791,266	-
Secured by 1-4 family residential, secured by second deeds of trust	502,373	623,745	-
Total consumer real estate	14,774,803	15,228,722	-
Commercial and industrial loans (except those secured by real estate)	887,084	1,486,503	-
Consumer and other	65,200	65,200	-
	\$47,729,672	\$52,458,684	\$-
With an allowance recorded			
Construction and land development			
Residential	\$-	\$-	\$-
Commercial	1,511,725	1,511,725	576,673
Total construction and land development	1,511,725	1,511,725	576,673
Commercial real estate			
Farmland	1,049,489	1,049,489	808,000
Commercial real estate - owner occupied	2,232,374	2,232,374	498,556
Commercial real estate - non-owner occupied	253,517	509,585	253,517
Multifamily	-	-	-
Total commercial real estate	3,535,380	3,791,448	1,560,073
Consumer real estate			
Home equity lines	269,450	269,450	39,000
Secured by 1-4 family residential, secured by first deeds of trust	831,350	831,350	71,301
Secured by 1-4 family residential, secured by second deeds of trust	331,943	380,227	37,054
Total consumer real estate	1,432,743	1,481,027	147,355
Commercial and industrial loans (except those secured by real estate)	64,672	64,672	37,600
Consumer and other	-	-	-
	\$6,544,520	\$6,848,872	\$2,321,701
Total			
Construction and land development			

Edgar Filing: Village Bank & Trust Financial Corp. - Form 10-Q

Residential	\$140,000	\$-	\$-
Commercial	8,595,572	12,167,662	576,673
Total construction and land development	8,735,572	12,167,662	576,673
Commercial real estate			
Farmland	1,049,489	1,049,489	808,000
Commercial real estate - owner occupied	9,454,290	9,499,874	498,556
Commercial real estate - non-owner occupied	14,774,567	15,228,635	253,517
Multifamily	3,035,772	3,035,772	-
Total commercial real estate	28,314,118	28,813,770	1,560,073
Consumer real estate			
Home equity lines	2,070,504	2,083,161	39,000
Secured by 1-4 family residential, secured by first deeds of trust	13,302,726	13,622,616	71,301
Secured by 1-4 family residential, secured by second deeds of trust	834,316	1,003,972	37,054
Total consumer real estate	16,207,546	16,709,749	147,355
Commercial and industrial loans (except those secured by real estate)	951,756	1,551,175	37,600
Consumer and other	65,200	65,200	-
	\$54,274,192	\$59,307,556	\$2,321,701

Edgar Filing: Village Bank & Trust Financial Corp. - Form 10-Q

December 31, 2012

	Recorded Investment	Unpaid Principal Balance	Related Allowance
With no related allowance recorded			
Construction and land development			
Residential	\$-	\$-	\$-
Commercial	8,254,440	13,625,670	-
Total construction and land development	8,254,440	13,625,670	-
Commercial real estate			
Farmland	1,049,489	1,049,489	-
Commercial real estate - owner occupied	8,250,071	8,715,684	-
Commercial real estate - non-owner occupied	13,777,787	14,124,016	-
Multifamily	2,825,274	2,825,274	-
Total commercial real estate	25,902,621	26,714,463	-
Consumer real estate			
Home equity lines	1,939,020	1,938,005	-
Secured by 1-4 family residential, secured by first deeds of trust	10,686,435	10,928,024	-
Secured by 1-4 family residential, secured by second deeds of trust	601,805	861,158	-
Total consumer real estate	13,227,260	13,727,187	-
Commercial and industrial loans (except those secured by real estate)	858,136	1,421,196	-
Consumer and other	50,415	50,390	-
	\$48,292,872	\$55,538,906	\$-
With an allowance recorded			
Construction and land development:			
Residential	\$-	\$-	\$-
Commercial	430,828	430,828	62,643
Total construction and land development	430,828	430,828	62,643
Commercial real estate:			
Farmland			
Commercial real estate - owner occupied	2,940,647	3,261,584	663,330
Commercial real estate - non-owner occupied	1,434,195	1,434,195	508,704
Multifamily	-	-	-
Total commercial real estate	4,374,842	4,695,779	1,172,034
Consumer real estate:			
Home equity lines	-	-	-
Secured by 1-4 family residential, secured by first deeds of trust	1,155,027	1,155,027	20,896
Secured by 1-4 family residential, secured by second deeds of trust	338,345	386,629	43,456
Total consumer real estate	1,493,372	1,541,656	64,352
Commercial and industrial loans (except those secured by real estate)	182,840	182,840	39,243
Consumer and other	-	-	-
	\$6,481,882	\$6,851,103	\$1,338,272
Total			
Construction and land development			

Edgar Filing: Village Bank & Trust Financial Corp. - Form 10-Q

Residential	\$-	\$-	\$-
Commercial	8,685,268	14,056,498	62,643
Total construction and land development	8,685,268	14,056,498	62,643
Commercial real estate			
Farmland	1,049,489	1,049,489	-
Commercial real estate - owner occupied	11,190,718	11,977,268	663,330
Commercial real estate - non-owner occupied	15,211,982	15,558,211	508,704
Multifamily	2,825,274	2,825,274	-
Total commercial real estate	30,277,463	31,410,242	1,172,034
Consumer real estate			
Home equity lines	1,939,020	1,938,005	-
Secured by 1-4 family residential, secured by first deeds of trust	11,841,462	12,083,051	20,896
Secured by 1-4 family residential, secured by second deeds of trust	940,150	1,247,787	43,456
Total consumer real estate	14,720,632	15,268,843	64,352
Commercial and industrial loans (except those secured by real estate)	1,040,976	1,604,036	39,243
Consumer and other	50,415	50,390	-
	\$54,774,754	\$62,390,009	\$1,338,272

Edgar Filing: Village Bank & Trust Financial Corp. - Form 10-Q

The following is a summary of average recorded investment in impaired loans with and without a valuation allowance and interest income recognized on those loans for periods indicated:

	For the Three Months Ended March 31, 2013		For the Three Months Ended March 31, 2012	
	Average Recorded Investment	Interest Income Recognized	Average Recorded Investment	Interest Income Recognized
With no related allowance recorded				
Construction and land development				
Residential	\$-	\$-	\$1,623,982	\$7,401
Commercial	7,406,223	60,175	13,733,356	122,256
Total construction and land development	7,406,223	60,175	15,357,338	129,657
Commercial real estate				
Farmland				
Commercial real estate - owner occupied	7,119,781	136,728	9,534,154	99,464
Commercial real estate - non-owner occupied	14,579,438	206,192	8,079,949	173,981
Multifamily	3,043,344	51,755	613,649	8,828
Total commercial real estate	24,742,563	394,675	18,227,752	282,273
Consumer real estate				
Home equity lines				
Secured by 1-4 family residential, secured by first deeds of trust	1,801,054	-	1,392,575	5,024
Secured by 1-4 family residential, secured by second deeds of trust	12,541,557	128,977	10,085,840	107,583
Total consumer real estate	507,002	6,789	488,266	5,550
Commercial and industrial loans (except those secured by real estate)	14,849,613	135,766	11,966,681	118,157
Consumer and other	897,988	8,944	1,255,796	8,612
	68,248	1,092	361,260	648
	\$47,964,635	\$600,652	\$47,168,827	\$539,347
With an allowance recorded				
Construction and land development				
Residential	\$-	\$-	\$179,863	\$-
Commercial	458,065	1,628	10,555,142	37,116
Total construction and land development	458,065	1,628	10,735,005	37,116
Commercial real estate				
Farmland				
Commercial real estate - owner occupied	1,049,489	1,100	-	-
Commercial real estate - non-owner occupied	2,400,696	11,935	4,673,921	-
Multifamily	256,067	-	961,039	-
Total commercial real estate	-	-	-	-
Consumer real estate	3,706,252	13,035	5,634,960	-
Home equity lines				
Secured by 1-4 family residential, secured by first deeds of trust	269,450	6,792	135,404	156
	835,505	6,076	2,430,635	10,377
	349,192	6,401	-	-

Edgar Filing: Village Bank & Trust Financial Corp. - Form 10-Q

Secured by 1-4 family residential, secured by second deeds of trust				
Total consumer real estate	1,454,147	19,269	2,566,039	10,533
Commercial and industrial loans (except those secured by real estate)	64,672	1,290	493,239	7,516
Consumer and other	-	-	-	-
	\$5,683,136	\$35,222	\$19,429,243	\$55,165
Total				
Construction and land development				
Residential	\$-	\$-	\$1,803,845	\$7,401
Commercial	7,864,288	61,803	24,288,498	159,372
Total construction and land development	7,864,288	61,803	26,092,343	166,773
Commercial real estate				
Farmland	1,049,489	1,100	-	-
Commercial real estate - owner occupied	9,520,477	148,663	14,208,075	99,464
Commercial real estate - non-owner occupied	14,835,505	206,192	9,040,988	173,981
Multifamily	3,043,344	51,755	613,649	8,828
Total commercial real estate	28,448,815	407,710	23,862,712	282,273
Consumer real estate				
Home equity lines	2,070,504	6,792	1,527,979	5,180
Secured by 1-4 family residential, secured by first deeds of trust	13,377,062	135,053	12,516,475	117,960
Secured by 1-4 family residential, secured by second deeds of trust	856,194	13,190	488,266	5,550
Total consumer real estate	16,303,760	155,035	14,532,720	128,690
Commercial and industrial loans (except those secured by real estate)	962,660	10,234	1,749,035	16,128
Consumer and other	68,248	1,092	361,260	648
	\$53,647,771	\$635,874	\$66,598,070	\$594,512

Included in impaired loans are loans classified as troubled debt restructurings (TDRs). A modification of a loan's terms constitutes a TDR if the creditor grants a concession to the borrower for economic or legal reasons related to the borrowers financial difficulties that it would not otherwise consider. For loans classified as impaired TDRs, the Company further evaluates the loans as performing or nonperforming. If, at the time of restructure, the loan is not

considered nonaccrual, it will be classified as performing. TDRs originally classified as nonperforming are able to be reclassified as performing if, subsequent to restructure, they experience six months of payment performance according to the restructured terms. The following is a summary of performing and nonaccrual TDRs and the related specific valuation allowance by portfolio segment as of the dates indicated.

	March 31, 2013			Specific Valuation Allowance
	Total	Performing	Nonaccrual	
Construction and land development				
Residential	\$-	\$-	\$-	\$-
Commercial	5,273,375	3,462,875	1,810,500	24,335
Total construction and land development	5,273,375	3,462,875	1,810,500	24,335
Commercial real estate				
Farmland	-	-	-	-
Commercial real estate - owner occupied	7,085,576	6,611,634	473,942	16,158
Commercial real estate - non-owner occupied	13,904,061	13,196,846	707,215	-
Multifamily	3,035,772	3,035,772	-	-
Total commercial real estate	24,025,409	22,844,252	1,181,157	16,158
Consumer real estate				
Home equity lines	-	-	-	-
Secured by 1-4 family residential, secured by first deeds of trust	7,447,130	3,572,375	3,874,755	33,299
Secured by 1-4 family residential, secured by second deeds of trust	331,943	-	331,943	37,054
Total consumer real estate	7,779,073	3,572,375	4,206,698	70,353
Commercial and industrial loans (except those secured by real estate)	321,477	123,234	198,243	-
Consumer and other	-	-	-	-
Total loans	\$37,399,334	\$30,002,736	\$7,396,598	\$110,846
Number of loans	78	51	27	4

Edgar Filing: Village Bank & Trust Financial Corp. - Form 10-Q

	December 31, 2012			Specific Valuation Allowance
	Total	Performing	Nonaccrual	
Construction and land development				
Commercial	\$6,116,248	\$3,728,403	\$2,387,845	\$-
Total construction and land development	6,116,248	3,728,403	2,387,845	-
Commercial real estate				
Commercial real estate - owner occupied	8,881,257	6,373,122	2,508,135	3,321
Commercial real estate - non-owner occupied	13,266,992	12,805,727	461,265	-
Multifamily	2,825,274	2,825,274	-	-
Total commercial real estate	24,973,523	22,004,123	2,969,400	3,321
Consumer real estate				
Home equity lines	-	-	-	-
Secured by 1-4 family residential, secured by first deeds of trust	7,011,329	3,431,124	3,580,205	15,633
Secured by 1-4 family residential, secured by second deeds of trust	338,344	-	338,344	43,456
Total consumer real estate	7,349,673	3,431,124	3,918,549	59,089
Commercial and industrial loans (except those secured by real estate)	380,427	5,803	374,624	39,243
Total	\$38,819,871	\$29,169,453	\$9,650,418	\$101,653
Number of loans	73	46	27	7

