FIRST COMMUNITY BANCSHARES INC /NV/
Form 10-K
March 03, 2015
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF

THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2014

Commission file number 000-19297

FIRST COMMUNITY BANCSHARES, INC.

(Exact name of registrant as specified in its charter)

Nevada	**55-0694814**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
P.O. Box 989	
Bluefield, Virginia	**24605-0989**
(Address of principal executive offices)	**(Zip Code)**

Registrant s telephone number, including area code: (276) 326-9000

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

Title of each class	**Name of each exchange on which registered**
Common Stock, $1.00 par value	NASDAQ Global Select

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

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

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

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. x Yes ¨ 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). x Yes ¨ No

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

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

Large accelerated filer	¨	Accelerated filer	x
Non-accelerated filer	¨ (Do not check if a smaller reporting company)	Smaller reporting company	¨

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

As of June 30, 2014, the aggregate market value of the registrant s voting and non-voting common stock held by non-affiliates was $200.41 million.

As of February 26, 2015, there were 18,545,619 shares outstanding of the registrant s Common Stock, $1.00 par value.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant s Proxy Statement for the Annual Meeting of Stockholders to be held April 28, 2015, are incorporated by reference in Part III of this Form 10-K.

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2014 FORM 10-K

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CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS

We may make forward-looking statements in filings with the Securities and Exchange Commission, including this Annual Report on Form 10-K and the accompanying Exhibits, filings incorporated by reference, reports to our shareholders, and other communications that we make in good faith pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. These forward-looking statements represent our beliefs, plans, objectives, goals, guidelines, expectations, anticipations, estimates, and intentions. These statements are not guarantees of future performance and involve certain risks, uncertainties, and assumptions that are based on various factors, many of which are beyond our control. The words may, could, should, would, believe, anticipate, estimate, expect, intend, plan, and other similar expression forward-looking statements. The following factors, among others, could cause our financial performance to differ materially from that expressed in such forward-looking statements:

- the strength of the U.S. economy in general and the strength of the local economies in which we conduct operations;
- the effects of, and changes in, trade, monetary, and fiscal policies and laws, including interest rate policies of the Federal Reserve System;
- inflation, interest rate, market and monetary fluctuations;
- our timely development of competitive new products and services and the acceptance of these products and services by new and existing customers;
- the willingness of customers to substitute competitors products and services for our products and services and vice versa;
- the impact of changes in financial services laws and regulations, including laws about taxes, banking, securities, and insurance, and the impact of the Dodd-Frank Wall Street Reform and Consumer Protection Act;
- the impact of the U.S. Department of the Treasury and federal banking regulators continued implementation of programs to address capital and liquidity in the banking system;
- further, future and proposed rules, including those that are part of the process outlined in the International Basel Committee on Banking Supervision s Basel III: A Global Regulatory Framework for More Resilient Banks and Banking Systems, which are expected to require banking institutions to increase levels of capital;
- technological changes;
- the effect of acquisitions, including, without limitation, the failure to achieve the expected revenue growth and/or expense savings from such acquisitions;
- the growth and profitability of our noninterest, or fee, income being less than expected;

unanticipated regulatory or judicial proceedings;

changes in consumer spending and saving habits; and

our success at managing the risks involved in the foregoing.

We caution that the foregoing list of important factors is not exclusive. If one or more of the factors affecting these forward-looking statements proves incorrect, our actual results, performance, or achievements could differ materially from those expressed in, or implied by, forward-looking statements contained in this Annual Report on Form 10-K and other reports we filed with the Securities and Exchange Commission. Therefore, we caution you not to place undue reliance on our forward-looking information and statements. We do not intend to update any forward-looking statements, whether written or oral, to reflect changes. These cautionary statements expressly qualify all forward-looking statements that apply to our Company. See Item 1A, Risk Factors, in Part I of this report.

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PART I

Item 1. Business.
Corporate Overview

First Community Bancshares, Inc. (the Company), a financial holding company, was founded in 1989 and incorporated under the laws of Nevada in 1997. The Company provides commercial banking products and services through its wholly owned subsidiary First Community Bank (the Bank), a Virginia-chartered banking institution founded in 1874. The Bank operates under the trade names First Community Bank in Virginia, West Virginia, and North Carolina and People s Community Bank, a Division of First Community Bank, in Tennessee. Unless the context suggests otherwise, the terms First Community, Company, we, our, and us in this Annual Report on Form 10-K refer to First Community Bancshares, Inc. and its subsidiaries as a consolidated entity. Our operations are guided by a strategic plan focusing on organic growth that may be supplemented by strategic acquisitions.

The Company provides insurance services through its wholly owned, full-service insurance agency subsidiary Greenpoint Insurance Group, Inc. (Greenpoint). Greenpoint operates under the Greenpoint name and under the trade names First Community Insurance Services (FCIS) and Carolina Insurers Associates in North Carolina, Carr & Hyde Insurance and FCIS in Virginia, and FCIS in West Virginia.

The Bank offers wealth management and investment advice through its wholly owned subsidiary First Community Wealth Management and the Bank s Trust Division. The Company is the common stockholder of FCBI Capital Trust (the Trust), which was created in October 2003 to issue trust preferred securities to raise capital for the Company.

The Company is a legal entity that is separate and distinct from its affiliates. As a financial holding company, the Company is required to act as a source of financial strength for its subsidiary bank. The Company s principal source of revenue is derived from dividends paid by the Bank, which are subject to certain restrictions by regulatory agencies and determined in relation to earnings, asset growth, and capital position. For additional information see Regulation and Supervision below.

Operations

We operate in one business segment: Community Banking. The Community Banking segment consists of commercial and consumer banking, lending activities, wealth management, and insurance services. Our principal executive office is located at One Community Place, Bluefield, Virginia. As of December 31, 2014, we operated 63 locations in 4 states: Virginia, West Virginia, North Carolina, and Tennessee. We serve a diverse base of individuals and businesses across a variety of industries, such as manufacturing, mining services, construction, retail, healthcare, military, and transportation. We have no material concentrations of deposits or loans related to any single customer or industry. See Item 6, Selected Financial Data, in Part II of this report for a summary of our financial performance.

We offer a wide range of services and products to our customers:

- demand deposit accounts, savings and money market accounts, certificates of deposit, and individual retirement arrangements;
- commercial, consumer, and real estate mortgage loans, and lines of credit;
- various credit card, debit card, and automated teller machine card services;
- corporate and personal trust services;
- investment management services; and

life, health, and property and casualty insurance products.

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Employees

As of December 31, 2014, we had 678 full-time equivalent employees. Our employees are not represented by collective bargaining agreements and we consider employee relations to be excellent.

Competition

The financial services industry is highly competitive and there is substantial competition in attracting deposit and loan relationships in our market areas. The ability of non-bank financial entities to provide services previously reserved for commercial banks has intensified competition. We compete with other commercial banks and financial service providers, including thrifts, savings and loan associations, credit unions, consumer finance companies, commercial finance and leasing companies, securities firms, brokerage firms, and insurance companies. Competition for deposits generally comes from other commercial banks, savings institutions, credit unions, mutual funds, and other investment alternatives. Factors that influence our ability to attract and retain deposits include interest rates, personalized services, quality and variety of financial offerings, convenience of office locations, automated services, and office hours. Competition for commercial and business loans generally comes from other commercial banks and commercial finance and leasing companies while competition for mortgage loans primarily comes from other commercial banks, savings institutions, mortgage banking firms, mortgage brokers, and insurance companies. Factors that influence our ability to originate loans include interest rates, loan origination fees, quality and variety of lending offerings, and personalized services. Our competitors may have greater resources and higher lending limits that allow them to offer services we do not provide. Competition could intensify in the future as a result of general and local economic conditions, industry consolidation, bank failures, technological developments, and banking regulatory reform. See Competition in the Executive Overview section in Part II, Item 7 of this report.

Available Information

Under the Securities Exchange Act of 1934, as amended (Exchange Act), we are required to file annual, quarterly, and current reports; proxy statements; and other information with the Securities and Exchange Commission (SEC). Any document we file with the SEC may be read and copied at the SEC s Public Reference Room at 100 F Street, N.E., Washington, D.C. 20549. Please call the SEC at (800) SEC-0330 for additional information about the public reference room. The SEC maintains a website at www.sec.gov that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC.

Our Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, and other information, including any amendments to those reports, are available free of charge on our website, www.fcbinc.com, as soon as reasonably practicable after such reports are filed with, or furnished to, the SEC. Investors are encouraged to access these reports and other information about our business. Information about our Board of Directors, executive officers, and corporate governance policies and principles is included on our website and includes the Standards of Conduct governing the Company s directors, officers, and employees; the charters of the standing committees of the Company s Board of Directors; and the Company s Insider Trading and Disclosure Policy. Additional information found on our website is not part of this report.

Regulation and Supervision

Banks and financial holding companies operate in a highly regulated industry and are subject to examination, supervision, and comprehensive regulation under applicable federal and state laws and various regulatory agencies. The regulations are intended primarily for the protection of depositors, the Deposit Insurance Fund (DIF) of the Federal Deposit Insurance Corporation (FDIC), and the banking system as a whole and are generally not for the protection of stockholders or creditors. Banking agencies have broad enforcement powers over banks and financial holding companies to impose substantial fines and penalties for violations of laws and regulations.

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The following discussion summarizes certain laws, rules, and regulations that affect our Company. These summaries are not intended to be complete and are qualified in their entirety by reference to the applicable statute or regulation. A change in laws, rules, and regulations may have a material effect on our Company.

Dodd-Frank Wall Street Reform and Consumer Protection Act

On July 21, 2010, sweeping financial regulatory reform legislation entitled the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) was signed into law. The Dodd-Frank Act implements far-reaching changes across the financial regulatory landscape, including the following provisions:

centralizes responsibility for consumer financial protection by creating a new agency, the Consumer Financial Protection Bureau (CFPB), responsible for implementing, examining and enforcing compliance with federal consumer financial laws;

requires financial holding companies, such as the Company, to be well capitalized and well managed as of July 21, 2011 (bank holding companies and banks must also be well capitalized and well managed to engage in interstate bank acquisitions);

imposes comprehensive regulation of the over-the-counter derivatives market, which would include certain provisions that would effectively prohibit insured depository institutions from conducting certain derivatives businesses in the institutions themselves;

implements corporate governance revisions, including executive compensation and proxy access by shareholders;

makes permanent the $250 thousand limit for federal deposit insurance;

repeals the federal prohibitions on the payment of interest on demand deposits, thereby permitting depository institutions to pay interest on business transaction and other accounts;

amends the Electronic Fund Transfer Act to, among other things, give the Board of Governors of the Federal Reserve System (Federal Reserve) the authority to establish rules regarding interchange fees charged for electronic debit transactions by payment card issuers having assets over $10 billion and enforces a new statutory requirement that such fees be reasonable and proportional to the actual cost of a transaction to the issuer; and

increases the authority of the Federal Reserve to examine bank holding companies, such as the Company, and their non-bank subsidiaries. Another section of the Dodd-Frank Act, the Mortgage Reform and Anti-Predatory Lending Act (Mortgage Reform Act), contains new underwriting and servicing standards for the mortgage industry, as well as restrictions on compensation for mortgage originators. The Mortgage Reform Act grants broad discretionary regulatory authority to the CFPB to prohibit or condition terms, acts, or practices relating to residential mortgage loans that the CFPB finds abusive, unfair, deceptive, or predatory, as well as to take other actions that the CFPB finds are necessary or proper to ensure that responsible affordable mortgage credit remains available to consumers. The Dodd-Frank Act also contains laws affecting the securitization of mortgages, and other assets, with requirements for risk retention by securitizers and requirements for regulating credit rating agencies. Many aspects of the Dodd-Frank Act continue to be subject to rulemaking and will take effect over several years, making it difficult to anticipate the financial impact on our Company, our customers, or the general financial industry. Provisions in the legislation that affect deposit insurance assessments, payment of interest on demand deposits, and interchange fees could increase costs associated with deposits, as well as place limitations on certain revenues those deposits may generate.

First Community Bancshares, Inc.

The Company is a financial holding company organized under the Gramm-Leach-Bliley Act of 1999 (GLB Act) and a bank holding company registered under the Bank Holding Company Act of 1956, as amended (BHC Act). The Company is subject to supervision, regulation, and examination by the Federal Reserve. The GLB Act, BHC Act, and other federal laws subject financial and bank holding companies to particular restrictions on the types of activities they may engage in and to a range of supervisory requirements and activities, including regulatory enforcement actions for violations of laws and regulations. The BHC Act generally provides for umbrella regulation of financial holding companies, such as the Company, by the Federal Reserve, as well as functional regulation of banking activities by bank regulators, securities activities by securities regulators, and insurance activities by insurance regulators.

The Company is also under the jurisdiction of the SEC and is subject to the disclosure and regulatory requirements of the Securities Act of 1933, as amended, and the Exchange Act as administered by the SEC. The Company s common stock is listed on the NASDAQ Global Select Market under the trading symbol FCBC, and is subject to the rules of NASDAQ for listed companies.

Regulatory Restrictions on Dividends: Source of Strength

The Federal Reserve s policy has historically required bank holding companies to act as a source of financial and managerial strength to their subsidiary banks. The Dodd-Frank Act codified this policy as a statutory requirement. Under this requirement, the Company is expected to commit resources to support the Bank, even when it may not be in a financial position to provide such resources. Federal Reserve policy states that bank holding companies may pay cash dividends on common stock only from income available over the past year if prospective earnings retention is consistent with the organization s expected future needs and financial condition. Bank holding companies should not maintain dividend levels that undermine their ability to be a source of strength to their banking subsidiaries. A bank holding company may be required to guarantee the capital restoration plan of an undercapitalized banking subsidiary in certain situations.

In addition, the Company and the Bank are subject to other regulatory policies and requirements relating to the payment of dividends, including requirements to maintain adequate capital above regulatory minimums. The appropriate federal regulatory authority may determine that the payment of dividends would be an unsafe or unsound practice, under certain circumstances regarding the financial condition of a bank holding company or a bank, and prohibit dividend payments. The appropriate federal regulatory authorities have stated that paying dividends that deplete a bank s capital base to an inadequate level would be an unsafe and unsound banking practice and that banking organizations should generally pay dividends only out of current operating earnings. In the current financial and economic environment, the Federal Reserve has discouraged payment ratios that are at maximum allowable levels, unless both asset quality and capital are very strong, and has noted that bank holding companies should carefully review their dividend policy.

Scope of Permissible Activities

Under the BHC Act, bank holding companies are limited to banking, managing or controlling banks, furnishing services to or performing services for their subsidiaries, or other activities that the Federal Reserve has determined to be closely related to banking or managing and controlling banks as to be a proper incident thereto. The BHC Act requires every bank holding company to obtain the prior approval of the Federal Reserve before acquiring direct or indirect ownership or control of more than 5% of the voting shares of any bank or all, or substantially all, of the assets of a bank. When approving bank acquisitions by bank holding companies, the Federal Reserve is required to consider the financial and managerial resources and future prospects of the bank holding company and the target bank, the convenience and needs of the communities to be served, and various competitive factors. The BHC Act also prohibits a bank holding company from acquiring direct or indirect control of more than 5% of the outstanding voting stock of any company engaged in a non-banking business

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unless such business is determined by the Federal Reserve to be so closely related to banking as to be a proper incident thereto.

Notwithstanding the foregoing, the GLB Act eliminated the barriers to affiliations among banks, securities firms, insurance companies, and other financial service providers and permits bank holding companies to become financial holding companies and thereby affiliate with securities firms and insurance companies and engage in other activities that are financial in nature. The GLB Act defines financial in nature to include securities underwriting, dealing, and market making; sponsoring mutual funds and investment companies; insurance underwriting and agency; merchant banking activities; and activities that the Federal Reserve has determined to be closely related to banking. Regulatory approval is not generally required for a financial holding company to acquire a company, other than a bank or savings association, engaged in activities that are financial in nature, or incidental to activities that are financial in nature, as determined by the Federal Reserve.

Under the GLB Act, a bank holding company may become a financial holding company by filing a declaration with the Federal Reserve if each of its subsidiary banks is well capitalized under the FDIC Improvement Act prompt corrective action provisions, is well managed, and has at least a satisfactory rating under the Community Reinvestment Act. The Company elected financial holding company status in December 2006. Since July 2011, the Company s status is dependent on maintaining a well-capitalized and well-managed status under applicable Federal Reserve regulations. If a financial holding company fails to meet these requirements, the Federal Reserve may impose corrective capital and/or managerial requirements on the financial holding company and place limitations on its ability to conduct the broader financial activities permissible for financial holding companies. The Federal Reserve may require divestiture of the holding company s depository institutions if the deficiencies persist.

The Dodd-Frank Act amended the BHC Act to require federal financial regulatory agencies to adopt rules that prohibit banks and their affiliates from engaging in proprietary trading and investing in and sponsoring certain unregistered investment companies (defined as hedge funds and private equity funds). The statutory provision is commonly called the Volcker Rule. The Federal Reserve adopted final rules implementing the Volcker Rule on December 10, 2013. The Volcker Rule became effective on July 21, 2012 and the final rules became effective on April 1, 2014, but the Federal Reserve issued an order on December 18, 2014, extending the period during which institutions have to conform their activities and investments to the requirements of the Volcker Rule to July 21, 2016. The Federal Reserve also announced its intention to grant an additional one-year extension of the conformance period to July 21, 2017. On January 14, 2014, the banking agencies approved an interim rule to permit banking entities to retain interests in certain collateralized debt obligations backed primarily by trust preferred securities from the prohibitions under the Volcker Rule. Although we continue to evaluate the impact of the Volcker Rule and the final rules adopted, we do not expect that the Volcker Rule will have a material effect on the operations of the Company and subsidiaries, as the Company does not engage in the businesses prohibited by the Volcker Rule. The Company may incur costs to adopt additional policies and systems to ensure compliance with the Volcker Rule, but any such costs are not expected to be material.

Anti-Tying Restrictions

Bank holding companies and their affiliates are prohibited from tying the provision of certain services, such as extensions of credit, to other services offered by a holding company or its affiliates.

Stock Repurchases

A bank holding company is required to give the Federal Reserve prior notice of any redemption or repurchase of its own equity securities, subject to certain exemptions, if the consideration to be paid, together with the consideration paid for any repurchases or redemptions in the preceding year, is equal to 10% or more of the company s consolidated net worth. The Federal Reserve may oppose the transaction if it believes that the transaction would constitute an unsafe or unsound practice or would violate any law or regulation.

