

COLONY BANKCORP INC
Form 10-Q
November 02, 2018

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, DC 20549

FORM 10-Q

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

FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 30, 2018 COMMISSION FILE NUMBER 0-12436

COLONY BANKCORP, INC.

(EXACT NAME OF REGISTRANT AS SPECIFIED IN ITS CHARTER)

GEORGIA 58-1492391
(STATE OR OTHER JURISDICTION OF (I.R.S. EMPLOYER
INCORPORATION OR ORGANIZATION) IDENTIFICATION NUMBER)

115 SOUTH GRANT STREET, FITZGERALD, GEORGIA 31750

ADDRESS OF PRINCIPAL EXECUTIVE OFFICES

229/426-6000

REGISTRANT'S TELEPHONE NUMBER INCLUDING AREA CODE

INDICATE BY CHECK MARK WHETHER THE REGISTRANT (1) HAS FILED ALL REPORTS REQUIRED TO BE FILED BY SECTIONS 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 DURING THE PRECEDING 12 MONTHS (OR FOR SUCH SHORTER PERIOD THAT THE REGISTRANT WAS REQUIRED TO FILE SUCH REPORTS), AND (2) HAS BEEN SUBJECT TO SUCH FILING REQUIREMENTS FOR THE PAST 90 DAYS.

YES NO

INDICATE BY CHECK MARK WHETHER THE REGISTRANT HAS SUBMITTED ELECTRONICALLY EVERY INTERACTIVE DATA FILE REQUIRED TO BE SUBMITTED PURSUANT TO RULE 405 OF REGULATION S-T (§232.405 OF THIS CHAPTER) DURING THE PRECEDING 12 MONTHS (OR FOR SUCH SHORTER PERIOD THAT THE REGISTRANT WAS REQUIRED TO SUBMIT AND POST SUCH FILES).

YES NO

INDICATE BY CHECK MARK WHETHER THE REGISTRANT IS A LARGE ACCELERATED FILER, AN ACCELERATED FILER, A NON-ACCELERATED FILER, SMALLER REPORTING COMPANY, OR AN EMERGING GROWTH COMPANY. SEE THE DEFINITIONS OF "LARGE ACCELERATED FILER," "ACCELERATED FILER," "SMALLER REPORTING COMPANY," AND "EMERGING GROWTH COMPANY" IN RULE 12b-2 OF THE EXCHANGE ACT.

LARGE ACCELERATED FILER
ACCELERATED FILER
NON-ACCELERATED FILER (DO NOT CHECK IF A SMALLER REPORTING COMPANY)
SMALLER REPORTING COMPANY
EMERGING GROWTH COMPANY

IF AN EMERGING GROWTH COMPANY, INDICATE BY CHECK MARK IF THE REGISTRANT HAS ELECTED NOT TO USE THE EXTENDED TRANSITION PERIOD FOR COMPLYING WITH ANY NEW OR REVISED FINANCIAL ACCOUNTING STANDARDS PROVIDED PURSUANT TO SECTION 13(a) OF THE EXCHANGE ACT.

INDICATE BY CHECK MARK WHETHER THE REGISTRANT IS A SHELL COMPANY (AS DEFINED IN RULE 12B-2 OF THE EXCHANGE ACT).

YES NO X

INDICATE THE NUMBER OF SHARES OUTSTANDING OF EACH OF THE ISSUER'S CLASSES OF COMMON STOCK, AS OF THE LATEST PRACTICABLE DATE.

<u>CLASS</u>	<u>OUTSTANDING AT NOVEMBER 2, 2018</u>
COMMON STOCK, \$1 PAR VALUE	8,444,908

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Forward Looking Statement Disclosure

Certain statements contained in this Quarterly Report that are not statements of historical fact constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 (the Act), notwithstanding that such statements are not specifically identified. In addition, certain statements may be contained in the Company's future filings with the SEC, in press releases, and in oral and written statements made by or with the approval of the Company that are not statements of historical fact and constitute forward-looking statements within the meaning of the Act. Examples of forward-looking statements include, but are not limited to: (i) projections of revenues, income or loss, earnings or loss per share, the payment or nonpayment of dividends, capital structure and other financial items; (ii) statements of plans and objectives of Colony Bankcorp, Inc. or its management or Board of Directors, including those relating to products or services; (iii) statements of future economic performance; and (iv) statements of assumptions underlying such statements. Words such as "believes," "anticipates," "expects," "intends," "targeted" and similar expressions are intended to identify forward-looking statements but are not the exclusive means of identifying such statements.

Forward-looking statements involve risks and uncertainties that may cause actual results to differ materially from those in such statements. Factors that could cause actual results to differ from those discussed in the forward-looking statements include, but are not limited to:

Local and regional economic conditions and the impact they may have on the Company and its customers and the Company's assessment of that impact.

Changes in estimates of future reserve requirements based upon the periodic review thereof under relevant regulatory and accounting requirements.

The effects of and changes in trade, monetary and fiscal policies and laws, including interest rate policies of the Federal Reserve Board.

Inflation, interest rate, market and monetary fluctuations.

Political instability.

Acts of war, terrorism or cyberterrorism.

The timely development and acceptance of new products and services and perceived overall value of these products and services by users.

Changes in consumer spending, borrowings and savings habits.

Technological changes.

Acquisitions and integration of acquired businesses.

The ability to increase market share and control expenses.

The effect of changes in laws and regulations (including laws and regulations concerning taxes, banking, securities and insurance) with which the Company and its subsidiary must comply.

The effect of changes in accounting policies and practices, as may be adopted by the regulatory agencies, as well as the Financial Accounting Standards Board and other accounting standard setters.

Changes in the Company's organization, compensation and benefit plans.

The costs and effects of litigation and of unexpected or adverse outcomes in such litigation.

Greater than expected costs or difficulties related to the integration of new lines of business.

The Company's success at managing the risks involved in the foregoing items.

Forward-looking statements speak only as of the date on which such statements are made. The Company undertakes no obligation to update any forward-looking statement to reflect events or circumstances after the date on which such statement is made, or to reflect the occurrence of unanticipated events.

Readers should carefully review all disclosures we file from time to time with the Securities and Exchange Commission ("SEC").

PART 1. FINANCIAL INFORMATION

ITEM 1

FINANCIAL STATEMENTS

THE FOLLOWING FINANCIAL STATEMENTS ARE PROVIDED FOR COLONY BANKCORP, INC. AND ITS WHOLLY-OWNED SUBSIDIARY BANK, COLONY BANK

A. CONSOLIDATED BALANCE SHEETS – SEPTEMBER 30, 2018 (UNAUDITED) AND DECEMBER 31, 2017 (AUDITED).

B. CONSOLIDATED STATEMENTS OF INCOME – FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2018 AND 2017 AND FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2018 AND 2017 (UNAUDITED).

C. CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME – FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2018 AND 2017 AND THE NINE MONTHS ENDED SEPTEMBER 30, 2018 AND 2017 (UNAUDITED).

D. CONSOLIDATED STATEMENTS OF CASH FLOWS – FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2018 AND 2017 (UNAUDITED).

THE CONSOLIDATED FINANCIAL STATEMENTS FURNISHED HAVE NOT BEEN AUDITED BY INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS, BUT REFLECT, IN THE OPINION OF MANAGEMENT, ALL ADJUSTMENTS (CONSISTING SOLELY OF NORMAL RECURRING ADJUSTMENTS) NECESSARY FOR A FAIR PRESENTATION OF THE RESULTS OF OPERATIONS FOR THE PERIODS PRESENTED.

THE RESULTS OF OPERATIONS FOR THE NINE MONTH PERIOD ENDED SEPTEMBER 30, 2018 ARE NOT NECESSARILY INDICATIVE OF THE RESULTS TO BE EXPECTED FOR THE FULL YEAR.

PART I (Continued)

Item 1 (Continued)

**COLONY
BANKCORP,
INC. AND
SUBSIDIARY
CONSOLIDATED
BALANCE
SHEETS
SEPTEMBER 30,
2018 AND
DECEMBER 31,
2017
(DOLLARS IN
THOUSANDS)**

	September 30, 2018 (Unaudited)	December 31, 2017 (Audited)
ASSETS		
Cash and Cash Equivalents		
Cash and Due from Banks	\$ 10,149	\$23,145
Interest-Bearing Deposits	21,764	34,668
Investment Securities		
Available for Sale, at Fair Value	318,032	354,247
Federal Home Loan Bank Stock, at Cost	3,594	3,043
Loans	779,443	765,284
Allowance for Loan Losses	(7,155)	(7,508)
Unearned Interest and Fees	(515)	(495)
	771,773	757,281
Premises and Equipment	27,744	27,639
Other Real Estate (Net of Allowance of \$815 and \$1,451 as of September 30, 2018 and December 31, 2017, Respectively)	2,173	4,256
Other Intangible Assets	18	45
Other Assets	30,949	28,431
Total Assets	\$ 1,186,196	\$ 1,232,755

LIABILITIES AND STOCKHOLDERS' EQUITY**Deposits**

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Noninterest-Bearing	\$ 177,261	\$ 190,928
Interest-Bearing	833,798	877,057
	1,011,059	1,067,985
Borrowed Money		
Subordinated Debentures	24,229	24,229
Other Borrowed Money	58,500	47,500
	82,729	71,729
Other Liabilities	3,420	2,718
Stockholders' Equity		
Common Stock, Par Value \$1 a Share; Authorized 20,000,000 Shares, Issued 8,444,908 and 8,439,258 Shares as of September 30, 2018 and December 31, 2017 respectively	8,445	8,439
Paid-In Capital	25,970	29,145
Retained Earnings	66,916	59,230
Accumulated Other Comprehensive (Loss), Net of Tax Benefits	(12,343)	(6,491)
	88,988	90,323
Total Liabilities and Stockholders' Equity	\$ 1,186,196	\$ 1,232,755

The accompanying notes are an integral part of these statements.

PART I (Continued)

Item 1 (Continued)

**COLONY
BANKCORP,
INC. AND
SUBSIDIARY
CONSOLIDATED
STATEMENTS
OF INCOME
THREE
MONTHS
ENDED
SEPTEMBER 30,
2018 AND 2017
AND NINE
MONTHS
ENDED
SEPTEMBER 30,
2018 AND 2017
(UNAUDITED)
(DOLLARS IN
THOUSANDS)**

	Three Months Ended		Nine Months Ended	
	September	September	September	September
	30, 2018	30, 2017	30, 2018	30, 2017
Interest Income				
Loans, Including Fees	\$10,255	\$9,754	\$30,048	\$28,884
Deposits with Other Banks	48	52	192	166
Investment Securities				
U.S. Government Agencies	1,847	1,684	5,635	4,932
State, County and Municipal	25	27	77	87
Corporate Debt	27	23	84	59
Dividends on Other Investments	49	38	134	109
	12,251	11,578	36,170	34,237
Interest Expense				
Deposits	1,564	1,191	4,165	3,559
Federal Funds Purchased	3	-	4	3
Borrowed Money	579	544	1,602	1,554
	2,146	1,735	5,771	5,116
Net Interest Income	10,105	9,843	30,399	29,121

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Provision for Loan Losses	61	-	131	335
Net Interest Income After Provision for Loan Losses	10,044	9,843	30,268	28,786
Noninterest Income				
Service Charges on Deposits	1,134	1,169	3,266	3,315
Other Service Charges, Commissions and Fees	803	741	2,414	2,300
Mortgage Fee Income	176	241	507	629
Securities Gains (Losses)	-	-	116	-
Other	292	273	860	974
	2,405	2,424	7,163	7,218
Noninterest Expenses				
Salaries and Employee Benefits	5,110	4,802	15,032	14,467
Occupancy and Equipment	1,052	1,014	3,077	2,965
Other	2,916	2,564	8,106	7,976
	9,078	8,380	26,215	25,408
Income Before Income Taxes	3,371	3,887	11,216	10,596
Income Taxes	676	1,265	2,264	3,424
Net Income	2,695	2,622	8,952	7,172
Preferred Stock Dividends	-	-	-	211
Net Income Available to Common Stockholders	\$2,695	\$2,622	\$8,952	\$6,961
Net Income Per Share of Common Stock				
Basic	\$0.32	\$0.31	\$1.06	\$0.82
Diluted	\$0.32	\$0.30	\$1.04	\$0.81
Cash Dividends Paid Per Share of Common Stock	\$0.05	\$0.025	\$0.15	\$0.075
Weighted Average Basic Shares Outstanding	8,439,415	8,439,258	8,439,310	8,439,258
Weighted Average Diluted Shares Outstanding	8,444,816	8,629,523	8,571,516	8,631,566

The accompanying notes are an integral part of these statements.