The following table provides information about TDRs identified during the indicated periods:

	March 31, 2013			December 31, 2012		
	Number of Loans	Pre- Modification	Post- Modification	Number of Loans	Pre- Modification	Post- Modification
		Recorded Balance	Recorded Balance		Recorded Balance	Recorded Balance
Construction and land development:						
Residential	-	\$ -	\$ -		\$ -	\$ -
Commercial	1	196,440	196,440	6	653,612	653,612
Total construction and land development	1	196,440	196,440	6	653,612	653,612
Commercial real estate:						
Farmland	-	-	-	-	-	-
Commercial real estate - owner occupied	1	277,272	277,272	1	522,715	522,715
Commercial real estate - non-owner occupied	-	-	-	6	2,102,231	2,102,231
Multifamily	-	-	-	-	-	-

Edgar Filing: Village Bank & Trust Financial Corp. - Form 10-Q

Total commercial real estate	1	277,272	277,272	7	2,624,946	2,624,946
Consumer real estate:						
Home equity lines	-	-	-	-	-	-
Secured by 1-4 family residential, secured by first deeds of trust	4	437,089	437,089	25	5,570,245	5,570,245
Secured by 1-4 family residential, secured by second deeds of trust	-	-	-	1	338,344	338,344
Total consumer real estate	4	437,089	437,089	26	5,908,589	5,908,589
Commercial and industrial loans (except those secured by real estate)	-	-	-	1	117,813	117,813
Consumer and other	-	-	-	-	-	-
	6	\$ 910,801	\$ 910,801	40	\$ 9,304,960	\$ 9,304,960

The following table provides information about defaults of TDRs for the period indicated:

	Three Months Ended March 31, 2013	
	Number of Loans	Recorded Balance
Defaults on TDRs		
Construction and land development		
Residential		
Commercial	4	\$1,403,928
Total construction and land development	4	1,403,928
Commercial real estate		
Farmland	-	-
Commercial real estate - owner occupied	1	473,942
Commercial real estate - non-owner occupied	-	-
Multifamily	1	473,942
Total commercial real estate		
Consumer real estate		
Home equity lines	-	-
Secured by 1-4 family residential, secured by first deeds of trust	3	414,216
Secured by 1-4 family residential, secured by second deeds of trust	-	-
Total consumer real estate	3	414,216
Commercial and industrial loans (except those secured by real estate)	3	206,760
Consumer and other	-	-
Total	11	\$2,498,846

Edgar Filing: Village Bank & Trust Financial Corp. - Form 10-Q

Activity in the allowance for loan losses is as follows for the periods indicated:

	Allowance for Loan Losses				Ending Balance
	Beginning Balance	Provision for Loan Losses	Charge-offs	Recoveries	
Three Months Ended March 31, 2013					
Construction and land development					
Residential	\$494,742	\$-	\$-	\$450	\$495,192
Commercial	4,611,410	15,000	(84,284)	-	4,542,126
Commercial real estate					
Farmland	-	808,000	-	-	808,000
Commercial real estate - owner occupied	1,358,863	-	(136,378)	-	1,222,485
Commercial real estate - non-owner occupied	816,852	-	(256,068)	-	560,784
Multifamily	23,434	-	-	-	23,434
Consumer real estate					
Home equity lines	658,135	-	(54,657)	200	603,678
Secured by 1-4 family residential, secured by first deeds of trust	1,358,102	-	(343,133)	8,026	1,022,995
Secured by 1-4 family residential, secured by second deeds of trust	223,307	-	(214,720)	3,035	11,622
Commercial and industrial loans (except those secured by real estate)	1,161,654	-	(288,831)	56,376	929,199
Consumer and other	101,328	-	(3,762)	2,884	100,450
Total	\$10,807,827	\$823,000	\$(1,381,833)	\$70,971	\$10,319,965
Year Ended December 31, 2012					
Construction and land development					
Residential	\$704,728	\$542,067	\$(797,286)	\$45,233	\$494,742
Commercial	6,798,177	3,444,160	(5,645,064)	14,137	4,611,410
Commercial real estate					
Farmland	-	-	-	-	-
Commercial real estate - owner occupied	1,496,466	623,552	(961,155)	200,000	1,358,863
Commercial real estate - non-owner occupied	1,548,899	(300,898)	(431,354)	205	816,852
Multifamily	406,635	(373,238)	(9,963)	-	23,434
Consumer real estate					
Home equity lines	860,307	668,614	(883,848)	13,062	658,135
Secured by 1-4 family residential, secured by first deeds of trust	1,881,470	2,610,905	(3,220,072)	85,799	1,358,102
Secured by 1-4 family residential, secured by second deeds of trust	397,504	468,192	(663,135)	20,746	223,307
Commercial and industrial loans (except those secured by real estate)	1,655,713	1,230,555	(1,879,517)	154,903	1,161,654
Consumer and other	321,525	181,091	(408,302)	7,014	101,328

Edgar Filing: Village Bank & Trust Financial Corp. - Form 10-Q

Total	\$16,071,424	\$9,095,000	\$(14,899,696)	\$541,099	\$10,807,827
	Allowance for Loan Losses				
	Beginning	Provision			Ending
	Balance	for	Charge-offs	Recoveries	Balance
	Balance	Loan			Balance
		Losses			
Three Months Ended March 31, 2012					
Construction and land development					
Residential	\$704,728	\$(16,552)	\$(59,250)	\$450	\$629,376
Commercial	6,798,177	1,028,575	(1,547,200)	-	6,279,552
Commercial real estate					
Farmland	-	-	-	-	-
Commercial real estate - owner occupied	1,496,466	379,264	(29,000)	-	1,846,730
Commercial real estate - non-owner occupied	1,548,899	(695,971)	(90,748)	205	762,385
Multifamily	406,635	(314,860)	-	-	91,775
Consumer real estate					
Home equity lines	860,307	32,099	(122,500)	692	770,598
Secured by 1-4 family residential, secured by first deeds of trust	1,881,470	364,980	(965,749)	60,800	1,341,501
Secured by 1-4 family residential, secured by second deeds of trust	397,504	128,294	(190,639)	193	335,352
Commercial and industrial loans (except those secured by real estate)	1,655,713	759,125	(260,402)	27,367	2,181,803
Consumer and other	321,525	70,046	(269,794)	1,104	122,881
Total	\$16,071,424	\$1,735,000	\$(3,535,283)	\$90,811	\$14,361,953

Edgar Filing: Village Bank & Trust Financial Corp. - Form 10-Q

Loans were evaluated for impairment as follows for the periods indicated:

	Individually	Collectively	Total
Three Months Ended March 31, 2013			
Construction and land development			
Residential	\$576,000	\$2,426,213	\$3,002,213
Commercial	23,702,091	12,506,761	36,208,852
Commercial real estate			
Farmland	1,388,359	1,182,595	2,570,954
Commercial real estate - owner occupied	58,403,265	23,055,270	81,458,535
Commercial real estate - non-owner occupied	35,892,993	11,577,142	47,470,135
Multifamily	7,227,452	1,680,504	8,907,956
Consumer real estate			
Home equity lines	2,172,383	22,442,081	24,614,464
Secured by 1-4 family residential, secured by first deeds of trust	13,664,311	65,132,125	78,796,436
Secured by 1-4 family residential, secured by second deeds of trust	551,467	8,116,181	8,667,648
Commercial and industrial loans (except those secured by real estate)	12,018,582	17,628,465	29,647,047
Consumer and other	-	2,660,252	2,660,252
		-	
Total	\$155,596,903	\$168,407,589	\$324,004,492
Year Ended December 31, 2012			
Construction and land development			
Residential	\$1,247,709	\$1,597,885	\$2,845,594
Commercial	27,351,857	13,857,974	41,209,831
Commercial real estate			
Farmland	1,391,501	1,189,796	2,581,297
Commercial real estate - owner occupied	67,167,587	25,604,945	92,772,532
Commercial real estate - non-owner occupied	41,801,577	12,749,240	54,550,817
Multifamily	6,461,639	1,516,750	7,978,389
Consumer real estate			
Home equity lines	2,185,040	23,336,357	25,521,397
Secured by 1-4 family residential, secured by first deeds of trust	15,526,551	65,261,874	80,788,425
Secured by 1-4 family residential, secured by second deeds of trust	557,600	8,959,645	9,517,245
Commercial and industrial loans (except those secured by real estate)	15,101,291	19,282,826	34,384,117
Consumer and other	-	2,760,622	2,760,622
Total	\$178,792,352	\$176,117,914	\$354,910,266

Note 6 – Deposits

Deposits as of March 31, 2013 and December 31, 2012 were as follows:

	March 31, 2013		December 31, 2012	
	Amount	%	Amount	%
Demand accounts	\$ 62,301,743	14.8 %	\$ 57,049,348	13.1 %
Interest checking accounts	43,567,794	10.3 %	45,861,199	10.5 %
Money market accounts	63,546,257	15.1 %	66,007,160	15.1 %
Savings accounts	20,469,642	4.9 %	20,922,112	4.8 %
Time deposits of \$100,000 and over	107,426,419	25.5 %	113,332,481	26.0 %
Other time deposits	124,107,390	29.4 %	133,150,662	30.5 %
Total	\$ 421,419,245	100.0 %	\$ 436,322,962	100.0 %

Note 7 – Trust preferred securities

During the first quarter of 2005, Southern Community Financial Capital Trust I, a wholly-owned subsidiary of the Company, was formed for the purpose of issuing redeemable securities. On February 24, 2005, \$5.2 million of Trust Preferred Capital Notes were issued through a pooled underwriting. The securities have a LIBOR-indexed floating rate of interest (three-month LIBOR plus 2.15%) which adjusts, and is payable, quarterly. The interest rate at March 31, 2013 was 2.43%. The securities were redeemable at par beginning on March 15, 2010 and each quarter after such date until the securities mature on March 15, 2035. No amounts have been redeemed at March 31, 2013 and there are no plans to do so. The principal asset of the Trust is \$5.2 million of the Company's junior subordinated debt securities with like maturities and like interest rates to the Trust Preferred Capital Notes.

During the third quarter of 2007, Village Financial Statutory Trust II, a wholly-owned subsidiary of the Company, was formed for the purpose of issuing redeemable securities. On September 20, 2007, \$3.6 million of Trust Preferred Capital Notes were issued through a pooled underwriting. The securities have a five year fixed income rate of 6.29% payable quarterly, converting after five years to a LIBOR-indexed floating rate of interest (three-month LIBOR plus 1.40%) which adjusts, and is also payable, quarterly. The securities may be redeemed at par at any time commencing in December 2012 until the securities mature in 2037. No amounts have been redeemed at March 31, 2013 and there are no plans to do so. The principal asset of the Trust is \$3.6 million of the Company's junior subordinated debt securities with like maturities and like interest rates to the Trust Preferred Capital Notes.

The Trust Preferred Capital Notes may be included in Tier 1 capital for regulatory capital adequacy determination purposes up to 25% of Tier 1 capital after its inclusion. The portion of the Trust Preferred Capital Notes not considered as Tier 1 capital may be included in Tier 2 capital.

The obligations of the Company with respect to the issuance of the Trust Preferred Capital Notes constitute a full and unconditional guarantee by the Company of the Trust's obligations with respect to the Trust Preferred Capital Notes. Subject to certain exceptions and limitations, the Company may elect from time to time to defer interest payments on the junior subordinated debt securities, which would result in a deferral of distribution payments on the related Trust Preferred Capital Notes and require a deferral of common dividends. In consideration of our

agreements with our regulators, which require regulatory approval to make interest payments on these securities, the Company has deferred an aggregate of \$716,347 in interest payments on the junior subordinated debt securities as March 31, 2013. The Company has been deferring interest payments since June 2011. Although we elected to defer payment of interest due, the amount has been accrued and is included in interest expense in the consolidated statement of operations.

Note 8 – Stock incentive plan

The Company has a stock incentive plan which authorizes the issuance of up to 455,000 shares of common stock to assist the Company in recruiting and retaining key personnel.

The following table summarizes stock options outstanding under the stock incentive plan at the indicated dates:

	Three Months Ended March 31,							
	2013			2012				
	Options	Weighted Average Exercise Price	Fair Value Per Share	Intrinsic Value	Options	Weighted Average Exercise Price	Fair Value Per Share	Intrinsic Value
Options outstanding, beginning of period	255,630	\$ 9.48	\$ 4.70		264,980	\$ 9.48	\$ 4.73	
Granted	-	-	-		-	-	-	
Forfeited	(1,000)	7.75	5.05		(450)	8.50	4.88	
Exercised	-	-	-		-	-	-	
Options outstanding, end of period	254,630	\$ 9.57	\$ 4.64	\$ -	264,530	\$ 9.65	\$ 4.73	\$ -
Options exercisable, end of period	249,630				261,530			

The fair value of the stock is calculated under the same methodology as stock options and the expense is recognized over the vesting period. Unamortized stock-based compensation related to nonvested share based compensation arrangements granted under the Incentive Plan as of March 31, 2013 and 2012 was \$2,249 and \$4,755 respectively. The time based unamortized compensation of \$2,249 is expected to be recognized over a weighted average period of 2.33 years.