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Capital Adequacy Requirements

The Federal Reserve uses two types of capital adequacy guidelines for holding companies: a two-tiered risk-based capital guideline and a leverage capital ratio guideline. The two-tiered risk-based capital guideline assigns risk weightings to all assets and certain off-balance sheet items. The guideline establishes a minimum ratio of Tier 1 capital to the aggregate dollar amount of risk-weighted assets (which amount is usually less than the aggregate dollar amount of such assets without risk weighting) and of total capital (Tier 1 capital plus Tier 2 capital, as adjusted) to the aggregate dollar amount of risk-weighted assets. The leverage ratio guideline establishes a minimum ratio of the holding company s Tier 1 capital to its total tangible assets (total assets less goodwill and certain identifiable intangibles) without risk-weighting. As discussed below, the Bank is subject to similar capital requirements.

Under both guidelines, Tier 1 capital is defined to include common shareholders equity comprised of retained earnings; qualifying noncumulative perpetual preferred stock and related surplus; qualifying cumulative perpetual preferred stock and related surplus; minority interests in the equity accounts of consolidated subsidiaries, which are limited to a maximum of 25% of Tier 1 capital; and certain trust preferred securities. The Dodd-Frank Act excludes trust preferred securities issued after May 19, 2010, from being included in Tier 1 capital, unless the issuing company is a bank holding company with less than $500 million in total assets. Trust preferred securities issued before that date continue to count as Tier 1 capital for bank holding companies with less than $15 billion in total assets, such as the Company. Goodwill and most intangible assets are deducted from Tier 1 capital. Tier 2 capital, sometimes referred to as supplementary capital, is defined to include, subject to limitation: perpetual preferred stock not included in Tier 1 capital; intermediate-term preferred stock and any related surplus; certain hybrid capital instruments; perpetual debt and mandatory convertible debt securities; allowances for loan and lease losses; and intermediate-term subordinated debt instruments. The maximum amount of qualifying Tier 2 capital is 100% of qualifying Tier 1 capital. Total capital equals Tier 1 capital, plus qualifying Tier 2 capital, minus investments in unconsolidated subsidiaries, reciprocal holdings of bank holding company capital securities, and deferred tax assets and other deductions. The Federal Reserve s current capital adequacy guidelines require that a bank holding company maintain a Tier 1 risk-based capital ratio of at least 4.0% and a total risk-based capital ratio of at least 8.0%. As of December 31, 2014, the Company s ratio of Tier 1 capital to total risk-weighted assets was 16.43% and ratio of total capital to risk-weighted assets was 17.68%.

The Federal Reserve uses a leverage ratio as an added tool to evaluate the capital adequacy of bank holding companies. The leverage ratio is a company s Tier 1 capital divided by its average total consolidated assets. Certain highly rated bank holding companies may maintain a minimum leverage ratio of 3.0%, but other bank holding companies are required to maintain a leverage ratio of 4.0% or more, depending on their condition. As of December 31, 2014, the Company s leverage ratio was 10.12%.

The federal banking agencies risk-based and leverage ratios are minimum supervisory ratios that generally apply to banking organizations that meet certain specified criteria, assuming that they have the highest regulatory rating. Banking organizations not meeting these criteria are expected to operate with capital positions well above the minimum ratios. Federal Reserve guidelines provide that regulatory agencies may set capital requirements for a particular banking organization that are higher than the minimum when circumstances warrant. These guidelines also provide that banking organizations experiencing internal growth or making acquisitions will be expected to maintain strong capital positions substantially above the minimum supervisory levels without significant reliance on intangible assets.

The current risk-based capital guidelines that apply to the Company and the Bank are based on the 1988 capital accord of the International Basel Committee on Banking Supervision, a committee of central banks and bank supervisors, implemented by the Federal Reserve. In July 2013, the Federal Reserve published the Basel III Capital Rules establishing a new comprehensive capital framework for U.S. banking organizations. The rules implement the Basel Committee s December 2010 framework known as Basel III for strengthening international capital standards as well as certain provisions of the Dodd-Frank Act. The Basel III Capital Rules substantially revise the risk-based capital requirements that apply to bank holding companies and depository institutions, including the Company and the Bank, compared to the current U.S. risk-based capital rules. The Basel III Capital Rules define the components of capital and address other issues affecting the numerator in banking institutions regulatory capital ratios. The Basel III Capital Rules address risk weights and other issues affecting the denominator in banking institutions regulatory capital ratios and replace the existing risk-weighting approach, which was derived from the Basel I capital accords of the Basel Committee, with a more risk-sensitive approach based, in part, on the standardized approach in the Basel Committee s 2004 Basel II capital accords. The Basel III Capital Rules also implement the requirements of Section 939A of the Dodd-Frank Act to remove references to credit ratings from the federal banking agencies rules. The Basel III Capital Rules are effective for the Company and the Bank, subject to a phase-in period, on January 1, 2015.

The Basel III Capital Rules, among other things, (1) introduce a new capital measure called Common Equity Tier 1 (CET1), (2) specify that Tier 1 capital consists of CET1 and Additional Tier 1 capital instruments meeting specified requirements, (3) define CET1 narrowly by requiring that most deductions/adjustments to regulatory capital measures be made to CET1 and not to the other components of capital, and (4) expand the scope of the deductions/adjustments as compared to existing regulations.

When fully phased in on January 1, 2019, the Basel III Capital Rules will require the Company and the Bank to maintain the following minimum ratios:

CET1 to risk-weighted assets of at least 4.5%, plus a 2.5% capital conservation buffer (which is added to the 4.5% CET1 ratio as that buffer is phased in, effectively resulting in a minimum ratio of CET1 to risk-weighted assets of at least 7% upon full implementation);

Tier 1 capital to risk-weighted assets of at least 6.0%, plus the capital conservation buffer (which is added to the 6.0% Tier 1 capital ratio as that buffer is phased in, effectively resulting in a minimum Tier 1 capital ratio of 8.5% upon full implementation);

Total capital (that is, Tier 1 plus Tier 2) to risk-weighted assets of at least 8.0%, plus the capital conservation buffer (which is added to the 8.0% total capital ratio as that buffer is phased in, effectively resulting in a minimum total capital ratio of 10.5% upon full implementation); and

Tier 1 capital to average assets (leverage ratio) of 4% (as compared to a current minimum leverage ratio of 3% for banking organizations that either have the highest supervisory rating or have implemented the appropriate federal regulatory authority s risk-adjusted measure for market risk).

The Basel III Capital Rules provide for a countercyclical capital buffer that applies to certain covered institutions; however, the buffer is not expected to apply to the Company or the Bank. The capital conservation buffer is designed to absorb losses during periods of economic stress. Banking institutions with a ratio of CET1 to risk-weighted assets above the minimum but below the conservation buffer (or below the combined capital conservation buffer and countercyclical capital buffer, when the latter is applied) will face constraints on dividends, equity repurchases and compensation based on the amount of the shortfall.

Under the Basel III Capital Rules, the following initial minimum capital ratios will be effective as of January 1, 2015:

4.5% CET1 to risk-weighted assets

6.0% Tier 1 capital to risk-weighted assets

8.0% Total capital to risk-weighted assets

The Basel III Capital Rules provide a number of deductions from and adjustments to CET1. These include, for example, the requirement that mortgage servicing rights, deferred tax assets arising from temporary differences that could not be realized through net operating loss carrybacks and significant investments in non-consolidated

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financial entities be deducted from CET1 to the extent that any one such category exceeds 10% of CET1 or all such categories in the aggregate exceed 15% of CET1. Under current capital standards, the effects of accumulated other comprehensive income (AOCI) items included in capital are excluded for the purposes of determining regulatory capital ratios. Under the Basel III Capital Rules, the effects of certain AOCI items are not excluded; however, non-advanced approaches banking organizations, including the Company and the Bank, may make a one-time permanent election to continue to exclude these items. The Company and the Bank expect to make this election to avoid significant changes in the level of capital depending upon the impact of interest rate fluctuations on the fair value of the Company s available-for-sale securities portfolio. The Basel III Capital Rules also prevent certain hybrid securities, such as trust preferred securities, as Tier 1 capital of bank holding companies, subject to phase-out. The rules do not require a phase-out of trust preferred securities issued before May 19, 2010, for holding companies of depository institutions with less than $15 billion in consolidated total assets, as of December 1, 2009, which includes the Company. Therefore, the Company s trust preferred securities that were issued before May 19, 2010, are permanently grandfathered in as Tier 1 or Tier 2 capital instruments,

Implementation of the deductions and other adjustments to CET1 will begin on January 1, 2015, and will be phased in over a four-year period (beginning at 40% on January 1, 2015, and an additional 20% per year thereafter). The implementation of the capital conservation buffer will begin on January 1, 2016, at 0.625% and will be phased in over a four-year period (increasing by that amount on each subsequent January 1, until it reaches 2.5% on January 1, 2019).

With respect to the Bank, the Basel III Capital Rules also revise the prompt corrective action regulations under Section 38 of the Federal Deposit Insurance Act, as discussed below under Prompt Corrective Action.

The Basel III Capital Rules prescribe a standardized approach for risk weightings that expand the risk-weighting categories from the current four Basel I-derived categories (0%, 20%, 50% and 100%) to a much larger and more risk-sensitive number of categories, depending on the nature of the assets, generally ranging from 0% for U.S. government and agency securities, to 600% for certain equity exposures, and resulting in higher risk weights for a variety of asset categories. The following changes, among others, to current rules that influence the Company s determination of risk-weighted assets include:

- applying a 150% risk weight (instead of a 100%) to certain high volatility commercial real estate acquisition, development, and construction loans;
- assigning a 150% risk weight to exposures (other than residential mortgage exposures) that are 90 days past due;
- providing for a 20% credit conversion factor for the unused portion of a commitment with an original maturity of one year or less that is not unconditionally cancellable (set at 0%);
- providing for a risk weight, generally not less than 20% with certain exceptions, for securities lending transactions based on the risk weight category of the underlying collateral securing the transaction;
- providing for a 100% risk weight for claims on securities firms; and
- eliminating the current 50% cap on the risk weight for OTC derivatives.

The Basel III Capital Rules provide more advantageous risk weights for derivatives and repurchase-style transactions cleared through a qualifying central counterparty and increase the scope of eligible guarantors and eligible collateral for purposes of credit risk mitigation. Management believes that, as of December 31, 2014, the Company and the Bank would meet all capital adequacy requirements under the Basel III Capital Rules on a fully phased-in basis as if such requirements were in effect.

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Liquidity Requirements

Historically, the regulation and monitoring of bank and bank holding company liquidity was addressed as a supervisory matter, without required formulaic measures. The Basel III liquidity framework requires banks and bank holding companies to measure their liquidity against specific liquidity tests that, although similar in some respects to liquidity measures historically applied by banks and regulators for management and supervisory purposes, going forward would be required by regulation. One test, referred to as the Liquidity Coverage Ratio (LCR), is designed to ensure that the banking entity maintains an adequate level of unencumbered high-quality liquid assets equal to the entity s expected net cash outflow for a 30-day time horizon (or, if greater, 25% of its expected total cash outflow) under an acute liquidity stress scenario. The other test, referred to as the Net Stable Funding Ratio (NSFR), is designed to promote more medium- and long-term funding of the assets and activities of banking entities over a one-year time horizon. These requirements will incent banking entities to increase their holdings of U.S. Treasury securities and other sovereign debt as a component of assets and increase long-term debt as a funding source. On September 3, 2014, the federal banking agencies finalized the rules implementing the LCR for advanced approaches banking organizations and a modified version of the LCR for bank holding companies with at least $50 billion in total consolidated assets that are not advanced approaches banking organizations, neither of which would apply to the Company or the Bank. The federal banking agencies have not yet proposed rules to implement the NSFR.

Incentive Compensation

In June 2010, the Federal Reserve, the Office of the Comptroller of the Currency (OCC), and the FDIC issued their final guidance on policies intended to ensure that the incentive compensation policies of banking organizations do not undermine the safety and soundness of such organizations by encouraging excessive risk taking. The final guidance, which covers all employees who have the ability to materially affect the risk profile of an organization, is based upon the key principles that a banking organization s incentive compensation arrangements should:

- provide incentives that do not encourage risk taking beyond the organization s ability to effectively identify and manage risks,
- comply with effective internal controls and risk management, and
- support strong corporate governance that includes active and effective oversight by the organization s board of directors.

The Federal Reserve indicated that all banking organizations are to evaluate their incentive compensation arrangements and related risk management, controls, and corporate governance processes and immediately address deficiencies in these arrangements or processes that are inconsistent with safety and soundness.

The Federal Reserve reviews, as part of their regular, risk-focused examination process, the incentive compensation arrangements of banking organizations, such as ours, that are not large, complex banking organizations. These reviews will be tailored to each organization based on the scope and complexity of the organization s activities and the prevalence of incentive compensation arrangements. The findings of the supervisory initiatives will be included in reports of examination. Deficiencies will be incorporated into the organization s supervisory ratings, which can affect the organization s ability to make acquisitions and take other actions. Enforcement actions may be taken against a banking organization if its incentive compensation arrangements, or related risk management control or governance processes, pose a risk to the organization s safety and soundness and the organization is not taking prompt and effective measures to correct the deficiencies.

In February 2011, the Federal Reserve, the OCC, and the FDIC approved a joint proposed rulemaking to implement Section 956 of the Dodd-Frank Act, which prohibits incentive-based compensation arrangements that encourage inappropriate risk taking by covered financial institutions and that are deemed excessive, or may lead to material losses.

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The scope and content of the U.S. banking regulators policies on executive compensation are continuing to develop and we expect those policies to continue evolving in the near future. It cannot be determined at this time whether compliance with such policies will adversely affect our ability to attract, hire, retain, and motivate key employees.

First Community Bank

The Bank is a Virginia state-chartered bank supervised and regulated by the Virginia Bureau of Financial Institutions (Virginia Bureau). As a member of the Federal Reserve, the Bank s primary federal regulator is the Federal Reserve Bank (FRB) of Richmond. The Virginia Bureau and FRB of Richmond are based in the Company s home state of Virginia. The regulations of these agencies govern most aspects of the Bank s business, including required reserves against deposits, loans, investments, mergers and acquisitions, borrowing, dividends, and location and number of branch offices.

Restrictions on Transactions with Affiliates and Insiders

Transactions between the Bank and its non-banking subsidiaries or affiliates, including the Company, are subject to Section 23A of the Federal Reserve Act the (FRA). In general, Section 23A imposes limits on the amount of such transactions, and requires certain levels of collateral for loans to affiliated parties. It also limits the amount of advances to third parties that are collateralized by the securities or obligations of the Company.

Affiliate transactions are also subject to Section 23B of the FRA that generally requires that certain transactions between the Bank and its affiliates be on terms substantially the same, or at least as favorable to the Bank, as those prevailing at the time for comparable transactions with or involving other non-affiliated persons. The Federal Reserve has issued Regulation W that codifies prior regulations under Sections 23A and 23B of the FRA and interpretive guidance with respect to affiliate transactions.

The Dodd-Frank Act generally enhances the restrictions on transactions with affiliates under Sections 23A and 23B of the FRA, including an expanded definition of covered transactions and increased amount of time for which collateral requirements on covered credit transactions must be satisfied. Insider transaction limitations are expanded through the strengthening of loan restrictions to insiders and the expansion of the types of transactions subject to the various limits, including derivatives transactions, repurchase agreements, reverse repurchase agreements, and securities lending or borrowing transactions. Restrictions are also placed on certain asset sales to and from an insider to an institution, such as the sales on market terms and, in certain circumstances, approved by the institution s board of directors.

The restrictions on loans to directors, executive officers, principal shareholders, and their related interests contained in the FRA and Regulation O apply to all insured institutions, their subsidiaries, and holding companies. These restrictions include limits on loans to one borrower and conditions that must be met before such a loan can be made. There is also an aggregate limitation on all loans to such persons. These loans cannot exceed the institution s total unimpaired capital and surplus, and the FDIC may determine that a lesser amount is appropriate.

Restrictions on Distribution of Subsidiary Bank Dividends and Assets

The Company s primary source of operating funds is dividends paid by the Bank. Capital adequacy requirements that apply to insured depository institutions serve to limit the amount of dividends that may be paid by the Bank. Under federal law, the Bank cannot pay a dividend if, after paying the dividend, it will be classified as undercapitalized. Further, prior approval of the FRB is required if cash dividends declared in any given year exceed the total of the Bank s net profits for such year, plus its retained profits for the preceding two years. Virginia law also imposes restrictions on the ability of Virginia-chartered banks to pay dividends if such dividends would impair a bank s paid-in capital. The payment of dividends by the Bank may also be limited by other factors, such as requirements to maintain capital above regulatory guidelines. The Virginia Bureau and the FRB of Richmond have the general authority to limit dividends paid by the Bank if such payments are deemed to constitute an unsafe and unsound practice.

Because the Company is a legal entity separate and distinct from its subsidiaries, its right to participate in the distribution of assets of any subsidiary upon the subsidiary s liquidation or reorganization will be subject to the prior claims of the subsidiary s creditors. In the event of liquidation or other resolution of an insured depository institution, such as the Bank, the claims of depositors and other general or subordinated creditors are entitled to a priority of payment over the claims of holders of any obligation of the institution to its shareholders, including any depository institution holding company or any shareholder or creditor thereof.

Examinations

Under the FDIC Improvement Act, all insured institutions must undergo regular on-site examination by their appropriate banking agency and such agency may assess the institution for its costs of conducting the examination. As a state-chartered Federal Reserve member bank, the Bank is subject to examination by the Virginia Bureau and FRB of Richmond. These examinations review areas such as capital adequacy, reserves, loan portfolio quality, investments, information systems, disaster recovery, contingency planning, management practices, and other compliance issues.

Capital Adequacy Requirements

The various federal bank regulatory agencies have adopted risk-based capital requirements for assessing the capital adequacy of banks and bank holding companies. The federal capital standards define capital and establish minimum capital requirements in relation to assets and off-balance sheet exposure, as adjusted for credit risk. The risk-based capital standards in effect are designed to make regulatory capital requirements more sensitive to differences in risk profile among bank holding companies and banks, to account for off-balance sheet exposure and to minimize disincentives for holding liquid assets. Assets and off-balance sheet items are assigned to broad risk categories, each with appropriate risk weights. The resulting capital ratios represent capital as a percentage of total risk-weighted assets and off-balance sheet items.