PART I (Continued)

Item 1 (Continued)

**COLONY
BANKCORP, INC.
AND SUBSIDIARY
CONSOLIDATED
STATEMENTS OF
COMPREHENSIVE
INCOME
THREE MONTHS
ENDED
SEPTEMBER 30,
2018 AND 2017
AND NINE
MONTHS ENDED
SEPTEMBER 30,
2018 AND 2017
(UNAUDITED)
(DOLLARS IN
THOUSANDS)**

	Three Months Ended September 30, 2018		Nine Months Ended September 30, 2018	
	September 30, 2017		September 30, 2017	
Net Income	\$2,695	\$ 2,622	\$8,952	\$ 7,172
Other Comprehensive Income:				
Gains (Losses) on Securities Arising During the Year	(1,945)	300	(7,291)	1,888
Tax Effect	408	(102)	1,531	(642)
Realized Gains on Sale of AFS Securities	-	-	(116)	-
Tax Effect	-	-	24	-
Change in Unrealized Gains (Losses) on Securities Available for Sale, Net of Reclassification Adjustment and Tax Effects	(1,537)	198	(5,852)	1,246
Comprehensive Income	\$1,158	\$ 2,820	\$3,100	\$ 8,418

The accompanying notes are an integral part of these statements.

PART I (Continued)

Item 1 (Continued)

**COLONY
BANKCORP,
INC. AND
SUBSIDIARY
CONSOLIDATED
STATEMENTS
OF CASH
FLOWS
NINE MONTHS
ENDED
SEPTEMBER 30,
2018 AND 2017
(UNAUDITED)
(DOLLARS IN
THOUSANDS)**

	Nine Months Ended	
	September	September
	30, 2018	30, 2017
CASH FLOWS FROM OPERATING ACTIVITIES		
Net Income	\$8,952	\$ 7,172
Adjustments to Reconcile Net Income to Net Cash Provided by Operating Activities:		
Depreciation	1,310	1,240
Provision for Loan Losses	131	335
Securities (Gains)	(116)	-
Amortization and Accretion	909	1,077
(Gain) on Sale of Other Real Estate and Repossessions	(168)	(111)
Provision for Losses on Other Real Estate	201	256
Increase in Cash Surrender Value of Life Insurance	(368)	(404)
Loss on Sale of Premises & Equipment	1	(11)
Provision for Losses on Premises & Equipment	170	-
Other Prepaids, Deferrals and Accruals, Net	813	1,344
	11,835	10,898
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchases of Investment Securities Available for Sale	(20,893)	(54,448)
Proceeds from Maturities, Calls, and Paydowns of Investment Securities:		
Available for Sale	37,667	40,698
Proceeds from Sale of Investment Securities Available for Sale	11,268	-

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Interest-Bearing Deposits in Other Banks	12,904	33,593
Net Loans to Customers	(15,380)	(18,360)
Purchase of Premises and Equipment	(2,256)	(913)
Proceeds from Sale of Other Real Estate and Repossessions	2,769	3,168
Federal Home Loan Bank Stock	(551)	(245)
Proceeds from Sale of Premises and Equipment	8	38
	25,536	3,531
CASH FLOWS FROM FINANCING ACTIVITIES		
Noninterest-Bearing Customer Deposits	(13,667)	3,647
Interest-Bearing Customer Deposits	(43,259)	(27,741)
Dividends Paid for Preferred Stock	-	(316)
Dividends Paid for Common Stock	(1,266)	(633)
Redemption of Preferred Stock	-	(9,360)
Repurchase of Warrants	(3,175)	-
Payments on Federal Home Loan Bank Advances	(26,500)	-
Proceeds from Federal Home Loan Bank Advances	39,000	5,000
Payments on Other Borrowed Money	(1,507)	(16)
Proceeds from Other Borrowed Money	7	5,016
	(50,367)	(24,403)
Net Decrease in Cash and Cash Equivalents	(12,996)	(9,974)
Cash and Cash Equivalents at Beginning of Period	23,145	28,822
Cash and Cash Equivalents at End of Period	\$10,149	\$ 18,848

The accompanying notes are an integral part of these statements.

PART I (Continued)

Item 1 (Continued)

COLONY BANKCORP, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(1) Summary of Significant Accounting Policies

Presentation

Colony Bankcorp, Inc. (the “Company”) is a bank holding company located in Fitzgerald, Georgia. The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiary, Colony Bank, Fitzgerald, Georgia (the “Bank”). All significant intercompany accounts have been eliminated in consolidation. The accounting and reporting policies of the Company conform to generally accepted accounting principles and practices utilized in the commercial banking industry.

All dollars in notes to consolidated financial statements are rounded to the nearest thousand, except for per share amounts.

The consolidated financial statements in this report are unaudited, except for the December 31, 2017 consolidated balance sheet. All adjustments consisting of normal recurring accruals which are, in the opinion of management, necessary for fair presentation of the interim consolidated financial statements, have been included and fairly and accurately present the financial position, results of operations and cash flows of the Company. The results of operations for the nine months ended September 30, 2018 are not necessarily indicative of the results which may be expected for the entire year.

Nature of Operations

The Bank provides a full range of retail and commercial banking services for consumers and small- to medium-size businesses located primarily in central, south and coastal Georgia. The Bank is headquartered in Fitzgerald, Georgia with banking offices in Albany, Ashburn, Broxton, Centerville, Columbus, Cordele, Douglas, Eastman, Fitzgerald, Leesburg, Moultrie, Quitman, Rochelle, Savannah, Soperton, Sylvester, Statesboro, Thomaston, Tifton, Valdosta and Warner Robins. Lending and investing activities are funded primarily by deposits gathered through its retail banking office network.

Use of Estimates

In preparing the financial statements, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the balance sheet date and revenues and expenses for the period. Actual results could differ significantly from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses and the valuation of real estate acquired in connection with foreclosures or in satisfaction of loans.

Reclassifications

In certain instances, amounts reported in prior years' consolidated financial statements have been reclassified to conform to statement presentations selected for 2018. Such reclassifications have not affected previously reported stockholders' equity or net income.

Concentrations of Credit Risk

Concentrations of credit risk can exist in relation to individual borrowers or groups of borrowers, certain types of collateral, certain types of industries, or certain geographic regions. The Company has a concentration in real estate loans as well as a geographic concentration that could pose an adverse credit risk. At September 30, 2018, approximately 87 percent of the Company's loan portfolio was concentrated in loans secured by real estate. A substantial portion of borrowers' ability to honor their contractual obligations is dependent upon the viability of the real estate economic sector. Collateral real estate values that secure land development, construction and speculative real estate loans in the Company's larger Metropolitan Statistical Area (MSA) markets have started showing signs of stabilization in values in recent years. In addition, a large portion of the Company's foreclosed assets are also located in these same geographic markets, making the recovery of the carrying amount of foreclosed assets susceptible to changes in market conditions. Management continues to monitor these concentrations and has considered these concentrations in its allowance for loan loss analysis.