Stock-based compensation expense was \$241 and \$1,589 for the three months ended March 31, 2013 and 2012 respectively.

Note 9 — Fair value

The fair value of an asset or liability is the price that would be received to sell that asset or paid to transfer that liability in an orderly transaction between market participants. A fair value measurement assumes that the transaction

to sell the asset or transfer the liability occurs in the principal market for the asset or liability or, in the absence of a principal market, the most advantageous market for the asset or liability. The price in the principal (or most advantageous) market used to measure the fair value of the asset or liability shall not be adjusted for transaction costs. An orderly transaction is a transaction that assumes exposure to the market for a period prior to the measurement date to allow for marketing activities that are usual and

customary for transaction involving such assets and liabilities; it is not a forced transaction. Market participants are buyers and sellers in the principal market that are independent, knowledgeable, able to transact and willing to transact.

FASB Codification Topic 820: Fair Value Measurements and Disclosures establishes a hierarchy for valuation inputs that gives the highest priority to quoted prices in active markets for identical assets or liabilities and the lowest priority to unobservable inputs. The fair values hierarch is as follows:

- Level 1 Inputs — Quoted prices (unadjusted) for identical assets or liabilities in active markets that the entity has the ability to access as of the measurement date.
- Level 2 Inputs — Significant other observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data.
- Level 3 Inputs- Significant unobservable inputs that reflect a company’s own assumptions about the assumptions that market participants would use in pricing an asset or liability.

The Company used the following methods to determine the fair value of each type of financial instrument:

Securities: Fair values for securities available-for-sale are obtained from an independent pricing service. The prices are not adjusted. The independent pricing service uses industry-standard models to price U.S. Government agency obligations and mortgage backed securities that consider various assumptions, including time value, yield curves, volatility factors, prepayment speeds, default rates, loss severity, current market and contractual prices for the underlying financial instruments, as well as other relevant economic measures. Securities of obligations of state and political subdivisions are valued using a type of matrix, or grid, pricing in which securities are benchmarked against the treasury rate based on credit rating. Substantially all assumptions used by the independent pricing service are observable in the marketplace, can be derived from observable data, or are supported by observable levels at which transactions are executed in the marketplace (Levels 1 and 2).

Impaired loans: The fair values of impaired loans are measured for impairment using the fair value of the collateral for collateral-dependent loans on a nonrecurring basis. Collateral may be in the form of real estate or business assets including equipment, inventory and accounts receivable. The vast majority of the Company’s collateral is real estate. The value of real estate collateral is determined utilizing an income or market valuation approach based on an appraisal conducted by an independent, licensed appraiser using observable market data (Level 2). However, if the collateral is a house or building in the process of construction or if an appraisal of the property is more than two years old, then a Level 3 valuation is considered to measure the fair value. The value of business equipment is based upon an outside appraisal if deemed significant using observable market data. Likewise, values for inventory and account receivables collateral are based on financial statement balances or aging reports (Level 3). Any fair value adjustments are recorded in the period incurred as provision for loan losses on the Consolidated Statements of Income.

Real Estate Owned: Real estate owned assets are adjusted to fair value upon transfer of the loans to foreclosed assets. Subsequently, real estate owned assets are carried at net realizable

value. Fair value is based upon independent market prices, appraised values of the collateral or management's estimation of the value of the collateral. When the fair value of the collateral is based on an observable market price or a current appraised value, the Company records the foreclosed asset as nonrecurring Level 2. When an appraised value is not available or management determines the fair value of the collateral is further impaired below the appraised value and there is no observable market price, the Company records the foreclosed asset as nonrecurring level 3.

Assets and liabilities measured at fair value under Topic 820 on a recurring and non-recurring basis are summarized below for the indicated dates:

	Carrying Value	Fair Value Measurement at March 31, 2013 Using (In thousands)		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Financial Assets - Recurring				
US Government Agencies	\$16,097	\$1,899	\$14,198	\$ -
MBS	1,513	-	1,513	-
Municipals	12,025	-	12,025	-
Residential loans held for sale	16,378	-	16,378	-
			-	
Financial Assets - Non-Recurring				
Impaired loans	54,274	-	45,750	8,524
Real estate owned	21,383	-	20,084	1,299

	Carrying Value	Fair Value Measurement at December 31, 2012 Using (In thousands)		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Financial Assets - Recurring				
US Government Agencies	\$11,387	\$5,000	\$6,387	\$ -
MBS	1,829	-	1,829	-
Municipals	11,938	2,918	9,020	-
Residential loans held for sale	24,188	-	24,188	-
			-	
Financial Assets - Non-Recurring				
Impaired loans	54,775	-	47,016	7,759
Real estate owned	20,204	-	18,675	1,529

Edgar Filing: Village Bank & Trust Financial Corp. - Form 10-Q

The following table presents qualitative information about level 3 fair value measurements for financial instruments measured at fair value at March 31, 2013:

	Fair Value Estimate	Valuation Techniques	Unobservable Input	Range (Weighted Average)
(In thousands)				
Impaired loans - real estate secured	\$ 7,064	Appraisal (1) or Internal Valuation (2)	Appraisal Adjustments Liquidation Expenses (3)	10%-30%
Impaired loans - non-real estate secured	\$ 1,460	Appraisal (1) or Discounted Cash Flow	Appraisal Adjustments Liquidation Expenses (3)	10%-20%
Real estate owned	\$ 1,299	Appraisal (1) or Internal Valuation (2)	Appraisal Adjustments Liquidation Expenses (3)	7%-30%

(1) Fair Value is generally determined through independent appraisals of the underlying collateral, which generally included various level 3 inputs which are not identifiable

(2) Internal valuations may be conducted to determine Fair Value for assets with nominal carrying balances

(3) Appraisals may be adjusted by management for qualitative factors such as economic conditions and estimated liquidation expenses

The following table presents the changes in the Level 3 fair value category for the three months ended March 31, 2013.

	Impaired Loans	Real Estate Owned	Total Assets
(In thousands)			
Balance at December 31, 2012	\$7,759	\$1,529	\$9,288
Total realized and unrealized gains (losses)			
Included in earnings	-	(130)	(130)
Included in other comprehensive income	-	-	-
Net transfers in and/or out of Level 3	765	(100)	665
Balance at March 31, 2013	\$8,524	\$1,299	\$9,823

In general, fair value of securities is based upon quoted market prices, where available. If such quoted market prices are not available, fair value is based upon market prices determined by an outside, independent entity that primarily uses as inputs, observable market-based parameters. Fair value of loans held for sale is based upon internally developed models that primarily use as inputs, observable market-based parameters. Valuation adjustments may be

made to ensure that financial instruments are recorded at fair value. These adjustments may include amounts to reflect counterparty credit quality, among other things, as well as unobservable parameters. Any such valuation adjustments are applied consistently over time. The Company valuation methodologies may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. While management believes the Company's valuation methodologies are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different estimate of fair value at the reporting date. Transfers between levels of the fair value hierarchy are recognized on the actual date of the event or circumstances that caused the transfer, which generally coincides with the Company's monthly and or quarter valuation process.

Cash and cash equivalents – The carrying amount of cash and cash equivalents approximates fair value.

Investment securities – The fair value of investment securities available-for-sale is estimated based on bid quotations received from independent pricing services for similar assets. The carrying amount of other investments approximates fair value.

Loans – For variable rate loans that reprice frequently and have no significant change in credit risk, fair values are based on carrying values. For all other loans, fair values are calculated by discounting the contractual cash flows using estimated market discount rates which reflect the credit and interest rate risk inherent in the loans, or by using the current rates at which similar loans would be made to borrowers with similar credit ratings and for the same remaining maturities.

Deposits – The fair value of deposits with no stated maturity, such as demand, interest checking and money market, and savings accounts, is equal to the amount payable on demand at year-end. The fair value of certificates of deposit is based on the discounted value of contractual cash flows using the rates currently offered for deposits of similar remaining maturities.

Borrowings – The fair value of borrowings is based on the discounted value of contractual cash flows using the rates currently offered for borrowings of similar remaining maturities.

Accrued interest – The carrying amounts of accrued interest receivable and payable approximate fair value.

	Level in Fair Value Hierarchy	March 31, 2013		December 31, 2012	
		Carrying Value	Estimated Fair Value	Carrying Value	Estimated Fair Value
Financial assets					
Cash	Level 1	\$ 12,340,643	\$ 12,340,643	\$ 13,945,105	\$ 13,945,105
Cash equivalents	Level 2	56,796,937	56,796,937	39,185,837	39,185,837
Investment securities available for sale	Level 1	1,898,730	1,898,730	7,918,420	7,918,420
Investment securities available for sale	Level 2	27,736,316	27,736,316	17,235,626	17,235,626
Federal Home Loan Bank stock	Level 2	1,867,300	1,867,300	2,121,900	2,121,900
Loans held for sale	Level 2	16,377,826	16,377,826	24,188,384	24,188,384
Loans	Level 2	261,016,472	265,851,990	290,115,508	294,476,846
Impaired loans	Level 2	45,750,544	45,750,544	47,016,065	47,016,065
Impaired loans	Level 3	8,523,648	8,523,648	7,758,689	7,758,689
Other real estate owned	Level 2	20,083,837	20,083,837	18,675,164	18,675,164
Other real estate owned	Level 3	1,298,994	1,298,994	1,528,527	1,528,527
Bank owned life insurance	Level 3	6,625,325	6,625,325	6,575,018	6,575,018
Accrued interest receivable	Level 2	1,580,147	1,580,147	1,676,518	1,676,518
Financial liabilities					
Deposits	Level 2	421,419,245	423,055,395	436,322,962	437,644,329

Edgar Filing: Village Bank & Trust Financial Corp. - Form 10-Q

FHLB borrowings	Level 2	27,000,000	27,423,217	28,000,000	28,424,029
Trust preferred securities	Level 2	8,764,000	7,537,040	8,764,000	7,537,040
Other borrowings	Level 2	1,882,346	1,882,346	4,851,811	4,851,811
Accrued interest payable	Level 2	981,527	981,527	911,635	911,635

Note 10 – Capital Purchase Program

On May 1, 2009, as part of the Capital Purchase Program established by the U.S. Department of the Treasury (the “Treasury”) under the Emergency Economic Stabilization Act of 2008 (“EESA”), the Company entered into a Letter Agreement and Securities Purchase Agreement—Standard Terms (collectively, the “Purchase Agreement”) with the Treasury, pursuant to which the Company sold (i) 14,738 shares of the Company’s Fixed Rate Cumulative Perpetual Preferred Stock, Series A, par value \$4.00 per share, having a liquidation preference of \$1,000 per share (the “Preferred Stock”) and (ii) a warrant (the “Warrant”) to purchase 499,029 shares of the Company’s common stock at an initial exercise price of \$4.43 per share, subject to certain anti-dilution and other adjustments, for an aggregate purchase price of \$14,738,000 in cash. The fair value of the preferred stock was estimated using discounted cash flow methodology at an assumed market equivalent rate of 13%, with 20 quarterly payments over a five year period. The fair value of the warrant was estimated using the Black-Scholes option pricing model, with assumptions of 25% volatility, a risk-free rate of 2.03%, a yield of 6.162% and an estimated life of 5 years. The value attributed to the warrant is being accreted as a discount on the preferred stock using the effective interest rate method over five years.

The Preferred Stock qualifies as Tier 1 capital and will pay cumulative dividends at a rate of 5% until May 1, 2014 and 9% thereafter, unless the shares are redeemed by the Company. The Preferred Stock is generally non-voting, other than on certain matters that could adversely affect the Preferred Stock.

The Warrant is immediately exercisable. The Warrant provides for the adjustment of the exercise price and the number of shares of common stock issuable upon exercise pursuant to customary anti-dilution provisions, such as upon stock splits or distributions of securities or other assets to holders of common stock, and upon certain issuances of common stock at or below a specified price relative to the then-current market price of common stock. The Warrant expires ten years from the issuance date. Pursuant to the Purchase Agreement, the Treasury has agreed not to exercise voting power with respect to any shares of common stock issued upon exercise of the Warrant.