As required by the Federal Reserve s risk-based capital requirements, state member banks must meet a minimum ratio of Tier 1 capital to total risk-weighted assets of 4.0% and a ratio of total capital to total risk-weighted assets of 8.0%. The capital categories for the Bank are the same as those for the Company. In addition to the risk-based capital requirements, the Federal Reserve has adopted regulations that supplement the risk-based guidelines to include a minimum leverage ratio of Tier 1 capital to quarterly average assets of 3.0%. The Federal Reserve has stressed that the foregoing standards are supervisory minimums and that a banking organization will be permitted to maintain such minimum levels of capital only if it receives the highest rating under the regulatory rating system and the banking organization is not experiencing or anticipating significant growth. All other banking organizations are required to maintain a leverage ratio of at least 4.0% to 5.0% of Tier 1 capital. See Capital Adequacy Requirements in the First Community Bancshares, Inc. section above.

Corrective Measures for Capital Deficiencies

The federal banking regulators are required to take prompt corrective action with respect to capital-deficient institutions. Agency regulations define, for each capital category, the levels at which institutions are well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized, and critically undercapitalized. A well-capitalized institution has a total risk-based capital ratio of 10.0% or higher, a Tier 1 risk-based capital ratio of 6.0% or higher, a leverage ratio of 5.0% or higher, and is not subject to any written agreement, order, or directive requiring it to maintain a specific capital level for any capital measure. An adequately capitalized institution has a total risk-based capital ratio of 8.0% or higher, a Tier 1 risk-based capital ratio of 4.0% or higher, a leverage ratio of 4.0% or higher (3.0% or higher if the bank was rated a composite 1 in its most recent examination report and is not experiencing significant growth), but does not meet the criteria for a well-capitalized bank. An undercapitalized institution has a total risk-based capital ratio that is less than 8.0%, a Tier 1 risk-based capital ratio of less than 4.0%, or a leverage ratio of less than 4.0%. A significantly undercapitalized institution has a total risk-based capital ratio of less than 6.0%, a Tier 1 risk-based capital ratio of less than 3.0%, or a leverage ratio of less than 3.0%. A critically undercapitalized institution s tangible equity is equal to or less than 2.0% of average quarterly tangible assets. An institution may be downgraded to, or deemed to be in, a capital category that is lower than indicated by its capital ratios if it is considered to be in an unsafe or unsound condition or if it receives an unsatisfactory examination rating with respect to certain matters. A bank s capital category is determined solely for applying prompt corrective action regulations, and the capital category may not constitute an accurate representation of the bank s financial condition or prospects for other purposes. The Bank was classified as well capitalized for purposes of the FDIC s prompt corrective action regulation as of December 31, 2014.

The Basel III Capital Rules revise the current prompt corrective action requirements effective January 1, 2015 by:

- introducing a CET1 ratio requirement at each level (other than critically undercapitalized), with the required CET1 ratio being 6.5% for well-capitalized status;

- increasing the minimum Tier 1 capital ratio requirement for each category (other than critically undercapitalized), with the minimum Tier 1 capital ratio for well-capitalized status being 8% (as compared to the current 6%); and

- eliminating the current provision that provides that a bank with a composite supervisory rating of 1 may have a 3% leverage ratio and still be adequately capitalized.

The Basel III Capital Rules do not change the total risk-based capital requirement for any prompt corrective action category.

In addition to requiring undercapitalized institutions to submit a capital restoration plan, agency regulations contain broad restrictions on certain activities of undercapitalized institutions, including asset growth, acquisitions, branch establishment, and expansion into new lines of business. With certain exceptions, an insured depository institution is prohibited from making capital distributions, including dividends, and is prohibited from paying management fees to control persons if the institution would be undercapitalized after any such distribution or payment.

As an institution s capital decreases, the federal regulators enforcement powers become more severe. A significantly undercapitalized institution is subject to mandated capital raising activities, restrictions on interest rates paid and transactions with affiliates, removal of management, and other restrictions. The FDIC has limited discretion in dealing with a critically undercapitalized institution and is generally required to appoint a receiver or conservator. Banks with risk-based capital and leverage ratios below the required minimums may be subject to certain administrative actions, including termination of deposit insurance upon notice and hearing or temporary suspension of insurance without a hearing if the institution has no tangible capital.

Deposit Insurance Assessments

The Bank s deposits are insured up to applicable limits by the DIF of the FDIC and are subject to deposit insurance assessments to maintain the DIF. The FDIC uses a risk-based assessment system to evaluate the risk of each financial institution based on three primary sources of information: its supervisory rating, its financial ratios, and its long-term debt issuer rating, if the institution has one. The FDIC s initial base assessment schedule can be adjusted up or down, and premiums in effect beginning April 1, 2011, ranged from 5 basis points in the lowest risk category to 35 basis points for banks in the highest risk category.

The Dodd-Frank Act requires the FDIC to increase the DIF s reserves against future losses, which will require increased deposit insurance premiums that are to be borne primarily by institutions with assets of greater than $10 billion. In October 2010, the FDIC addressed plans to bolster the DIF by increasing the required reserve ratio for the industry to 1.35% (ratio of reserves to insured deposits) by September 30, 2020, as required by the Dodd-Frank Act. The FDIC also proposed to raise its industry target ratio of reserves to insured deposits to 2.00%, 65 basis points above the statutory minimum.

In February 2011, the FDIC adopted new rules that amend its current deposit insurance assessment regulations. The new rules implement a provision in the Dodd-Frank Act that changed the assessment base for deposit insurance premiums from one based on domestic deposits to one based on average consolidated total assets minus average tangible equity. The rules also changed the assessment rate schedules for insured depository institutions so that approximately the same amount of revenue would be collected using the new assessment base as would be collected using the current rate schedule and the schedules previously proposed by the FDIC in October 2010. The new rules also revised the risk-based assessment system for large insured depository institutions, which generally include institutions with at least $10 billion in total assets and highly complex institutions, by requiring the FDIC to use a scorecard method to calculate assessment rates for all such institutions. The Bank is not considered a highly complex institution for these purposes.

Under the Federal Deposit Insurance Act, as amended (FDIA), the FDIC may terminate deposit insurance upon a finding that the institution has engaged in unsafe and unsound practices, is in an unsafe or unsound condition to continue operations, or has violated any applicable law, regulation, rule, order, or condition imposed by the FDIC.

In addition to deposit insurance assessments by the DIF, all FDIC-insured depository institutions must pay an annual assessment to provide funds for the repayment of debt obligations of the Financing Corporation (FICO). The FICO is a government-sponsored entity that was formed to borrow the money necessary to carry out the closing and ultimate disposition of failed thrift institutions by the Resolution Trust Corporation. The Bank s FICO assessments, which are set quarterly, totaled $147 thousand in 2014 and $154 thousand in 2013. The Bank s FDIC deposit insurance assessments and premiums totaled $1.59 million in 2014 and $1.72 million in 2013.

Safety and Soundness Standards

The FDIA requires that the federal bank regulatory agencies prescribe standards, by regulations or guidelines, relating to internal controls, information and internal audit systems, loan documentation, credit underwriting, interest rate risk exposure, asset growth, asset quality, earnings, stock valuation and compensation, fees and benefits, and other operational and managerial standards the agencies deem appropriate. Guidelines adopted by the federal bank regulatory agencies establish general standards relating to internal controls and information systems, internal audit systems, loan documentation, credit underwriting, interest rate exposure, asset growth and compensation, fees and benefits. In general, the guidelines require, among other things, appropriate systems and practices to identify and manage the risk and exposures specified in the guidelines. The guidelines prohibit excessive compensation as an unsafe and unsound practice and describe compensation as excessive when the amounts paid are unreasonable or disproportionate to the services performed by an executive officer, employee, director, or principal stockholder. The agencies adopted regulations that authorize them to order an institution that has been given notice by an agency not satisfying any of such safety and soundness standards to submit a compliance plan. If an institution fails to submit an acceptable compliance plan or fails in any material respect to implement an acceptable compliance plan, after being so notified, the agency must issue an order directing action to correct the deficiency and may issue an order directing other actions of the types to which an undercapitalized institution is subject under the prompt corrective action provisions of the FDIA. If an institution fails to follow such an order, the agency may seek to enforce such order in judicial proceedings and to impose civil money penalties. See Corrective Measures for Capital Deficiencies in the Bank section above.

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Enforcement Powers

The FDIC and the other federal banking agencies have broad enforcement powers, including the power to terminate deposit insurance, impose substantial fines and other civil and criminal penalties, and appoint a conservator or receiver. Failure to follow applicable laws, regulations, and supervisory agreements could subject us, including officers, directors, and other institution-affiliated parties, to administrative sanctions and potentially substantial civil money penalties. The appropriate federal banking agency may appoint the FDIC as conservator or receiver for a banking institution (or the FDIC may appoint itself, under certain circumstances) if certain circumstances exist, including, without limitation, the banking institution is undercapitalized and has no reasonable prospect of becoming adequately capitalized; fails to become adequately capitalized when required to do so; fails to submit a timely and acceptable capital restoration plan; or materially fails to implement an accepted capital restoration plan.

Consumer Laws and Regulations

In addition to the laws and regulations discussed in this report, the Bank is also subject to certain consumer laws and regulations that are designed to protect consumers in transactions with banks. While the list set forth is not exhaustive, these laws and regulations include the Truth in Lending Act, the Home Mortgage Disclosure Act, the Electronic Funds Transfer Act, the Expedited Funds Availability Act, the Equal Credit Opportunity Act, the Fair Credit Reporting Act, the Right to Financial Privacy Act, the Fair Housing Act, and various state counterparts. These laws and regulations mandate certain disclosure requirements and regulate the manner in which financial institutions must deal with customers when taking deposits or making loans to such customers. The Bank must follow the applicable provisions of these consumer protection laws and regulations as part of their ongoing customer relations.

Federal law contains extensive customer privacy protection provisions. Under these provisions, a financial institution must provide to its customers, at the start of the customer relationship and annually thereafter, the institution s policies and procedures regarding the handling of customers nonpublic personal financial information. These provisions also provide that, except for certain limited exceptions, a financial institution may provide such personal information to unaffiliated third parties only if the institution discloses to the customer that such information may be so provided and the customer is given the opportunity to opt out of such disclosure.

The Dodd-Frank Act centralized responsibility for consumer financial protection by creating the CFPB, which implements, examines, and enforces compliance with federal consumer protection laws. The CFPB has broad rulemaking, supervisory and enforcement authority over consumer financial products and services, including deposit products, residential mortgages, home-equity loans, and credit cards. The CFPB s functions include investigating consumer complaints, rulemaking, supervising and examining banks consumer transactions, and enforcing rules related to consumer financial products and services. Banks with less than $10 billion in assets, such as the Bank, will be subject to these federal consumer financial laws and will continue to be examined for compliance with these laws by their primary federal banking agency.

Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act

The Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001 (USA Patriot Act) was enacted in October 2001. The USA Patriot Act has broadened existing anti-money laundering legislation while imposing new compliance and due diligence obligations on banks and other financial institutions, with a particular focus on detecting and reporting money laundering transactions involving domestic or international customers. The U.S. Department of the Treasury (Treasury) has issued and will continue to issue regulations clarifying the USA Patriot Act s requirements. The USA Patriot Act requires all financial institutions, as defined, to establish certain anti-money laundering compliance and due diligence programs. Recently, the regulatory agencies have intensified their examination procedures of the USA

Patriot Act s anti-money laundering and Bank Secrecy Act requirements. We believe our controls and procedures complied with the USA Patriot Act as of December 31, 2014.

Interstate Banking and Branching

Federal banking agencies are authorized to approve interstate bank merger transactions without regard to whether the transaction is prohibited by the law of any state, unless the home state of one of the banks has opted out of the interstate bank merger provisions of the Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994, as amended, (Riegle-Neal Act) or by adopting a law after the date of enactment of the Riegle-Neal Act and before June 1, 1997, that applies equally to all out-of-state banks and expressly prohibits merger transactions involving out-of-state banks. Interstate acquisitions of branches are permitted only if the law of the state in which the branch is located permits such acquisitions. Such interstate bank mergers and branch acquisitions are also subject to the nationwide and statewide insured deposit concentration limitations described in the Riegle-Neal Act.

Before the enactment of the Dodd-Frank Act, national and state-chartered banks were generally permitted to branch across state lines by merging with banks in other states if allowed by the applicable states laws. However, interstate branching is now permitted for all national and state-chartered banks as a result of the Dodd-Frank Act, provided that a state bank chartered by the state in which the branch is to be located would also be permitted to establish a branch, thus effectively giving out-of-state banks parity with in-state banks with respect to de novo branching.

Item 1A. Risk Factors.

The risk factors described below discuss potential events, trends, or other circumstances that could adversely affect our business, financial condition, results of operations, cash flows, liquidity, access to capital resources, and, consequently, cause the market value of our common stock to decline. These risks could cause our future results to differ materially from historical results and expectations of future financial performance. If any of the risks occur and the market price of our common stock declines significantly, individuals may lose all, or part, of their investment in our Company. Individuals should carefully consider our risk factors and the additional information included in, or incorporated by reference to, this report before making an investment decision. There may be risks and uncertainties that we have not identified or that we have deemed immaterial that could adversely affect our business; therefore, the following risk factors are not intended to be an exhaustive list of all risks we face. All forward-looking statements are qualified by the risks described below.

Risks Related to Our Business

The current economic environment poses significant challenges.

From December 2007 through June 2009, the U.S. economy faced a severe economic crisis and experienced the worst economic downturn since the Great Depression of the 1930s. Although the domestic economy continued a modest recovery in 2014, business activity across a wide range of industries and regions in the U.S. continues to remain reduced and local governments and many businesses continue to experience financial difficulty. While reflecting some improvement, unemployment levels remain elevated. There can be no assurance that these conditions will continue to improve nor that these conditions will not worsen.

Our financial performance is generally highly dependent upon the business environment in the markets we operate and the U.S. as a whole, which includes the ability of borrowers to pay interest, repay principal on outstanding loans, the value of collateral securing those loans, and demand for loans and other products and services we offer. A favorable business environment is generally characterized by, among other factors, economic growth, efficient capital markets, low inflation, low unemployment, high business and investor confidence, and strong business earnings. Unfavorable or uncertain economic and market conditions can be caused by declines in economic growth, business activity, investor or business confidence; limitations on the

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availability, or increases, in the cost of credit and capital; increases in inflation or interest rates; high unemployment; natural disasters; or a combination of these or other factors.

During recent years, the business environment has been adverse for many households and businesses in the U.S. and worldwide. Although economic conditions have improved since the recession, there can be no assurance that this improvement will continue. Economic pressure on consumers and uncertainty about continuing economic improvement may result in changes in consumer and business spending, borrowing, and savings habits. Such

conditions could adversely affect the credit quality of the Bank s loans and the Company s business, financial condition, and results of operations.

We are subject to interest rate risk.

Our earnings and cash flows are largely dependent upon net interest income. Net interest income is the difference between interest income earned on interest-earning assets, such as loans and securities, and interest expense paid on interest-bearing liabilities, such as deposits and borrowed funds. Interest rates are highly sensitive to many factors that are beyond our control, including general economic conditions and policies of various governmental and regulatory agencies, particularly, the Federal Reserve. Changes in monetary policy and interest rates could influence the interest we receive on loans and securities and the amount of interest we pay on deposits and borrowings. Further, such changes could also affect our ability to originate loans and obtain deposits and the fair value of our financial assets and liabilities. If the interest rates paid on deposits and other borrowings increase at a faster rate than the interest rates received on loans and other investments, our net interest income and earnings could be adversely affected. Conversely, if interest rates received on loans and other investments fall more quickly than interest rates paid on deposits and other borrowings, our net interest income and earnings could also be adversely affected.

Our estimated allowance for loan losses may not be adequate to cover actual losses.

Like all financial institutions, we maintain an allowance for loan losses to provide for probable loan losses. Our allowance may not be adequate to cover actual loan losses, and future loan loss provisions could materially and adversely affect our operating results. The appropriate level of the allowance is determined by management and inherently involves a high degree of subjectivity and significant estimates of current credit risks and future trends, which may undergo material changes. Our allowance is determined by analyzing historical loan losses, current trends in delinquencies and charge-offs, plans for problem loan resolution, changes in the size and composition of the loan portfolio, and industry information. Management s estimates also include considerations about the impact of economic events, which are uncertain. Future losses are susceptible to changes in economic, operating, and other conditions, including changes in interest rates, which may be beyond our control, and charge-offs may exceed our current estimates. Federal regulatory agencies regularly review our loans and allowance for loan losses as an integral part of the examination process. We believe our allowance for loan losses is adequate to provide for probable losses. There is no assurance that we will not, or that regulators will not require us to, increase our allowance in future periods, which could materially and adversely affect our earnings and profitability.

Non-covered nonperforming assets were $19.92 million as of December 31, 2014, $27.79 million as of December 31, 2013, and $35.69 million as of December 31, 2012. We incurred net charge-offs of $2.89 million in 2014, $10.35 million in 2013, and $6.11 million in 2012. Our allowance for loan losses was $20.23 million as of December 31, 2014, $24.08 million as of December 31, 2013, and $25.77 million as of December 31, 2012. Our provision for loan losses charged to operations was $145 thousand in 2014, $8.21 million in 2013, and $5.68 million in 2012. A provision recovery was realized for purchased credit impaired (PCI) loans of $697 thousand in 2014, which included a recovery of $275 thousand included in the provision charged to operations and $422 thousand was recorded through the FDIC indemnification asset. The provision attributed to PCI loans was $747 thousand in 2013, of which $296 thousand was included in the provision charged to operations and $451 thousand was recorded through the FDIC indemnification asset. There was no provision before 2013 for PCI

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loans. As of December 31, 2014, the allowance attributed to non-PCI loans as a percentage of non-covered nonperforming loans was 151.85% and the allowance attributed to non-PCI loans as a percentage of total non-covered loans was 1.29%. If nonperforming assets or net charge-offs increase in future periods, we may be required to increase our allowance for loan losses, which could have an adverse effect on our future results of operations.

Our level of credit risk may increase due to our focus on commercial, small business, and middle market customers who may have significant vulnerability to economic conditions.

