CAPITAL CITY BANK GROUP INC
Form 10-Q
November 02, 2018

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

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

For the Quarterly Period Ended September 30, 2018

OR

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

For the transition period from ____________ to ____________

Commission File Number: 0-13358

(Exact name of registrant as specified in its charter)

Florida	**59-2273542**

(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
217 North Monroe Street, Tallahassee, Florida	**32301**
(Address of principal executive office)	(Zip Code)

(850) 402-7821
(Registrant's telephone number, including area code)

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

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

Large accelerated filer [ ]	Accelerated filer [X]	Non-accelerated filer [ ] (Do not check if 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 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]

At October 31, 2018, 17,058,521 shares of the Registrant's Common Stock, $.01 par value, were outstanding.

CAPITAL CITY BANK GROUP, INC.

QUARTERLY REPORT ON FORM 10-Q

FOR THE PERIOD ENDED SEPTEMBER 30, 2018

TABLE OF CONTENTS

INTRODUCTORY NOTE

Caution Concerning Forward-Looking Statements

This Quarterly Report on Form 10-Q contains “forward-looking statements” within the meaning of the Private Securities Litigation Reform Act of 1995. These forward-looking statements include, among others, statements about our beliefs, plans, objectives, goals, expectations, estimates and intentions that are subject to significant risks and uncertainties and are subject to change based on various factors, many of which are beyond our control. The words “may,” “could,” “should,” “would,” “believe,” “anticipate,” “estimate,” “expect,” “intend,” “plan,” “target,” “goal,” and similar expressions are identify forward-looking statements.

All forward-looking statements, by their nature, are subject to risks and uncertainties. Our actual future results may differ materially from those set forth in our forward-looking statements.

Our ability to achieve our financial objectives could be adversely affected by the factors discussed in detail in Part I, Item 2. “Management’s Discussion and Analysis of Financial Condition and Results of Operations” and Part II, Item 1A. “Risk Factors” in this Quarterly Report on Form 10-Q and the following sections of our Annual Report on Form 10-K for the year ended December 31, 2017 (the “2017 Form 10-K”): (a) “Introductory Note” in Part I, Item 1. “Business”; (b) “Risk Factors” in Part I, Item 1A, as updated in our subsequent quarterly reports filed on Form 10-Q; and (c) “Introduction” in “Management’s Discussion and Analysis of Financial Condition and Results of Operations,” in Part II, Item 7, as well as:

- our ability to successfully manage interest rate risk, liquidity risk, and other risks inherent to our industry;
- legislative or regulatory changes, the ability to repay and qualified mortgage standards;
- the effects of security breaches and computer viruses that may affect our computer systems or fraud related to debit card products;
- the accuracy of our financial statement estimates and assumptions, including the estimates used for our loan loss provision, deferred tax asset valuation and pension plan;
- the frequency and magnitude of foreclosure of our loans;
- the effects of our lack of a diversified loan portfolio, including the risks of geographic and industry concentrations;
- the strength of the United States economy in general and the strength of the local economies in which we conduct operations;
- our ability to declare and pay dividends, the payment of which is now subject to our compliance with heightened capital requirements;

- changes in the securities and real estate markets;
- changes in monetary and fiscal policies of the U.S. Government;
- inflation, interest rate, market and monetary fluctuations;
- the effects of harsh weather conditions, including hurricanes, and man-made disasters;
- our ability to comply with the extensive laws and regulations to which we are subject, including the laws for each jurisdiction where we operate;
- the willingness of clients to accept third-party products and services rather than our products and services and vice versa;
- increased competition and its effect on pricing;
- technological changes;
- negative publicity and the impact on our reputation;
- changes in consumer spending and saving habits;
- growth and profitability of our noninterest income;
- changes in accounting principles, policies, practices or guidelines;
- the limited trading activity of our common stock;
- the concentration of ownership of our common stock;
- anti-takeover provisions under federal and state law as well as our Articles of Incorporation and our Bylaws;
- other risks described from time to time in our filings with the Securities and Exchange Commission; and
- our ability to manage the risks involved in the foregoing.

However, other factors besides those listed in *Item 1A Risk Factors* or discussed in this Form 10-Q also could adversely affect our results, and you should not consider any such list of factors to be a complete set of all potential risks or uncertainties. Any forward-looking statements made by us or on our behalf speak only as of the date they are made. We do not undertake to update any forward-looking statement, except as required by applicable law.

PART I. FINANCIAL INFORMATION
Item 1.

CAPITAL CITY BANK GROUP, INC.
CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION

(Dollars in Thousands)	**(Unaudited) September 30, 2018**	**December 31, 2017**
ASSETS		
Cash and Due From Banks	$ 48,423	$ 58,419
Federal Funds Sold and Interest Bearing Deposits	26,839	227,023
Total Cash and Cash Equivalents	75,262	285,442
Investment Securities, Available for Sale, at fair value	484,243	480,911
Investment Securities, Held to Maturity, at amortized cost (fair value of $223,531 and $215,007)	227,923	216,679
Total Investment Securities	712,166	697,590
Loans Held For Sale	8,297	4,817
Loans, Net of Unearned Income	1,773,754	1,653,492
Allowance for Loan Losses	(14,219)	(13,307)
Loans, Net	1,759,535	1,640,185
Premises and Equipment, net	89,567	91,698
Goodwill	84,811	84,811
Other Real Estate Owned	2,720	3,941
Other Assets	86,832	90,310
Total Assets	$ 2,819,190	$ 2,898,794
LIABILITIES		
Deposits:		
Noninterest Bearing Deposits	$ 934,146	$ 874,583
Interest Bearing Deposits	1,447,070	1,595,294
Total Deposits	2,381,216	2,469,877
Short-Term Borrowings	16,644	7,480
Subordinated Notes Payable	52,887	52,887
Other Long-Term Borrowings	12,456	13,967
Other Liabilities	57,971	70,373
Total Liabilities	2,521,174	2,614,584
SHAREOWNERS' EQUITY		
Preferred Stock, $.01 par value; 3,000,000 shares authorized; no shares issued and outstanding	-	-
Common Stock, $.01 par value; 90,000,000 shares authorized; 17,058,521 and 16,988,951 shares	171	170

issued and outstanding at September 30, 2018 and December 31, 2017, respectively		
Additional Paid-In Capital	38,325	36,674
Retained Earnings	293,254	279,410
Accumulated Other Comprehensive Loss, net of tax	(33,734)	(32,044)
Total Shareowners’ Equity	298,016	284,210
Total Liabilities and Shareowners' Equity	$ 2,819,190	$ 2,898,794

The accompanying Notes to Consolidated Financial Statements are an integral part of these statements.

CAPITAL CITY BANK GROUP, INC.
CONSOLIDATED STATEMENTS OF INCOME
(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
(Dollars in Thousands, Except Per Share Data)	**2018**	**2017**	**2018**	**2017**
INTEREST INCOME				
Loans, including Fees	$ 21,618	$ 19,479	$ 61,686	$ 56,204
Investment Securities:				
Taxable	3,290	2,150	8,757	5,832
Tax Exempt	182	266	633	795
Federal Funds Sold and Interest Bearing Deposits	302	446	1,949	1,472
Total Interest Income	25,392	22,341	73,025	64,303
INTEREST EXPENSE				
Deposits	1,068	530	2,931	1,199
Short-Term Borrowings	41	15	57	77
Subordinated Notes Payable	568	420	1,595	1,203
Other Long-Term Borrowings	92	115	286	331
Total Interest Expense	1,769	1,080	4,869	2,810
NET INTEREST INCOME	23,623	21,261	68,156	61,493
Provision for Loan Losses	904	490	2,464	1,389
Net Interest Income After Provision For Loan Losses	22,719	20,771	65,692	60,104
NONINTEREST INCOME				
Deposit Fees	5,207	5,153	14,921	15,295
Bank Card Fees	2,828	2,688	8,548	8,361
Wealth Management Fees	2,181	2,197	6,391	6,112
Mortgage Banking Fees	1,343	1,480	3,606	4,344
Other	1,749	1,478	4,861	4,737
Total Noninterest Income	13,308	12,996	38,327	38,849
NONINTEREST EXPENSE				
Compensation	15,891	15,711	47,599	47,211
Occupancy, net	4,645	4,501	13,699	13,437
Other Real Estate Owned, net	347	(118)	1,221	780
Other	7,816	6,613	22,479	21,122
Total Noninterest Expense	28,699	26,707	84,998	82,550
INCOME BEFORE INCOME TAXES	7,328	7,060	19,021	16,403
Income Tax Expense	1,338	2,505	1,255	5,543
NET INCOME	**$ 5,990**	**$ 4,555**	**$ 17,766**	**$ 10,860**

BASIC NET INCOME PER SHARE	**$ 0.35**	**$ 0.27**	**$ 1.04**	**$ 0.64**
DILUTED NET INCOME PER SHARE	**$ 0.35**	**$ 0.27**	**$ 1.04**	**$ 0.64**
Average Common Basic Shares Outstanding	17,056	16,965	17,043	16,946
Average Common Diluted Shares Outstanding	17,125	17,044	17,102	17,009

The accompanying Notes to Consolidated Financial Statements are an integral part of these statements.