As required by the Federal Reserve Bank of Richmond, the Company notified the U.S. Treasury in May 2011 that the Company was going to defer the payment of the quarterly cash dividend of \$184,225 due on May 16, 2011, and subsequent quarterly payments, on the Fixed Rate Cumulative Perpetual Preferred Stock, Series A. The total arrearage on such preferred stock as of March 31, 2013 was \$1,565,912. This amount has been accrued for and is included in other liabilities in the consolidated balance sheet.

In June 2012 the Treasury asked to allow an observer at the Company’s meetings of its board of directors. The observer started attending board meetings in August 2012. The Treasury has the contractual right to nominate up to two members to the board of directors upon the Company’s sixth missed dividend payment. The Company has deferred eight dividend payments as of March 31, 2013. However, Treasury has not indicated that it will nominate two directors to the board of directors.

The Bank is subject to various regulatory capital requirements administered by the federal and state banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory and possible additional discretionary, actions by regulators that, if undertaken, could have a direct material effect on the Bank’s financial statements. Under the capital adequacy guidelines and the regulatory framework for prompt corrective action, the Bank must meet specific capital guidelines that involve quantitative measures of the Bank’s assets, liabilities, and

certain off-balance-sheet items as calculated under regulatory accounting practices. The Bank's capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

Note 11 – Commitments and contingencies

Off-balance-sheet risk – The Company is a party to financial instruments with off-balance-sheet risk in the normal course of business to meet the financial needs of its customers. These financial instruments include commitments to extend credit and standby letters of credit. These instruments involve, to varying degrees, elements of credit and interest-rate risk in excess of the amounts recognized in the financial statements. The contract amounts of these instruments reflect the extent of involvement that the Company has in particular classes of instruments.

The Company's exposure to credit loss in the event of non-performance by the other party to the financial instrument for commitments to extend credit, and to potential credit loss associated with letters of credit issued, is represented by the contractual amount of those instruments. The Company uses the same credit policies in making commitments and conditional obligations as it does for loans and other such on-balance sheet instruments.

The Company had outstanding the following approximate off-balance-sheet financial instruments whose contract amounts represent credit risk at the dates indicated:

	March 31, 2013	December 31, 2012
Undisbursed credit lines	\$ 32,983,000	\$ 35,780,000
Commitments to extend or originate credit	36,131,000	25,016,000
Standby letter of credit	2,906,000	3,314,000
 Total commitments to extend credit	 \$ 72,020,000	 \$ 64,110,000

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require the payment of a fee. Historically, many commitments expire without being drawn upon; therefore, the total commitment amounts shown in the above table are not necessarily indicative of future cash requirements. The Company evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, as deemed necessary by the Company upon extension of credit is based on management's credit evaluation of the customer. Collateral held varies but may include personal or income-producing commercial real estate, accounts receivable, inventory and equipment.

Concentrations of credit risk – All of the Company's loans, commitments to extend credit, and standby letters of credit have been granted to customers in the Company's market area. Although the Company is building a diversified loan portfolio, a substantial portion of its clients' ability to honor contracts is reliant upon the economic stability of the Richmond, Virginia area, including the real estate markets in the area. The concentrations of credit by type of loan are set forth in Note 5. The distribution of commitments to extend credit approximates the distribution of loans outstanding.

Consent Order – In February 2012, the Bank entered into a Stipulation and Consent to the Issuance of a Consent Order (“Consent Agreement”) with the Federal Deposit Insurance Corporation and the Virginia Bureau of Financial Institutions (the “Supervisory Authorities”), and the Supervisory Authorities have issued the related Consent Order (the “Order”) effective February 3, 2012. The description of the Consent Agreement and the Order is set forth below:

Management. The Order requires that the Bank have and retain qualified management, including at a minimum a chief executive officer, senior lending officer and chief operating officer, with qualifications and experience commensurate with their assigned duties and responsibilities within 90 days from the effective date of the order. Within 30 days of the effective date of the Order, the Bank must retain a bank consultant to develop a written analysis and assessment of the Bank’s management and staffing needs for the purpose of providing qualified management for the Bank. Within 30 days from receipt of the consultant’s management report, the Bank must formulate a written management plan that incorporates the findings of the management report, a plan of action in response to each recommendation contained in the management report, and a timeframe for completing each action.

Capital Requirements. Within 90 days from the effective date of the Order and during the life of the Order, the Bank must have Tier 1 capital equal to or greater than 8 percent of its total assets, and total risk-based capital equal to or greater than 11 percent of the Bank’s total risk-weighted assets. Within 90 days from the effective date of the Order, the Bank must submit a written capital plan to the Supervisory Authorities. The capital plan must include a contingency plan in the event that the Bank fails to maintain the minimum capital ratios required in the Order, submit a capital plan that is acceptable to the Supervisory Authorities, or implement or adhere to the capital plan.

Charge-offs. The Order requires the Bank to eliminate from its books, by charge-off or collection, all assets or portions of assets classified “Loss” and 50 percent of those classified “Doubtful”. If an asset is classified “Doubtful”, the Bank may, in the alternative, charge off the amount that is considered uncollectible in accordance with the Bank’s written analysis of loan or lease impairment. The Order also prevents the Bank from extending, directly or indirectly, any additional credit to, or for the benefit of, any borrower who has a loan or other extension of credit from the Bank that has been charged off or classified, on whole or in part, “loss” or “doubtful” and is uncollected. The Bank may not extend, directly or indirectly, any additional credit to any borrower who has a loan or other extension of credit from the Bank that has been classified “substandard.” These limitations do not apply if the Bank’s failure to extend further credit to a particular borrower would be detrimental to the best interests of the Bank.

Asset Growth. While the Order is in effect, the Bank must notify the Supervisory Authorities at least 60 days prior to undertaking asset growth that exceeds 10% or more per year or initiating material changes in asset or liability composition. The Bank’s asset growth cannot result in noncompliance with the capital maintenance provisions of the Order unless the Bank receives prior written approval from the Supervisory Authorities.

Restriction on Dividends and Other Payments. While the Order is in effect, the Bank cannot declare or pay dividends, pay bonuses, or pay any form of payment outside the ordinary course of business resulting in a reduction of capital without the prior written approval of the Supervisory Authorities. In addition, the Bank cannot make any distributions of interest, principal, or other sums on subordinated debentures without prior written approval of the Supervisory Authorities.

Brokered Deposits. The Order provides that the Bank may not accept, renew, or roll over any brokered deposits unless it is in compliance with the requirements of the FDIC regulations governing brokered deposits. These regulations prohibit undercapitalized institutions from accepting, renewing, or rolling over any brokered deposits and also prohibit undercapitalized institutions from soliciting deposits by offering an effective yield that exceeds by more than 75 basis points the prevailing effective yields on insured deposits of comparable maturity in the institution's market area. An "adequately capitalized" institution may not accept, renew, or roll over brokered deposits unless it has applied for and been granted a waiver by the FDIC.

Written Plans and Other Material Terms. Under the terms of the Order, the Bank is required to prepare and submit the following written plans or reports to the FDIC and the Commissioner:

- Plan to improve liquidity, contingency funding, interest rate risk, and asset liability management
- Plan to reduce assets of \$250,000 or greater classified "doubtful" and "substandard"
- Revised lending and collection policy to provide effective guidance and control over the Bank's lending and credit administration functions
- Effective internal loan review and grading system
- Policy for managing the Bank's other real estate
- Business/strategic plan covering the overall operation of the Bank
- Plan and comprehensive budget for all categories of income and expense for the year 2011
- Policy and procedures for managing interest rate risk
- Assessment of the Bank's information technology function

Under the Order, the Bank's board of directors has agreed to increase its participation in the affairs of the Bank, including assuming full responsibility for the approval of policies and objectives for the supervision of all of the Bank's activities. The Bank must also establish a board committee to monitor and coordinate compliance with the Order.

The Order will remain in effect until modified or terminated by the Supervisory Authorities.

While subject to the Consent Order, we expect that our management and board of directors will be required to focus considerable time and attention on taking corrective actions to comply with the terms. In addition, certain provisions of the Consent Order described above could adversely impact the Company's businesses and results of operations.

Written Agreement – In June 2012, the Company entered into a written agreement ("Written Agreement") with the Federal Reserve Bank of Richmond ("Reserve Bank"). Under the terms of the Written Agreement, the Company agreed to develop and submit to the Reserve Bank for approval within the time periods specified therein written plans to maintain sufficient capital and

correct any violations of section 23A of the Federal Reserve Act and Regulation W. In addition, the Company will submit a written statement of its planned sources and uses of cash for debt service, operation expenses, and other purposes.

The Company also has agreed that it will not, without prior regulatory approval:

- pay or declare any dividends;
- take any other form of payment representing a reduction in Bank's capital;
- make any distributions of interest, principal or other sums on subordinated debentures or trust preferred securities;
- incur, increase or guarantee any debt;
- purchase or deem any shares of its stock.

Since entering into the Order and the Written Agreement, the Company has taken numerous steps to comply with the terms of the consent order.

Note 12 – Income Taxes

The net deferred tax asset is included in other assets on the balance sheet. Accounting Standards Codification Topic 740, Income Taxes, requires that companies assess whether a valuation allowance should be established against their deferred tax assets based on the consideration of all available evidence using a “more likely than not” standard. Management considers both positive and negative evidence and analyzes changes in near-term market conditions as well as other factors which may impact future operating results. In making such judgments, significant weight is given to evidence that can be objectively verified. The deferred tax assets are analyzed quarterly for changes affecting realization. Management determined that as of March 31, 2013, the objective negative evidence represented by the Company's recent losses outweighed the more subjective positive evidence and, as a result, recognized a valuation allowance for all of the net deferred tax asset of approximately \$10,368,000.

Note 13 – Recent accounting pronouncements

In February 2013, the Financial Accounting Standards Board (FASB) issued ASU 2013-02, Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income, which is intended to improve the reporting of reclassifications out of accumulated other comprehensive income. The ASU requires an entity to report, either on the face of the income statement or in the notes to the financial statements, the effect of significant reclassifications out of accumulated other comprehensive income on the respective line items in the income statement if the amount being reclassified is required to be reclassified in its entirety to net income. For other amounts that are not required to be reclassified in their entirety to net income in the same reporting period, an entity is required to cross-reference other required disclosures that provide additional detail about those amounts. This ASU is effective prospectively in the first quarter of 2013, and is not expected to have a material effect on the Company's consolidated financial statements.

In June 2011, the FASB issued ASU No. 2011-05, Presentation of Comprehensive Income ("ASU 2011-05"). ASU 2011-05 requires an entity to present the total of comprehensive income, the components of net income and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. ASU 2011-05 eliminates the option to present the components of other comprehensive income as part of the statement of equity. ASU 2011-05 became effective for the Company on January 1, 2012. In connection with the application of ASU 2011-05, the Company's financial statements now include separate statements of comprehensive income.

In May 2011, the FASB issued ASU No. 2011-04, Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs. The Company adopted ASU 2011-04, which generally aligns the principles of fair value measurements with International Financial Reporting Standards (IFRSs), in its consolidated financial statements in the first quarter 2012. The provisions of ASU 2011-04 clarify the application of existing fair value measurement requirements, and expand the disclosure requirements for fair value measurements. The increased provisions of ASU 2011-04 did not have a material effect on the Company's consolidated financial statements.

ITEM 2 – MANAGEMENT’S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION

Caution about forward-looking statements

In addition to historical information, this report may contain forward-looking statements. For this purpose, any statement, that is not a statement of historical fact may be deemed to be a forward-looking statement. These forward-looking statements may include statements regarding profitability, liquidity, allowance for loan losses, interest rate sensitivity, market risk, growth strategy and financial and other goals. Forward-looking statements often use words such as “believes,” “expects,” “plans,” “may,” “will,” “should,” “projects,” “contemplates,” “anticipates,” “forecasts” or other words of similar meaning. You can also identify them by the fact that they do not relate strictly to historical or current facts. Forward-looking statements are subject to numerous assumptions, risks and uncertainties, and actual results could differ materially from historical results or those anticipated by such statements.