Commercial business and real estate loans are generally considered riskier than single family residential loans because larger balances are extended to single borrowers or groups of related borrowers. Commercial business and real estate loans involve risks because the borrowers ability to repay the loans typically depends on the success of the business operations or the properties securing the loans. The majority of our commercial business loans are made to small business or middle market customers. Commercial business and real estate loans made or acquired in recent years may not have experienced a complete business or economic cycle. As of December 31, 2014, our commercial business loans totaled $87.40 million, or 5.17% of our total loan portfolio, and our commercial real estate loans totaled $769.61 million, or 45.55% of our total loan portfolio. As of the same date, our largest outstanding commercial business loan was $7.00 million and largest outstanding commercial real estate loan was $11.32 million.

In addition to commercial business and real estate loans, we hold a portfolio of commercial construction loans. Construction loans generally have a higher risk of loss primarily due to the critical nature of certain assumptions and estimates used to value the initial property value upon completion of construction compared to the estimated costs, including interest. If estimates prove inaccurate, final property values may fall below related loan amounts. As of December 31, 2014, our commercial construction loans totaled $54.37 million, or 3.22% of our total loan portfolio. As of the same date, our largest outstanding commercial construction loan was $6.70 million.

We may suffer losses in our loan portfolio despite our underwriting practices.

We seek to mitigate the risks inherent in our loan portfolio by adhering to specific underwriting practices. These practices include the analysis of borrowers prior credit histories, financial statements, tax returns, and cash flow projections; valuation of collateral based on independent appraisers reports; and verification of liquid assets. We believe our underwriting criteria are appropriate for the various loan types we offer; however, losses may occur that exceed the reserves established in our allowance for loan losses.

Changes in the fair value of our investment securities may reduce stockholders equity and net income.

Changes in unrealized gains and losses on available-for-sale securities, net of the related tax effect, impact stockholders equity through AOCI. The unrealized gain or loss represents the difference between the estimated fair value and the amortized cost of the securities. A decline in the estimated fair value of the portfolio results in a decline in stockholders equity, book value per common share, and tangible book value per common share. The decrease is recorded even though the securities are not sold or held for sale. If a debt security is never sold and no credit impairment exists, the decrease is recovered at the security s maturity. Equity securities have no stated maturity; therefore, declines in fair value may or may not be recovered over time. As of December 31, 2014, the fair value of securities available for sale was $326.12 million and the aggregate unrealized losses on those securities were $12.26 million.

We conduct quarterly reviews of our securities portfolio to determine if the declines are other-than-temporary. We consider the following factors in our analysis of debt securities: our intent to sell the securities, the evidence available to determine if it is more likely than not that we will have to sell the securities before recovery of the amortized cost, and the probable credit losses. Probable credit losses are evaluated using the present value of future cash flows; the severity and duration of the decline in fair value below amortized cost; the financial condition and near-term prospects of the issuer; whether the decline is related to issuer conditions, general market, or industry conditions; the payment structure; the failure to make scheduled interest or principal payments; and changes to the securities rating by rating agencies. Decreases in the fair value of debt securities caused by changes in interest rates are generally considered temporary, which is consistent with our experience. If we determine that fair value decreases are other-than-temporary, the security is written down to a new cost basis and the resulting loss is charged to earnings as a component of noninterest income. We recognized other-than-temporary impairment (OTTI) charges of $705 thousand in our debt securities portfolio in 2014.

Factors we consider in our analysis of equity securities include: our intent to sell the security before recovery of the cost; the severity and duration of the decline in fair value below cost; the financial condition and near-term prospects of the issuer; and whether the decline appears to be related to issuer conditions, general market, or industry conditions. We recognized OTTI charges of $32 thousand in our equity securities portfolio in 2014.

We continue to monitor the fair value of our securities portfolio as part of our ongoing OTTI evaluation process. No assurance can be given that we will not need to recognize OTTI charges in the future. Additional OTTI charges may materially affect our financial condition and earnings.

We are subject to extensive regulation, possible enforcement, and other legal action.

We operate in a highly regulated industry subject to examination, supervision, and comprehensive regulation by various federal and state governmental authorities, laws, and judicial and administrative decisions that impose requirements and restrictions on our operations. Banking regulations are primarily intended to protect depositors funds, federal deposit insurance funds, and the banking system as a whole, not stockholders. Congress and federal regulatory agencies continually review banking laws, regulations, and policies for possible changes. Changes to statutes, regulations, and regulatory policies, including changes in the interpretation or implementation, may cause substantial and unpredictable effects, require additional costs, limit the types of financial services and products offered, or allow non-banks to offer competing financial services and products. The Dodd-Frank Act, enacted in July 2010, instituted major changes to banking and financial institutions regulatory regimes. Failure to follow laws, regulations, and policies may result in sanctions by regulatory agencies and civil money penalties, which could have material adverse effects on our reputation, business, financial condition, and results of operations. We have policies and procedures designed to prevent violations; however, there is no assurance that violations will not occur. Existing and future laws, regulations, and policies yet to be adopted may make compliance more difficult or expensive; restrict our ability to originate, broker, or sell loans; further limit or restrict commissions, interest, and other charges earned on loans we originate or sell; and adversely affect our business, financial condition, and results of operations.

The Bank s ability to pay dividends is subject to regulatory limitations, to the extent such dividends are required, that may affect the Company s ability to pay expenses and dividends to shareholders.

The Company is a separate legal entity from the Bank. The Company depends on its other subsidiaries and the Bank s cash, liquidity, and payment of dividends to the Company to pay operating expenses and dividends to stockholders. There is no assurance that the Bank will have the capacity to pay dividends to the Company in the future or that the Company will not require dividends from the Bank to satisfy obligations. The Bank s dividend payment is governed by various statutes and regulations. Depending on factors such as the Bank s financial condition, the FRB of Richmond or the Virginia Bureau, the Bank s primary regulators, may deem dividends or other payments an unsafe or unsound practice. The Company may not be able to service obligations as they become due if the Bank is unable to pay dividends sufficient to satisfy the Company s obligations, including required payments to the Trust or dividends on our Series A Noncumulative Convertible Preferred Stock (Series A Preferred Stock) or our common stock. Consequently, the inability to receive dividends from the Bank could adversely affect the Company s financial condition, results of operations, cash flows, and prospects.

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We face strong competition from other financial institutions, financial service companies, and organizations that offer services similar to our offerings.

We primarily conduct our operations in Virginia, West Virginia, North Carolina, and Tennessee. We may be unsuccessful against current and future competitors in regions that offer products and services similar to those we offer; therefore, increased competition may result in reduced loan originations and deposits. Our competitors include savings associations, national banks, regional banks, and community banks. We also face competition from finance companies, brokerage firms, insurance companies, credit unions, mortgage banks, and other financial intermediaries. In particular, our competitors include state and national banks and major financial companies with resources that may provide a marketplace advantage by expanding and maintaining numerous banking locations and mounting extensive promotional and advertising campaigns.

Financial institutions with larger capitalization and financial intermediaries not subject to bank regulatory restrictions have higher lending limits that enable them to serve the credit needs of larger clients and, to the extent they are more diversified than us, may be able to offer the same products and services at more competitive rates and prices. If we are unable to attract and retain banking clients, our loan and deposit growth, general business, financial condition, and prospects may be negatively affected.

Potential acquisitions may disrupt our business and dilute stockholder value.

We may seek merger or acquisition partners that are culturally similar, have experienced management, and possess either significant market presence or the potential for improved profitability through financial management, economies of scale, or expanded services. Risks inherent in acquiring other banks, businesses, and banking branches may include the following:

- potential exposure to unknown or contingent liabilities of the target company;
- exposure to potential asset quality issues of the target company;
- difficulty, expense, and delays of integrating the operations and personnel of the target company;
- potential disruption to our business;
- potential diversion of management s time and attention;
- loss of key employees and customers of the target company;
- difficulty in estimating the value of the target company;
- potential changes in banking or tax laws or regulations that may affect the target company;
- unexpected costs and delays;
- the target company s performance does not meet our growth and profitability expectations;

limited experience in new markets or product areas;

increased time, expenses, and personnel as a result of strain on our infrastructure, staff, internal controls, and management; and

potential short-term decreases in profitability.

We regularly evaluate merger and acquisition opportunities and conduct due diligence activities related to possible transactions with other financial institutions and financial services companies. As a result, merger or acquisition discussions and, in some cases, negotiations may take place and future mergers or acquisitions involving the payment of cash or the issuance of debt or equity securities may occur at any time. Acquisitions

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typically involve goodwill, a purchase premium over the acquired company s book and market values; therefore, dilution of our tangible book value and net income per common share may occur. If we are unable to realize revenue increases, cost savings, geographic or product presence growth, or other projected benefits from acquisitions; our financial condition and results of operations may be adversely affected.

We may engage in FDIC-assisted transactions.

We may acquire assets and liabilities of failed financial institutions that are in FDIC receivership. FDIC-assisted acquisitions include risks inherent in acquiring other banks, businesses, and banking branches, as well as risks specific to each transaction. FDIC-assisted acquisitions generally provide limited diligence and term negotiation and may require additional resources, expenses, and time to service acquired loans, including PCI loans, integrate personnel and operating systems, and establish processes to service acquired assets. Acquisitions may also require us to raise additional capital that could have a dilutive effect on existing stockholders. If we are unable to manage these risks, FDIC-assisted acquisitions could have a material adverse effect on our business, financial condition, and results of operations.

Our ability to receive benefits under FDIC loss share agreements is subject to compliance with certain requirements, oversight and interpretation, and contractual term limitations.

We receive benefits under loss share agreements in connection with the FDIC-assisted acquisition of Waccamaw Bank (Waccamaw) in June 2012. Under these loss share agreements, the FDIC agreed to cover 80% of most loans and foreclosed real estate losses. Loans covered under the agreements represented 7.24% of our total loans held for investment as of December 31, 2014, compared to 13.21% as of June 30, 2012. We are subject to certain obligations under the agreements that prescribe and specify how to manage, service, report, and request reimbursement for losses incurred on covered assets. Our obligations under the loss share agreements are extensive, and failure to follow any obligations could result in a specific asset, or group of assets, losing loss share coverage. Reimbursement requests are subject to FDIC review and may be delayed or disallowed if we do not comply with our obligations. Losses projected to occur during the loss share term may not be realized until after the expiration of the applicable agreement; consequently, those losses may have a material adverse impact on our results of operations. Our current loss estimates only include those projected to occur during the loss share period we expect reimbursement from the FDIC at the applicable reimbursement rate. We are subject to FDIC audits to ensure compliance with the loss share agreements. The loss share agreements are subject to interpretation by the FDIC and us; therefore, disagreements about the coverage of losses, expenses, and contingencies may arise.

Our accounting estimates and risk management processes rely on analytical and forecasting models.

The processes we use to estimate probable loan losses and to measure the fair value of financial instruments, as well as the processes used to estimate the effects of changing interest rates and other market measures on our financial condition and results of operations, depends upon analytical and forecasting models. These models reflect assumptions that may not be accurate, particularly in times of market stress or other unforeseen circumstances. Even if these assumptions are adequate, the models may prove to be inadequate or inaccurate because of other flaws in their design or their implementation. If the models we use for interest rate risk and asset-liability management are inadequate, we may incur increased or unexpected losses upon changes in market interest rates or other market measures. If the models used for determining probable loan losses are inadequate, the allowance for loan losses may not be sufficient to support future charge-offs. If the models we use to measure the fair value of financial instruments are inadequate, the fair value of such financial instruments may fluctuate unexpectedly or may not accurately reflect what we could realize upon the sale or settlement of such financial instruments. Any such failure in our analytical or forecasting models could have a material adverse effect on our business, financial condition, and results of operations.

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The repeal of the federal prohibitions on payment of interest on demand deposits could increase our interest expense.

All federal prohibitions on the ability of financial institutions to pay interest on demand deposit accounts were repealed as part of the Dodd-Frank Act beginning on July 21, 2011. As a result, some financial institutions have commenced offering interest on demand deposits to compete for customers. We do not yet know what interest rates other institutions may offer as market interest rates begin to increase. Our interest expense will increase and net interest margin will decrease if we begin offering interest on demand deposits to attract additional customers or maintain current customers, which could have a material adverse effect on our business, financial condition, and results of operations.

Attractive acquisition opportunities may not be available in the future.

We expect banking and financial companies, many with significantly greater resources, to compete for the acquisition of financial services businesses. This competition could increase the price of potential acquisitions that we believe are attractive. If we fail to receive proper regulatory approval, we will not be able to consummate an acquisition. Our regulators consider our capital, liquidity, profitability, regulatory compliance, level of goodwill and intangible assets, and other factors when considering acquisition and expansion proposals. Future acquisitions may be dilutive to our earnings and equity per share of our common stock and Series A Preferred Stock.

Our goodwill may be determined to be impaired.

As of December 31, 2014, our carrying balance of goodwill was $100.72 million. We test goodwill for impairment annually, or more often if necessary, using quantitative and qualitative factors. When available, quoted market prices in active markets are the best evidence of fair value and are used as the basis for measuring impairment. Other acceptable valuation methods include present value measurements based on multiples of earnings, revenues, or similar performance measures. If the carrying amount of goodwill exceeds its implied fair value, goodwill is determined to be impaired. Impairment charges may cause an adverse effect on our earnings and financial position. We recognized no goodwill impairment in 2014.

We may lose members of our management team and have difficulty attracting skilled personnel.

Our success depends, in large part, on our ability to attract and retain key people. Competition for the best people can be intense. The unexpected loss of key personnel could have a material adverse impact on our business due to the loss of certain skills, market knowledge, and industry experience and the difficulty of promptly finding qualified replacement personnel. Certain existing and proposed regulatory guidance on compensation may also negatively affect our ability to retain and attract skilled personnel.

We may be required to pay higher FDIC insurance premiums or special assessments.

Our deposits are insured up to applicable limits by the FDIC s DIF and we are subject to deposit insurance premiums and assessments to maintain deposit insurance. We are unable to predict future insurance assessment rates; however, deterioration in our risk-based capital ratios or adjustments to base assessment rates may result in higher insurance premiums or special assessments. The deterioration of banking and economic conditions and financial institution failures deplete the FDIC s DIF and reduce the ratio of reserves to insured deposits. If the DIF is unable to meet funding requirements, increases in deposit insurance premium rates or special assessments may also be required. Future assessments, increases, or required prepayments related to FDIC insurance premiums may negatively affect our financial condition and results of operations.

We may require additional capital in the future that may not be available when needed.

We may need to raise additional capital in the future to strengthen our capital position, increase our liquidity, satisfy obligations, or pursue growth objectives. Our ability to raise additional capital depends on current conditions in capital markets, which are outside our control, and our financial performance. Certain economic conditions and declining market confidence may increase our cost of funds and limit our access to customary sources of capital, such as borrowings with other financial institutions, repurchase agreements, and availability under the FRB s discount window. Events that limit access to capital markets and the inability to obtain capital may have a materially adverse effect on our business, financial condition, results of operations, and market value of common stock. We cannot provide any assurance that additional capital will be available, on acceptable terms or at all, in the future.

Liquidity risk could impair our ability to fund operations.

Liquidity is essential to our business and the inability to raise funds through deposits, borrowings, equity and debt offerings, or other sources could have a materially adverse effect on our liquidity. Company specific factors such as a decline in our credit rating, an increase in the cost of capital from financial capital markets, a decrease in business activity due to adverse regulatory action or other company specific event, or a decrease in depositor or investor confidence may impair our access to funding with acceptable terms adequate to finance our activities. General factors related to the financial services industry such as a severe disruption in financial markets, a decrease in industry expectations, or a decrease in business activity due to political or environmental events may impair our access to liquidity.

We are subject to credit risk associated with the financial condition of other financial institutions.

Financial institutions are interrelated as a result of trading, clearing, counterparty, and other relationships. We have exposure to different industries and counterparties, and we routinely execute transactions with counterparties in the financial services industry, including brokers and dealers, commercial banks, investment banks, investment companies, and other institutional clients. Our ability to engage in routine funding transactions could be adversely affected by the failure, actions, and commercial soundness of other financial institutions. These transactions may expose us to credit risk if our counterparty or client defaults on their contractual obligation. Our credit risk may increase if the collateral we hold cannot be realized or liquidated at prices sufficient to recover the full amount of the loan or derivative exposure due to us. In the event of default, we may be required to provide collateral to secure the obligation to the counterparties. In the event of a bankruptcy or insolvency proceeding involving one of such counterparties, we may experience delays in recovering the assets posted as collateral or may incur a loss to the extent that the counterparty was holding collateral in excess of the obligation to such counterparty. Losses from routine funding transactions could have a material adverse effect on our financial condition and results of operations.

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

A significant portion of our loan portfolio is secured by real property. In the ordinary course of business, we foreclose on and take title to properties that secure certain loans. Hazardous or toxic substances could be found on properties we own. If substances are present, we may be liable for remediation costs, personal injury claims, and property damage and our ability to use or sell the property would be limited. We have policies and procedures in place that require environmental reviews before initiating foreclosure actions on real property; however, these reviews may not detect all potential environmental hazards. Environmental laws that require us to incur substantial remediation costs, which could materially reduce the affected property s value, and other liabilities associated with environmental hazards could have a material adverse effect on our financial condition and results of operations.

Our controls and procedures may fail or be circumvented.

We review our internal controls over financial reporting quarterly and enhance controls in response to these assessments, internal and external audit, and regulatory recommendations. A control system, no matter how well conceived and operated, include certain assumptions and can only provide reasonable assurance that the objectives of the control system are met. These controls may be circumvented by individual acts, collusion, or management override. Any failure or circumvention related to our controls and procedures or failure to follow regulations related to controls and procedures could have a material adverse effect on our business, reputation, results of operations, and financial condition.

We continue to encounter technological change.

The financial services industry continues to experience rapid technological change with the introduction of new, and increasingly complex, technology-driven products and services. The effective use of technology increases operational efficiency that enables financial service institutions to reduce costs. Our future success depends, in part, on our ability to provide products and services that satisfactorily meet the financial needs of our customers, as well as to realize additional efficiencies in our operations. We may fail to use technology-driven products and services effectively to better serve our customers and increase operational efficiency or sufficiently invest in technology solutions and upgrades to ensure systems are operating properly. Further, many of our competitors have substantially greater resources to invest in technology, which may adversely affect our ability to compete.

We are subject to information security risks associated with technology.

We rely on communication and information systems, including those provided by third-party vendors, to conduct our business operations. Our security risks increase as our reliance on technology increases; consequently, the expectation to safeguard information by monitoring systems for potential failures, disruptions, and breakdowns has also increased. Risks associated with technology include security breaches, operational failures and service interruptions, and reputational damages. These risks also apply to our third-party service providers. Our third-party vendors include large entities with significant market presence in their respective fields; therefore, their services could be difficult to replace quickly if there are operational failures or service interruptions.