PART I (Continued)

Item 1 (Continued)

(1) Summary of Significant Accounting Policies (Continued)

Concentrations of Credit Risk (Continued)

The success of the Company is dependent, to a certain extent, upon the economic conditions in the geographic markets it serves. Adverse changes in the economic conditions in these geographic markets would likely have a material adverse effect on the Company's results of operations and financial condition. The operating results of the Company depend primarily on its net interest income. Accordingly, operations are subject to risks and uncertainties surrounding the exposure to changes in the interest rate environment.

At times, the Company may have cash and cash equivalents at financial institutions in excess of federal deposit insurance limits. The Company places its cash and cash equivalents with high credit quality financial institutions whose credit ratings are monitored by management to minimize credit risk.

Investment Securities

The Company classifies its investment securities as trading, available for sale or held to maturity. Securities that are held principally for resale in the near term are classified as trading. Trading securities are carried at fair value, with realized and unrealized gains and losses included in noninterest income. Currently, no securities are classified as trading. Securities acquired with both the intent and ability to be held to maturity are classified as held to maturity and reported at amortized cost. All securities not classified as trading or held to maturity are considered available for sale. Securities available for sale are reported at estimated fair value. Unrealized gains and losses on securities available for sale are excluded from earnings and are reported, net of deferred taxes, in accumulated other comprehensive income (loss), a component of stockholders' equity. Gains and losses from sales of securities available for sale are computed using the specific identification method. Securities available for sale includes securities which may be sold to meet liquidity needs arising from unanticipated deposit and loan fluctuations, changes in regulatory capital requirements, or unforeseen changes in market conditions.

The Company evaluates each investment security held to maturity and available for sale security in a loss position for other-than-temporary impairment (OTTI). In estimating other-than-temporary impairment losses, management

considers such factors as the length of time and the extent to which the market value has been below cost, the financial condition of the issuer and the Company's intent to sell and whether it is more likely than not that the Company will be required to sell the security before anticipated recovery of the amortized cost basis. If the Company intends to sell or if it is more likely than not that the Company will be required to sell the security before recovery, the OTTI write-down is recognized in earnings. If the Company does not intend to sell the security or it is not more likely than not that it will be required to sell the security before recovery, the OTTI write-down is separated into an amount representing credit loss, which is recognized in earnings and an amount related to all other factors, which is recognized in other comprehensive income (loss).

Federal Home Loan Bank Stock

Investment in stock of a Federal Home Loan Bank (FHLB) is required for every federally insured institution that utilizes its services. FHLB stock is considered restricted, as defined in the accounting standards. The FHLB stock is reported in the consolidated financial statements at cost. Dividend income is recognized when earned.

Loans

Loans that the Company has the ability and intent to hold for the foreseeable future or until maturity are recorded at their principal amount outstanding, net of unearned interest and fees. Loan origination fees, net of certain direct origination costs, are deferred and amortized over the estimated terms of the loans using the straight-line method. Interest income on loans is recognized using the effective interest method.

A loan is considered to be delinquent when payments have not been made according to contractual terms, typically evidenced by nonpayment of a monthly installment by the due date.

When management believes there is sufficient doubt as to the collectability of principal or interest on any loan or generally when loans are 90 days or more past due, the accrual of applicable interest is discontinued and the loan is designated as nonaccrual, unless the loan is well secured and in the process of collection. Interest payments received on nonaccrual loans are either applied against principal or reported as income, according to management's judgment as to the collectability of principal. Loans are returned to an accrual status when factors indicating doubtful collectability on a timely basis no longer exist.

PART I (Continued)

Item 1 (Continued)

(1) Summary of Significant Accounting Policies (Continued)

Loans Modified in a Troubled Debt Restructuring (“TDR”)

Loans are considered to have been modified in a TDR when, due to a borrower’s financial difficulty, the Company makes certain concessions to the borrower that it would not otherwise consider for new debt with similar risk characteristics. Modifications may include interest rate reductions, principal or interest forgiveness, forbearance, and other actions intended to minimize economic loss and to avoid foreclosure or repossession of the collateral. Generally, a non-accrual loan that has been modified in a TDR remains on non-accrual status for a period of 6 months to demonstrate that the borrower is able to meet the terms of the modified loan. However, performance prior to the modification, or significant events that coincide with the modification, are included in assessing whether the borrower can meet the new terms and may result in the loan being returned to accrual status at the time of loan modification or after a shorter performance period. If the borrower’s ability to meet the revised payment schedule is uncertain, the loan remains on non-accrual status. Once a loan is modified in a troubled debt restructuring it is accounted for as an impaired loan, regardless of its accrual status, until the loan is paid in full, sold or charged off. A TDR may cease being classified as impaired if the loan is subsequently modified at market terms and, has performed according to the modified terms for at least six months, and there has not been any prior principal forgiveness on a cumulative basis.

Allowance for Loan Losses

The allowance for loan losses is established as losses are estimated to have occurred through a provision for loan losses charged to earnings. Loan losses are charged against the allowance when management believes the inability to collect a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance.

The allowance for loan losses is evaluated on a regular basis by management and is based upon management’s periodic review of the collectability of the loans in light of historical experience, the nature and volume of the loan portfolio, adverse situations that may affect the borrower’s ability to repay, estimated value of any underlying collateral and prevailing economic conditions. This evaluation is inherently subjective, as it requires estimates that are susceptible to significant revisions as more information becomes available.

The allowance consists of specific, historical and general components. The specific component relates to loans that are classified as either doubtful, substandard or special mention. For such loans that are also classified as impaired, an allowance is established when the discounted cash flows (or collateral value or observable market price) of the impaired loan are lower than the carrying value of that loan. The historical component covers nonclassified loans and is based on historical loss experience adjusted for qualitative factors. A general component is maintained to cover uncertainties that could affect management's estimate of probable losses. The general component of the allowance reflects the margin of imprecision inherent in the underlying assumptions used in the methodologies for estimating specific and historical losses in the portfolio. General valuation allowances are based on internal and external qualitative risk factors such as (1) changes in lending policies and procedures, including changes in underwriting standards and collections, charge offs, and recovery practices, (2) changes in international, national, regional, and local conditions, (3) changes in the nature and volume of the portfolio and terms of loans, (4) changes in the experience, depth, and ability of lending management, (5) changes in the volume and severity of past due loans and other similar conditions, (6) changes in the quality of the organization's loan review system, (7) changes in the value of underlying collateral for collateral dependent loans, (8) the existence and effect of any concentrations of credit and changes in the levels of such concentrations, and (9) the effect of other external factors (i.e. competition, legal and regulatory requirements) on the level of estimated credit losses.