There are many factors that could have a material adverse effect on the operations and future prospects of the Company including, but not limited to:

- the inability of the Bank to comply with the requirements of agreements with its regulators;
- the inability to reduce nonperforming assets consisting of nonaccrual loans and foreclosed real estate;
 - our inability to improve our regulatory capital position;
- the risks of changes in interest rates on levels, composition and costs of deposits, loan demand, and the values and liquidity of loan collateral, securities, and interest sensitive assets and liabilities;
 - changes in assumptions underlying the establishment of allowances for loan losses, and other estimates;
- changes in market conditions, specifically declines in the residential and commercial real estate market, volatility and disruption of the capital and credit markets, soundness of other financial institutions we do business with;
 - risks inherent in making loans such as repayment risks and fluctuating collateral values;
- changes in operations of Village Bank Mortgage Corporation as a result of the activity in the residential real estate market;
- legislative and regulatory changes, including the Dodd-Frank Act Wall Street Reform and Consumer Protection Act and other changes in banking, securities, and tax laws and regulations and their application by our regulators, and changes in scope and cost of FDIC insurance and other coverages;
- exposure to repurchase loans sold to investors for which borrowers failed to provide full and accurate information on or related to their loan application or for which appraisals have not been acceptable or when the loan was not underwritten in accordance with the loan program specified by the loan investor;
 - the effects of future economic, business and market conditions;
 - governmental monetary and fiscal policies;
 - changes in accounting policies, rules and practices;
 - maintaining capital levels adequate to remain well capitalized;
 - reliance on our management team, including our ability to attract and retain key personnel;
- competition with other banks and financial institutions, and companies outside of the banking industry, including those companies that have substantially greater access to capital and other resources;
 - demand, development and acceptance of new products and services;
 - problems with technology utilized by us;
 - changing trends in customer profiles and behavior; and

- other factors described from time to time in our reports filed with the SEC.

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

General

The Company's primary source of earnings is net interest income, and its principal market risk exposure is interest rate risk. The Company is not able to predict market interest rate fluctuations and its asset/liability management strategy may not prevent interest rate changes from having a material adverse effect on the Company's results of operations and financial condition.

Although we endeavor to minimize the credit risk inherent in the Company's loan portfolio, we must necessarily make various assumptions and judgments about the collectability of the loan portfolio based on our experience and evaluation of economic conditions. If such assumptions or judgments prove to be incorrect, the current allowance for loan losses may not be sufficient to cover loan losses and additions to the allowance may be necessary, which would have a negative impact on net income. Over the last three years, the Company has recorded record provisions for loan losses due primarily to loans collateralized by real estate located in its principal market area.

There is intense competition in all areas in which the Company conducts its business. The Company competes with banks and other financial institutions, including savings and loan associations, savings banks, finance companies, and credit unions. Many of these competitors have substantially greater resources and lending limits and provide a wider array of banking services. To a limited extent, the Company also competes with other providers of financial services, such as money market mutual funds, brokerage firms, consumer finance companies and insurance companies. Competition is based on a number of factors, including prices, interest rates, services, availability of products and geographic location.

At the beginning of 2012, our business strategy included efforts to reduce our total assets and liabilities due to a continued depressed economy as well as capital limitations at the time. These efforts resulted in declines of approximately \$72 million in total assets and approximately \$60 million in total liabilities in 2012. With the sale of a branch completed in the first quarter of 2013, we further reduced our total assets and liabilities by approximately \$18 million. This strategy helped strengthen our regulatory capital ratios in 2012 and the first quarter of 2013. While we do not anticipate significant growth in 2013, we do not expect to continue our efforts to reduce total assets and liabilities.

Results of Operations

The following presents management's discussion and analysis of the financial condition of the Company at March 31, 2013 and December 31, 2012 and the results of operations for the Company for the three months ended March 31, 2013 and 2012. This discussion should be read in conjunction with the Company's condensed consolidated financial statements and the notes thereto appearing elsewhere in this Quarterly Report.

Income Statement Analysis

Summary

For the three months ended March 31, 2013, the Company had a net loss of \$(511,000) and a net loss available to common shareholders of \$(732,000), or \$(0.17) per fully diluted share, compared to a net loss of \$(1,400,000) and a net loss available to common shareholders of \$(1,621,000) or \$(0.38) per fully diluted basis, for the same period in 2012. The key factors in the decrease in the loss were decreases in the provision for loan losses of \$912,000 and the gain on the sale of a branch of \$598,000, offset by the increase in expenses associated with foreclosed real estate of \$456,000 from \$1,119,000 for the first quarter of 2012 to \$1,575,000 for the first quarter of 2013. The decrease in the provision for loan losses is attributable to an improving loan portfolio as well as a decline in need due to the decline in total loans. However, as we resolve nonperforming loans through foreclosure, costs associated with foreclosed real estate will continue to be a significant expense.

Our cost of deposits declined from 1.34% for the first quarter of 2012 to 1.12% for the first quarter of 2013. This decline in cost of deposits is a result of the repricing of higher cost certificates of deposit during the low interest rate environment that has existed for the last three years as well as an effort to change our deposit mix so that we are not so dependent on higher cost deposits. Our mortgage company's profit increased slightly in the first quarter of 2013 compared to 2012 by \$8,000 despite the mortgage company closing \$57,961,000 in mortgage loans in the first quarter of 2013 compared to \$64,121,000 in the first quarter of 2012.

Net interest income

Net interest income, which represents the difference between interest earned on interest-earning assets and interest incurred on interest-bearing liabilities, is the Company's primary source of earnings. Net interest income can be affected by changes in market interest rates as well as the level and composition of assets, liabilities and shareholders' equity. Net interest spread is the difference between the average rate earned on interest-earning assets and the average rate paid on interest-bearing liabilities. The net yield on interest-earning assets ("net interest margin") is calculated by dividing tax equivalent net interest income by average interest-earning assets. Generally, the net interest margin will exceed the net interest spread because a portion of interest-earning assets are funded by various noninterest-bearing sources, principally noninterest-bearing deposits and shareholders' equity.

Net interest income for the first quarter of \$4,089,000 represents a decrease of \$332,000, or 8%, compared to the first quarter of 2012, and a decrease of \$625,000, or 13%, compared to the fourth quarter of 2012.

Compared to the first quarter of 2012, average interest-earning assets for the first quarter of 2013 decreased by \$65,689,000, or 13%. The decrease in average interest-earning assets was due

primarily to decreases in portfolio loans of \$74,597,000, offset by increases in loans held for sale of \$3,090,000 and federal funds sold of \$7,119,000. The decline in average interest-earning assets was somewhat mitigated by an increase in the average yield on interest-earning assets from 4.85% for the first quarter of 2012 to 4.96% for the first quarter of 2013. These fluctuations resulted in a decline in interest income from the first quarter of 2012 to the first quarter of 2013 of \$714,000, or 12%.

Average interest-bearing liabilities for the first quarter of 2013 decreased by \$42,513,000, or 9%, compared to the first quarter of 2012. The decrease in interest-bearing liabilities was due to declines in average deposits of \$32,363,000 and average borrowings of \$10,150,000. The average cost of interest-bearing liabilities decreased to 1.23% for the first quarter of 2013 from 1.45% for the first quarter of 2012. The principal reason for the decrease in liability costs was the maintenance of short-term interest rates at a low level by the Federal Reserve. The continuing low interest rates have allowed us to reduce our cost of funds as certificates of deposit and borrowings mature. See our discussion of interest rate sensitivity below for more information.

The Company's net interest margin is not a measurement under accounting principles generally accepted in the United States, but it is a common measure used by the financial services industry to determine how profitably earning assets are funded. Our net interest margin over the last several quarters is provided in the following table:

Quarter Ended	Net Interest Margin
March 31, 2012	3.53%
June 30, 2012	3.65%
September 30, 2012	3.70%
December 31, 2012	4.25%
March 31, 2013	3.79%

The significant increase in the net interest margin in the fourth quarter of 2012 is attributable to the recapture of interest on returning approximately \$14.4 million of nonaccrual loans to accrual status during the quarter. The net interest margin for the first quarter of 2013 is more consistent with the net interest margin for the first three quarters of 2012 and the trend over the last five quarters has been improving. This improving net interest margin is a result of a declining cost of funds which decreased by 22 basis points from the first quarter of 2012 to the first quarter of 2013.

The following table illustrates average balances of total interest-earning assets and total interest-bearing liabilities for the periods indicated, showing the average distribution of assets, liabilities, shareholders' equity and related income, expense and corresponding weighted-average yields and rates. The average balances used in these tables and other statistical data were calculated using daily average balances. We had no tax exempt assets for the periods presented.

Edgar Filing: Village Bank & Trust Financial Corp. - Form 10-Q

Average Balance Sheets
(in thousands)

	Three Months Ended March 31, 2013				Three Months Ended March 31, 2012			
	Average Balance	Interest Income/ Expense	Annualized Yield Rate		Average Balance	Interest Income/ Expense	Annualized Yield Rate	
Loans	\$345,623	\$4,977	5.84	%	\$420,220	\$5,768	5.52	%
Investment securities	30,007	188	2.54	%	31,307	150	1.93	%
Loans held for sale	16,201	166	4.16	%	13,111	131	4.01	%
Federal funds and other	45,776	25	0.22	%	38,657	21	0.22	%
Total interest earning assets	437,607	5,356	4.96	%	503,296	6,070	4.85	%
Allowance for loan losses and deferred fees	(10,591)				(11,845)			
Cash and due from banks	13,159				15,305			
Premises and equipment, net	25,530				26,710			
Other assets	37,950				33,255			
Total assets	\$503,655				\$566,720			
Interest bearing deposits								
Interest checking	\$43,329	\$35	0.32	%	\$42,168	\$40	0.38	%
Money market	66,293	61	0.37	%	73,422	76	0.42	%
Savings	20,908	23	0.45	%	16,186	21	0.52	%
Certificates	245,906	924	1.52	%	277,023	1,221	1.77	%
Total	376,436	1,043	1.12	%	408,799	1,358	1.34	%
Borrowings	39,655	224	2.29	%	49,805	291	2.35	%
Total interest bearing liabilities	416,091	1,267	1.23	%	458,604	1,649	1.45	%
Noninterest bearing deposits	55,216				63,206			
Other liabilities	7,170				3,675			
Total liabilities	478,477				525,486			
Equity capital	25,178				41,234			
Total liabilities and capital	\$503,655				\$566,720			
Net interest income before provision for loan losses		\$4,089				\$4,421		
Interest spread - average yield on interest earning assets, less average rate on interest bearing liabilities			3.74	%			3.40	%
Annualized net interest margin (net interest income expressed as			3.79	%			3.53	%

percentage of average earning
assets)

Provision for loan losses

There was a provision for loan losses for the three months ended March 31, 2013 of \$823,000 compared to a provision of \$1,735,000 for the same period in 2012. The decline in the provision for loan losses for the first quarter of 2013 was primarily driven by an \$88 million decline in loans outstanding from March 31, 2012 to March 31, 2013 as well as a decline in the impairment on specific nonperforming loans. The provision for loan losses for the first quarter of 2013 was primarily attributable to one nonperforming loan relationship for which the collateral was determined to be deficient. While we are encouraged by this decline in the provision for loan losses, overall asset quality continues to be a concern as there continues to be uncertainty in the economy and the level of nonperforming assets remains significant.

Noninterest income

Noninterest income increased from \$2,688,000 for the first quarter of 2012 to \$3,606,000 for the same period in 2013, an increase of \$918,000, or 34%. This increase in noninterest income was primarily the result of higher gains on loan sales from increased loan production by our mortgage banking subsidiary of \$205,000, and the gain on the sale of the Robious branch of \$598,000.

Noninterest expense

Noninterest expense for the three months ended March 31, 2013 was \$7,384,000 compared to \$6,775,000 for the three months ended March 31, 2012, an increase of \$609,000 or 9%. The most significant increases in noninterest expense occurred in expenses related to foreclosed real estate of \$456,000 and salaries and benefits of \$341,000. The increase in expenses related to foreclosed real estate is a result of our efforts to foreclose on troubled loans and the disposition of the collateral, and the increase in salaries and benefits is primarily attributable to increases in commissions paid to mortgage loan officers.

Income taxes

Certain items of income and expense are reported in different periods for financial reporting and tax return purposes. The tax effects of these temporary differences are recognized currently in the deferred income tax provision or benefit. Deferred tax assets or liabilities are computed based on the difference between the financial statement and income tax bases of assets and liabilities using the applicable enacted marginal tax rate.

The net deferred tax asset is included in other assets on the balance sheet. Accounting Standards Codification Topic 740, Income Taxes, requires that companies assess whether a valuation allowance should be established against their deferred tax assets based on the consideration of all available evidence using a “more likely than not” standard. Management considers both positive and negative evidence and analyzes changes in near-term market conditions as well as other factors which may impact future operating results. In making such judgments, significant weight is given to evidence that can be objectively verified. The deferred tax assets are analyzed quarterly for changes affecting realization. Management determined that as of December 31, 2012, the objective negative evidence represented by the Company’s recent losses outweighed the more subjective positive evidence and, as a result, recognized a valuation allowance on its net deferred tax asset of approximately \$10,158,000. At March 31, 2013, management continues to believe that the objective negative evidence represented by the Company’s continued losses in the first quarter outweighed the more subjective positive evidence and, as a result, recognized an addition to the valuation allowance on its net deferred tax asset of approximately \$210,000. The net operating losses available to offset future taxable income amounted to \$14,684,000 at March 31, 2013 and expire through 2031.