We rely on our technology-driven systems to conduct daily business and accounting operations that include the collection, processing, and retention of confidential financial and client information. We may be vulnerable to security breaches, such as employee error, cyber-attacks, and viruses, beyond our control. In addition to security breaches, programming errors, vandalism, natural disasters, terrorist attacks, and third-party vendor disruptions may cause operational failures and service interruptions to our communication and information systems. Further, our systems may be temporarily disrupted during implementation or upgrade. Security breaches and service interruptions related to our information systems could damage our reputation, which may cause us to lose customers, subject us to regulatory scrutiny, or expose us to civil litigation and financial liability.

We periodically review our information security policies, procedures, disaster recovery plans, and financial condition of third-party vendors; however, there is no assurance that security risks will not occur, or if they do occur that our processes and procedures are implemented properly to accurately address such risks. Security risks, including those of third-party vendors, could affect our ability to deliver products and services to our customers, cause us to incur significant expense, or damage our reputation, which may have a material adverse effect on our financial condition and results of operations.

We may be subject to claims and litigation pertaining to intellectual property.

Banking and other financial services companies, such as the Company, rely on technology companies to provide information technology products and services necessary to support the Company s day-to-day operations. Technology companies often enter into litigation based on allegations of patent infringement or other violations of intellectual property rights. In addition, patent holding companies seek to monetize patents they have purchased or otherwise obtained. Competitors of the Company s vendors, or other individuals or companies, have from time to time claimed to hold intellectual property sold to the Company by its vendors. Such claims may increase in the future as the financial services sector becomes more reliant on information technology vendors. The plaintiffs in these actions often seek injunctions and substantial damages.

Regardless of the scope or validity of such patents or other intellectual property rights, or the merits of any claims by potential or actual litigants, the Company may have to engage in protracted litigation. Such litigation is often expensive, time consuming, disruptive to the Company s operations, and distracting to management. If the Company is found to infringe upon one or more patents or other intellectual property rights, it may be required to pay substantial damages or royalties to a third party. In certain cases, the Company may consider entering into licensing agreements for disputed intellectual property, although no assurance can be given that such licenses can be obtained on acceptable terms or that litigation will not occur. These licenses may also significantly increase the Company s operating expenses. If legal matters related to intellectual property claims were resolved against the Company or settled, the Company could be required to make payments in amounts that could have a material adverse effect on its business, financial condition, and results of operations.

Severe weather, natural disasters, acts of war or terrorism, and other external events could significantly affect our business.

Severe weather, natural disasters, acts of war or terrorism, and other adverse external events could have a significant impact on our ability to conduct business. These events could affect the stability of our deposit base, impair the ability of borrowers to repay outstanding loans, impair the value of collateral securing loans, cause significant property damage, result in a loss of revenue, and/or cause us to incur additional expenses. Any such events could have a material adverse effect on our business, which, in turn, could have a material adverse effect on our financial condition and results of operations.

Risks Associated with Our Common Stock

Our common stock price can be volatile.

Stock price volatility may make it more difficult for our stockholders to resell their common stock when desired. The following factors, among others, may cause our common stock price to fluctuate significantly:

- actual or expected variations in quarterly results of operations;
- recommendations by securities analysts;
- operating and stock price performance of comparable companies, as deemed by investors;
- news reports relating to trends, concerns, and other issues in the financial services industry;
- perceptions in the marketplace about our Company or competitors;
- new technology used, or services offered, by competitors;
- significant acquisitions or business combinations, strategic partnerships, joint ventures, or capital commitments by, or involving, our Company or competitors;

- failure to integrate acquisitions or realize expected benefits from acquisitions;
- changes in government regulations; and
- geopolitical conditions, such as acts or threats of terrorism or military action.

General market fluctuations; industry factors; political conditions; and general economic conditions and events, such as economic slowdowns, recessions, interest rate changes, or credit loss trends, could also cause our common stock price to decrease regardless of operating results.

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The trading volume in our common stock is less than that of other larger financial services companies.

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

We may not continue to pay dividends on our common stock in the future.

Our common stockholders are only entitled to receive dividends when declared by our Board of Directors out of funds legally available for such payments. Although we have historically declared cash dividends on our common stock, we are not required to do so, and may reduce or eliminate our common stock dividend in the future. This could adversely affect the market price of our common stock. As a financial holding company, the Company s ability to declare and pay dividends is dependent on certain federal regulatory considerations, including the guidelines of the Federal Reserve regarding capital adequacy and dividends.

An investment in our common stock is not an insured deposit.

Our common stock is not a bank deposit and, therefore, is not insured against loss by the FDIC, any other deposit insurance fund, or by any other public or private entity. Investment in our common stock is inherently risky for the reasons described in this Risk Factors section and elsewhere in this report and is subject to the same market forces that affect the price of common stock in any company. As a result, holders of our common stock could lose some, or all, of their investment.

Certain banking laws may have an anti-takeover effect.

Provisions of federal banking laws, including regulatory approval requirements, could make it more difficult to be acquired by a third party, even if perceived to be beneficial to our shareholders. These provisions effectively inhibit a non-negotiated merger or other business combination, which could adversely affect the market price of our common stock.

Our Series A Preferred Stock ranks senior to our common stock.

Our Series A Preferred Stock carries a 6% dividend rate. Each share of Series A Preferred Stock is convertible into 69 shares of our common stock at any time and mandatorily converts on May 20, 2016. At our option, we may redeem the Series A Preferred Stock at face value. The Series A Preferred Stock ranks senior to shares of our common stock. As a result, we make dividend payments on our Series A Preferred Stock before our common stock, and in the event of bankruptcy, dissolution, or liquidation, the holders of Series A Preferred Stock will be satisfied before distributions are made to holders of our common stock. If we do not remain current in the payment of dividends on the Series A Preferred Stock, dividends may not be paid on our common stock. Dividends declared on the Series A Preferred Stock reduce any net income available to our common stockholders and earnings per common share. As of December 31, 2014, 15,151 shares of Series A Preferred Stock were outstanding.

Item 1B. Unresolved Staff Comments.

None.

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Item 2. Properties.

Our corporate headquarters is located at One Community Place, Bluefield, Virginia. Our community bank subsidiary, the Bank, provides financial services through a network of 53 branch locations throughout Virginia, West Virginia, North Carolina, and Tennessee. We have 21 branches in West Virginia, 19 branches in Virginia, 11 branches in North Carolina, and 2 branches in Tennessee. We own 46 branches and lease the remaining 7 branches. Our insurance subsidiary s, Greenpoint s, headquarters is located in High Point, North Carolina. Greenpoint provides insurances services through a network of 11 offices throughout Virginia, West Virginia, and North Carolina. We operate 4 insurance offices in North Carolina, 4 offices in West Virginia, and 3 offices in Virginia. We own 1 office, lease 5 offices, and operate 5 offices within our branch network. We also lease 2 loan production offices and own 1 wealth management office. There were no mortgages or liens against any properties. A list of all branch and ATM locations can be found on our website at www.fcbinc.com. Information contained on our website is not part of this report. See Note 8, Premises, Equipment, and Leases, to the Consolidated Financial Statements in Part II, Item 8 of this report.

Item 3. Legal Proceedings.

We are currently a defendant in various legal actions and asserted claims in the normal course of business. Although we are unable to assess the ultimate outcome of each of these matters with certainty, we are of the belief that the resolution of these actions should not have a material adverse effect on our financial position, results of operations, or cash flows.

Item 4. Mine Safety Disclosures.

None.

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PART II

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

Market Information, Holders and Dividends

Our common stock is traded on the NASDAQ Global Select Market under the symbol FCBC . As of February 26, 2015, there were 2,727 record holders and 18,545,619 outstanding shares of our common stock. The following table presents our common stock s high and low market price and cash dividends paid per share, by quarter, during the periods indicated:

	Year Ended December 31,					
	2014			2013		
	Market Price		Cash Dividends per	Market Price		Cash Dividends per
	High	Low	Common Share	High	Low	Common Share
First quarter	$ 17.05	$ 15.46	$ 0.12	$ 16.27	$ 15.20	$ 0.12
Second quarter	16.85	13.87	0.12	15.76	14.82	0.12
Third quarter	16.45	13.53	0.13	17.85	15.05	0.12
Fourth quarter	16.58	14.39	0.13	17.64	15.57	0.12

The Company s ability to pay dividends on its common stock is dependent on the Bank s ability to pay dividends to the Company, which is subject to various regulatory restrictions and limitations. See Regulatory Restrictions on Dividends; Source of Strength in the Regulation and Supervision First Community Bancshares, Inc. section and Restrictions on Distribution of Subsidiary Bank Dividends and Assets in the Regulation and Supervision First Community Bank section in Part I, Item 1 of this report. We pay common stock dividends only if all accrued and unpaid dividends are fully paid on our outstanding Series A Preferred Stock. Our Series A Preferred Stock outstanding totaled 15,151 shares as of December 31, 2014, and 15,251 shares as of December 31, 2013. Series A Preferred Stock cash dividends totaled $910 thousand in 2014, $992 thousand in 2013, and $1.12 million in 2012. Common stock cash dividends totaled $9.20 million in 2014, $9.48 million in 2013, and $8.16 million in 2012. Cash dividends paid per common share totaled $0.50 in 2014, $0.48 in 2013, and $0.43 in 2012.

Purchases of Equity Securities

We repurchased 132,773 shares of our common stock in 2014, 1,739,601 shares in 2013, and 67,438 shares in 2012. The following table provides information regarding purchases of our common stock made by us or on our behalf by any affiliated purchaser, as defined in Rule 10b-18(a)(3) under the Exchange Act, during the dates indicated:

	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of a Publicly Announced Plan	Maximum Number of Shares that May Yet be Purchased Under the Plan [1]
October 1-31, 2014		$		903,236
November 1-30, 2014				903,236
December 1-31, 2014				906,536
Total		$		

(1) Our stock repurchase plan, as amended, authorizes the purchase and retention of up to 3,000,000 shares. The plan has no expiration date and is currently in effect. No determination has been made to terminate the plan or to cease making purchases. We held 2,093,464 shares in treasury as of December 31, 2014.

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Stock Performance Graph

The following graph, compiled by SNL Financial LC (SNL), compares our cumulative total shareholder return on our common stock for the five-year period ended December 31, 2014, with the cumulative total return of the S&P 500 Index, the NASDAQ Composite Index, and SNL s Asset Size & Regional Peer Group. The Asset Size & Regional Peer Group consists of 51 bank holding companies with total assets between $1 billion and $5 billion that are located in the Southeast Region of the United States and traded on NASDAQ, the OTC Bulletin Board, and pink sheets. The cumulative returns assume reinvestment of dividends.

	Year Ended December 31,					
	2009	**2010**	**2011**	**2012**	**2013**	**2014**
First Community Bancshares, Inc.	100.00	127.63	110.07	145.30	156.63	159.64
S&P 500 Index	100.00	115.06	117.49	136.30	180.44	205.14
NASDAQ Composite Index	100.00	118.15	117.22	138.02	193.47	222.16
SNL Asset & Regional Peer Group(1)	100.00	105.70	84.67	94.36	120.88	134.53

(1) Includes the following institutions: Access National Corporation; American National Bankshares Inc.; Ameris Bancorp; Bear State Financial, Inc.; BNC Bancorp; Burke & Herbert Bank & Trust Company; C&F Financial Corporation; Capital City Bank Group, Inc.; Cardinal Financial Corporation; Carolina Financial Corporation; Carter Bank & Trust; CenterState Banks, Inc.; City Holding Company; CNB Corporation; CNLBancshares, Inc.; Colony Bankcorp, Inc.; Community Bankers Trust Corporation; CommunityOne Bancorp; Eastern Virginia Bankshares, Inc.; Fidelity Southern Corporation; First Bancorp; First Bancshares, Inc.; First Citizens Bancshares, Inc.; First Security Group, Inc.; Franklin Financial Network, Inc.; Hamilton State Bancshares, Inc.; Hampton Roads Bankshares, Inc.; HomeTrust Bancshares, Inc.; Middleburg Financial Corporation; Monarch Financial Holdings, Inc.; MVB Financial Corp.; National Bankshares, Inc.; NewBridge Bancorp; Palmetto Bancshares, Inc.; Park Sterling Corporation; Peoples Bancorp of North Carolina, Inc.; Premier Financial Bancorp, Inc.; Seacoast Banking Corporation of Florida; ServisFirst Bancshares, Inc.; Simmons First National Corporation; Southeastern Bank Financial Corporation; Southern BancShares (N.C.), Inc.; Southern First Bancshares, Inc.; Square 1 Financial, Inc.; State Bank Financial Corporation; Stonegate Bank; Summit Financial Group, Inc.; TowneBank; USAmeriBancorp, Inc.; WashingtonFirst Bankshares, Inc.; and Wilson Bank Holding Company. The returns of each of the foregoing institutions have been weighted according to their respective stock market capitalization at the beginning of each period for which a return is indicated.

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Item 6. Selected Financial Data.

The following table presents our consolidated selected financial data, derived from audited financial statements, as of and for the five years ended December 31, 2014. The table should be read in conjunction with Item 7, Management s Discussion and Analysis of Financial Condition and Results of Operations, and Item 8, Financial Statements and Supplementary Data, of this report.

	Year Ended December 31,				
(Amounts in thousands, except share and per share data)	**2014**	**2013**	**2012**	**2011**	**2010**
Selected Balance Sheet Data					
Investment securities	$ 384,065	$ 520,388	$ 535,174	$ 485,920	$ 484,701
Loans held for sale	1,792	883	6,672	5,820	4,694
Loans held for investment, net of unearned income	1,689,416	1,710,721	1,724,653	1,396,067	1,386,206
Allowance for loan losses	20,227	24,077	25,770	26,205	26,482
Total assets	2,607,936	2,602,514	2,728,867	2,164,789	2,244,238
Average assets	2,608,570	2,661,602	2,510,931	2,195,639	2,263,055
Deposits	2,000,759	1,950,742	2,030,175	1,543,467	1,620,955
Borrowings	229,741	300,396	313,553	295,141	332,087
Total liabilities	2,256,562	2,273,908	2,372,544	1,859,060	1,974,360
Preferred stock	15,151	15,251	17,421	18,921	
Total stockholders equity	351,374	328,606	356,323	305,729	269,878
Average stockholders equity	342,619	355,611	334,901	295,150	269,446
Summary of Operations					
Interest income	$ 106,108	$ 109,476	$ 109,656	$ 94,176	$ 103,582
Interest expense	15,290	17,834	19,600	22,147	29,725
Net interest income	90,818	91,642	90,056	72,029	73,857
Provision for loan losses charged to operations	145	8,208	5,678	9,047	14,757
Noninterest income	30,003	29,771	36,710	35,534	40,508
Noninterest expense	82,862	78,985	78,383	68,915	69,943
Income tax expense	12,324	10,908	14,128	9,573	7,818
Net income	25,490	23,312	28,577	20,028	21,847
Dividends on preferred stock	910	1,024	1,058	703	
Net income available to common shareholders	24,580	22,288	27,519	19,325	21,847
Selected Share and Per Share Data					
Basic earnings per common share	$ 1.34	$ 1.13	$ 1.44	$ 1.08	$ 1.23
Diluted earnings per common share	1.31	1.11	1.40	1.07	1.23
Book value per common share at year-end (1)	18.06	16.79	16.76	15.96	15.11
Cash dividends per common share	0.50	0.48	0.43	0.40	0.40
Weighted average basic shares outstanding	18,406,363	19,792,099	19,127,065	17,877,421	17,802,009
Weighted average diluted shares outstanding	19,483,054	20,961,800	20,419,569	18,687,521	17,815,106
Selected Ratios					
Return on average assets	0.94%	0.84%	1.10%	0.88%	0.97%
Return on average common equity	7.51%	6.57%	8.70%	6.81%	8.11%
Average equity to average assets	13.13%	13.36%	13.34%	13.44%	11.91%
Dividend payout	37.44%	42.62%	29.89%	37.00%	32.52%
Total risk-based capital ratio	17.68%	16.44%	16.70%	18.15%	15.33%
Tier 1 risk-based capital ratio	16.43%	15.19%	15.44%	16.89%	14.07%
Leverage ratio	10.12%	9.95%	9.96%	11.50%	9.44%

(1) Book value per common share is defined as stockholders equity divided by as-converted common shares outstanding.
(2) NM Not meaningful

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

Unless the context suggests otherwise, the terms First Community, Company, we, our, and us refer to First Community Bancshares, Inc. and subsidiaries as a consolidated entity. The following Management s Discussion and Analysis of Financial Condition and Results of Operations (MD&A) is intended to help the reader understand our financial condition, changes in financial condition, and results of operations. This MD&A contains forward-looking statements and should be read in conjunction with our consolidated financial statements, accompanying notes, and other financial information included in this report.

Executive Overview

First Community Bancshares, Inc. (the Company) is a financial holding company, headquartered in Bluefield, Virginia, that provides commercial banking services through its wholly-owned subsidiary First Community Bank (the Bank). The Bank operates under the trade names First Community Bank in West Virginia, Virginia, and North Carolina and People s Community Bank, a Division of First Community Bank, in Tennessee. The Bank has positioned itself as a regional community bank that provides an alternative to larger banks, which often place less emphasis on personal relationships, and smaller community banks, which lack the capital and resources to efficiently serve customer needs. The Company provides insurance services through its wholly-owned subsidiary Greenpoint Insurance Group, Inc. (Greenpoint), which operates under the Greenpoint name and under the trade names First Community Insurance Services (FCIS) and Carolina Insurers Associates in North Carolina, Carr & Hyde Insurance and FCIS in Virginia, and FCIS in West Virginia. The Bank offers wealth management and investment advice through its wholly-owned subsidiary First Community Wealth Management (FCWM) and the Bank s Trust Division.

Our efforts are focused on building financial partnerships and creating enduring and complete relationships with businesses and individuals through a personal and local approach to banking and financial services. Our operations are guided by a strategic plan focusing on organic growth that may be supplemented by strategic acquisitions. While our mission remains that of a community bank, management believes that entry into new markets may accelerate our growth rate by diversifying the demographics of our customer base and by generally increasing our sales and service network.

Economy

The regional economies we operate in have shown positive and stable aspects. The following list summarizes economic activity in the regions we operate:

West Virginia and Southwest Virginia These economies have significant exposure to extractive industries, such as coal, timber, and natural gas. Unemployment levels have generally been lower than the national average.