Loans identified as losses by management, internal loan review and/or regulatory agencies are charged off.

A loan is considered impaired when, based on current information and events, it is probable that the Company will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record and the amount of the shortfall in relation to the principal and interest owed. Impairment is measured on a loan-by-loan basis by either the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's obtainable market price or the fair value of the collateral if the loan is collateral dependent.

PART I (Continued)

Item 1 (Continued)

(1) Summary of Significant Accounting Policies (Continued)

Allowance for Loan Losses (Continued)

A significant portion of the Company's impaired loans are deemed to be collateral dependent. Management therefore measures impairment on these loans based on the fair value of the collateral. Collateral values are determined based on appraisals performed by qualified licensed appraisers hired by the Company or by senior members of the Company's credit administration staff. The decision whether or not to obtain an external third-party appraisal usually depends on the type of property being evaluated. External appraisals are usually obtained on more complex, income producing properties such as hotels, shopping centers and businesses. Less complex properties such as residential lots, farm land and single family houses may be evaluated internally by senior credit administration staff. When the Company does obtain appraisals from external third-parties, the values utilized in the impairment calculation are "as is" or current market values. The appraisals, whether prepared internally or externally, may utilize a single valuation approach or a combination of approaches including the comparable sales, income and cost approach. Appraised amounts used in the impairment calculation are typically discounted 10 percent to account for selling and marketing costs, if the repayment of the loan is to come from the sale of the collateral. Although appraisals are not obtained each year on all impaired loans, the collateral values used in the impairment calculations are evaluated quarterly by management. Based on management's knowledge of the collateral and the current real estate market conditions, appraised values may be further discounted to reflect facts and circumstances known to management since the most recent appraisal was performed.

Adjustments are routinely made in the appraisal process by the appraisers to adjust for differences between the comparable sales and income data available. Such adjustments are typically significant and result in a level 3 classification of the inputs for determining fair value. Because of the high degree of judgment required in estimating the fair value of collateral underlying impaired loans and because of the relationship between fair value and general economic conditions, we consider the fair value of impaired loans to be highly sensitive to changes in market conditions.

Premises and Equipment

Premises and equipment are recorded at acquisition cost net of accumulated depreciation.

Depreciation is charged to operations over the estimated useful lives of the assets. The estimated useful lives and methods of depreciation are as follows:

Description	Life in Years	Method
Banking Premises	15-40	Straight-Line and Accelerated
Furniture and Equipment	5 - 10	Straight-Line and Accelerated

Expenditures for major renewals and betterments are capitalized. Maintenance and repairs are charged to operations as incurred. When property and equipment are retired or sold, the cost and accumulated depreciation are removed from the respective accounts and any gain or loss is reflected in other income or expense.

Intangible Assets

Intangible assets consist of core deposit intangibles acquired in connection with a business combination. The core deposit intangible is initially recognized based on a valuation performed as of the consummation date. The core deposit intangible is amortized by the straight-line method over the average remaining life of the acquired customer deposits.

Transfers of Financial Assets

Transfers of financial assets are accounted for as sales, when control over the assets has been surrendered. Control over transferred assets is deemed to be surrendered when (1) the assets have been isolated from the Company, (2) the transferee obtains the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred assets and (3) the Company does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity.

PART I (Continued)

Item 1 (Continued)

(1) Summary of Significant Accounting Policies (Continued)

Statement of Cash Flows

For reporting cash flows, cash and cash equivalents include cash on hand, noninterest-bearing amounts due from banks and federal funds sold. Cash flows from demand deposits, interest-bearing checking accounts, savings accounts, loans and certificates of deposit are reported net.

Advertising Costs

The Company expenses the cost of advertising in the periods in which those costs are incurred.

Income Taxes

The provision for income taxes is based upon income for financial statement purposes, adjusted for nontaxable income and nondeductible expenses. Deferred income taxes have been provided when different accounting methods have been used in determining income for income tax purposes and for financial reporting purposes.

Deferred tax assets and liabilities are recognized based on future tax consequences attributable to differences arising from the financial statement carrying values of assets and liabilities and their tax bases. The differences relate primarily to depreciable assets (use of different depreciation methods for financial statement and income tax purposes) and allowance for loan losses (use of the allowance method for financial statement purposes and the direct write-off method for tax purposes). In the event of changes in the tax laws, deferred tax assets and liabilities are adjusted in the period of the enactment of those changes, with effects included in the income tax provision. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion or all of the deferred tax assets will not be realized. The Company and its subsidiary file a consolidated federal income tax return. The subsidiary pays its proportional share of federal income taxes to the Company based on its taxable income.

Positions taken in the Company's tax returns may be subject to challenge by the taxing authorities upon examination. Uncertain tax positions are initially recognized in the consolidated financial statements when it is more likely than not the position will be sustained upon examination by the tax authorities. Such tax positions are both initially and subsequently measured as the largest amount of tax benefit that is greater than 50 percent likely of being realized upon settlement with the tax authority, assuming full knowledge of the position and all relevant facts. The Company provides for interest and, in some cases, penalties on tax positions that may be challenged by the taxing authorities. Interest expense is recognized beginning in the first period that such interest would begin accruing. Penalties are recognized in the period that the Company claims the position in the tax return. Interest and penalties on income tax uncertainties are classified within income tax expense in the consolidated statement of income.

Other Real Estate

Other real estate generally represents real estate acquired through foreclosure and is initially recorded at estimated fair value at the date of acquisition less the cost of disposal. Losses from the acquisition of property in full or partial satisfaction of debt are recorded as loan losses. Properties are evaluated regularly to ensure the recorded amounts are supported by current fair values, and valuation allowances are recorded as necessary to reduce the carrying amount to fair value less estimated cost of disposal. Routine holding costs and gains or losses upon disposition are included in other noninterest expense.

Bank-Owned Life Insurance

The Company has purchased life insurance on the lives of certain key members of management and directors. The life insurance policies are recorded at the amount that can be realized under the insurance contract at the balance sheet date, which is the cash surrender value adjusted for other charges or amounts due that are probable at settlement, if applicable. Increases in the cash surrender value are recorded as other income in the consolidated statements of income. The cash surrender value of the insurance contracts is recorded in other assets on the consolidated balance sheets in the amount of \$17,457 and \$17,089 as of September 30, 2018 and December 31, 2017, respectively.