Commercial banking organizations conducting business in Virginia are not subject to Virginia income taxes. Instead, they are subject to a franchise tax based on bank capital. The Company recorded a franchise tax expense of \$42,000 for the three months ended March 31, 2012. Due to the Company’s adjusted capital level we were not subject to franchise tax expense in the first quarter of 2013.

Balance Sheet Analysis

Our total assets decreased to \$491,054,000 at March 31, 2013 from \$510,087,000 at December 31, 2012, a decrease of \$19,033,000, or 4%. During the first quarter of 2013 there were decreases in net loans of \$30,423,000, loans held for sale of \$7,810,000 and premises and equipment of \$1,823,000 offset by an increase in liquid assets (cash and due from banks, federal funds sold and investment securities available for sale) of \$20,488,000. The branch sale discussed previously was the primary driver of the decline for the quarter.

Loans

A management objective is to maintain the quality of the loan portfolio. The Company seeks to achieve this objective by maintaining rigorous underwriting standards coupled with regular evaluation of the creditworthiness of and the designation of lending limits for each borrower. The portfolio strategies include seeking industry and loan size diversification in order to minimize credit exposure and originating loans in markets with which the Company is familiar.

The Company's real estate loan portfolios, which represent approximately 90% of all loans, are secured by mortgages on real property located principally in the Commonwealth of Virginia. Sources of repayment are from the borrower's operating profits, cash flows and liquidation of pledged collateral. The Company's commercial loan portfolio represents approximately 9% of all loans. Loans in this category are typically made to individuals, small and medium-sized businesses and range between \$250,000 and \$2.5 million. Based on underwriting standards, commercial and industrial loans may be secured in whole or in part by collateral such as liquid assets, accounts receivable, equipment, inventory, and real property. The collateral securing any loan may depend on the type of loan and may vary in value based on market conditions. The remainder of our loan portfolio is in consumer loans which represent approximately 1% of the total.

The following table presents the composition of our loan portfolio (excluding mortgage loans held for sale) at the dates indicated (in thousands):

	March 31, 2013		December 31, 2012			
	Amount	%	Amount	%		
Construction and land development						
Residential	\$3,002	0.93	%	\$2,845	0.80	%
Commercial	36,209	11.18	%	41,210	11.61	%
Total construction and land development	39,211	12.11	%	44,055	12.41	%
Commercial real estate						
Farmland	2,571	0.79	%	2,581	0.73	%
Commercial real estate - owner occupied	81,459	25.14	%	92,773	26.14	%
Commercial real estate - non-owner occupied	47,470	14.65	%	54,551	15.37	%
Multifamily	8,908	2.75	%	7,979	2.25	%
Total commercial real estate	140,408	43.33	%	157,884	44.49	%
Consumer real estate						
Home equity lines	24,614	7.60	%	25,521	7.19	%
Secured by 1-4 family residential, secured by first deeds of trust	78,796	24.32	%	80,788	22.76	%
Secured by 1-4 family residential, secured by second deeds of trust	8,668	2.67	%	9,517	2.68	%
Total consumer real estate	112,078	34.59	%	115,827	32.63	%
Commercial and industrial loans (except those secured by real estate)	29,647	9.15	%	34,384	9.69	%
Consumer and other	2,660	0.82	%	2,761	0.78	%
Total Loans	324,004	100.0	%	354,910	100.0	%
Deferred loan cost (unearned income), net	783			788		
Less: Allowance for loan losses	(10,320)			(10,808)		
	\$314,467			\$344,890		

The decline in our total loan portfolio for the first quarter of 2013 was primarily due to the branch sale which included the sale of approximately \$12 million in loans, as well as management's strategy to decrease our level of assets to improve our regulatory capital ratios and reduce our overhead expenses.

The Company assigns risk rating classifications to its loans. These risk ratings are divided into the following groups:

- Risk rated 1 to 4 loans are considered of sufficient quality to preclude an adverse rating. 1-4 assets generally are well protected by the current net worth and paying capacity of the obligor or by the value of the asset or underlying collateral;
 - Risk rated 5 loans are defined as having potential weaknesses that deserve management's close attention;
- Risk rated 6 loans are inadequately protected by the current sound worth and paying capacity of the obligor or of the collateral pledged, if any, and;
- Risk rated 7 loans have all the weaknesses inherent in substandard loans, with the added characteristics that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions and values, highly questionable and improbable.

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

Allowance for loan losses

We monitor and maintain an allowance for loan losses to absorb an estimate of probable losses inherent in the loan portfolio. We maintain policies and procedures that address the systems of controls over the following areas of maintenance of the allowance: the systematic methodology used to determine the appropriate level of the allowance to provide assurance they are maintained in accordance with accounting principles generally accepted in the United States of America; the accounting policies for loan charge-offs and recoveries; the assessment and measurement of impairment in the loan portfolio; and the loan grading system.

The allowance reflects management's best estimate of probable losses within the existing loan portfolio and of the risk inherent in various components of the loan portfolio, including loans identified as impaired as required by FASB Codification Topic 310: Receivables. Loans evaluated individually for impairment include non-performing loans, such as loans on non-accrual, loans past due by 90 days or more, restructured loans and other loans selected by management. The evaluations are based upon discounted expected cash flows or collateral valuations. If the evaluation shows that a loan is individually impaired, then a specific reserve is established for the amount of impairment.

Loans are grouped by similar characteristics, including the type of loan, the assigned loan classification and the general collateral type. A loss rate reflecting the expected loss inherent in a group of loans is derived based upon historical net charge-off rates, the predominant collateral type for the group and the terms of the loan. The resulting estimate of losses for groups of loans is adjusted for relevant environmental factors and other conditions of the portfolio of loans and leases, including: borrower and industry concentrations; levels and trends in delinquencies, charge-offs and recoveries; changes in underwriting standards and risk selection; level of experience, ability and depth

of lending management; and national and local economic conditions.

The amounts of estimated impairment for individually evaluated loans and groups of loans are added together for a total estimate of loan losses. This estimate of losses is compared to our allowance for loan losses as of the evaluation date and, if the estimate of losses is greater than the allowance, an additional provision to the allowance would be made. If the estimate of losses is less than the allowance, the degree to which the allowance exceeds the estimate is evaluated to determine whether the allowance falls outside a range of estimates. We recognize the inherent imprecision in estimates of losses due to various uncertainties and variability related to the factors used, and therefore a reasonable range around the estimate of losses is derived and used to ascertain whether the allowance is too high. If different assumptions or conditions were to prevail and it is determined that the allowance is not adequate to absorb the new estimate of probable losses, an additional provision for loan losses would be made, which amount may be material to the financial statements.

The allowance for loan losses at March 31, 2013 was \$10,320,000, compared to \$10,808,000 at December 31, 2012. The ratio of the allowance for loan losses to gross portfolio loans (net of unearned income and excluding mortgage loans held for sale) at March 31, 2013 and December 31, 2012 was 3.18% and 3.04%, respectively. The decrease in the allowance for loan losses for the first quarter of 2013 was primarily a result of charge-offs recognized during the quarter for which specific provisions for loan losses had been previously provided. The provision for loan losses for the first quarter of 2013 was attributable to one nonperforming loan relationship for which the collateral was determined to be deficient. We believe the amount of the allowance for loan losses at March 31, 2013 is adequate to absorb the losses that can reasonably be anticipated from the loan portfolio at that date.

Edgar Filing: Village Bank & Trust Financial Corp. - Form 10-Q

The following table presents an analysis of the changes in the allowance for loan losses for the periods indicated (in thousands).

	Three Months Ended March 31,		
	2013	2012	
Beginning balance	\$10,808	\$16,071	
Provision for loan losses	823	1,735	
Charge-offs			
Construction and land development			
Residential	-	(59)	
Commercial	(84)	(1,547)	
Commercial real estate			
Commercial real estate - owner occupied	(136)	(29)	
Commercial real estate - non-owner occupied	(256)	(91)	
Consumer real estate			
Home equity lines	(55)	(122)	
Secured by 1-4 family residential, secured by first deeds of trust	(343)	(966)	
Secured by 1-4 family residential, secured by second deeds of trust	(215)	(191)	
Commercial and industrial loans (except those secured by real estate)	(289)	(260)	
Consumer and other	(4)	(270)	
Total charge-offs	(1,382)	(3,535)	
Recoveries			
Construction and land development			
Residential	1	1	
Consumer real estate			
Home equity lines	-	1	
Secured by 1-4 family residential, secured by first deeds of trust	8	61	
Secured by 1-4 family residential, secured by second deeds of trust	3	-	
Commercial and industrial loans (except those secured by real estate)	56	27	
Consumer and other	3	1	
Total recoveries	71	91	
Net charge-offs	(1,311)	(3,444)	
Ending balance	\$10,320	\$14,362	
Loans outstanding at end of period(1)	\$324,787	\$412,732	
Ratio of allowance for loan losses as a percent of loans outstanding at end of period	3.18	% 3.48	%
Average loans outstanding for the period(1)	\$345,623	\$420,220	

Ratio of net charge-offs to average loans outstanding for the period	0.38	%	0.82	%
---	------	---	------	---

(1) Loans are net of unearned income.

44

The allowance for loan losses as a percentage of net loans decreased from 3.48% at March 31, 2012 to 3.18% at March 31, 2013 primarily as a result of a significant charge-offs recognized during the prior year for which specific provisions for loan losses had been previously provided.

Asset quality

The following table summarizes asset quality information at the dates indicated (dollars in thousands).

	March 31, 2013	December 31, 2012	March 31, 2012		
Nonaccrual loans	\$24,271	\$25,605	\$54,900		
Foreclosed properties	21,383	20,204	14,590		
Total nonperforming assets	\$45,654	\$45,809	\$69,490		
Restructured loans still accruing	\$30,003	\$38,820	\$15,321		
Loans past due 90 days and still accruing (not included in nonaccrual loans above)	\$120	\$115	\$-		
Nonperforming assets to loans (1)	14.1	% 12.9	% 16.8	%	%
Nonperforming assets to total assets	9.3	% 9.0	% 12.5	%	%
Allowance for loan losses to nonaccrual loans	42.5	% 42.2	% 26.2	%	%

(1) Loans are net of deferred fees and costs.

The following table presents an analysis of the changes in nonperforming assets for the three months ended March 31, 2013 (dollars in thousands).

	Nonaccrual Loans	Foreclosed Properties	Total
Balance December 31, 2012	\$25,605	\$20,204	\$45,809
Additions, net	4,860	69	4,929
Transfers to OREO	(3,484)	3,484	-
Repayments	(1,398)	-	(1,398)
Charge-offs	(1,313)	(1,044)	(2,357)
Sales		(1,330)	(1,330)
Balance March 31, 2013	\$24,271	\$21,383	\$45,654

Until a nonperforming restructured loan has performed in accordance with its restructured terms for a minimum of six months, it will remain on nonaccrual status.

Interest is accrued on outstanding loan principal balances, unless the Company considers collection to be doubtful. Commercial and unsecured consumer loans are designated as non-accrual when the Company considers collection of expected principal and interest doubtful. Mortgage loans and most other types of consumer loans past due 90 days or more may remain on accrual status if management determines that concern over our ability to collect principal and interest is not significant. When loans are placed in non-accrual status, previously accrued and unpaid interest is reversed against interest income in the current period and interest is subsequently recognized only to the extent cash is received. Interest accruals are resumed on such loans only when in the judgment of management, the loans are estimated to be fully collectible as to both principal and interest.

Of the total nonaccrual loans of \$24,271,000 at March 31, 2013 that were considered impaired, 18 loans totaling \$6,544,000 had specific allowances for loan losses totaling \$2,322,000. This compares to \$25,605,000 in nonaccrual loans at December 31, 2012 of which 15 loans totaling \$4,648,000 had specific allowances for loan losses of \$1,338,000.

Cumulative interest income that would have been recorded had nonaccrual loans been performing would have been approximately \$1,143,000 and \$1,808,000 at March 31, 2013 and 2012, respectively.