CAPITAL CITY BANK GROUP, INC.
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
(Dollars in Thousands)	**2018**	**2017**	**2018**	**2017**
NET INCOME	$ 5,990	$ 4,555	$ 17,766	$ 10,860
Other comprehensive income, before tax:				
Change in net unrealized gain/loss on securities available for sale	(553)	(99)	(2,306)	516
Amortization of unrealized losses on securities transferred from available for sale to held to maturity	13	19	42	57
Total Investment Securities	(540)	(80)	(2,264)	573
Other comprehensive (loss) income, before tax	(540)	(80)	(2,264)	573
Deferred tax (benefit) expense related to other comprehensive income	(137)	(31)	(574)	222
Other comprehensive (loss) income, net of tax	(403)	(49)	(1,690)	351
TOTAL COMPREHENSIVE INCOME	$ 5,587	$ 4,506	$ 16,076	$ 11,211

The accompanying Notes to Consolidated Financial Statements are an integral part of these statements.

CAPITAL CITY BANK GROUP, INC.
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREOWNERS' EQUITY
(Unaudited)

(Dollars In Thousands, Except Share Data)	**Shares Outstanding**	**Common Stock**	**Additional Paid-In Capital**	**Retained Earnings**	**Accumulated Other Comprehensive Loss, Net of Taxes**	**Total**
Balance, January 1, 2017	16,844,698	$ 168	$ 34,188	$ 267,037	$ (26,225)	$ 275,168
Net Income	-	-	-	10,860	-	10,860
Other Comprehensive Income, net of tax	-	-	-	-	351	351
Cash Dividends ($0.1700 per share)	-	-	-	(2,884)	-	(2,884)
Stock Based Compensation	-	-	1,196	-	-	1,196
Impact of Transactions Under Compensation Plans, net	121,349	2	508	-	-	510
Balance, September 30, 2017	16,966,047	$ 170	$ 35,892	$ 275,013	$ (25,874)	$ 285,201
Balance, January 1, 2018	16,988,951	$ 170	$ 36,674	$ 279,410	$ (32,044)	$ 284,210
Net Income	-	-	-	17,766	-	17,766
Other Comprehensive Loss, net of tax	-	-	-	-	(1,690)	(1,690)
Cash Dividends ($0.2300 per share)	-	-	-	(3,922)	-	(3,922)
Stock Based Compensation	-	-	978	-	-	978
Impact of Transactions Under Compensation Plans, net	69,570	1	673	-	-	674
Balance, September 30, 2018	17,058,521	$ 171	$ 38,325	$ 293,254	$ (33,734)	$ 298,016

The accompanying Notes to Consolidated Financial Statements are an integral part of these statements.

CAPITAL CITY BANK GROUP, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	Nine Months Ended September 30,	
(Dollars in Thousands)	**2018**	**2017**
CASH FLOWS FROM OPERATING ACTIVITIES		
Net Income	$ 17,766	$ 10,860
Adjustments to Reconcile Net Income to		
Cash Provided by Operating Activities:		
Provision for Loan Losses	2,464	1,389
Depreciation	4,845	4,966
Amortization of Premiums, Discounts, and Fees, net	5,253	4,928
Net (Increase) Decrease in Loans Held-for-Sale	(3,480)	3,086
Stock Compensation	978	1,196
Net Tax Benefit From Stock-Based Compensation	(41)	(223)
Deferred Income Taxes	1,847	247
Net Loss on Sales and Write-Downs of Other Real Estate Owned	941	456
Loss on Disposal of Premises and Equipment	57	276
Net Decrease in Other Assets	3,040	2,559
Net (Decrease) Increase in Other Liabilities	(12,208)	6,487
Net Cash Provided By Operating Activities	21,462	36,227
CASH FLOWS FROM INVESTING ACTIVITIES		
Securities Held to Maturity:		
Purchases	(102,428)	(60,703)
Payments, Maturities, and Calls	89,932	53,031
Securities Available for Sale:		
Purchases	(129,502)	(122,949)
Payments, Maturities, and Calls	119,092	130,997
Purchases of Loans Held for Investment	(25,048)	(44,083)
Net Increase in Loans	(98,007)	(27,327)
Proceeds From Sales of Other Real Estate Owned	1,540	5,952
Purchases of Premises and Equipment	(2,771)	(3,052)
Net Cash Used In Investing Activities	(147,192)	(68,134)
CASH FLOWS FROM FINANCING ACTIVITIES		
Net Decrease in Deposits	(88,661)	(64,669)
Net Increase (Decrease) in Short-Term Borrowings	9,164	(3,020)
Repayment of Other Long-Term Borrowings	(1,511)	(2,786)
Dividends Paid	(3,922)	(2,884)
Issuance of Common Stock Under Compensation Plans	480	333
Net Cash Used In Financing Activities	(84,450)	(73,026)
NET DECREASE IN CASH AND CASH EQUIVALENTS	(210,180)	(104,933)
Cash and Cash Equivalents at Beginning of Period	285,442	296,047
Cash and Cash Equivalents at End of Period	$ 75,262	$ 191,114

Supplemental Cash Flow Disclosures:		
Interest Paid	$ 4,837	$ 2,825
Income Taxes Paid	$ 151	$ 4,044
Noncash Investing and Financing Activities:		
Loans Transferred to Other Real Estate Owned	$ 1,260	$ 2,024

The accompanying Notes to Consolidated Financial Statements are an integral part of these statements.

CAPITAL CITY BANK GROUP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES

Nature of Operations. Capital City Bank Group, Inc. ("CCBG" or the "Company") provides a full range of banking and banking-related services to individual and corporate clients through its subsidiary, Capital City Bank, with banking offices located in Florida, Georgia, and Alabama. The Company is subject to competition from other financial institutions, is subject to regulation by certain government agencies and undergoes periodic examinations by those regulatory authorities.

Basis of Presentation. The consolidated financial statements in this Quarterly Report on Form 10-Q include the accounts of CCBG and its wholly-owned subsidiary, Capital City Bank ("CCB" or the "Bank"). All material inter-company transactions and accounts have been eliminated. Certain previously reported amounts have been reclassified to conform to the current year's presentation.

The accompanying unaudited consolidated financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included.

The consolidated statement of financial condition at December 31, 2017 has been derived from the audited consolidated financial statements at that date, but does not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. For further information, refer to the consolidated financial statements and footnotes thereto included in the Company's annual report on Form 10-K for the year ended December 31, 2017.

Income Taxes. For the first nine months of 2018, the Company realized income tax expense of $1.3 million, which reflected three discrete tax benefit items totaling $3.3 million resulting from the effect of federal tax reform, enacted in December 2017, specifically related to pension plan contributions made in 2018 for the plan year 2017. The discrete tax items for 2018 totaled $1.5 million for the first quarter, $1.4 million for the second quarter and $0.4 million for the third quarter. Absent these discrete items, the Company's effective tax rate was approximately 24%.

Accounting Changes

Revenue Recognition. Accounting Standards Codification ("ASC") 606, Revenue from Contracts with Customers ("ASC 606"), establishes principles for reporting information about the nature, amount, timing and uncertainty of revenue and cash flows arising from the entity's contracts to provide goods or services to customers. The core principle requires an entity to recognize revenue to depict the transfer of goods or services to customers in an amount that reflects the consideration that it expects to be entitled to receive in exchange for those goods or services recognized as performance obligations are satisfied.

The majority of the Company’s revenue-generating transactions are not subject to ASC 606, including revenue generated from financial instruments, such as our loans, letters of credit, and investment securities, and revenue related to the sale of residential mortgages in the secondary market, as these activities are subject to other GAAP discussed elsewhere within our disclosures. Descriptions of the major revenue-generating activities that are within the scope of ASC 606, which are presented in the accompanying statements of income as components of non-interest income are as follows:

Deposit Fees - these represent general service fees for monthly account maintenance and activity- or transaction-based fees and consist of transaction-based revenue, time-based revenue (service period), item-based revenue or some other individual attribute-based revenue. Revenue is recognized when the Company’s performance obligation is completed which is generally monthly for account maintenance services or when a transaction has been completed. Payment for such performance obligations are generally received at the time the performance obligations are satisfied.