PART I (Continued)

Item 1 (Continued)

(1) Summary of Significant Accounting Policies (Continued)

Comprehensive Income

Accounting principles generally require that recognized revenue, expenses, gains and losses be included in net income. Certain changes in assets and liabilities, such as unrealized gains and losses on securities available for sale, represent equity changes from economic events of the period other than transactions with owners and are not reported in the consolidated statements of income but as a separate component of the equity section of the consolidated balance sheets. Such items are considered components of other comprehensive income (loss). Accounting standards codification requires the presentation in the consolidated financial statements of net income and all items of other comprehensive income (loss) as total comprehensive income (loss).

Off-Balance Sheet Credit Related Financial Instruments

In the ordinary course of business, the Company has entered into commitments to extend credit, commercial letters of credit and standby letters of credit. Such financial instruments are recorded when they are funded.

Changes in Accounting Principles and Effects of New Accounting Pronouncements

ASU 2014-09, *Revenue from Contracts with Customers (Topic 606)*. On January 1, 2018, the Company adopted ASU 2014-09 and all subsequent amendments to the ASU and ASC 606 which (1) creates a single framework for recognizing revenue from contracts with customers that fall within its scope and (2) revises when it is appropriate to recognize a gain (loss) from the transfer of nonfinancial assets, such as other real estate owned. The majority of the Company's revenues came from interest income and other sources, including loans and investment securities, that are outside the scope of ASC 606. With the exception of gain/losses on the sale of other real estate owned, the Company's services that fall within the scope of ASC 606 are presented within noninterest income and are recognized as revenue as the Company satisfies its obligations to the customer. Services within the scope of ASC 606 reported in noninterest income include service charges on deposit accounts, debit card interchange fees, and ATM fees. The net of gains and losses on the sale of other real estate owned are recorded in other noninterest expenses in the Company's consolidated statements of income. The adoption of ASC 606 did not change the timing or amount of revenue recognized for the

Company. Accordingly, no cumulative effect adjustment was recorded under the modified retrospective transition method. See Note 15 for further discussion on the Company's accounting policies for revenue source within the scope of ASC 606.

ASU 2016-01, *Financial Instruments – Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities*. ASU 2016-01, among other things, (i) requires equity investments, with certain exceptions, to be measured at fair value with changes in fair value recognized in net income, (ii) simplifies the impairment assessment of equity investments without readily determinable fair values by requiring a qualitative assessment to identify impairment, (iii) eliminates the requirement for public business entities to disclose the methods and significant assumptions used to estimate the fair value that is required to be disclosed for financial instruments measured at amortized cost on the balance sheet, (iv) requires public business entities to use the exit price notion when measuring the fair value of financial instruments for disclosure purposes, (v) requires an entity to present separately in other comprehensive income the portion of the total change in the fair value of a liability resulting from a change in the instrument-specific credit risk when the entity has elected to measure the liability at fair value in accordance with the fair value option for financial instruments, (vi) requires separate presentation of financial assets and financial liabilities by measurement category and form of financial asset on the balance sheet or the accompanying notes to the financial statements and (viii) clarifies that an entity should evaluate the need for a valuation allowance on a deferred tax asset related to available-for-sale. ASU 2016-01 is effective for the Company on January 1, 2018. The adoption of this standard did not have a material impact on the Company's consolidated financial statements.

ASU 2016-02, *Leases (Topic 842)*. This ASU requires lessees to put most leases on their balance sheets but recognize expenses in the income statement in a manner similar to current accounting treatment. This ASU changes the guidance on sale-leaseback transactions, initial direct costs and lease execution costs, and, for lessors, modifies the classification criteria and the accounting for sales-type and direct financing leases. For public business entities, this ASU is effective for annual periods beginning after December 15, 2018, and interim periods therein. Entities are required to use a modified retrospective approach for leases that exist or are entered into after the beginning of the earliest comparative period in the financial statements. The Company is evaluating the impact of this ASU on its financial statements and disclosures.

PART I (Continued)

Item 1 (Continued)

(1) Summary of Significant Accounting Policies (Continued)

Changes in Accounting Principles and Effects of New Accounting Pronouncements (Continued)

ASU 2016-13, *Financial Instruments – Credit Losses (Topic 326)*. This ASU sets forth a “current expected credit loss” (CECL) model which requires the Company to measure all expected credit losses for financial instruments held at the reporting date based on historical experience, current conditions and reasonable supported forecasts. This replaces the existing incurred loss model and is applicable to the measurement of credit losses on financial assets measured at amortized cost and applies to some off-balance sheet credit exposures. This ASU is effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. The Company is currently assessing the impact of the adoption of this ASU on its consolidated financial statements.

ASU 2016-15, *Statement of Cash Flows (Topic 230) - Classification of Certain Cash Receipts and Cash Payments*. ASU 2016-15 provides guidance related to certain cash flow issues in order to reduce the current and potential future diversity in practice. ASU 2016-15 is effective for us on January 1, 2018 and did not have a significant impact on our financial statements.

ASU 2017-08, *Premium Amortization on Purchased Callable Debt Securities*. This ASU shortens the amortization period for the premium on certain purchased callable debt securities to the earliest call date. Today, entities generally amortize the premium over the contractual life of the security. The new guidance does not change the accounting for purchased callable debt securities held at a discount; the discount continues to be amortized to maturity. ASU No. 2017-08 is effective for interim and annual reporting periods beginning after December 15, 2018; early adoption is permitted. The guidance calls for a modified retrospective transition approach under which a cumulative-effect adjustment will be made to retained earnings as of the beginning of the first reporting period in which the guidance is adopted. The Company is currently evaluating the provisions of ASU No. 2017-08 to determine the potential impact the new standard will have on the Company’s Consolidated Financial Statements.

ASU 2018-02, *Income Statement – Reporting Comprehensive Income (Topic 220). Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income*. This ASU allows an entity to elect a reclassification from accumulated other comprehensive income (AOCI) to retained earnings for stranded tax effects resulting from the Tax Cuts and Jobs Act (TCJ Act). ASU 2018-02 is effective for all entities for fiscal years beginning after December 15, 2018, and interim periods within those fiscal years, with early adoption permitted. The Company elected to early

adopt the provisions of ASU 2018-02 in the fourth quarter of 2017 and, as a result, reclassified \$1.1 million from AOCI to retained earnings as of December 31, 2017.