Deposits

Deposits as of March 31, 2013 and December 31, 2012 were as follows:

	March 31, 2013		December 31, 2012		
	Amount	%	Amount	%	
Demand accounts	\$62,301,743	14.8	% \$57,049,348	13.1	%
Interest checking accounts	43,567,794	10.3	% 45,861,199	10.5	%
Money market accounts	63,546,257	15.1	% 66,007,160	15.1	%
Savings accounts	20,469,642	4.9	% 20,922,112	4.8	%
Time deposits of \$100,000 and over	107,426,419	25.5	% 113,332,481	26.0	%
Other time deposits	124,107,390	29.4	% 133,150,662	30.5	%
Total	\$421,419,245	100.0	% \$436,322,962	100.0	%

Total deposits decreased by \$14,904,000, or 3.4%, from \$436,323,000 at December 31, 2012 to \$421,419,000 at March 31, 2013, as compared to a decrease of \$20,128,000, or 4.1%, during the first three months of 2012. Checking and savings accounts increased by \$2,507,000, money market accounts decreased by \$2,461,000 and time deposits decreased by \$14,949,000. The decline in time deposits was a result of the branch sale as well as repricing maturing time deposits at rates below market for noncore depositors. The cost of our interest bearing deposits declined to 1.12% for the first quarter of 2013 compared to 1.20% for the fourth quarter of 2012 and 1.34% for the first quarter of 2012.

The variety of deposit accounts that we offer has allowed us to be competitive in obtaining funds and has allowed us to respond with flexibility to, although not to eliminate, the threat of disintermediation (the flow of funds away from depository institutions such as banking institutions into direct investment vehicles such as government and corporate securities). Our ability to attract and retain deposits, and our cost of funds, has been, and is expected to continue to be, significantly affected by money market conditions.

Borrowings

We utilize borrowings to supplement deposits when they are available at a lower overall cost to us or they can be invested at a positive rate of return.

As a member of the Federal Home Loan Bank of Atlanta (“FHLB”), the Bank is required to own capital stock in the FHLB and is authorized to apply for borrowings from the FHLB. Each FHLB credit program has its own interest rate, which may be fixed or variable, and range of maturities. The FHLB may prescribe the acceptable uses to which the advances may be put, as well as on the size of the advances and repayment provisions. Borrowings from the FHLB were \$27,000,000 and \$28,000,000 at March 31, 2013 and December 31, 2012, respectively. The FHLB advances are secured by the pledge of residential mortgage loans.

Capital resources

Stockholders' equity at March 31, 2013 was \$24,226,000, compared to \$24,965,000 at December 31, 2012. On May 1, 2009, the Company received a \$14,738,000 investment by the United States Department of the Treasury under its Capital Purchase Program (the TARP Program). The TARP Program is a voluntary program designed to provide capital for healthy banks to improve the flow of funds from banks to their customers. Under the TARP Program, the Company issued to the Treasury \$14,738,000 of preferred stock and warrants to purchase 499,030 shares of the Company's common stock at a purchase price of \$4.43 per share. The preferred stock issued by the Company under the TARP Capital Purchase Program carries a 5% dividend until May 1, 2014, and 9% thereafter, unless the shares are redeemed by the Company. The \$739,000 decrease in equity during the first three months of 2013 was primarily due to the net loss available to common shareholders of \$(732,000).

During the first quarter of 2005, the Company issued \$5.2 million in Trust Preferred Capital Notes to increase its regulatory capital and to help fund its expected growth in 2005. During the third quarter of 2007, the Company issued \$3.6 million in Trust Preferred Capital Notes to partially fund the construction of an 80,000 square foot building completed in 2008. The Trust Preferred Capital Notes may be included in Tier 1 capital for regulatory capital adequacy determination purposes up to 25% of Tier 1 capital after its inclusion.

The Company is currently prohibited by its Written Agreement with the Reserve Bank from making dividend or interest payments on the TARP program preferred stock or trust preferred capital notes without prior regulatory approval. In addition, the Consent Order with the FDIC and BFI provides that the Bank will not pay any dividends, pay bonuses or make any other form of payment outside the ordinary course of business resulting in a reduction in capital, without regulatory approval. At March 31, 2013, the aggregate amount of all of the Company's total accrued but deferred dividend payments on TARP was \$1,565,912 and interest payments on trust preferred capital notes was \$716,347.

In June 2012 as a result of the unpaid dividends, Treasury requested that an observer appointed by Treasury be allowed to attend the Company's meetings of its board of directors. The observer started attending board meetings in August 2012. Treasury has the contractual right to nominate up to two members to the board of directors upon the Company's sixth deferred dividend payment. The Company has deferred eight dividend payments as of March 31, 2013. However, Treasury has not indicated at this time it will nominate two directors to our board.

The Company is currently evaluating potential sources of additional capital, with the objective is to become compliant with the capital requirements of the Consent Order as soon as practically possible. In addition the Company is considering various alternatives for the repayment of the preferred stock issued under the TARP Program. However, no assurance can be given that sources of new capital will be received.

The following table presents the composition of regulatory capital and the capital ratios for the Company at the dates indicated (dollars in thousands).

	March 31, 2013	December 31, 2012		
Tier 1 capital				
Preferred stock	\$ 59	\$ 59		
Common stock	17,007	17,007		
Additional paid-in capital	40,705	40,705		
Retained earnings (deficit)	(33,906)	(33,174)		
Warrant surplus	732	732		
Discount on preferred stock	(162)	(199)		
Qualifying trust preferred securities	3,062	3,306		
Less intangible assets	(369)	(393)		
Total Tier 1 capital	27,128	28,043		
Tier 2 capital				
Qualifying trust preferred securities	5,702	5,458		
Allowance for loan losses	4,406	4,795		
Total Tier 2 capital	10,108	10,253		
Total risk-based capital	37,236	38,296		
Risk-weighted assets	\$ 346,599	\$ 377,572		
Average assets	\$ 500,511	\$ 505,046		
Capital ratios				
Leverage ratio (Tier 1 capital to average assets)	5.42	%	5.55	%
Tier 1 capital to risk-weighted assets	7.83	%	7.43	%
Total capital to risk-weighted assets	10.74	%	10.14	%
Equity to total assets	5.09	%	4.89	%

The following table presents the composition of regulatory capital and the capital ratios for the Bank at the dates indicated (dollars in thousands).

	March 31, 2013	December 31, 2012		
Tier 1 capital				
Common stock	\$ 6,849	\$ 6,849		
Additional paid-in capital	55,407	55,406		
Retained earnings (deficit)	(29,349)	(28,925)		
Less intangible assets	(369)	(393)		
Total Tier 1 capital	32,538	32,937		
Tier 2 capital				
Allowance for loan losses	4,405	4,769		
Total Tier 2 capital	4,405	4,769		
Total risk-based capital	36,943	37,706		
Risk-weighted assets	\$ 346,452	\$ 375,451		
Average assets	\$ 500,084	\$ 505,150		
Capital ratios				
Leverage ratio (Tier 1 capital to average assets)	6.51	%	6.52	%
Tier 1 capital to risk-weighted assets	9.39	%	8.77	%
Total capital to risk-weighted assets	10.66	%	10.04	%
Equity to total assets	6.71	%	6.55	%

Federal regulatory agencies are required by law to adopt regulations defining five capital tiers: well capitalized, adequately capitalized, under capitalized, significantly under capitalized, and critically under capitalized. The Bank met the ratio requirements to be categorized as a “well capitalized” institution as of December 31, 2012, 2011 and 2010. However, due to the minimum capital ratios required by the Consent Order, the Bank currently is considered adequately capitalized. The Consent Order requires the Bank to maintain a leverage ratio of at least 8% and a total capital to risk-weighted assets ratio of at least 11%. At March 31, 2013, the Bank’s leverage ratio was 6.51% and the total capital to risk-weighted assets ratio was 10.66%. As required by the Consent Order the Bank has provided a capital plan to the FDIC and BFI that demonstrates how the Bank will come into compliance with the required minimum capital ratios set forth in the Consent Order. When capital falls below the “well capitalized” requirement, consequences can include: new branch approval could be withheld; more frequent examinations by the FDIC; brokered deposits cannot be renewed without a waiver from the FDIC; and other potential limitations as described in FDIC Rules and Regulations sections 337.6 and 303, and FDIC Act section 29. In addition, the FDIC insurance assessment increases when an institution falls below the “well capitalized” classification.

Liquidity

Liquidity represents the ability of a company to convert assets into cash or cash equivalents without significant loss, and the ability to raise additional funds by increasing liabilities. Liquidity management involves monitoring our sources and uses of funds in order to meet our day-to-day

cash flow requirements while maximizing profits. Liquidity management is made more complicated because different balance sheet components are subject to varying degrees of management control. For example, the timing of maturities of our investment portfolio is fairly predictable and subject to a high degree of control at the time investment decisions are made. However, net deposit inflows and outflows are far less predictable and are not subject to the same degree of control.

At March 31, 2013, our liquid assets, consisting of cash, cash equivalents and investment securities available for sale totaled \$98,773,000, or 20% of total assets. Investment securities traditionally provide a secondary source of liquidity since they can be converted into cash in a timely manner. However, approximately \$5,889,000 of these securities are pledged against borrowings. Therefore, the related borrowings would need to be repaid prior to the securities being sold in order for these securities to be converted to cash.

Our holdings of liquid assets plus the ability to maintain and expand our deposit base and borrowing capabilities serve as our principal sources of liquidity. We plan to meet our future cash needs through the liquidation of temporary investments, the generation of deposits, and from additional borrowings. In addition, we will receive cash upon the maturity and sale of loans and the maturity of investment securities. We maintain two federal funds lines of credit with correspondent banks totaling \$22 million for which there were no borrowings against the lines at March 31, 2013.

At March 31, 2013, we had commitments to originate \$70,020,000 of loans. Fixed commitments to incur capital expenditures were less than \$25,000 at March 31, 2013. Certificates of deposit scheduled to mature in the 12-month period ending March 31, 2014 totaled \$82,588,000. We believe that a significant portion of such deposits will remain with us. We further believe that deposit growth, loan repayments and other sources of funds will be adequate to meet our foreseeable short-term and long-term liquidity needs.

Interest rate sensitivity

An important element of asset/liability management is the monitoring of our sensitivity to interest rate movements. In order to measure the effects of interest rates on our net interest income, management takes into consideration the expected cash flows from the securities and loan portfolios and the expected magnitude of the repricing of specific asset and liability categories. We evaluate interest sensitivity risk and then formulate guidelines to manage this risk based on management's outlook regarding the economy, forecasted interest rate movements and other business factors. Our goal is to maximize and stabilize the net interest margin by limiting exposure to interest rate changes.

Contractual principal repayments of loans do not necessarily reflect the actual term of our loan portfolio. The average lives of mortgage loans are substantially less than their contractual terms because of loan prepayments and because of enforcement of due-on-sale clauses, which gives us the right to declare a loan immediately due and payable in the event, among other things, the borrower sells the real property subject to the mortgage and the loan is not repaid. In addition, certain borrowers increase their equity in the security property by making payments in excess of those required under the terms of the mortgage.

The sale of fixed rate loans is intended to protect us from precipitous changes in the general level of interest rates. The valuation of adjustable rate mortgage loans is not as directly dependent on the level of interest rates as is the value of fixed rate loans. As with other investments, we regularly monitor the appropriateness of the level of adjustable rate mortgage loans in our portfolio and may decide from time to time to sell such loans and reinvest the proceeds in other adjustable rate investments.

The data in the following table reflects repricing or expected maturities of various assets and liabilities at March 31, 2013. The gap analysis represents the difference between interest-sensitive assets and liabilities in a specific time interval. Interest sensitivity gap analysis presents a position that existed at one particular point in time, and assumes that assets and liabilities with similar repricing characteristics will reprice at the same time and to the same degree.

Village Bank and Trust Financial Corp.
Interest Rate Sensitivity GAP Analysis
March 31, 2013
(In thousands)

	Within 3 Months	3 to 6 Months	6 to 12 Months	13 to 36 Months	More than 36 Months	Total
Interest Rate Sensitive Assets						
Loans (1)						
Fixed rate	\$6,175	\$10,981	\$13,716	\$21,503	\$77,040	\$129,415
Variable rate	40,767	10,732	25,653	34,475	82,962	194,589
Investment securities	-	-	-	-	29,635	29,635
Loans held for sale	16,378	-	-	-	-	16,378
Federal funds sold	56,797	-	-	-	-	56,797
Total rate sensitive assets	120,117	21,713	39,369	55,978	189,637	426,814
Cumulative rate sensitive assets	120,117	141,830	181,199	237,177	426,814	
Interest Rate Sensitive Liabilities						
Interest checking	-	-	-	43,568	-	43,568
Money market accounts	63,546	-	-	-	-	63,546
Savings	-	-	-	20,470	-	20,470
Certificates of deposit	13,461	28,733	40,394	94,233	54,713	231,534
FHLB advances	4,000	5,000	1,000	16,000	1,000	27,000
Trust Preferred Securities	-	-	-	-	8,764	8,764
Other borrowings	1,882	-	-	-	-	1,882
Total rate sensitive liabilities	82,889	33,733	41,394	174,271	64,477	396,764
Cumulative rate sensitive liabilities	82,889	116,622	158,016	332,287	396,764	
Rate sensitivity gap for period	\$37,228	\$(12,020)	\$(2,025)	\$(118,293)	\$125,160	\$30,050
Cumulative rate sensitivity gap	\$37,228	\$25,208	\$23,183	\$(95,110)	\$30,050	
Ratio of cumulative gap to total assets	7.6	% 5.1	% 4.7	% (19.4)	% 6.1	%

Ratio of cumulative rate sensitive assets to cumulative rate sensitive liabilities	144.9	%	121.6	%	114.7	%	71.4	%	107.6	%
Ratio of cumulative gap to cumulative rate sensitive assets	31.0	%	17.8	%	12.8	%	(40.1))%	7.0	%

(1) Includes nonaccrual loans of approximately \$24,271,000, which are spread throughout the categories.