Wealth Management - trust fees and retail brokerage fees – trust fees represent monthly fees due from wealth management clients as consideration for managing the client’s assets. Trust services include custody of assets, investment management, fees for trust services and similar fiduciary activities. Revenue is recognized when the Company’s performance obligation is completed each month or quarter, which is the time that payment is received. Also, retail brokerage fees are received from a third party broker-dealer, for which the Company acts as an agent, as part of a revenue-sharing agreement for fees earned from customers that are referred to the third party. These fees are for transactional and advisory services and are paid by the third party on a monthly basis and recognized ratably throughout the quarter as the Company’s performance obligation is satisfied.

Bank Card Fees – bank card related fees primarily includes interchange income from client use of consumer and business debit cards. Interchange income is a fee paid by a merchant bank to the card-issuing bank through the interchange network. Interchange fees are set by the credit card associations and are based on cardholder purchase volumes. The Company records interchange income as transactions occur.

Gains and Losses from the Sale of Bank Owned Property – the performance obligation in the sale of other real estate owned typically will be the delivery of control over the property to the buyer. If the Company is not providing the financing of the sale, the transaction price is typically identified in the purchase and sale agreement. However, if the Company provides seller financing, the Company must determine a transaction price, depending on if the sale contract is at market terms and taking into account the credit risk inherent in the arrangement.

Other non-interest income primarily includes items such as mortgage banking fees (gains from the sale of residential mortgage loans held for sale), bank-owned life insurance, and safe deposit box fees none of which are subject to the requirements of ASC 606.

The Company has made no significant judgments in applying the revenue guidance prescribed in ASC 606 that affects the determination of the amount and timing of revenue from the above-described contracts with clients.

The Company has applied ASC 606 using the modified retrospective approach effective on January 1, 2018 to all existing contracts with clients covered under the scope of the standard. The Company did not have an aggregate effect of modification resulting from adoption of ASC 606, and no financial statement line items were affected by this change in accounting standard.

Equity Securities. Beginning January 1, 2018, upon adoption of ASU 2016-01, equity securities with readily determinable fair values are stated at fair value with realized and unrealized gains and losses reported in income. For periods prior to January 1, 2018, equity securities were classified as available-for-sale and stated at fair value with unrealized gains and losses reported as a separate component of AOCI, net of tax. Equity securities without readily determinable fair values are recorded at cost less any impairment, if any. Upon adoption, the Company reclassified one security in the amount of $0.8 million to other assets in accordance with this accounting standard.

Employee Benefit Plans. Accounting Standards Update ("ASU") 2017-07, Compensation – Retirement Benefits (Topic 715) requires that an employer report the service cost component in the same line item or items as other compensation costs arising from services rendered by the pertinent employees during the period. The other components of net benefit cost are required to be presented in the income statement separately from the service cost component and outside a subtotal of income from operations, if one is presented. If a separate line item or items are used to present the other components of net benefit cost, that line item or items must be appropriately described. If a separate line item or items are not used, the line item or items used in the income statement to present the other components of net benefit cost must be disclosed. In accordance with this accounting standard, the Company reclassified the non-service cost components of its net periodic benefit cost to other noninterest expense in the accompanying statements of income (See Note 5 – Employee Benefit Plans). Prior year amounts were retrospectively adjusted in accordance with the accounting standard. The effects on the statements of income were as follows:

Period Presented	Line Item	
(Dollars in Thousands)	Compensation	Other Expense
Three Months Ended September 30, 2018	($457)	$457
Three Months Ended September 30, 2017	($638)	$638
Nine Months Ended September 30, 2018	($1,371)	$1,371
Nine Months Ended September 30, 2017	($1,926)	$1,926

NOTE 2 – INVESTMENT SECURITIES

Investment Portfolio Composition. The amortized cost and related market value of investment securities available-for-sale and
held-to-maturity were as follows:

	September 30, 2018				December 31, 2017			
	Amortized Cost	Unrealized Gains	Unrealized Losses	Market Value	Amortized Cost	Unrealized Gain	Unrealized Losses	Market Value
Available for Sale								
U.S. Government Treasury	$272,335	$ -	$ 4,222	$268,113	$237,505	$ -	$ 2,164	$235,341
U.S. Government Agency	153,087	625	621	153,091	144,324	727	407	144,644
States and Political Subdivisions	54,115	-	276	53,839	91,533	2	378	91,157
Mortgage-Backed Securities	922	50	-	972	1,102	83	-	1,185
Equity Securities(1)	8,228	-	-	8,228	8,584	-	-	8,584
Total	$488,687	$ 675	$ 5,119	$484,243	$483,048	$ 812	$ 2,949	$480,911
Held to Maturity								
U.S. Government Treasury	$ 35,103	$ -	$ 702	$ 34,401	$ 98,256	$ -	$ 441	$ 97,815
States and Political Subdivisions	6,566	-	45	6,521	6,996	-	41	6,955
Mortgage-Backed Securities	186,254	207	3,852	182,609	111,427	22	1,212	110,237
Total	$227,923	$ 207	$ 4,599	$223,531	$216,679	$ 22	$ 1,694	$215,007
Total Investment Securities	$716,610	$ 882	$ 9,718	$707,774	$699,727	$ 834	$ 4,643	$695,918

(1) *Includes Federal Home Loan Bank and Federal Reserve Bank stock, recorded at cost of $3.4 million, $4.8 million, respectively, at September 30, 2018 and includes Federal Home Loan Bank, Federal Reserve Bank and FNBB Inc. stock recorded at cost of $3.1 million, $4.8 million, and $0.8 million, respectively, at December 31, 2017. The FNBB, Inc. equity investment was reclassified to other assets at March 31, 2018 in accordance with ASU 2016-01, which was adopted prospectively as allowed by the standard.*

Securities with an amortized cost of $234.5 million and $328.1 million at September 30, 2018 and December 31, 2017, respectively, were pledged to secure public deposits and for other purposes.

The Bank, as a member of the Federal Home Loan Bank of Atlanta ("FHLB"), is required to own capital stock in the FHLB based generally upon the balances of residential and commercial real estate loans, and FHLB advances. FHLB stock which is included in equity securities is pledged to secure FHLB advances. No ready market exists for this stock, and it has no quoted market value; however, redemption of this stock has historically been at par value.

As a member of the Federal Reserve Bank of Atlanta, the Bank is required to maintain stock in the Federal Reserve Bank of Atlanta based on a specified ratio relative to the Bank's capital. Federal Reserve Bank stock is carried at cost.

Maturity Distribution. At September 30, 2018, the Company's investment securities had the following maturity distribution based on contractual maturity. Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations. Mortgage-backed securities and certain amortizing U.S. government agency securities are shown separately because they are not due at a certain maturity date.

	Available for Sale		Held to Maturity	
(Dollars in Thousands)	**Amortized Cost**	**Market Value**	**Amortized Cost**	**Market Value**
Due in one year or less	$ 120,134	$ 119,269	$ 13,099	$ 12,963
Due after one year through five years	232,224	228,353	28,570	27,959
Mortgage-Backed Securities	922	972	186,254	182,609
U.S. Government Agency	127,179	127,421	-	-
Equity Securities	8,228	8,228	-	-
Total	$ 488,687	$ 484,243	$ 227,923	$ 223,531

Unrealized Losses on Investment Securities. The following table summarizes the investment securities with unrealized losses aggregated by major security type and length of time in a continuous unrealized loss position:

	Less Than 12 Months		Greater Than 12 Months		Total	
(Dollars in Thousands)	**Market Value**	**Unrealized Losses**	**Market Value**	**Unrealized Losses**	**Market Value**	**Unrealized Losses**
September 30, 2018						
Available for Sale						
U.S. Government Treasury	$ 92,259	$ 1,005	$ 175,854	$ 3,217	$268,113	$ 4,222
U.S. Government Agency	63,475	351	29,223	270	92,698	621
States and Political Subdivisions	34,928	164	14,831	112	49,759	276
Mortgage-Backed Securities	10	-	2	-	12	-
Total	190,672	1,520	219,910	3,599	410,582	5,119
Held to Maturity						
U.S. Government Treasury	4,900	112	29,501	590	34,401	702
States and Political Subdivisions	6,026	38	495	7	6,521	45
Mortgage-Backed Securities	90,516	1,498	55,089	2,354	145,605	3,852
Total	$ 101,442	$ 1,648	$ 85,085	$ 2,951	$186,527	$ 4,599
December 31, 2017						
Available for Sale						
U.S. Government Treasury	$ 155,443	$ 963	$ 79,900	$ 1,201	$235,343	$ 2,164
U.S. Government Agency	45,737	150	25,757	257	71,494	407
States and Political Subdivisions	82,999	320	5,549	58	88,548	378
Mortgage-Backed Securities	2	-	-	-	2	-
Total	284,181	1,433	111,206	1,516	395,387	2,949
Held to Maturity						
U.S. Government Treasury	77,861	298	14,939	143	92,800	441
States and Political Subdivisions	6,955	41	-	-	6,955	41
Mortgage-Backed Securities	56,030	469	30,216	743	86,246	1,212
Total	$ 140,846	$ 808	$ 45,155	$ 886	$186,001	$ 1,694

Management evaluates securities for other than temporary impairment at least quarterly, and more frequently when economic or market concerns warrant such evaluation. Declines in the fair value of available-for-sale ("AFS") and held-to-maturity ("HTM") securities below their cost that are deemed to be other than temporary are reflected in earnings as realized losses. In estimating other-than-temporary impairment losses, the Company considers, (i) whether it has decided to sell the security, (ii) whether it is more likely than not that the Company will have to sell the security before its market value recovers, and (iii) whether the present value of expected cash flows is sufficient to recover the entire amortized cost basis. When assessing a security's expected cash flows, the Company considers, among other things, (i) the length of time and the extent to which the fair value has been less than cost and (ii) the financial condition and near-term prospects of the issuer. In analyzing an issuer's financial condition, management considers whether the securities are issued by the federal government or its agencies, whether downgrades by rating agencies have occurred, regulatory issues, and analysts' reports.

At September 30, 2018, there were 541 positions (combined AFS and HTM) with unrealized losses totaling $9.7 million, of which 63 of these positions were U.S. government treasury securities guaranteed by the U.S. government and 309 of these positions were U.S. government agency and mortgage-backed securities issued by U.S. government sponsored entities, with the remaining 169 positions being municipal securities. Because the declines in the market value of these securities are attributable to changes in interest rates and not credit quality, and because the Company has the present ability and intent to hold these investments until there is a recovery in fair value, which may be at maturity, the Company does not consider these investments to be other-than-temporarily impaired at September 30, 2018.

NOTE 3 – LOANS, NET

Loan Portfolio Composition. The composition of the loan portfolio was as follows:

(Dollars in Thousands)	**September 30, 2018**	**December 31, 2017**
Commercial, Financial and Agricultural	$ 239,044	$ 218,166
Real Estate – Construction	87,672	77,966
Real Estate – Commercial Mortgage	596,391	535,707
Real Estate – Residential[1]	342,063	311,906
Real Estate – Home Equity	212,942	229,513
Consumer[2]	295,642	280,234
Loans, Net of Unearned Income	$ 1,773,754	$ 1,653,492

(1) *Includes loans in process with outstanding balances of $10.1 million and $9.1 million at September 30, 2018 and December 31, 2017, respectively.*

(2) *Includes overdraft balances of $1.6 million and $1.6 million at September 30, 2018 and December 31, 2017, respectively.*

Net deferred costs included in loans were $1.6 million at September 30, 2018 and $1.5 million at December 31, 2017.

The Company has pledged a blanket floating lien on all 1-4 family residential mortgage loans, commercial real estate mortgage loans, and home equity loans to support available borrowing capacity at the FHLB and has pledged a blanket floating lien on all consumer loans, commercial loans, and construction loans to support available borrowing capacity at the Federal Reserve Bank of Atlanta.

Nonaccrual Loans. Loans are generally placed on nonaccrual status if principal or interest payments become 90 days past due and/or management deems the collectability of the principal and/or interest to be doubtful. Loans are returned to accrual status when the principal and interest amounts contractually due are brought current or when future payments are reasonably assured.

The following table presents the recorded investment in nonaccrual loans and loans past due over 90 days and still on accrual by class of loans.

	September 30, 2018		December 31, 2017	
(Dollars in Thousands)	**Nonaccrual**	**90 + Days**	**Nonaccrual**	**90 + Days**
Commercial, Financial and Agricultural	$ 338	$ -	$ 629	$ -
Real Estate – Construction	1,098	-	297	-
Real Estate – Commercial Mortgage	2,316	126	2,370	-
Real Estate – Residential	2,140	-	1,938	-
Real Estate – Home Equity	902	-	1,748	-
Consumer	73	-	177	36
Total Nonaccrual Loans	$ 6,867	$ 126	$ 7,159	$ 36

Loan Portfolio Aging. A loan is defined as a past due loan when one full payment is past due or a contractual maturity is over 30 days past due ("DPD").

The following table presents the aging of the recorded investment in accruing past due loans by class of loans.

(Dollars in Thousands)	**30-59 DPD**	**60-89 DPD**	**90 + DPD**	**Total Past Due**	**Total Current**	**Total Loans[1]**
September 30, 2018						
Commercial, Financial and Agricultural	$ 71	$ 65	$ -	$ 136	$ 238,570	$ 239,044
Real Estate – Construction	-	-	-	-	86,574	87,672
Real Estate – Commercial Mortgage	280	176	126	582	593,493	596,391
Real Estate – Residential	613	727	-	1,340	338,583	342,063
Real Estate – Home Equity	354	76	-	430	211,610	212,942
Consumer	1,059	263	-	1,322	294,247	295,642
Total Past Due Loans	$ 2,377	$ 1,307	$ 126	$ 3,810	$ 1,763,077	$ 1,773,754
December 31, 2017						
Commercial, Financial and Agricultural	$ 87	$ 55	$ -	$ 142	$ 217,395	$ 218,166
Real Estate – Construction	811	-	-	811	76,858	77,966
Real Estate – Commercial Mortgage	437	195	-	632	532,705	535,707
Real Estate – Residential	701	446	-	1,147	308,821	311,906
Real Estate – Home Equity	80	2	-	82	227,683	229,513
Consumer	1,316	413	36	1,765	278,292	280,234
Total Past Due Loans	$ 3,432	$ 1,111	$ 36	$ 4,579	$ 1,641,754	$ 1,653,492

[1] Total Loans include nonaccrual loans

Allowance for Loan Losses. The allowance for loan losses is a reserve established through a provision for loan losses charged to expense, which represents management's best estimate of incurred losses within the existing portfolio of loans. Loans are charged-off to the allowance when losses are deemed to be probable and reasonably quantifiable.

The following table details the activity in the allowance for loan losses by portfolio class. Allocation of a portion of the allowance to one category of loans does not preclude its availability to absorb losses in other categories.

(Dollars in Thousands)	Commercial, Financial, Agricultural	Real Estate Construction	Real Estate Commercial Mortgage	Real Estate Residential	Real Estate Home Equity	Consumer	Total
Three Months Ended September 30, 2018							
Beginning Balance	$ 1,214	$ 283	$ 4,432	$ 3,146	$ 2,294	$ 2,194	$ 13,563
Provision for Loan Losses	388	86	(30)	50	120	290	904
Charge-Offs	(268)	-	(25)	(106)	(112)	(463)	(974)
Recoveries	78	-	222	107	47	272	726
Net Charge-Offs	(190)	-	197	1	(65)	(191)	(248)
Ending Balance	$ 1,412	$ 369	$ 4,599	$ 3,197	$ 2,349	$ 2,293	$ 14,219
Nine Months Ended September 30, 2018							
Beginning Balance	$ 1,191	$ 122	$ 4,346	$ 3,206	$ 2,506	$ 1,936	$ 13,307
Provision for Loan Losses	481	253	208	123	140	1,259	2,464
Charge-Offs	(591)	(7)	(315)	(669)	(427)	(1,667)	(3,676)
Recoveries	331	1	360	537	130	765	2,124
Net Charge-Offs	(260)	(6)	45	(132)	(297)	(902)	(1,552)
Ending Balance	$ 1,412	$ 369	$ 4,599	$ 3,197	$ 2,349	$ 2,293	$ 14,219
Three Months Ended September 30, 2017							
Beginning Balance	$ 1,095	$ 114	$ 3,825	$ 3,384	$ 2,524	$ 2,300	$ 13,242
Provision for Loan Losses	208	(26)	286	(32)	(103)	157	490
Charge-Offs	(276)	-	(94)	(125)	(50)	(455)	(1,000)
Recoveries	79	50	69	60	84	265	607
Net Charge-Offs	(197)	50	(25)	(65)	34	(190)	(393)
Ending Balance	$ 1,106	$ 138	$ 4,086	$ 3,287	$ 2,455	$ 2,267	$ 13,339
Nine Months Ended September 30, 2017							
Beginning Balance	$ 1,198	$ 168	$ 4,315	$ 3,445	$ 2,297	$ 2,008	$ 13,431
Provision for Loan Losses	401	(80)	264	(348)	148	1,004	1,389
Charge-Offs	(693)	-	(643)	(285)	(142)	(1,616)	(3,379)
Recoveries	200	50	150	475	152	871	1,898
Net Charge-Offs	(493)	50	(493)	190	10	(745)	(1,481)
Ending Balance	$ 1,106	$ 138	$ 4,086	$ 3,287	$ 2,455	$ 2,267	$ 13,339

15

The following table details the amount of the allowance for loan losses by portfolio class disaggregated on the basis of the Company's impairment methodology.