ASU 2018-13, *Disclosure Framework – Changes to the Disclosure Requirements for Fair Value Measurement (Topic 820)*. This ASU modifies the disclosure requirements on fair value measurements. ASU 2018-13 is effective for interim and annual reporting periods after December 15, 2019; early adoption is permitted. The Company is currently evaluating the provisions of ASU 2018-13 to determine the potential impact the new standard will have on the Company's Consolidated Financial Statements.

PART I (Continued)

Item 1 (Continued)

(2) Investment Securities

Investment securities as of September 30, 2018 and December 31, 2017 are summarized as follows:

September 30, 2018	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Securities Available for Sale:				
U. S. Government Agencies Mortgage-Backed	\$ 326,676	\$ 52	\$ (15,550)	\$ 311,178
State, County & Municipal	4,024	4	(56)	3,972
Corporate Bonds	2,956	-	(74)	2,882
	\$ 333,656	\$ 56	\$ (15,680)	\$ 318,032

December 31, 2017	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Securities Available for Sale:				
U. S. Government Agencies Mortgage-Backed	\$ 354,931	\$ 258	\$ (8,466)	\$ 346,723
State, County & Municipal	4,493	23	(23)	4,493
Corporate Bonds	2,048	12	-	2,060
Asset-Backed	993	-	(22)	971
	\$ 362,465	\$ 293	\$ (8,511)	\$ 354,247

The amortized cost and fair value of investment securities as of September 30, 2018, by contractual maturity, are shown hereafter. Expected maturities may differ from contractual maturities for certain investments because issuers may have the right to call or prepay obligations with or without call or prepayment penalties. This is often the case with mortgage-backed securities, which are disclosed separately in the table below.

Securities

	Available for Sale	
	Amortized Fair	
	Cost	Value
Due In One Year or Less	\$ 358	\$ 356
Due After One Year Through Five Years	4,311	4,232
Due After Five Years Through Ten Years	1,134	1,136
Due After Ten Years	1,177	1,130
	\$6,980	\$6,854
 Mortgage-Backed Securities	 326,676	 311,178
	\$333,656	\$318,032

Proceeds from the sale of investments available for sale totaled \$11,268 for the first nine months of 2018. The sale of investments available for sale during the first nine months of 2018 resulted in gross realized gains of \$116 and losses of \$0. The Bank did not sell any investments during the first nine months of 2017. Therefore the Bank did not have any proceeds, gains or losses during the first nine months of 2017.

Investment securities having a carrying value approximating \$126,869 and \$175,484 as of September 30, 2018 and December 31, 2017, respectively, were pledged to secure public deposits and for other purposes.

PART I (Continued)

Item 1 (Continued)

(2) Investment Securities (Continued)

Information pertaining to securities with gross unrealized losses at September 30, 2018 and December 31, 2017 aggregated by investment category and length of time that individual securities have been in a continuous loss position, follows:

	Less Than 12 Months		12 Months or Greater		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
September 30, 2018						
U. S. Government Agencies	\$96,095	\$ (3,370)	\$209,451	\$ (12,180)	\$305,546	\$ (15,550)
Mortgage-Backed						
State, County and Municipal	2,498	(21)	1,258	(35)	3,756	(56)
Corporate Bonds	2,000	(35)	882	(39)	2,882	(74)
	\$100,593	\$ (3,426)	\$211,591	\$ (12,254)	\$312,184	\$ (15,680)
December 31, 2017						
U.S. Government Agencies	\$120,139	\$ (1,655)	\$190,196	\$ (6,811)	\$310,335	\$ (8,466)
Mortgage-Backed						
State, County and Municipal	2,598	(23)	-	-	2,598	(23)
Asset-Backed	971	(22)	-	-	971	(22)
	\$123,708	\$ (1,700)	\$190,196	\$ (6,811)	\$313,904	\$ (8,511)

Management evaluates securities for other-than-temporary impairment at least on a quarterly basis, and more frequently when economic or market concerns warrant such evaluation. Consideration is given to (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer and (3) the intent and ability of the Company to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value.

At September 30, 2018, 151 securities have unrealized losses which have depreciated 4.78 percent from the Company's amortized cost basis. These securities are guaranteed by either the U.S. Government, other governments or

U.S. corporations. In analyzing an issuer's financial condition, management considers whether the securities are issued by the federal government or its agencies, whether downgrades by bond rating agencies have occurred and the results of reviews of the issuer's financial condition. The unrealized losses are largely due to increases in market interest rates over the yields available at the time the underlying securities were purchased. As management has the ability to hold debt securities until maturity, or for the foreseeable future if classified as available-for-sale, no declines are deemed to be other than temporary.

PART I (Continued)

Item 1 (Continued)

(3) Loans

The following table presents the composition of loans segregated by class of loans, as of September 30, 2018 and December 31, 2017.

	September 30, 2018	December 31, 2017
Commercial and Agricultural		
Commercial	\$ 47,292	\$48,122
Agricultural	21,415	16,443
Real Estate		
Commercial Construction	53,570	45,214
Residential Construction	12,897	8,583
Commercial	349,408	351,172
Residential	189,153	194,049
Farmland	70,069	67,768
Consumer and Other		
Consumer	18,623	18,956
Other	17,016	14,977
Total Loans	\$ 779,443	\$765,284

Commercial and industrial loans are extended to a diverse group of businesses within the Company's market area. These loans are often underwritten based on the borrower's ability to service the debt from income from the business. Real estate construction loans often require loan funds to be advanced prior to completion of the project. Due to uncertainties inherent in estimating construction costs, changes in interest rates and other economic conditions, these loans often pose a higher risk than other types of loans. Consumer loans are originated at the Bank level. These loans are generally smaller loan amounts spread across many individual borrowers to help minimize risk.

Credit Quality Indicators. As part of the ongoing monitoring of the credit quality of the loan portfolio, management tracks certain credit quality indicators including trends related to (i) the risk grade assigned to commercial and consumer loans, (ii) the level of classified commercial loans, (iii) net charge-offs, (iv) nonperforming loans, and (v)

the general economic conditions in the Company's geographic markets.

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PART I (Continued)

Item 1 (Continued)

The Company uses a risk grading matrix to assign a risk grade to each of its loans. Loans are graded on a scale of 1 to 8. A description of the general characteristics of the grades is as follows:

(3) Loans (Continued)

Grades 1 and 2 – Borrowers with these assigned grades range in risk from virtual absence of risk to minimal risk. Such loans may be secured by Company-issued and controlled certificates of deposit or properly-margined equity securities or bonds. Other loans comprising these grades are made to companies that have been in existence for a long period of time with many years of consecutive profits and strong equity, good liquidity, excellent debt service ability and unblemished past performance, or to exceptionally strong individuals with collateral of unquestioned value that fully secures the loans. Loans in this category fall into the “pass” classification.