Central North Carolina This economy has suffered in recent years due to foreign competition in the furniture and textile industries and consolidation in the financial services industry. Despite these detractions, these economies continue to benefit from large regional and national companies operating in the Triad and Central Piedmont regions.

Central Virginia This economy has, in recent years, benefited from key corporate and government activities.

Eastern Tennessee This economy continues to benefit from the stability of higher education, healthcare services, and tourism.

Competition

We continue to encounter strong competition for growth in loans and deposits and increased market share. Many of the markets we target are being entered into by other banks located in nearby and distant markets. The expansion of banks, credit unions, and other non-depository financial institutions over recent years has

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intensified competitive pressures on core deposit generation and retention. Competitive factors that influence our Company include pressure on interest yields, product fees, loan structure, and loan terms; however, we have countered these pressures with our relationship style of banking, competitive pricing, cost efficiencies, and disciplined approach to loan underwriting.

Recent Acquisition and Divestiture Activity

Our consolidated financial statements reflect acquisition and divestiture activity from the transaction date; therefore, comparisons between fiscal years are affected by varying levels of assets, liabilities, income, and expense.

On May 31, 2012, we completed the acquisition of Peoples Bank of Virginia (Peoples), a full service community bank headquartered in Richmond, Virginia. At acquisition, Peoples had total assets of $275.76 million, loans of $184.84 million, and deposits of $232.75 million. Goodwill recorded in the acquisition was $10.32 million.

On June 8, 2012, we entered into a purchase and assumption agreement with loss share arrangements with the FDIC to purchase certain assets and assume substantially all customer deposits and certain liabilities of Waccamaw, a full service community bank headquartered in Whiteville, North Carolina. Under the loss share agreements, the FDIC covers 80% of most loan and foreclosed real estate losses. At acquisition, Waccamaw had total assets of $500.64 million, loans of $318.35 million, and deposits of $414.13 million. Goodwill recorded in the acquisition was $10.62 million.

On October 24, 2014, we completed the purchase of seven branches, six in Southwestern Virginia and one in Central North Carolina, from Bank of America, National Association. At acquisition, we assumed total deposits of $318.88 million for a deposit premium of $5.79 million. Additionally, we purchased the real estate or assumed the leases associated with the branches. No loans were included in the transaction.

On December 12, 2014, we completed the sale of thirteen branches, ten in Southeastern North Carolina and three in South Carolina, to CresCom Bank (CresCom), headquartered in Charleston, South Carolina. At closing, CresCom assumed total deposits of $215.19 million and purchased total loans of $70.04 million. We received a deposit premium from CresCom of $6.45 million. The transaction excluded loans covered under FDIC loss share agreements. In connection with the transaction we recorded a net gain of $755 thousand, which included a $6.45 million goodwill allocation.

***Insurance Service*s**

We offer insurance services through Greenpoint, a full-service insurance agency that provides commercial and personal lines of insurance. Revenues are primarily derived from commissions paid by issuing companies on the sale of policies. Commission revenue totaled $6.56 million in 2014, an increase of $622 thousand, or 10.48%, compared to the same period of 2013, which is primarily due to an increase in direct bill property and casualty insurance income and contingency income. Commission revenue totaled $5.93 million in 2013, an increase of $190 thousand, or 3.31%, compared to the same period of 2012, which was due to an increase in direct bill property and casualty insurance income.

Wealth Management Services

We offer trust management, estate administration, and investment advisory services through FCWM and the Bank s Trust Division, which reported combined assets under management of $712 million as of December 31, 2014, and $706 million as of December 31, 2013. These assets are not our assets, but are managed under various fee-based arrangements as fiduciary or agent. The Trust Division manages inter vivos trusts and trusts under will, develops and administers employee benefit and individual retirement plans, and manages and settles estates.

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Fiduciary fees for these services are charged on a schedule related to the size, nature, and complexity of the account. Revenues consist primarily of commissions on assets under management and investment advisory fees.

Critical Accounting Estimates

We prepare our consolidated financial statements in accordance with generally accepted accounting principles (GAAP) in the United States and conform to general practices within the banking industry. Our financial position and results of operations require management to make judgments and estimates to develop the amounts reflected and disclosed in the consolidated financial statements. Different assumptions in the application of these estimates could result in material changes to our consolidated financial position and consolidated results of operations. Estimates, assumptions, and judgments, which are periodically evaluated, are based on historical experience and other factors, including expectations of future events believed to be reasonable under the circumstances. These estimates are generally necessary when assets and liabilities are required to be recorded at estimated fair value, a decline in the value of an asset carried on the financial statements at fair value warrants an impairment write-down or establishment of a valuation reserve, or an asset or liability needs to be recorded based upon the probability of occurrence of a future event. Carrying assets and liabilities at fair value inherently results in more financial statement volatility. Fair values and information used to record valuation adjustments for certain assets and liabilities are based either on quoted market prices or, when available, are provided by third-party sources. When third-party information is not available, management estimates valuation adjustments primarily through the use of financial modeling techniques and appraisal estimates.

Our accounting policies are fundamental in understanding MD&A and the disclosures presented in Item 8, Financial Statements and Supplementary Data, of this report. See Note 1, Summary of Significant Accounting Policies, to the Consolidated Financial Statements in Item 8 of this report. These policies may involve significant estimates and assumptions that have a material impact on our financial condition or operating performance due to the levels of subjectivity and judgment necessary to account for highly uncertain matters or the susceptibility of such matters to change. Based on the valuation techniques used and the sensitivity of financial statement amounts to the methods, assumptions, and estimates underlying those amounts, we have identified the establishment and determination of investment securities, the allowance for loan losses, business combinations, intangible assets, and income taxes as the accounting areas that require the most subjective or complex judgments.

Investment Securities

Independent third parties are used to determine the fair values of our investment securities. Inputs provided by third parties are reviewed and corroborated by management. Evaluations of the causes of the unrealized losses are performed to determine whether the impairment is temporary or other-than-temporary in nature. We review our investment portfolio quarterly for indications of OTTI. The analysis differs depending upon the type of investment security being analyzed. The following factors, among others, are considered in determining whether a security is other-than-temporarily impaired: our intent and ability to hold the security for a period of time sufficient to allow for any expected recovery in fair value or whether it is more likely than not we will be required to sell the security before recovering its fair value; the severity of the loss and the length of time fair value has been below amortized cost; the expectation of the security s future performance; and the creditworthiness of the security s issuer. If the impairment is determined to be other-than-temporary, the value of the security is reduced and a corresponding charge to earnings is recognized. See Note 3, Investment Securities, to the Consolidated Financial Statements in Item 8 of this report.

Allowance for Loan Losses

Our quarterly review of the allowance methodology and relevant factors serves as the primary means management evaluates the adequacy of the allowance for loan losses. The determination of our allowance for loan losses requires management to make significant estimates and assumptions. While management uses its best

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judgment and available information, the ultimate adequacy of the allowance is dependent upon a variety of factors beyond our control, including the performance of our loan portfolio, the economy, changes in interest rates, and the view of regulatory authorities. These uncertainties may result in material changes to the allowance for loan losses in the near term; however, the amount of the change cannot reasonably be estimated.

The Company s allowance for loan losses consists of reserves assigned to specific loans and credit relationships and general reserves assigned to loans not separately identified that have been segmented into groups with similar risk characteristics using our internal risk grades. General reserve allocations are based on management s judgments of qualitative and quantitative factors about macro and micro economic conditions reflected within the loan portfolio and the economy. Factors considered in this evaluation include, but are not limited to, probable losses from loan and other credit arrangements, general economic conditions, changes in credit concentrations or pledged collateral, historical loan loss experience, and trends in portfolio volume, maturities, composition, delinquencies, and nonaccruals. Historical loss rates for each risk grade of commercial loans are adjusted by environmental factors to estimate the amount of reserve needed by segment. Individually significant loans require additional analysis that may include the borrower s underlying cash flow and capacity for debt repayment, specific business conditions, and value of secondary sources of repayment; consequently, this analysis may result in the identification of weakness and a corresponding need for a specific reserve.

Third-party collateral valuations are regularly obtained and evaluated to help management determine the potential credit impairment and the amount of impairment to record. Internal collateral valuations are generally performed within two to four weeks of identifying the initial potential impairment. The internal evaluation compares the original appraisal to current local real estate market conditions and considers experience and expected liquidation costs. When a third-party evaluation is received, it is reviewed for reasonableness. Once the evaluation is reviewed and accepted, discounts are applied to fair market value, based on, but not limited to, our historical liquidation experience for like collateral, resulting in an estimated net realizable value. The estimated net realizable value is compared to the outstanding loan balance to determine the appropriate amount of specific impairment reserve. Specific reserves are generally recorded for impaired loans while third-party evaluations are in process and for impaired loans that continue to make some form of payment. While waiting for receipt of the third-party appraisal, we regularly review the relationship to identify any potential adverse developments and begin the tasks necessary to gain control of the collateral and prepare it for liquidation, including, but not limited to, engagement of counsel, inspection of collateral, and continued communication with the borrower.

Generally, the only difference between current appraised value, adjusted for liquidation costs, and the carrying amount of the loan, less the specific reserve, is any downward adjustment to appraised value that we determine appropriate, such as the costs to sell the property. Impaired loans that do not meet certain criteria and do not have a specific reserve have typically been written down through partial charge-offs to net realizable value. Based on prior experience, the Company rarely returns loans to performing status after they have been partially charged off. Impaired credits move quickly through the process towards ultimate resolution except in cases involving bankruptcy and various state judicial processes, which may extend the time for ultimate resolution.

Management uses an independent third party to assist in determining the changes in cash flows and the amount of possible impairment related to our purchased performing loans and PCI loan pools. PCI loan pools are evaluated separately from non-PCI loans in the determination of the allowance. See Note 6, Allowance for Loan Losses, to the Consolidated Financial Statements in Item 8 of this report.

Business Combinations

The Company may engage in business combinations with other companies. Under the acquisition method of accounting, all identifiable acquired assets, including purchased loans, and liabilities are recorded at fair value. Fair values are subject to refinement for up to one year after the closing date of the acquisition as additional information about the closing date fair values becomes available. Management makes significant estimates and exercises significant judgment in accounting for business combinations. Any excess of the purchase price over the fair value of net assets acquired is recorded as goodwill. If the price of the acquired business is less than the net assets acquired, a gain on the purchase is recorded. Financial assets and liabilities are typically valued using discount models that apply current discount rates to streams of cash flow. Valuation methods require assumptions, which can result in alternate valuations, varying levels of goodwill, or bargain purchase gains, and in some cases amortization expense or accretion income. Management must also make estimates for the useful or economic lives of certain acquired assets and liabilities. We review the purchased loan portfolio quarterly for changes in cash flows and possible impairment using input provided from an independent third party. Management s assumptions about purchased loans and intangible assets may significantly influence the allowance for loan losses. See Note 2, Acquisitions, Divestitures, and Branching Activity, and Note 6, Allowance for Loan Losses, to the Consolidated Financial Statements in Item 8 of this report.

The Company may also engage in FDIC-assisted business combinations. In 2012, we entered into a purchase and assumption agreement with loss share arrangements with the FDIC to purchase certain assets and assume substantially all customer deposits and certain liabilities of Waccamaw. Under the loss share agreements the FDIC agreed to cover 80% of covered assets, which consist of most loan and other real estate losses. Gains and recoveries on covered assets offset prior losses or are paid to the FDIC at the loss share percentage at the time of recovery. The loss share agreement for single family covered assets provides FDIC loss sharing and recovery reimbursement to the FDIC for ten years. The loss share agreement for commercial covered assets provides for FDIC loss sharing for five years and recovery reimbursement to the FDIC for eight years. Under the acquisition method of accounting, the FDIC indemnification asset was recorded at fair value using projected cash flows based on expected reimbursements and the applicable loss share percentages. We incur expenses related to covered assets, and certain of these costs are reimbursable from the FDIC through monthly and quarterly claims we submit. Estimated reimbursements from the FDIC are netted against covered expenses in the statements of income. We regularly review the fair value of the FDIC indemnification asset with input from a third-party provider. Post-acquisition adjustments to the indemnification asset are measured on the same basis as the underlying covered assets. See Note 7, FDIC Indemnification Asset, to the Consolidated Financial Statements in Item 8 of this report.

Intangible Assets

Goodwill represents the excess of the purchase price over the fair value of net assets acquired in a business combination. Goodwill is allocated to the appropriate reporting unit when acquired. We maintain two reporting units, Community Banking and Insurance Services. Goodwill is tested annually in the fourth quarter using a qualitative assessment to determine if it is more likely than not that the fair value of each reporting unit is less than its carrying amount. Qualitative factors may include macroeconomic conditions, industry and market considerations, our financial performance, and changes in our stock price. If we conclude that it is more likely than not that the fair value of either reporting unit is less than its carrying amount, we perform a two-step quantitative goodwill impairment test. Step 1 consists of calculating and comparing the fair value of each reporting unit to its carrying amount, including goodwill. If the fair value of a reporting unit is greater than its book value, no goodwill impairment exists. If the carrying amount of a reporting unit is greater than its calculated fair value, goodwill impairment may exist and Step 2 is required to determine the amount of the impairment loss.

Core deposit intangible assets represent the future earnings potential of acquired deposit relationships. These deposits are amortized over their estimated remaining useful lives, as determined by management. Other identifiable intangible assets primarily represent the rights arising from contractual arrangements and use the straight-line amortization method. See Note 9, Goodwill and Other Intangible Assets, to the Consolidated Financial Statements in Item 8 of this report.

Income Taxes

The establishment of provisions for federal and state income taxes is a complex area of accounting that involves judgments and estimates in applying relevant tax statutes. We operate in many state tax jurisdictions, which

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requires the appropriate allocation of income and expense to each state based on a variety of apportionment or allocation bases. Audits by federal and state tax authorities may reveal liabilities that differ from our estimates and provisions. We continually evaluate our exposure to possible tax assessments arising from audits and record an estimate of possible exposure based on current facts and circumstances.

We measure deferred tax assets and liabilities using enacted income tax rates applicable to the period temporary differences are expected to be realized or settled. As changes in tax laws and rates are enacted, we adjust deferred tax assets and liabilities through the provision for income taxes. When evidence indicates that it is more likely than not that some, or all, of the deferred tax asset is not recoverable, we may record a valuation allowance to reduce the carrying value of the asset. Increases or decreases in the valuation allowance result in increases or decreases to the provision for income taxes. See Note 16, Income Taxes, to the Consolidated Financial Statements in Item 8 of this report.

Performance Overview

Highlights of our results of operations in 2014, and financial condition as of December 31, 2014, include the following:

- Our non-covered loan portfolio increased $8.14 million compared to year-end 2013.
- We realized the positive resolution of a sizable, problem credit which resulted in enhanced accretion income, reduced specific reserves, and recovery of prior-years charge-offs.
- Our allowance for loan losses was reduced $3.85 million compared to year-end 2013. In 2014, we released $3.26 million of specific reserves related to impaired loans and removed $682 thousand of the allowance related to the branch divestiture.
- Our credit quality metrics continued to improve as non-covered nonaccrual loans decreased $8.61 million, non-covered nonperforming loans decreased $7.19 million, and non-covered nonperforming assets decreased $7.87 million compared to year-end 2013.
- Non-covered nonperforming loans as a percentage of total non-covered loans decreased 46 basis points to 0.85% and non-covered nonperforming assets as a percentage of total non-covered assets decreased 34 basis points to 0.80% compared to year-end 2013.
- Non-covered delinquent loans decreased $8.88 million compared to year-end 2013.
- We prepaid long-term borrowings of $60 million in keeping with our strategic goal of reducing high cost, wholesale debt.
- In October we completed the purchase of seven branches from Bank of America and assumed total deposits of $319 million in the transaction.
- In December we completed the sale of thirteen branches to CresCom with deposits of approximately $215 million and loans of approximately $70 million. The sale resulted in a net gain of $755 thousand.
- As a result of branch acquisition and divestiture activity, we consolidated and strengthened our franchise.

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Results of Operations

Net Income

The following table presents our net income and related information in the periods indicated:

(Amounts in thousands, except per share data)	Year Ended December 31, 2014	2013	2012	2014 Compared to 2013 Increase (Decrease)	% Change	2013 Compared to 2012 Increase (Decrease)	% Change
Net income	$ 25,490	$ 23,312	$ 28,577	$ 2,178	9.34%	$ (5,265)	-18.42%
Net income available to common shareholders	24,580	22,288	27,519	2,292	10.28%	(5,231)	-19.01%
Basic earnings per common share	1.34	1.13	1.44	0.21	18.58%	(0.31)	-21.53%
Diluted earings per common share	1.31	1.11	1.40	0.20	18.02%	(0.29)	-20.71%
Return on average assets	0.94%	0.84%	1.10%	0.10%	11.90%	-0.26%	-23.64%
Return on average common equity	7.51%	6.57%	8.70%	0.94%	14.31%	-2.13%	-24.48%

2014 Compared to 2013. Net income increased in 2014 primarily due to a recovery of provision for loan losses, a decrease in the net amortization related to the FDIC indemnification asset, a decrease in other operating expenses, and a net gain on branch divestitures. These gains and expense decreases were offset by Federal Home Loan Bank (FHLB) debt prepayment fees, a net loss on the sale of securities, expenses related to acquisition and divestiture activity, a decrease in other operating income, and decrease in net interest income.

2013 Compared to 2012. Net income decreased in 2013 due to net amortization related to the FDIC indemnification asset, an increased provision for loan losses, a one-time contractual severance payment, and a decrease in other operating income resulting from an out-of-period adjustment in 2012. These decreases were offset by a reduction in merger related expenses and a decline in interest expense on deposits and borrowings.

During our core system conversion in 2012, we discovered that certain loan charge-offs reported in prior periods, beginning in 2007, were overstated due to not recognizing the impact of interest payments that had been applied to principal for loans on nonaccrual status. The overstated charge-offs resulted in an overstated provision for loan losses and corresponding understated pre-tax income. Management analyzed the error and determined that prior years were not materially misstated and correcting the error in 2012 would not materially misstate 2012 results. We recorded a $2.39 million increase (out-of-period adjustment) to other income in 2012 to correct the understatement of pre-tax income.