(Dollars in Thousands	Commercial, Financial, Agricultural	Real Estate Construction	Real Estate Commercial Mortgage	Real Estate Residential	Real Estate Home Equity	Consumer	Total
September 30, 2018							
Period-end amount Allocated to:							
Loans Individually Evaluated for Impairment	$ 185	$ 181	$ 1,719	$ 954	$ 357	$ 1	$ 3,397
Loans Collectively Evaluated for Impairment	1,227	188	2,880	2,243	1,992	2,292	10,822
Ending Balance	$ 1,412	$ 369	$ 4,599	$ 3,197	$ 2,349	$ 2,293	$ 14,219
December 31, 2017							
Period-end amount Allocated to:							
Loans Individually Evaluated for Impairment	$ 215	$ 1	$ 2,165	$ 1,220	$ 515	$ 1	$ 4,117
Loans Collectively Evaluated for Impairment	976	121	2,181	1,986	1,991	1,935	9,190
Ending Balance	$ 1,191	$ 122	$ 4,346	$ 3,206	$ 2,506	$ 1,936	$ 13,307
September 30, 2017							
Period-end amount Allocated to:							
Loans Individually Evaluated for Impairment	$ 88	$ 24	$ 1,846	$ 1,196	$ 454	$ 3	$ 3,611
Loans Collectively Evaluated for Impairment	1,018	114	2,240	2,091	2,001	2,264	9,728
Ending Balance	$ 1,106	$ 138	$ 4,086	$ 3,287	$ 2,455	$ 2,267	$ 13,339

The Company's recorded investment in loans related to each balance in the allowance for loan losses by portfolio class and disaggregated on the basis of the Company's impairment methodology was as follows:

(Dollars in Thousands)	**Commercial, Financial, Agricultural**	**Real Estate Construction**	**Real Estate Commercial Mortgage**	**Real Estate Residential**	**Real Estate Home Equity**	**Consumer**	**Total**
September 30, 2018							
Individually Evaluated for Impairment	$ 987	$ 1,159	$ 18,572	$ 11,369	$ 2,241	$ 90	$ 34,418
Collectively Evaluated for Impairment	238,057	86,513	577,819	330,694	210,701	295,552	1,739,336
Total	$ 239,044	$ 87,672	$ 596,391	$ 342,063	$ 212,942	$ 295,642	$1,773,754
December 31, 2017							
Individually Evaluated for Impairment	$ 1,378	$ 361	$ 19,280	$ 12,871	$ 3,332	$ 113	$ 37,335
Collectively Evaluated for Impairment	216,788	77,605	516,427	299,035	226,181	280,121	1,616,157
Total	$ 218,166	$ 77,966	$ 535,707	$ 311,906	$ 229,513	$ 280,234	$1,653,492
September 30, 2017							
Individually Evaluated for Impairment	$ 847	$ 363	$ 20,716	$ 13,258	$ 2,915	$ 132	$ 38,231
Collectively Evaluated for Impairment	215,116	67,450	506,615	302,325	225,584	275,017	1,592,107
Total	$ 215,963	$ 67,813	$ 527,331	$ 315,583	$ 228,499	$ 275,149	$1,630,338

Impaired Loans. Loans are deemed to be impaired when, based on current information and events, it is probable that the Company will not be able to collect all amounts due (principal and interest payments), according to the contractual terms of the loan agreement. Loans, for which the terms have been modified, and for which the borrower is experiencing financial difficulties, are considered troubled debt restructurings and classified as impaired.

The following table presents loans individually evaluated for impairment by class of loans.

(Dollars in Thousands)	Unpaid Principal Balance	Recorded Investment With No Allowance	Recorded Investment With Allowance	Related Allowance
September 30, 2018				
Commercial, Financial and Agricultural	$ 987	$ 105	$ 882	$ 185
Real Estate – Construction	1,159	61	1,098	181
Real Estate – Commercial Mortgage	18,572	2,071	16,501	1,719
Real Estate – Residential	11,369	1,914	9,455	954
Real Estate – Home Equity	2,241	719	1,522	357
Consumer	90	51	39	1
Total	$ 34,418	$ 4,921	$ 29,497	$ 3,397
December 31, 2017				
Commercial, Financial and Agricultural	$ 1,378	$ 118	$ 1,260	$ 215
Real Estate – Construction	361	297	64	1
Real Estate – Commercial Mortgage	19,280	1,763	17,517	2,165
Real Estate – Residential	12,871	1,516	11,355	1,220
Real Estate – Home Equity	3,332	1,157	2,175	515
Consumer	113	45	68	1
Total	$ 37,335	$ 4,896	$ 32,439	$ 4,117

The following table summarizes the average recorded investment and interest income recognized by class of impaired loans.

	Three Months Ended September 30,				Nine Months Ended September 30,			
	2018		2017		2018		2017	
(Dollars in Thousands)	Average Recorded Investment	Total Interest Income	Average Recorded Investment	Total Interest Income	Average Recorded Investment	Total Interest Income	Average Recorded Investment	Total Interest Income
Commercial, Financial and Agricultural	$ 1,040	$ 19	$ 963	$ 12	$ 1,185	$ 69	$ 1,051	$ 35
Real Estate – Construction	915	2	363	-	716	3	334	2
Real Estate – Commercial Mortgage	18,470	167	21,109	219	18,666	511	22,283	662
Real Estate – Residential	11,393	133	14,068	162	12,215	417	14,608	516
Real Estate – Home Equity	2,415	23	3,114	28	2,840	74	3,280	81
Consumer	92	2	136	2	102	6	148	6
Total	$ 34,325	$ 346	$ 39,753	$ 423	$ 35,724	$ 1,080	$ 41,704	$ 1,302

Credit Risk Management. The Company has adopted comprehensive lending policies, underwriting standards and loan review procedures designed to maximize loan income within an acceptable level of risk. Management and the Board of Directors review and approve these policies and procedures on a regular basis (at least annually).

Reporting systems are used to monitor loan originations, loan quality, concentrations of credit, loan delinquencies and nonperforming loans and potential problem loans. Management and the Credit Risk Oversight Committee periodically review our lines of business to monitor asset quality trends and the appropriateness of credit policies. In addition, total borrower exposure limits are established and concentration risk is monitored. As part of this process, the overall composition of the portfolio is reviewed to gauge diversification of risk, client concentrations, industry group, loan type, geographic area, or other relevant classifications of loans. Specific segments of the loan portfolio are monitored and reported to the Board on a quarterly basis and have strategic plans in place to supplement Board approved credit policies governing exposure limits and underwriting standards. Detailed below are the types of loans within the Company's loan portfolio and risk characteristics unique to each.

Commercial, Financial, and Agricultural – Loans in this category are primarily made based on identified cash flows of the borrower with consideration given to underlying collateral and personal or other guarantees. Lending policy establishes debt service coverage ratio limits that require a borrower's cash flow to be sufficient to cover principal and interest payments on all new and existing debt. The majority of these loans are secured by the assets being financed or other business assets such as accounts receivable, inventory, or equipment. Collateral values are determined based upon third party appraisals and evaluations. Loan to value ratios at origination are governed by established policy guidelines.

Real Estate Construction – Loans in this category consist of short-term construction loans, revolving and non-revolving credit lines and construction/permanent loans made to individuals and investors to finance the acquisition, development, construction or rehabilitation of real property. These loans are primarily made based on identified cash flows of the borrower or project and generally secured by the property being financed, including 1-4 family residential properties and commercial properties that are either owner-occupied or investment in nature. These properties may include either vacant or improved property. Construction loans are generally based upon estimates of costs and value associated with the completed project. Collateral values are determined based upon third party appraisals and evaluations. Loan to value ratios at origination are governed by established policy guidelines. The disbursement of funds for construction loans is made in relation to the progress of the project and as such these loans are closely monitored by on-site inspections.