At March 31, 2013, our balance sheet is asset sensitive for the next twelve months, meaning that our assets reprice more quickly than our liabilities during that period, and liability sensitive for the next thirteen to thirty-six months, meaning that our liabilities will reprice more quickly than our assets during that period, with a ratio of cumulative gap to total assets ranging from a positive gap of 7.6% for the first three months to a negative gap of (19.4)% for the thirteen to thirty-six month period. A negative gap can adversely affect earnings in periods of increasing interest rates. Given the Federal Reserve's recent announcement that it will maintain short-term interest rates at current levels until the end of 2014, we do not expect interest rates to increase in the foreseeable future. However, we believe our balance sheet should be asset sensitive and, accordingly, we have adopted pricing policies to lengthen the maturities/repricing of our liabilities relative to the maturities/pricing of our assets.

Critical accounting policies

General

The accounting and reporting policies of the Company and its subsidiary are in accordance with accounting principles generally accepted in the United States of America (“GAAP”) and conform to general practices within the banking industry. The Company’s financial position and results of operations are affected by management’s application of accounting policies, including estimates, assumptions and judgments made to arrive at the carrying value of assets and liabilities, and amounts reported for revenues, expenses and related disclosures. Different assumptions in the application of these policies could result in material changes in the Company’s consolidated financial position and/or results of operations.

The more critical accounting and reporting policies include the Company’s accounting for the allowance for loan losses, troubled debt restructurings, real estate acquired in settlement of loans and income taxes. The Company’s accounting policies are fundamental to understanding the Company’s consolidated financial position and consolidated results of operations.

The following is a summary of the Company’s critical accounting policies that are highly dependent on estimates, assumptions, and judgments.

Allowance for loan losses

We monitor and maintain an allowance for loan losses to absorb an estimate of probable losses inherent in the loan portfolio. We maintain policies and procedures that address the systems of controls over the following areas of maintenance of the allowance: the systematic methodology used to determine the appropriate level of the allowance to provide assurance they are maintained in accordance with accounting principles generally accepted in the United States of America; the accounting policies for loan charge-offs and recoveries; the assessment and measurement of impairment in the loan portfolio; and the loan grading system.

The allowance reflects management’s best estimate of probable losses within the existing loan portfolio and of the risk inherent in various components of the loan portfolio, including loans identified as impaired as required by FASB Codification Topic 310: Receivables. Loans evaluated individually for impairment include non-performing loans, such as loans on non-accrual, loans past due by 90 days or more, restructured loans and other loans selected by management. The evaluations are based upon discounted expected cash flows or collateral valuations. If the evaluation shows that a loan is individually impaired, then a specific reserve is established for the amount of impairment.

Loans are grouped by similar characteristics, including the type of loan, the assigned loan classification and the general collateral type. A loss rate reflecting the expected loss inherent in a group of loans is derived based upon estimates of default rates for a given loan grade, the predominant collateral type for the group and the terms of the loan. The resulting estimate of losses for groups of loans is adjusted for relevant environmental factors and other conditions of the portfolio of loans and leases, including: borrower and industry concentrations; levels and trends in delinquencies, charge-offs and recoveries; changes in underwriting standards and risk selection; level of experience, ability and depth of lending management; and national and local economic conditions.

The amounts of estimated impairment for individually evaluated loans and groups of loans are added together for a total estimate of loan losses. This estimate of losses is compared to our allowance for loan losses as of the evaluation date and, if the estimate of losses is greater than the allowance, an additional provision to the allowance would be made. If the estimate of losses is less than the allowance, the degree to which the allowance exceeds the estimate is evaluated to determine whether the allowance falls outside a range of estimates. If the estimate of losses is below the range of reasonable estimates, the allowance would be reduced by way of a credit to the provision for loan losses. We recognize the inherent imprecision in estimates of losses due to various uncertainties and variability related to the factors used, and therefore a reasonable range around the estimate of losses is derived and used to ascertain whether the allowance is too high. If different assumptions or conditions were to prevail and it is determined that the allowance is not adequate to absorb the new estimate of probable losses, an additional provision for loan losses would be made, which amount may be material to the financial statements.

Troubled debt restructurings

A loan is accounted for as a troubled debt restructuring if we, for economic or legal reasons, grant a concession to a borrower considered to be experiencing financial difficulties that we would not otherwise consider. A troubled debt restructuring may involve the receipt of assets from the debtor in partial or full satisfaction of the loan, or a modification of terms such as a reduction of the stated interest rate or balance of the loan, a reduction of accrued interest, an extension of the maturity date or renewal of the loan at a stated interest rate lower than the current market rate for a new loan with similar risk, or some combination of these concessions. Troubled debt restructurings can be in either accrual or nonaccrual status. Nonaccrual troubled debt restructurings are included in nonperforming loans. Accruing troubled debt restructurings are generally excluded from nonperforming loans as it is considered probable that all contractual principal and interest due under the restructured terms will be collected. Troubled debt restructurings generally remain categorized as nonperforming loans and leases until a six-month payment history has been maintained.

In accordance with current accounting guidance, loans modified as troubled debt restructurings are, by definition, considered to be impaired loans. Impairment for these loans is measured on a loan-by-loan basis similar to other impaired loans as described above under Allowance for loan losses. Certain loans modified as troubled debt restructurings may have been previously measured for impairment under a general allowance methodology (i.e., pooling), thus at the time the loan is modified as a troubled debt restructuring the allowance will be impacted by the difference between the results of these two measurement methodologies. Loans modified as troubled debt restructurings that subsequently default are factored into the determination of the allowance in the same manner as other defaulted loans.

Real estate acquired in settlement of loans

Real estate acquired in settlement of loans represent properties acquired through foreclosure or physical possession. Write-downs to fair value of foreclosed assets at the time of transfer are charged to allowance for loan losses. Subsequent to foreclosure, the Company periodically evaluates the value of foreclosed assets held for sale and records an impairment charge for any subsequent declines in fair value less selling costs. Subsequent declines in value are charged to operations. Fair value is based on an assessment of information available at the end of a reporting period and depends upon a number of factors, including historical experience, economic conditions, and issues specific to individual properties. The evaluation of these factors involves subjective estimates and judgments that may change.

Income taxes

The Company uses the asset and liability method of accounting for income taxes. Under this method, deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. If current available information raises doubt as to the realization of the deferred tax assets, a valuation allowance may be established. Management considers the determination of this valuation allowance to be a critical accounting policy due to the need to exercise significant judgment in evaluating the amount and timing of recognition of deferred tax liabilities and assets, including projections of future taxable income. These judgments and estimates are reviewed on a continual basis as regulatory and business factors change. A valuation allowance for deferred tax assets may be required if the amounts of taxes recoverable through loss carry backs decline, or if management projects lower levels of future taxable income. Management determined that as of December 31, 2012 and March 31, 2013, the objective negative evidence represented by the Company's recent losses outweighed the more subjective positive evidence and, as a result, recognized a valuation allowance of \$10,158,000 and \$10,368,000, respectively, representing 100% of the net deferred tax asset at the indicated date.

New accounting standards

In February 2013, the Financial Accounting Standards Board (FASB) issued ASU 2013-02, Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income, which is intended to improve the reporting of reclassifications out of accumulated other comprehensive income. The ASU requires an entity to report, either on the face of the income statement or in the notes to the financial statements, the effect of significant reclassifications out of accumulated other comprehensive income on the respective line items in the income statement if the amount being reclassified is required to be reclassified in its entirety to net income. For other amounts that are not required to be reclassified in their entirety to net income in the same reporting period, an entity is required to cross-reference other required disclosures that provide additional detail about those amounts. This ASU is effective prospectively in the first quarter of 2013. The Company has included the required disclosures from ASU 2013-02 in the consolidated financial statements.

Impact of inflation and changing prices

The Company's consolidated financial statements included herein have been prepared in accordance with generally accepted accounting principles in the United States, which require the Company to measure financial position and operating results primarily in terms of historical dollars. Changes in the relative value of money due to inflation or recession are generally not considered. The primary effect of inflation on the operations of the Company is reflected in increased operating costs. In management's opinion, changes in interest rates affect the financial condition of a financial institution to a far greater degree than changes in the inflation rate. While interest rates are greatly influenced by changes in the inflation rate, they do not necessarily change at the same rate or in the same magnitude as the inflation rate. Interest rates are highly sensitive to many factors that are beyond the control of the Company, including changes in the expected rate of inflation, the influence of general and local economic conditions and the monetary and fiscal policies of the United States government, its agencies and various other governmental regulatory authorities.

ITEM 3 – QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Not Applicable.

ITEM 4 – CONTROLS AND PROCEDURES

The Company's Chief Executive Officer and Chief Financial Officer evaluated the effectiveness of the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934 (the "Exchange Act")) as of March 31, 2013. Based on that evaluation, management concluded that the Company's disclosure controls and procedures were effective as of March 31, 2013 in ensuring that all material information required to be disclosed in reports that it files or submits under the Exchange Act is recorded, processed summarized and reported with the time periods specified in SEC rules and regulations and that such information is accumulated and communicated to the Company's management, including the Company's Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

The Company's management is also responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act. There were no changes in our internal control over financial reporting identified in connection with the evaluation of it that occurred during the Company's last fiscal quarter that materially affected, or are reasonably likely to materially affect, internal control over financial reporting.

PART II – OTHER INFORMATION

ITEM 1 – LEGAL PROCEEDINGS

Not applicable.

ITEM 2 – UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

Not applicable.

ITEM 3 – DEFAULTS UPON SENIOR SECURITIES

In consideration of our agreements with our regulators, which require regulatory approval to make dividend payment on our preferred stock, the Company notified the U.S. Treasury in May 2011 that the Company was going to defer the payment of the quarterly cash dividend of \$184,225 due on May 16, 2011, and subsequent quarterly payments, on the Preferred Stock. The total arrearage on such preferred stock as of March 31, 2013 was \$1,565,912.

ITEM 4 – MINE SAFETY DISCLOSURES

ITEM 5 – OTHER INFORMATION

Not applicable.

ITEM 6 – EXHIBITS

31.1 Certification of Chief Executive Officer

31.2 Certification of Chief Financial Officer

32.1 Statement of Chief executive Officer and Chief Financial Officer
Pursuant to 18 U.S.C. Section 1350

101 The following materials from the Village Bank and Trust Financial Corp. Quarterly Report on Form 10-Q for the quarter ended March 31, 2013 formatted in eXtensible Business Reporting Language (XBRL): (i) Consolidated Balance Sheets, (ii) Consolidated Statements of Income, (iii) Consolidated Statements of Stockholders' Equity, (iv) Consolidated Statements of Cash Flows, and (v) Notes to Condensed Consolidated Financial Statements.

SIGNATURES

In accordance with the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this Report to be signed on its behalf by the undersigned, thereunto duly authorized.

VILLAGE BANK AND TRUST FINANCIAL CORP.
(Registrant)

Date: May 15,
2013

By: /s/ Thomas W. Winfree

Thomas W. Winfree
President and
Chief Executive Officer

Date: May 15,
2013

By: /s/ C. Harril Whitehurst,
Jr.

C. Harril Whitehurst, Jr.
Senior Vice President and
Chief Financial Officer

EXHIBIT INDEX

Exhibit Number	Document
31.1	Certification of Chief Executive Officer
31.2	Certification of Chief Financial Officer
32.1	Statement of Chief executive Officer and Chief Financial Officer Pursuant to 18 U.S.C. Section 1350
101	The following materials from the Village Bank and Trust Financial Corp. Quarterly Report on Form 10-Q for the quarter ended March 31, 2013 formatted in eXtensible Business Reporting Language (XBRL): (i) Consolidated Balance Sheets, (ii) Consolidated Statements of Income, (iii) Consolidated Statements of Stockholders' Equity, (iv) Consolidated Statements of Cash Flows, and (v) Notes to Condensed Consolidated Financial Statements.