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Net Interest Income

Net interest income, our largest contributor to earnings, comprised 75.17% of total net interest and noninterest income in 2014, 75.48% in 2013, and 71.04% in 2012. For the following discussion, net interest income is presented on a tax equivalent basis to provide a comparison among all types of interest earning assets. The tax equivalent basis adjusts for the tax-favored status of income from certain loans and investments. Although non-GAAP, management believes this financial measure is more widely used in the financial services industry and provides better comparability of net interest income arising from taxable and tax-exempt sources. We use this non-GAAP financial measure to monitor net interest income performance and manage the composition of our balance sheet. The following table presents our average consolidated balance sheets in the periods indicated:

	Year Ended December 31,								
	2014			2013			2012		
(Amounts in thousands)	Average Balance	Interest (1)	Average Yield/ Rate (1)	Average Balance	Interest (1)	Average Yield/ Rate (1)	Average Balance	Interest (1)	Average Yield/ Rate (1)
Assets									
Earning assets									
Loans (2)	$ 1,744,520	$ 95,707	5.49%	$ 1,699,614	$ 96,768	5.69%	$ 1,611,557	$ 96,803	6.01%
Securities available for sale	410,136	12,400	3.02%	543,697	15,184	2.79%	502,416	15,170	3.02%
Securities held to maturity	20,843	267	1.28%	667	54	8.10%	2,622	171	6.52%
Interest-bearing deposits	98,090	291	0.30%	63,566	211	0.33%	77,851	259	0.33%
Total earning assets	2,273,589	$ 108,665	4.78%	2,307,544	$ 112,217	4.86%	2,194,446	$ 112,403	5.12%
Other assets	334,981			354,058			316,485		
Total assets	$ 2,608,570			$ 2,661,602			$ 2,510,931		
Liabilities									
Interest-bearing deposits									
Demand deposits	$ 366,932	$ 206	0.06%	$ 361,979	$ 240	0.07%	$ 306,019	$ 185	0.06%
Savings deposits	535,256	514	0.10%	516,247	584	0.11%	471,406	556	0.12%
Time deposits	704,518	6,588	0.94%	772,741	7,999	1.04%	776,901	9,231	1.19%
Total interest-bearing deposits	1,606,706	7,308	0.45%	1,650,967	8,823	0.53%	1,554,326	9,972	0.64%
Borrowings									
Federal funds purchased	892	3	0.34%	632	2	0.32%	490	2	0.41%
Retail repurchase agreements	72,917	97	0.13%	69,141	265	0.38%	78,608	449	0.57%
Wholesale repurchase agreements	50,000	1,878	3.76%	53,118	1,890	3.56%	55,163	2,023	3.67%
FHLB advances and other borrowings	147,504	6,004	4.07%	168,399	6,854	4.07%	175,333	7,154	4.08%
Total borrowings	271,313	7,982	2.94%	291,290	9,011	3.09%	309,594	9,628	3.11%
Total interest-bearing liabilities	1,878,019	15,290	0.81%	1,942,257	17,834	0.92%	1,863,920	19,600	1.05%
Noninterest-bearing demand deposits	367,315			342,919			286,950		
Other liabilities	20,617			20,815			25,160		

Total liabilities	2,265,951			2,305,991			2,176,030		
Stockholders equity	342,619			355,611			334,901		
Total liabilities and equity	$ 2,608,570			$ 2,661,602			$ 2,510,931		
Net interest income, tax equivalent		$ 93,375			$ 94,383			$ 92,803	
Net interest rate spread [3]			3.97%			3.94%			4.07%
Net interest margin [4]			4.11%			4.09%			4.23%

(1) Fully taxable equivalent at the rate of 35% (FTE). The FTE basis adjusts for the tax benefits of income on certain tax exempt loans and investments using the federal statutory rate of 35% for each period presented. The Company believes this measure to be the preferred industry measurement of net interest income and provides relevant comparison between taxable and nontaxable amounts.
(2) Nonaccrual loans are included in average balances outstanding but with no related interest income during the period of nonaccrual.
(3) Represents the difference between the yield on earning assets and cost of funds.
(4) Represents tax equivalent net interest income divided by average earning assets.

The following table presents the impact on tax equivalent net interest income resulting from changes in volume (the average volume times the prior year s average rate), rate (the average rate times the prior year s average volume), and rate/volume (the average volume column times the change in average rate) in the periods indicated:

	Year Ended December 31, 2014 Compared to 2013 Dollar Increase (Decrease) due to				Year Ended December 31, 2013 Compared to 2012 Dollar Increase (Decrease) due to			
(Amounts in thousands)	**Volume**	**Rate**	**Rate/ Volume**	**Total**	**Volume**	**Rate**	**Rate/ Volume**	**Total**
Interest earned on [1]:								
Loans	2,555	(3,399)	(217)	(1,061)	5,292	(5,157)	(170)	(35)
Securities available for sale	(3,726)	1,250	(308)	(2,784)	1,246	(1,155)	(77)	14
Securities held to maturity	1,634	(45)	(1,376)	213	(127)	41	(31)	(117)
Interest-bearing deposits with other banks	114	(19)	(15)	80	(47)		(1)	(48)
Total interest-earning assets	577	(2,213)	(1,916)	(3,552)	6,364	(6,271)	(279)	(186)
Interest paid on [1]:								
Demand deposits	3	(36)	(1)	(34)	33	31	(9)	55
Savings deposits	21	(52)	(39)	(70)	54	(47)	21	28
Time deposits	(709)	(773)	71	(1,411)	(50)	(1,165)	(17)	(1,232)
Federal funds purchased	1			1				
Retail repurchase agreements	14	(173)	(9)	(168)	(54)	(149)	19	(184)
Wholesale repurchase agreements	(111)	107	(8)	(12)	(75)	(61)	3	(133)
FHLB advances and other Borrowings	(850)			(850)	(282)	(18)		(300)
Total interest-bearing liabilities	(1,631)	(927)	14	(2,544)	(374)	(1,409)	17	(1,766)
Change in net interest income, tax equivalent	2,208	(1,286)	(1,930)	(1,008)	$ 6,738	$ (4,862)	$ (296)	$ 1,580

(1) Fully taxable equivalent at the rate of 35%.

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The following table reconciles the difference between net interest income under GAAP and net interest income on a tax equivalent basis in the periods indicated:

	Year Ended December 31,		
(Amounts in thousands)	2014	2013	2012
Net interest income, GAAP basis	$ 90,818	$ 91,642	$ 90,056
Tax equivalent adjustment (1)	2,557	2,741	2,747
Net interest income, tax equivalent	$ 93,375	$ 94,383	$ 92,803

(1) Fully taxable equivalent at the rate of 35% (FTE). The FTE basis adjusts for the tax benefits of income on certain tax exempt loans and investments using the federal statutory rate of 35% for each period presented. We believe this measure is the preferred industry measurement of net interest income and provides relevant comparison between taxable and nontaxable amounts.

Interest and yield on loans include accretion income from acquired loan portfolios. In 2014, accretion income was further enhanced by discount accretion recorded as a result of the positive resolution of a sizable credit. The following table presents net interest margin and related average balance sheet information excluding the impact of non-cash purchase accounting accretion and sizable non-recurring discount accretion in the periods indicated:

	Year Ended December 31,					
	2014		2013		2012	
(Amounts in thousands)	Interest (1)	Average Yield/ Rate (1)	Interest (1)	Average Yield/ Rate (1)	Interest (1)	Average Yield/ Rate (1)
Earning assets						
Loans (2)	$ 95,707	5.49%	$ 96,768	5.69%	$ 96,803	6.01%
Accretion income	11,469		14,726		12,871	
Less: cash accretion income	4,412		7,023		4,158	
Non-cash accretion income	7,057		7,703		8,713	
Non-recurring discount accretion	2,588					
Loans, normalized	86,062	4.93%	89,065	5.24%	88,090	5.47%
Other earning assets	12,958	2.45%	15,449	2.54%	15,600	2.68%
Total earning assets	99,020	4.36%	104,514	4.53%	103,690	4.73%
Total interest-bearing liabilities	15,290	0.81%	17,834	0.92%	19,600	1.05%
Net interest income, tax equivalent	$ 83,730		$ 86,680		$ 84,090	
Net interest rate spread (3)		3.55%		3.61%		3.67%
Net interest margin (4)		3.68%		3.76%		3.83%

(1) Fully taxable equivalent at the rate of 35% (FTE). The FTE basis adjusts for the tax benefits of income on certain tax exempt loans and investments using the federal statutory rate of 35% for each period presented. The Company believes this measure to be the preferred industry measurement of net interest income and provides relevant comparison between taxable and nontaxable amounts.

(2) Nonaccrual loans are included in average balances outstanding but with no related interest income during the period of nonaccrual.

(3) Represents the difference between the yield on earning assets and cost of funds.
(4) Represents tax equivalent net interest income divided by average earning assets.

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2014 Compared to 2013. Net interest income under GAAP decreased $824 thousand, or 0.90%, and tax equivalent net interest income decreased $1.01 million, or 1.07%, in 2014. Changes in the average balances of and yields/rates on earning assets and interest-bearing liabilities resulted in a 3 basis point increase in the net interest rate spread and a 2 basis point increase in the net interest margin.

Loan interest accretion totaled $11.47 million in 2014 and $14.73 million in 2013. Interest accretion income received in cash totaled $4.41 million in 2014 and $7.02 million in 2013. Accretion income was enhanced in 2014 by non-recurring discount accretion of $2.59 million related to the positive resolution of a sizable credit. Excluding non-cash and non-recurring discount accretion income, the yield on loans decreased 31 basis points compared to a decrease of 20 basis points under GAAP. Excluding non-cash and non-recurring discount accretion income, the net interest margin decreased 8 basis points compared to an increase of 2 basis points under GAAP. The impact of purchase accounting interest accretion is expected to decline in future periods due to acquired loan portfolio attrition.

Average earning assets decreased $33.96 million, or 1.47%, due to a decrease in securities available for sale offset by increases in the noncovered loan portfolio, securities held to maturity, and deposits with other banks. The yield on earning assets decreased 8 basis points, which was largely due to a 20 basis point decrease in the yield on loans, a result of the continued low rate environment. During 2014, we purchased short-term bonds in the held-to-maturity category to provide for the funding necessary to extinguish certain wholesale borrowings as they come due. Interest-bearing deposits with banks are primarily comprised of excess liquidity kept at the FRB of Richmond bearing overnight market rates.

As of December 31, 2014, interest-bearing liabilities included interest-bearing deposits; retail repurchase agreements, consisting of collateralized retail deposits and commercial treasury accounts; wholesale repurchase agreements; FHLB advances; and other borrowings. Average interest-bearing liabilities decreased $64.24 million, or 3.31%, primarily due to the decline in average time deposits and FHLB borrowings. In 2014, we prepaid $60 million of FHLB convertible advances, of which $50 million bore a 4.21% interest rate and $10 million bore a 4.15% interest rate. The yield on interest-bearing liabilities decreased 11 basis points due to an 8 basis point decrease in the rate on interest-bearing deposits and a 15 basis point decrease in the rate on borrowings. Average interest-bearing deposits decreased $44.26 million, or 2.68%, which was driven by a $68.22 million, or 8.83%, decrease in average time deposits, partially offset by increases in average interest-bearing demand deposits of $4.95 million, or 1.37%, and average savings deposits, which include money market and savings accounts, of $19.01 million, or 3.68%. Average borrowings decreased $19.98 million, or 6.86%, largely due to decreases in FHLB and other borrowings.

2013 Compared to 2012. Net interest income under GAAP increased $1.59 million, or 1.76%, and tax equivalent net interest income increased $1.58 million, or 1.70%, in 2013. Changes in the average balances of and yields/rates on earning assets and interest-bearing liabilities resulted in a 13 basis point decrease in the net interest rate spread and a 14 basis point decrease in the net interest margin.

Loan interest accretion totaled $14.73 million in 2013 and $12.87 million in 2012. Interest accretion income received in cash totaled $7.02 million in 2013 and $4.16 million in 2012. Excluding non-cash accretion income, the yield on loans decreased 23 basis points compared to a decrease of 31 basis points under GAAP. Excluding non-cash accretion income, the net interest margin decreased 7 basis points compared to a decrease of 14 basis points under GAAP.

Average earning assets increased $113.10 million, or 5.15%, primarily resulting from a full year impact of the increased loan portfolio from the Peoples and Waccamaw acquisitions and loan growth in our non-acquired portfolio. The yield on earning assets decreased 26 basis points, which was largely due to a 32 basis point decrease in the yield on loans, due to the continued low rate environment, and a 23 basis point decrease in the yield on available-for-sale securities, due to new investment and reinvestment of sales proceeds, maturities, prepayments, and cash in lower yielding securities.

As of December 31, 2013, interest-bearing liabilities included interest-bearing deposits; federal funds purchased; retail repurchase agreements, consisting of collateralized retail deposits and commercial treasury accounts; wholesale repurchase agreements; FHLB advances; and other borrowings. Average interest-bearing liabilities increased $78.34 million, or 4.20%, in 2013 primarily resulting from a full year impact of the increased deposit portfolio from the Peoples and Waccamaw acquisitions. The yield on interest-bearing liabilities decreased 13 basis points, which was largely due to an 11 basis point decrease in the rate on interest-bearing deposits. Average interest-bearing deposits increased $96.64 million, or 6.22%. Average interest-bearing demand deposits increased $55.96 million, or 18.29%, and savings deposits, which include money market accounts and savings accounts, increased $44.84 million, or 9.51%, while average time deposits decreased $4.16 million. Average borrowings decreased $18.30 million, or 5.91%, largely due to the prepayment of FHLB borrowings of $11.47 million and wholesale repurchase agreements of $8.15 million acquired from Waccamaw.

Provision for Loan Losses

2014 Compared to 2013. The provision for loan losses is the amount added to the allowance for loan losses after net charge-offs have been deducted to bring the allowance to a level management determines necessary to absorb probable losses in the existing loan portfolio. The provision charged to operations decreased $8.06 million due to a $3.26 million decrease in specific reserves on loans identified as impaired, lower average loss rates, lower classified asset levels, and significantly lower net charge-offs. Net charge-offs in 2014 included a $1.60 million recovery related to the positive resolution of a sizable problem credit. In addition, activity in the allowance in 2014 included the removal of $682 thousand of the allowance due to loans transferred in the branch divestiture. A recovery of $697 thousand was attributed to the PCI provision largely due to better than expected performance in the Waccamaw PCI loan portfolio, of which $422 thousand was recorded through the FDIC indemnification asset to reflect the indemnified portion of the post-acquisition exposure and $275 thousand was applied to operations. See Allowance for Loan Losses in the Financial Condition section below.

2013 Compared to 2012. The provision charged to operations was increased by $2.53 million due to a significant increase in loan charge-offs, primarily attributable to losses created by the sale of four problem loans totaling $2.64 million, and adding a provision for the acquired PCI portfolio. The provision attributed to PCI loans was $747 thousand, of which $296 thousand was charged to operations and $451 thousand was recorded through the FDIC indemnification asset. No provision was recorded for PCI loans in 2012. See Allowance for Loan Losses in the Financial Condition section below.

Noninterest Income

Noninterest income consists of all revenues not included in interest and fee income related to earning assets. Noninterest income comprised 24.83% of total net interest and noninterest income in 2014, 24.52% in 2013, and 28.96% in 2012.

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The following table presents the components of, and changes in, noninterest income in the periods indicated:

(Amounts in thousands)	Year Ended December 31, 2014	2013	2012	2014 Compared to 2013 Increase (Decrease)	% Change	2013 Compared to 2012 Increase (Decrease)	% Change
Wealth management	$ 3,030	$ 3,412	$ 3,701	$ (382)	-11.20%	$ (289)	-7.81%
Service charges on deposit accounts	13,828	13,558	14,063	270	1.99%	(505)	-3.59%
Other service charges and fees	7,581	7,151	6,462	430	6.01%	689	10.66%
Insurance commissions	6,555	5,933	5,743	622	10.48%	190	3.31%
Net impairment loss	(737)	(320)	(942)	(417)	-130.31%	622	66.03%
Net (loss) gain on sale of securities	(1,385)	399	483	(1,784)	-447.12%	(84)	-17.39%
Net FDIC indemnification asset (amortization) accretion	(3,979)	(5,597)	458	1,618	28.91%	(6,055)	
Net gain on branch divestiture	755			755			
Other operating income	4,355	5,235	6,742	(880)	-16.81%	(1,507)	-22.35%
Noninterest income	$ 30,003	$ 29,771	$ 36,710	$ 232	0.78%	$ (6,939)	-18.90%

2014 Compared to 2013. Noninterest income increased $232 thousand, or 0.78%, in 2014. Wealth management revenues, which include fees and commissions for trust and investment advisory services, decreased due to a decline in FCWM income. Service charges on deposit accounts and other service charges and fees increased primarily from increases in monthly service charges on demand deposit accounts, credit card income, and interchange income offset by a decrease in nonsufficient fee income. Insurance commissions increased largely due to increased levels of contingent profit-sharing commissions and a general increase in premium commissions. We incurred OTTI charges of $737 thousand in 2014 compared to $320 thousand in 2013 related to a non-Agency mortgage-backed security (MBS) and certain equity securities. We realized a net loss of $1.39 million on the sale of securities in 2014, which was driven by the sale of our only remaining non-Agency MBS at a loss of $1.62 million. See Note 3, Investment Securities, to the Consolidated Financial Statements in Item 8 of this report. We recorded net amortization related to the FDIC indemnification asset of $3.98 million. We realized a net gain of $755 thousand on the sale of thirteen branches to CresCom Bank during the fourth quarter of 2014. Other operating income decreased primarily due to a $540 thousand decrease in secondary market income, a $378 thousand decrease from a loyalty incentive received from a third-party vendor in 2013, and a $296 thousand decrease in gains recognized from debt prepayments in 2013. These decreases in other operating income were offset by a $536 thousand benefit related to bank owned life insurance and $400 thousand litigation settlement.

Excluding the impact from OTTI charges, the sale of securities, the net amortization on the FDIC indemnification asset, the net gain on branch divestitures, the net gain on debt prepayments, and non-recurring insurance benefit, noninterest income decreased $180 thousand, or 0.51%, to $34.81 million in 2014 compared with $34.99 million in 2013.