Real Estate Commercial Mortgage – Loans in this category consists of commercial mortgage loans secured by property that is either owner-occupied or investment in nature. These loans are primarily made based on identified cash flows of the borrower or project with consideration given to underlying real estate collateral and personal guarantees. Lending policy establishes debt service coverage ratios and loan to value ratios specific to the property type. Collateral values are determined based upon third party appraisals and evaluations.

Real Estate Residential – Residential mortgage loans held in the Company's loan portfolio are made to borrowers that demonstrate the ability to make scheduled payments with full consideration to underwriting factors such as current income, employment status, current assets, and other financial resources, credit history, and the value of the collateral. Collateral consists of mortgage liens on 1-4 family residential properties. Collateral values are determined based upon third party appraisals and evaluations. The Company does not originate sub-prime loans.

Real Estate Home Equity – Home equity loans and lines are made to qualified individuals for legitimate purposes generally secured by senior or junior mortgage liens on owner-occupied 1-4 family homes or vacation homes. Borrower qualifications include favorable credit history combined with supportive income and debt ratio requirements and combined loan to value ratios within established policy guidelines. Collateral values are determined based upon third party appraisals and evaluations.

Consumer Loans – This loan portfolio includes personal installment loans, direct and indirect automobile financing, and overdraft lines of credit. The majority of the consumer loan portfolio consists of indirect and direct automobile loans. Lending policy establishes maximum debt to income ratios, minimum credit scores, and includes guidelines for verification of applicants' income and receipt of credit reports.

Credit Quality Indicators. As part of the ongoing monitoring of the Company's loan portfolio quality, management categorizes loans into risk categories based on relevant information about the ability of borrowers to service their debt such as: current financial information, historical payment performance, credit documentation, and current economic/market trends, among other factors. Risk ratings are assigned to each loan and revised as needed through established monitoring procedures for individual loan relationships over a predetermined amount and review of smaller balance homogenous loan pools. The Company uses the definitions noted below for categorizing and managing its criticized loans. Loans categorized as "Pass" do not meet the criteria set forth for the Special Mention, Substandard, or Doubtful categories and are not considered criticized.

Special Mention – Loans in this category are presently protected from loss, but weaknesses are apparent which, if not corrected, could cause future problems. Loans in this category may not meet required underwriting criteria and have no mitigating factors. More than the ordinary amount of attention is warranted for these loans.

Substandard – Loans in this category exhibit well-defined weaknesses that would typically bring normal repayment into jeopardy. These loans are no longer adequately protected due to well-defined weaknesses that affect the repayment capacity of the borrower. The possibility of loss is much more evident and above average supervision is required for these loans.

Doubtful – Loans in this category have all the weaknesses inherent in a loan categorized as Substandard, with the characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions, and values, highly questionable and improbable.

The following table presents the risk category of loans by segment.

(Dollars in Thousands)	**Commercial, Financial, Agriculture**	**Real Estate**	**Consumer**	**Total Criticized Loans**
September 30, 2018				
Special Mention	$ 357	$ 12,674	$ 56	$ 13,087
Substandard	594	26,058	386	27,038
Doubtful	-	-	-	-
Total Criticized Loans	$ 951	$ 38,732	$ 442	$ 40,125
December 31, 2017				
Special Mention	$ 7,879	$ 13,324	$ 65	$ 21,268
Substandard	1,057	29,291	654	31,002
Doubtful	-	-	-	-
Total Criticized Loans	$ 8,936	$ 42,615	$ 719	$ 52,270

Troubled Debt Restructurings ("TDRs"). TDRs are loans in which the borrower is experiencing financial difficulty and the Company has granted an economic concession to the borrower that it would not otherwise consider. In these instances, as part of a work-out alternative, the Company will make concessions including the extension of the loan term, a principal moratorium, a reduction in the interest rate, or a combination thereof. The impact of the TDR modifications and defaults are factored into the allowance for loan losses on a loan-by-loan basis as all TDRs are, by definition, impaired loans. Thus, specific reserves are established based upon the results of either a discounted cash flow analysis or the underlying collateral value, if the loan is deemed to be collateral dependent. A TDR classification can be removed if the borrower's financial condition improves such that the borrower is no longer in financial difficulty, the loan has not had any forgiveness of principal or interest, and the loan is subsequently refinanced or restructured at market terms and qualifies as a new loan.

The following table presents loans classified as TDRs.

	September 30, 2018		December 31, 2017	
(Dollars in Thousands)	Accruing	Nonaccruing	Accruing	Nonaccruing
Commercial, Financial and Agricultural	$ 650	$ 219	$ 822	$ -
Real Estate – Construction	61	-	64	-
Real Estate – Commercial Mortgage	15,847	1,226	17,058	1,636
Real Estate – Residential	9,980	1,120	11,666	503
Real Estate – Home Equity	2,033	97	2,441	186
Consumer	90	-	113	-
Total TDRs	$ 28,661	$ 2,662	$ 32,164	$ 2,325

Loans classified as TDRs during the periods indicated are presented in the table below. The modifications made during the reporting period involved either an extension of the loan term, an interest rate adjustment, or a principal moratorium, and the financial impact of these modifications was not material.

	Three Months Ended September 30, 2018			Nine Months Ended September 30, 2018		
(Dollars in Thousands)	Number of Contracts	Pre-Modified Recorded Investment	Post-Modified Recorded Investment	Number of Contracts	Pre-Modified Recorded Investment	Post-Modified Recorded Investment
Commercial, Financial and Agricultural	-	$ -	$ -	1	$ 498	$ 230
Real Estate – Construction	-	-	-	-	-	-
Real Estate – Commercial Mortgage	-	-	-	1	227	228
Real Estate – Residential	1	72	76	2	105	108
Real Estate – Home Equity	-	-	-	1	27	27
Consumer	-	-	-	-	-	-
Total TDRs	1	$ 72	$ 76	5	$ 857	$ 593

	Three Months Ended September 30, 2017			Nine Months Ended September 30, 2017		
(Dollars in Thousands)	Number of Contracts	Pre-Modified Recorded Investment	Post-Modified Recorded Investment	Number of Contracts	Pre-Modified Recorded Investment	Post-Modified Recorded Investment
Commercial, Financial and Agricultural	1	$ 32	$ 22	1	$ 32	$ 22
Real Estate – Construction	-	-	-	1	64	65
Real Estate – Commercial Mortgage	1	160	70	1	160	70
Real Estate – Residential	1	101	102	2	316	283
Real Estate – Home Equity	3	149	147	4	205	203
Consumer	-	-	-	-	-	-

Total TDRs	6	$ 442	$ 341	9	$ 777	$ 643

20

For the three and nine months ended September 30, 2018, the loans modified as TDRs within the previous 12 months that have substantially defaulted are presented below. For the three and nine month period ended September 30, 2017, there were no loans modified as TDRs within the previous 12 months that have substantially defaulted.

	Three Months Ended September 30, 2018		**Nine Months Ended September 30, 2018**	
(Dollars in Thousands)	**Number of Contracts**	**Post-Modified Recorded Investment[1]**	**Number of Contracts**	**Post-Modified Recorded Investment[1]**
Commercial, Financial and Agricultural	-	$ -	-	$ -
Real Estate – Construction	-	-	-	-
Real Estate – Commercial Mortgage	-	-	1	64
Real Estate – Residential	-	-	-	-
Real Estate – Home Equity	-	-	-	-
Consumer	-	-	-	-
Total TDRs	-	$ -	1	$ 64

[1] *Recorded investment reflects charge-offs and additional funds advanced at time of restructure, if applicable.*

The following table provides information on how TDRs were modified during the periods indicated.

	Three Months Ended September 30, 2018		**Nine Months Ended September 30, 2018**	
(Dollars in Thousands)	Number of Contracts	Recorded Investment[1]	Number of Contracts	Recorded Investment[1]
Extended amortization	1	$ 76	2	$ 303
Interest rate adjustment	-	-	1	33
Extended amortization and interest rate adjustment	-	-	1	27
Principal moratorium	-	-	1	230
Total TDRs	1	$ 76	5	$ 593

	Three Months Ended September 30, 2017		**Nine Months Ended September 30, 2017**	
(Dollars in Thousands)	Number of Contracts	Recorded Investment[1]	Number of Contracts	Recorded Investment[1]
Extended amortization	1	$ 70	1	$ 70
Interest rate adjustment	-	-	3	302
Extended amortization and interest rate adjustment	4	249	4	249

Other	1		22	1		22
Total TDRs	6	$	341	9	$	643

(1) *Recorded investment reflects charge-offs and additional funds advanced at time of restructure, if applicable.*

NOTE 4 – OTHER REAL ESTATE OWNED

The following table presents other real estate owned activity for the periods indicated.