Grades 3 and 4 – Loans assigned these “pass” risk grades are made to borrowers with acceptable credit quality and risk. The risk ranges from loans with no significant weaknesses in repayment capacity and collateral protection to acceptable loans with one or more risk factors considered to be more than average.

Grade 5 – This grade includes “special mention” loans on management’s watch list and is intended to be used on a temporary basis for pass grade loans where risk-modifying action is intended in the short-term.

Grade 6 – This grade includes “substandard” loans in accordance with regulatory guidelines. This category includes borrowers with well-defined weaknesses that jeopardize the payment of the debt in accordance with the agreed terms. Loans considered to be impaired are assigned this grade, and these loans often have assigned loss allocations as part of the allowance for loan and lease losses. Generally, loans on which interest accrual has been stopped would be included in this grade.

Grades 7 and 8 – These grades correspond to regulatory classification definitions of “doubtful” and “loss,” respectively. In practice, any loan with these grades would be for a very short period of time, and generally the Company has no loans with these assigned grades. Management manages the Company’s problem loans in such a way that uncollectible loans or uncollectible portions of loans are charged off immediately with any residual, collectible amounts assigned a risk grade of 6.

The following table presents the loan portfolio by credit quality indicator (risk grade) as of September 30, 2018 and December 31, 2017. Those loans with a risk grade of 1, 2, 3 or 4 have been combined in the pass column for

presentation purposes. For the period ending September 30, 2018, the Company did not have any loans classified as “doubtful” or a “loss”.

September 30, 2018

	Pass	Special Mention	Substandard	Total Loans
Commercial and Agricultural				
Commercial	\$45,612	\$ 847	\$ 833	\$47,292
Agricultural	20,026	919	470	21,415
Real Estate				
Commercial Construction	52,181	631	758	53,570
Residential Construction	12,897	-	-	12,897
Commercial	335,844	7,000	6,564	349,408
Residential	173,987	4,543	10,623	189,153
Farmland	66,002	2,002	2,065	70,069
Consumer and Other				
Consumer	18,239	38	346	18,623
Other	17,010	6	-	17,016
Total Loans	\$741,798	\$ 15,986	\$ 21,659	\$779,443

PART I (Continued)

Item 1 (Continued)

(3) Loans (Continued)**December 31, 2017**

	Pass	Special Mention	Substandard	Total Loans
Commercial and Agricultural				
Commercial	\$46,469	\$ 825	\$ 828	\$48,122
Agricultural	15,868	175	400	16,443
Real Estate				
Commercial Construction	41,282	578	3,354	45,214
Residential Construction	8,583	-	-	8,583
Commercial	338,776	7,663	4,733	351,172
Residential	177,963	4,865	11,221	194,049
Farmland	66,335	444	989	67,768
Consumer and Other				
Consumer	18,496	53	407	18,956
Other	14,969	8	-	14,977
Total Loans	\$728,741	\$ 14,611	\$ 21,932	\$765,284

A loan's risk grade is assigned at the inception of the loan and is based on the financial strength of the borrower and the type of collateral. Loan risk grades are subject to reassessment at various times throughout the year as part of the Company's ongoing loan review process. Loans with an assigned risk grade of 6 or below and an outstanding balance of \$250,000 or more are reassessed on a quarterly basis. During this reassessment process individual reserves may be identified and placed against certain loans which are not considered impaired.

In assessing the overall economic condition of the markets in which it operates, the Company monitors the unemployment rates for its major service areas. The unemployment rates are reviewed on a quarterly basis as part of the allowance for loan loss determination.

Loans are considered past due if the required principal and interest payments have not been received as of the date such payments were due. Generally, loans are placed on nonaccrual status if principal or interest payments become 90 days past due or when, in management's opinion, the borrower may be unable to meet payment obligations as they

become due, as well as when required by regulatory provision. Loans may be placed on nonaccrual status regardless of whether or not such loans are considered past due.

PART I (Continued)

Item 1 (Continued)

(3) Loans (Continued)

The following table represents an age analysis of past due loans and nonaccrual loans, segregated by class of loans, as of September 30, 2018 and December 31, 2017:

September 30, 2018

	Accruing Loans 90 Days			Nonaccrual Loans	Current Loans	Total Loans
	30-89 Days Past Due	or More Past Due	Total Accruing Loans Past Due			
Commercial and Agricultural						
Commercial	\$376	\$ -	\$ 376	\$ 471	\$46,445	\$47,292
Agricultural	65	-	65	423	20,927	21,415
Real Estate						
Commercial Construction	141	-	141	505	52,924	53,570
Residential Construction	-	-	-	-	12,897	12,897
Commercial	895	-	895	2,277	346,236	349,408
Residential	2,485	-	2,485	2,219	184,449	189,153
Farmland	58	-	58	2,066	67,945	70,069
Consumer and Other						
Consumer	141	1	142	175	18,306	18,623
Other	9	-	9	-	17,007	17,016
Total Loans	\$4,170	\$ 1	\$ 4,171	\$ 8,136	\$767,136	\$779,443

December 31, 2017

	Accruing Loans 90 Days			Nonaccrual Loans
	30-89 Days	or More	Total Accruing	

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	Past Due	Past Due	Loans Past Due		Current Loans	Total Loans
Commercial and Agricultural						
Commercial	\$329	\$ -	\$ 329	\$ 598	\$47,195	\$48,122
Agricultural	111	-	111	399	15,933	16,443
Real Estate						
Commercial Construction	27	-	27	477	44,710	45,214
Residential Construction	119	-	119	-	8,464	8,583
Commercial	919	-	919	2,172	348,081	351,172
Residential	2,482	-	2,482	2,830	188,737	194,049
Farmland	318	-	318	839	66,611	67,768
Consumer and Other						
Consumer	246	-	246	188	18,522	18,956
Other	7	-	7	-	14,970	14,977
Total Loans	\$4,558	\$ -	\$ 4,558	\$ 7,503	\$753,223	\$765,284

PART I (Continued)

Item 1 (Continued)

(3) Loans (Continued)

The following table details impaired loan data as of September 30, 2018:

September 30, 2018

Unpaid Contractual Principal Balance	Impaired Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized	Interest Income Collected
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With No Related Allowance Recorded