2013 Compared to 2012. Noninterest income decreased $6.94 million, or 18.90%, in 2013. Wealth management revenues decreased due to the departure of certain employees at FCWM. Other service charges and fees increased primarily from interchange fee income. We incurred OTTI charges of $320 thousand in 2013 compared to $942 thousand in 2012, related to a non-Agency MBS, and realized a net gain of $399 thousand on the sale of securities. See Note 3, Investment Securities, to the Consolidated Financial Statements in Item 8 of this report. We recorded net amortization related to the FDIC indemnification asset of $5.60 million due to improved loss estimates in the covered Waccamaw loan portfolio. Other operating income decreased in 2013 primarily due to the out-of-period adjustment in 2012 that positively affected income. Excluding the out-of-period adjustment, other operating income increased $888 thousand, or 20.43%, in 2013. Significant components of other operating income also included a loyalty incentive from a third-party vendor of $353 thousand, increases in dividend income of $327 thousand, a net gain on debt prepayments of $296 thousand, and a decrease in rental income of $209 thousand.

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Excluding the impact from OTTI charges, the net gain on the sale of securities, the net accretion/amortization on the FDIC indemnification asset, the net gain on debt prepayments, and the out-of-period adjustment, noninterest income increased $677 thousand, or 1.97%, to $34.99 million in 2013 compared with $34.32 million in 2012.

Noninterest Expense

The following table presents the components of, and changes in, noninterest expense in the periods indicated:

	Year Ended December 31,			2014 Compared to 2013		2013 Compared to 2012	
(Amounts in thousands)	2014	2013	2012	Increase (Decrease)	% Change	Increase (Decrease)	% Change
Salaries and employee benefits	$ 40,713	$ 41,235	$ 38,667	$ (522)	-1.27%	$ 2,568	6.64%
Occupancy of bank premises	6,338	7,033	6,872	(695)	-9.88%	161	2.34%
Furniture and equipment	4,952	4,966	4,145	(14)	-0.28%	821	19.81%
Amortization of intangible assets	787	729	804	58	7.96%	(75)	-9.33%
FDIC premiums and assessments	1,672	1,717	1,612	(45)	-2.62%	105	6.51%
FHLB debt prepayment	5,008			5,008			
Merger, acquisition, and divestiture expense	1,150	57	5,093	1,093	1917.54%	(5,036)	-98.88%
Other operating expense	22,242	23,248	21,190	(1,006)	-4.33%	2,058	9.71%
Total noninterest expense	$ 82,862	$ 78,985	$ 78,383	$ 3,877	4.91%	$ 602	0.77%

2014 Compared to 2013. Noninterest expense increased $3.88 million, or 4.91%, in 2014. Salaries and employee benefits decreased due to a one-time charge to accrue for contractual executive severance of $1.07 million in 2013. Exclusive of the severance charge, salaries and employee benefits increased $549 thousand, or 1.37%. Employee benefits included an increase in incentive compensation of $836 thousand. Full-time equivalent employees totaled 678 as of December 31, 2014, compared to 729 as of December 31, 2013. The decrease was primarily due to branch consolidation and divestiture activities offset by the Bank of America branch acquisition. Occupancy, furniture, and equipment expense decreased $709 thousand, or 5.91%, which was primarily due to branch closures between the periods. In 2014, we prepaid a $50 million FHLB convertible advance with a May 2017 maturity and 4.21% interest rate and $10 million of a $50 million FHLB convertible advance with a May 2017 maturity and 4.15% interest rate, which resulted in a prepayment penalty of $5.01 million. Expenses related to branch acquisition and divestiture activities totaled $1.15 million in 2014 in connection with the acquisition of seven branches from Bank of America and the sale of thirteen branches to CresCom compared to $57 thousand in 2013. The decrease in other operating expense included a $684 thousand decrease in marketing expenses and a $528 thousand decrease in legal expenses offset by an increase in interchange expense of $497 thousand. Other operating expense also included an increase in the net loss on sales and expenses related to other real estate owned (OREO) of $56 thousand to $2.09 million in 2014 compared to $2.04 million in 2013.

2013 Compared to 2012. Noninterest expense increased $602 thousand, or 0.77%, in 2013. Salaries and employee benefits increased largely from a one-time charge to accrue for contractual executive severance of $1.07 million. Exclusive of the severance charge, salaries and employee benefits increased $1.50 million, or 3.87%. Employee benefits included increases in medical expense of $735 thousand, incentive stock compensation expense of $368 thousand, and retirement plan expense of $342 thousand. Salaries and employee benefits attributed to the Peoples and Waccamaw acquisitions totaled $5.05 million in 2013, which represents an increase of $1.26 million compared to 2012. Full-time equivalent employees totaled 729 as of December 31, 2013, compared to 760 as of December 31, 2012. Occupancy, furniture, and equipment expense increased $982 thousand, or 8.91%, which included increased depreciation costs in connection with the Waccamaw acquisition and core operating system of $856 thousand. We incurred merger related costs of $57 thousand in 2013 compared to $5.09 million in 2012 in connection with the Peoples and Waccamaw acquisitions. The increase in other operating expense included charges related to seven scheduled branch closures/consolidations of

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$1.52 million, which occurred in the first half of 2014, and a net loss on sales and expenses on OREO of $2.04 million in 2013 compared to $1.89 million in 2012. Significant components of other operating expense also included increases in legal fees of $469 thousand, incentive stock compensation expense to directors of $158 thousand, and communication expenses of $157 thousand.

Income Tax Expense

2014 Compared to 2013. Income tax as a percentage of pretax income may vary significantly from statutory rates due to permanent differences, which are items of income and expense excluded by law from the calculation of taxable income. Our most significant permanent differences generally include interest income on municipal securities and increases in the cash surrender value of officers life insurance policies, which are both exempt from federal income tax. Income tax expense increased $2.18 million, or 9.34%, and the effective rate increased 71 basis points to 32.59% in 2014. The increase in the effective tax rate was largely due to an increase in taxable revenues as a percentage of net earnings and a decrease in the relative amounts of nontaxable revenues.

2013 Compared to 2012. Income tax expense decreased $3.22 million, or 22.79%, and the effective rate decreased 121 basis points to 31.88% in 2013. The decrease in the effective tax rate was largely due to a decrease in taxable revenues as a percentage of net earnings.

Non-GAAP Financial Measures

The efficiency ratio is a non-GAAP financial measure that management believes provides investors with important information about our operating expense control and efficiency of operations. Management also believes this ratio focuses attention on our core operating performance over time and is highly useful in comparing period-to-period operating performance of core business operations. However, this measure is supplemental and is not a substitute for an analysis of performance based on GAAP measures. Our efficiency may not be comparable to efficiency ratios reported by other financial institutions.

We calculate our efficiency ratio by dividing adjusted noninterest expense by the sum of tax equivalent net interest income and adjusted noninterest income. Adjusted noninterest expense excludes expenses and losses related to OREO, which may vary significantly from period to period without substantially affecting operations, and other non-core, nonrecurring items. Noninterest income excludes securities gains and losses, which may vary significantly from period to period without substantially affecting operations; OTTI charges; and other non-core, nonrecurring items. Our non-GAAP efficiency ratio measure is different from the GAAP-based efficiency ratio calculation that uses noninterest expense and income from the consolidated statements of income.

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The following table presents GAAP and non-GAAP efficiency ratio components and calculations in the period indicated:

	Year Ended December 31,		
(Amounts in thousands)	**2014**	**2013**	**2012**
GAAP-based efficiency ratio			
Noninterest expense	$ 82,862	$ 78,985	$ 78,383
Net interest income plus noninterest income	120,821	121,413	126,766
GAAP-based efficiency ratio	68.58%	65.05%	61.83%
Non-GAAP efficiency ratio			
Noninterest expense	$ 82,862	$ 78,985	$ 78,383
Non-GAAP adjustments:			
Merger, acquisition, and divestiture expense	(1,150)	(57)	(5,093)
FHLB debt prepayment fees	(5,008)		
OREO expense and net loss	(2,094)	(2,037)	(1,893)
Other non-core, non-recurring expense items	(1,573)	(2,700)	
Total non-GAAP adjustments	(9,825)	(4,794)	(6,986)
Adjusted noninterest expense	73,037	74,191	71,397
Net interest income plus noninterest income	120,821	121,413	126,766
Non-GAAP adjustments:			
Tax equivalency adjustment	2,557	2,741	2,747
Net impairment losses recognized in earnings	737	320	942
Net loss (gain) on sale of securities	1,385	(399)	(483)
Net gain on debt prepayment		(296)	
Prospective correction of prior period understatment			(2,395)
Net gain on branch divestiture	(755)		
Other non-core, non-recurring income items	(936)		
Total non-GAAP adjustments	2,988	2,366	811
Adjusted net interest income plus noninterest income	123,809	123,779	127,577
Non-GAAP efficiency ratio	58.99%	59.94%	55.96%

Financial Condition

Total assets were $2.61 billion as of December 31, 2014, an increase of $5.42 million, or 0.21%, compared with $2.60 billion as of December 31, 2013. Total liabilities were $2.26 billion as of December 31, 2014, a decrease of $17.35 million, or 0.76%, compared with $2.27 billion as of December 31, 2013. Our book value per as-converted common share was $18.06 as of December 31, 2014, an increase of $1.27, compared with $16.79 as of December 31, 2013.

Cash and Cash Equivalents

Cash and cash equivalents as of December 31, 2014, increased $181.09 million compared to December 31, 2013. The increase was primarily due to branch acquisition and divestiture activity in which the Company assumed significantly more deposits than loans and other assets sold.

Investment Securities

Available-for-sale securities as of December 31, 2014, decreased $193.70 million, or 37.26%, compared to December 31, 2013. The decrease in the available-for-sale securities portfolio was part of our strategic initiative to shift our mix of earning assets towards loans. Held-to-maturity securities as of December 31, 2014, increased

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$57.95 million compared to $568 thousand as of December 31, 2013 due to the purchase of short-term bonds to provide funding to extinguish certain wholesale borrowings when due. Investment securities classified as held to maturity are comprised primarily of U.S. Agency securities and high-grade municipal bonds.

The following table presents the market value as a percentage amortized cost, the average life, and the average duration of the investment portfolios:

	December 31,					
	2014			2013		
	Available for Sale	Held to Maturity	Total	Available for Sale	Held to Maturity	Total
Market value to fair value	97.95%	99.90%	98.24%	95.97%	101.94%	95.98%
Average life (in years)	8.39	2.95	7.58	7.54	1.33	7.53
Average duration (in years)	7.37	2.83	6.70	6.41	1.25	6.40

The following table details the amortized cost and fair value of investment securities as of the dates indicated:

	December 31,					
	2014		2013		2012	
(Amounts in thousands)	Amortized Cost	Fair Value	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Available for Sale						
U.S. Treasury securities	$	$	$ 9,708	$ 9,013	$	$
Municipal securities	134,784	138,915	147,049	144,280	151,119	159,217
Single issue trust preferred securites	55,822	46,137	55,764	46,234	55,707	44,646
Corporate securities	5,000	5,109	5,000	4,871		
Mortgage-backed securities:						
Agency	137,110	135,717	306,319	300,386	310,323	315,897
Non-Agency Alt-A residential			12,543	9,789	14,215	11,067
Total mortgage-backed securities	137,110	135,717	318,862	310,175	324,538	326,964
Equity securities	226	239	5,259	5,247	3,446	3,531
Total available for sale	$ 332,942	$ 326,117	$ 541,642	$ 519,820	$ 534,810	$ 534,358
Held to Maturity						
U.S. Agency securities	$ 46,987	$ 46,955	$ 568	$ 579	$ 816	$ 832
Municipal securities	379	386				
Corporate securities	10,582	10,548				
Total held to maturity	$ 57,948	$ 57,889	$ 568	$ 579	$ 816	$ 832

Investment securities are reviewed quarterly for possible OTTI. The review includes an analysis of each individual investment s facts and circumstances, such as the length of time fair value has been below cost, the timing and amount of contractual cash flows, the expectation for that security s performance, the creditworthiness of the issuer, and our intent to hold the security to recovery or maturity. If a decline in value is determined to be other-than-temporary, the value of the security is reduced and a corresponding charge to noninterest income is recognized. If a debt security is determined to be other-than-temporarily impaired, we determine the amount of the impairment due to credit, recognized in earnings, and the amount due to other factors, recognized in other comprehensive income.

We recognized credit-related OTTI charges in earnings associated with debt securities beneficially owned of $705 thousand in 2014, $320 thousand in 2013, and $942 thousand in 2012. These charges were related to a non-Agency MBS that was subsequently sold in November 2014. We recognized OTTI charges in earnings associated with certain equity securities of $32 thousand in 2014 and no charges in 2013 or 2012. See Note 3, Investment Securities, to the Consolidated Financial Statements in Item 8 of this report.

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Loans Held for Sale

Loans held for sale as of December 31, 2014, increased $909 thousand to $1.79 million compared to December 31, 2013. Loans held for sale consist of mortgage loans sold on a best efforts basis into the secondary market; thus, we do not retain the interest rate risk involved in these long-term commitments. The gross notional amount of outstanding commitments to originate mortgage loans in the secondary market totaled $1.39 million for 9 commitments as of December 31, 2014, and $3.68 million for 19 commitments as of December 31, 2013.

Loans Held for Investment

Loans held for investment as of December 31, 2014, decreased $21.31 million, or 1.25%, compared to December 31, 2013. Our loans held for investment are grouped into three segments (commercial loans, consumer real estate loans, and consumer and other loans) with each segment divided into various classes. Covered loans are defined as loans acquired in FDIC-assisted transactions that are covered by loss share agreements. Our covered loan portfolio as of December 31, 2014, decreased $29.44 million, or 19.41%, compared to December 31, 2013, due to continued runoff in the covered Waccamaw portfolio. The non-covered loan portfolio as of December 31, 2014, increased $8.14 million, or 0.52%, compared to December 31, 2013, primarily due to strong growth in commercial real estate originations in Southern West Virginia and Central North Carolina markets, which was offset by loans sold in the branch divestiture. The average loan to deposit ratio was 88.37% as of December 31, 2014, compared to 85.24% as of December 31, 2013. The held for investment portfolio continues to be diversified among loan types and industry segments. See Note 4, Loans, to the Consolidated Financial Statements in Item 8 of this report.

The following table presents loans, net of unearned income with non-covered loans disaggregated by class, as of the periods indicated. There were no covered loans before 2012.

			December 31,		
(Amounts in thousands)	**2014**	**2013**	**2012**	**2011**	**2010**
Non-covered loans held for investment					
Commercial loans					
Construction, development, and other land	$ 41,271	$ 35,255	$ 57,434	$ 61,768	$ 83,812
Commercial and industrial	83,099	95,455	88,738	91,939	94,123
Multi-family residential	97,480	70,197	65,694	77,050	67,824
Single family non-owner occupied	135,171	135,559	135,912	106,743	104,960
Non-farm, non-residential	473,906	475,911	448,810	336,005	351,904
Agricultural	1,599	2,324	1,709	1,374	1,342
Farmland	29,517	32,614	34,570	37,161	36,954
Total commercial loans	862,043	847,315	832,867	712,040	740,919
Consumer real estate loans					
Home equity lines	110,957	111,770	111,081	111,387	111,620
Single family owner occupied	485,475	496,012	473,547	473,067	444,197
Owner occupied construction	32,799	28,703	16,223	19,577	18,349
Total consumer real estate loans	629,231	636,485	600,851	604,031	574,166
Consumer and other loans					
Consumer loans	69,347	71,313	78,163	67,129	63,475
Other	6,555	3,926	5,666	12,867	7,646
Total consumer and other loans	75,902	75,239	83,829	79,996	71,121
Non-covered loans held for investment	1,567,176	1,559,039	1,517,547	1,396,067	1,386,206
Covered loans held for investment	122,240	151,682	207,106		
Total loans held for investment	1,689,416	1,710,721	1,724,653	1,396,067	1,386,206
Allowance for loan losses	20,227	24,077	25,770	26,205	26,482
Total loans held for investment, less allowance	$ 1,669,189	$ 1,686,644	$ 1,698,883	$ 1,369,862	$ 1,359,724

Loans held for sale	$	1,792	$	883	$	6,672	$	5,820	$	4,694

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The following table presents covered loans disaggregated by class as of the periods indicated:

	December 31,		
(Amounts in thousands)	**2014**	**2013**	**2012**
Commercial loans			
Construction, development, and other land	$ 13,100	$ 15,865	$ 26,595
Commercial and industrial	2,662	3,325	6,948
Multi-family residential	1,584	1,933	2,611
Single family non-owner occupied	5,918	7,449	11,428
Non-farm, non-residential	25,317	34,646	48,565
Agricultural	43	164	144
Farmland	716	873	1,091
Total commercial loans	49,340	64,255	97,382
Consumer real estate loans			
Home equity lines	60,391	69,206	81,445
Single family owner occupied	11,968	16,919	22,961
Owner occupied construction	453	1,184	1,644
Total consumer real estate loans	72,812	87,309	106,050
Consumer and other loans			
Consumer loans	88	118	3,674
Total consumer and other loans	88	118	3,674
Total covered loans held for investment	$122,240	$ 151,682	$ 207,106

The following table details the percentage of loans to total loans in the non-covered portfolio, by loan class, as of the periods indicated:

	December 31,				
	2014	**2013**	**2012**	**2011**	**2010**
Non-covered loans					
Commercial loans					
Construction, development, and other land	2.64%	2.26%	3.78%	4.42%	6.05%
Commercial and industrial	5.30%	6.12%	5.85%	6.58%	6.79%
Multi-family residential	6.22%	4.50%	4.33%	5.52%	4.89%
Single family non-owner occupied	8.63%	8.70%	8.96%	7.65%	7.57%
Non-farm, non-residential	30.24%	30.53%	29.57%	24.07%	25.39%
Agricultural	0.10%	0.15%	0.11%	0.10%	0.10%
Farmland	1.88%	2.09%	2.28%	2.66%	2.67%
Consumer real estate loans					
Home equity lines	7.08%	7.17%	7.32%	7.98%	8.05%
Single family owner occupied	30.98%	31.82%	31.21%	33.89%	32.04%
Owner occupied construction	2.09%	1.84%	1.07%	1.40%	1.32%
Consumer and other loans					
Consumer loans	4.42%	4.57%	5.15%	4.81%	4.58%
Other	0.42%	0.25%	0.37%	0.92%	0.55%
Total loans	100.00%	100.00%	100.00%	100.00%	100.00%

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The following table details the percentage of loans to total loans in the covered portfolio, by loan class, as of the periods indicated:

	December 31,		
	2014	2013	2012
Covered loans			
Commercial loans			
Construction, development, and other land	10.72%	10.46%	12.84%
Commercial and industrial	2.18%	2.19%	3.35%
Multi-family residential	1.30%		