	Three Months Ended September 30,		Nine Months Ended September 30,	
(Dollars in Thousands)	**2018**	**2017**	**2018**	**2017**
Beginning Balance	$ 3,373	$ 7,968	$ 3,941	$ 10,638
Additions	420	339	1,260	2,024
Valuation Write-downs	(224)	(350)	(856)	(1,118)
Sales	(849)	(1,970)	(1,625)	(5,291)
Other	-	-	-	(266)
Ending Balance	$ 2,720	$ 5,987	$ 2,720	$ 5,987

Net expenses applicable to other real estate owned include the following:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(Dollars in Thousands)	**2018**	**2017**	**2018**	**2017**
Gains from the Sale of Properties	$ (46)	$ (711)	$ (127)	$ (980)
Losses from the Sale of Properties	70	123	212	318
Rental Income from Properties	(3)	(19)	(9)	(73)
Property Carrying Costs	102	139	289	397
Valuation Adjustments	224	350	856	1,118
Total	$ 347	$ (118)	$ 1,221	$ 780

As of September 30, 2018, the Company had $0.7 million of loans secured by residential real estate in the process of foreclosure**.**

NOTE 5 - EMPLOYEE BENEFIT PLANS

The Company has a defined benefit pension plan covering substantially all full-time and eligible part-time associates and a Supplemental Executive Retirement Plan (“SERP”) covering its executive officers.

The components of the net periodic benefit cost for the Company's qualified benefit pension plan were as follows:

	Three Months Ended September 30,		**Nine Months Ended September 30,**	
(Dollars in Thousands)	**2018**	**2017**	**2018**	**2017**
Service Cost	$ 1,721	$ 1,688	$ 5,163	$ 5,064
Interest Cost	1,415	1,437	4,246	4,312
Expected Return on Plan Assets	(2,391)	(2,006)	(7,173)	(6,019)
Prior Service Cost Amortization	50	56	150	167
Net Loss Amortization	918	953	2,754	2,859
Net Periodic Benefit Cost	$ 1,713	$ 2,128	$ 5,140	$ 6,383
Discount Rate	3.71%	4.21%	3.71%	4.21%
Long-term Rate of Return on Assets	7.25%	7.25%	7.25%	7.25%

The components of the net periodic benefit cost for the Company's SERP were as follows:

	Three Months Ended September 30,		**Nine Months Ended September 30,**	
(Dollars in Thousands)	**2018**	**2017**	**2018**	**2017**
Interest Cost	$ 57	$ 48	$ 170	$ 143
Net Loss Amortization	406	149	1,220	448
Net Periodic Benefit Cost	$ 463	$ 197	$ 1,390	$ 591
Discount Rate	3.53%	3.92%	3.53%	3.92%

The service cost component of net periodic benefit cost is reflected in compensation expense in the accompanying statements of income. The other components of net periodic cost are included in "other" within the noninterest expense category in the statements of income. See Note 1 – Significant Accounting Policies for additional information.

During the first nine months of 2018, the Company contributed $23 million (first quarter - $10 million, second quarter - $10 million, third quarter - $3 million) to its defined benefit pension plan for the 2017 plan year.

NOTE 6 - COMMITMENTS AND CONTINGENCIES

Lending Commitments. The Company is a party to financial instruments with off-balance sheet risks in the normal course of business to meet the financing needs of its clients. These financial instruments consist of commitments to extend credit and standby letters of credit.

The Company's maximum exposure to credit loss under standby letters of credit and commitments to extend credit is represented by the contractual amount of those instruments. The Company uses the same credit policies in establishing commitments and issuing letters of credit as it does for on-balance sheet instruments. The amounts associated with the Company's off-balance sheet obligations were as follows:

	September 30, 2018			**December 31, 2017**		
(Dollars in Thousands)	**Fixed**	**Variable**	**Total**	**Fixed**	**Variable**	**Total**
Commitments to Extend Credit [1]	$ 96,591	$ 365,224	$ 461,815	$ 78,390	$ 366,750	$ 445,140
Standby Letters of Credit	4,363	-	4,363	4,678	-	4,678
Total	$ 100,954	$ 365,224	$ 466,178	$ 83,068	$ 366,750	$ 449,818

(1) *Commitments include unfunded loans, revolving lines of credit, and other unused commitments.*

Commitments to extend credit are agreements to lend to a client so 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 payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements.

Standby letters of credit are conditional commitments issued by the Company to guarantee the performance of a client to a third party. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities. In general, management does not anticipate any material losses as a result of participating in these types of transactions. However, any potential losses arising from such transactions are reserved for in the same manner as management reserves for its other credit facilities.

For both on- and off-balance sheet financial instruments, the Company requires collateral to support such instruments when it is deemed necessary. The Company evaluates each client's creditworthiness on a case-by-case basis. The amount of collateral obtained upon extension of credit is based on management's credit evaluation of the counterparty. Collateral held varies, but may include deposits held in financial institutions; U.S. Treasury securities; other marketable securities; real estate; accounts receivable; property, plant and equipment; and inventory.

Contingencies. The Company is a party to lawsuits and claims arising out of the normal course of business. In management's opinion, there are no known pending claims or litigation, the outcome of which would, individually or in the aggregate, have a material effect on the consolidated results of operations, financial position, or cash flows of the Company.

Indemnification Obligation. The Company is a member of the Visa U.S.A. network. Visa U.S.A member banks are required to indemnify it for potential future settlement of certain litigation (the "Covered Litigation") that relates to several antitrust lawsuits challenging the practices of Visa and MasterCard International. In 2008, the Company, as a member of the Visa U.S.A. network, obtained Class B shares of Visa, Inc. upon its initial public offering. Since its initial public offering, Visa, Inc. has funded a litigation reserve for the Covered Litigation resulting in a reduction in the Class B shares held by the Company. During the first quarter of 2011, the Company sold its remaining Class B shares. Associated with this sale, the Company entered into a swap contract with the purchaser of the shares that requires a payment to the counterparty in the event that Visa, Inc. makes subsequent revisions to the conversion ratio for its Class B shares. Fixed charges included in the swap liability are payable quarterly until the litigation reserve is fully liquidated and at which time the aforementioned swap contract will be terminated. Quarterly fixed payments approximate $123,000. Conversion ratio payments and ongoing fixed quarterly charges are reflected in earnings in the period incurred.

NOTE 7 – FAIR VALUE MEASUREMENTS

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 occurring in the principal market (or most advantageous market in the absence of a principal market) for such asset or liability. In estimating fair value, the Company utilizes valuation techniques that are consistent with the market approach, the income approach and/or the cost approach. Such valuation techniques are consistently applied. Inputs to valuation techniques include the assumptions that market participants would use in pricing an asset or liability. ASC Topic 820 establishes a fair value 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 value hierarchy is as follows:

- *Level 1 Inputs* - Unadjusted quoted prices in active markets for identical assets or liabilities that the reporting entity has the ability to access at the measurement date.

- *Level 2 Inputs* - Inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. These might include quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, inputs other than quoted prices that are observable for the asset or liability (such as interest rates, volatilities, prepayment speeds, credit risks, etc.) or inputs that are derived principally from, or corroborated, by market data by correlation or other means.

- *Level 3 Inputs* - Unobservable inputs for determining the fair values of assets or liabilities that reflect an entity's own assumptions about the assumptions that market participants would use in pricing the assets or liabilities.

Assets and Liabilities Measured at Fair Value on a Recurring Basis

Securities Available for Sale. U.S. Treasury securities are reported at fair value utilizing Level 1 inputs. Other securities classified as available for sale are reported at fair value utilizing Level 2 inputs. For these securities, the Company obtains fair value measurements from an independent pricing service. The fair value measurements consider observable data that may include dealer quotes, market spreads, cash flows, the U.S. Treasury yield curve, live trading levels, trade execution data, credit information and the bond’s terms and conditions, among other things.

In general, the Company does not purchase securities that have a complicated structure. The Company’s entire portfolio consists of traditional investments, nearly all of which are U.S. Treasury obligations, federal agency bullet or mortgage pass-through securities, or general obligation or revenue based municipal bonds. Pricing for such instruments is easily obtained. Quarterly, the Company will validate, on a sample basis, prices supplied by the independent pricing service by comparison to prices obtained from third-party sources or derived using internal models.

Fair Value Swap. The Company entered into a stand-alone derivative contract with the purchaser of its Visa Class B shares. The valuation represents the amount due and payable to the counterparty based upon the revised share conversion rate, if any, during the period. At September 30, 2018, there were no amounts payable.

A summary of fair values for assets and liabilities consisted of the following:

(Dollars in Thousands)	**Level 1 Inputs**	**Level 2 Inputs**	**Level 3 Inputs**	**Total Fair Value**
September 30, 2018				
ASSETS:				
Securities Available for Sale:				
U.S. Government Treasury	$ 268,113	$ -	$ -	$ 268,113
U.S. Government Agency	-	153,091	-	153,091
States and Political Subdivisions	-	53,839	-	53,839
Mortgage-Backed Securities	-	972	-	972
Equity Securities	-	8,228	-	8,228
December 31, 2017				
ASSETS:				
Securities Available for Sale:				
U.S. Government Treasury	$ 235,341	$ -	$ -	$ 235,341
U.S. Government Agency	-	144,644	-	144,644
States and Political Subdivisions	-	91,157	-	91,157
Mortgage-Backed Securities	-	1,185	-	1,185
Equity Securities	-	8,584	-	8,584

Assets Measured at Fair Value on a Non-Recurring Basis

Certain assets are measured at fair value on a non-recurring basis (i.e., the assets are not measured at fair value on an ongoing basis but are subject to fair value adjustments in certain circumstances). An example would be assets exhibiting evidence of impairment. The following is a description of valuation methodologies used for assets measured on a non-recurring basis.

Impaired Loans. Impairment for collateral dependent loans is measured using the fair value of the collateral less selling costs. The fair value of collateral is determined by an independent valuation or professional appraisal in conformance with banking regulations. Collateral values are estimated using Level 3 inputs due to the volatility in the real estate market, and the judgment and estimation involved in the real estate appraisal process. Impaired loans are reviewed and evaluated on at least a quarterly basis for additional impairment and adjusted accordingly. Valuation techniques are consistent with those techniques applied in prior periods. Impaired collateral dependent loans had a carrying value of $6.3 million with a valuation allowance of $0.8 million at September 30, 2018 and $6.1 million and $1.1 million, respectively, at December 31, 2017.

Loans Held for Sale. These loans are carried at the lower of cost or fair value and are adjusted to fair value on a non-recurring basis. Fair value is based on observable markets rates for comparable loan products, which is considered a Level 2 fair value measurement.

Other Real Estate Owned. During the first nine months of 2018, certain foreclosed assets, upon initial recognition, were measured and reported at fair value through a charge-off to the allowance for loan losses based on the fair value of the foreclosed asset less estimated cost to sell. The fair value of the foreclosed asset is determined by an independent valuation or professional appraisal in conformance with banking regulations. On an ongoing basis, we obtain updated appraisals on foreclosed assets and realize valuation adjustments as necessary. The fair value of foreclosed assets is estimated using Level 3 inputs due to the judgment and estimation involved in the real estate valuation process.

Assets and Liabilities Disclosed at Fair Value

The Company is required to disclose the estimated fair value of financial instruments, both assets and liabilities, for which it is practical to estimate fair value and the following is a description of valuation methodologies used for those assets and liabilities.

Cash and Short-Term Investments. The carrying amount of cash and short-term investments is used to approximate fair value, given the short time frame to maturity and as such assets do not present unanticipated credit concerns.

Securities Held to Maturity. Securities held to maturity are valued in accordance with the methodology previously noted in this footnote under the caption "Assets and Liabilities Measured at Fair Value on a Recurring Basis – Securities Available for Sale".

Loans. The loan portfolio is segregated into categories and the fair value of each loan category is calculated using present value techniques based upon projected cash flows and estimated discount rates. For values reported prior to 2018, the discount rates used to projecting cash flows reflected the credit and interest rate risks inherent in each loan category. The calculated present values are then reduced by an allocation of the allowance for loan losses against each respective loan category. Pursuant to the adoption of ASU 2016-01, *Recognition and Measurement of Financial Assets and Financial Liabilities*, for values reported for the 2018 period, fair value reflects the incorporation of a liquidity discount to meet the objective of “exit price” valuation.

Deposits. The fair value of Noninterest Bearing Deposits, NOW Accounts, Money Market Accounts and Savings Accounts are the amounts payable on demand at the reporting date. The fair value of fixed maturity certificates of deposit is estimated using present value techniques and rates currently offered for deposits of similar remaining maturities.

Subordinated Notes Payable. The fair value of each note is calculated using present value techniques, based upon projected cash flows and estimated discount rates as well as rates being offered for similar obligations.

Short-Term and Long-Term Borrowings. The fair value of each note is calculated using present value techniques, based upon projected cash flows and estimated discount rates as well as rates being offered for similar debt.

A summary of estimated fair values of significant financial instruments consisted of the following:

	September 30, 2018			
(Dollars in Thousands)	**Carrying Value**	**Level 1 Inputs**	**Level 2 Inputs**	**Level 3 Inputs**
ASSETS:				
Cash	$ 48,423	$ 48,423	$ -	$ -
Short-Term Investments	26,839	26,839	-	-
Investment Securities, Available for Sale	484,243	268,113	216,130	-
Investment Securities, Held to Maturity	227,923	34,401	189,130	-
Equity Securities(1)	3,600	-	3,600	-
Loans Held for Sale	8,297	-	8,297	-
Loans, Net of Allowance for Loan Losses	1,759,535	-	-	1,723,355
LIABILITIES:				
Deposits	$ 2,381,216	$ -	$ 2,379,106	$ -
Short-Term Borrowings	16,644	-	16,644	-
Subordinated Notes Payable	52,887	-	41,575	-
Long-Term Borrowings	12,456	-	12,330	-

	December 31, 2017			
(Dollars in Thousands)	**Carrying Value**	**Level 1 Inputs**	**Level 2 Inputs**	**Level 3 Inputs**
ASSETS:				
Cash	$ 58,419	$ 58,419	$ -	$ -
Short-Term Investments	227,023	227,023	-	-
Investment Securities, Available for Sale	480,911	235,341	245,570	-
Investment Securities, Held to Maturity	216,679	97,815	117,192	-
Loans Held for Sale	4,817	-	4,817	-
Loans, Net of Allowance for Loan Losses	1,640,185	-	-	1,625,310
LIABILITIES:				
Deposits	$ 2,469,877	$ -	$ 2,382,818	$ -
Short-Term Borrowings	7,480	-	7,482	-
Subordinated Notes Payable	52,887	-	41,718	-
Long-Term Borrowings	13,967	-	14,081	-

(1) *Not readily marketable securities - reflected in other assets.*

All non-financial instruments are excluded from the above table. The disclosures also do not include goodwill. Accordingly, the aggregate fair value amounts presented do not represent the underlying value of the Company.

NOTE 8 – OTHER COMPREHENSIVE INCOME

The amounts allocated to other comprehensive income are presented in the table below. Reclassification adjustments related to securities held for sale are included in net gain/loss on securities transactions in the accompanying consolidated statements of comprehensive income. For the periods presented, reclassifications adjustments related to securities held for sale was not material.

(Dollars in Thousands)		**Before Tax Amount**		**Tax (Expense) Benefit**		**Net of Tax Amount**
Three Months Ended September 30, 2018						
Investment Securities:						
Change in net unrealized gain/loss on securities available for sale	$	(553)	$	140	$	(413)
Amortization of losses on securities transferred from available for sale to held to maturity		13		(3)		10
Total Other Comprehensive Loss	$	(540)	$	137	$	(403)
Nine Months Ended September 30, 2018						
Investment Securities:						
Change in net unrealized gain/loss on securities available for sale	$	(2,306)	$	585	$	(1,721)
Amortization of losses on securities transferred from available for sale to held to maturity		42		(11)		31
Total Other Comprehensive Loss	$	(2,264)	$	574	$	(1,690)

(Dollars in Thousands)		**Before Tax Amount**		**Tax (Expense) Benefit**		**Net of Tax Amount**
Three Months Ended September 30, 2017						
Investment Securities:						
Change in net unrealized gain/loss on securities available for sale	$	(99)	$	38	$	(61)
Amortization of losses on securities transferred from available for sale to held to maturity		19		(7)		12
Total Other Comprehensive Loss	$	(80)	$	31	$	(49)