

WILSON BANK HOLDING CO  
Form 10-Q  
November 09, 2015  
Table of Contents

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2015

or

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_  
Commission File Number 0-20402

WILSON BANK HOLDING COMPANY  
(Exact name of registrant as specified in its charter)

Tennessee 62-1497076  
(State or other jurisdiction of (I.R.S. Employer  
incorporation or organization) Identification No.)

623 West Main Street, Lebanon, TN 37087  
(Address of principal executive offices) (Zip Code)

(615) 444-2265  
(Registrant's telephone number, including area code)

Not Applicable

(Former name, former address and former fiscal year, if changed since last report)

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

No

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

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

Large accelerated filer  Accelerated filer

Non-accelerated filer  (Do not check if a smaller reporting company) Smaller reporting company

Edgar Filing: WILSON BANK HOLDING CO - Form 10-Q

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

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

Common stock outstanding: 7,650,645 shares at November 9, 2015

---

Table of Contents

Part I:	<u>FINANCIAL INFORMATION</u>	<u>3</u>
Item 1.	<u>Financial Statements.</u>	<u>3</u>
The unaudited consolidated financial statements of the Company and its subsidiary are as follows:		
	<u>Consolidated Balance Sheets — September 30, 2015 and December 31, 2014.</u>	<u>3</u>
	<u>Consolidated Statements of Earnings — For the three months and nine months ended September 30, 2015 and 2014.</u>	<u>4</u>
	<u>Consolidated Statements of Comprehensive Earnings — For the three months and nine months ended September 30, 2015 and 2014.</u>	<u>5</u>
	<u>Consolidated Statements of Cash Flows — For the nine months ended September 30, 2015 and 2014.</u>	<u>6</u>
Item 2.	<u>Management’s Discussion and Analysis of Financial Condition and Results of Operations.</u>	<u>27</u>
Item 3.	<u>Quantitative and Qualitative Disclosures About Market Risk.</u>	<u>39</u>
	Disclosures required by Item 3 are incorporated by reference to Management’s Discussion and Analysis of Financial Condition and Results of Operations.	
Item 4.	<u>Controls and Procedures.</u>	<u>39</u>
Part II:	<u>OTHER INFORMATION</u>	<u>40</u>
Item 1.	<u>Legal Proceedings.</u>	<u>40</u>
Item 1A.	<u>Risk Factors.</u>	<u>40</u>
Item 2.	<u>Unregistered Sales of Equity Securities and Use of Proceeds.</u>	<u>40</u>
Item 3.	<u>Defaults Upon Senior Securities.</u>	<u>40</u>
Item 4.	<u>Mine Safety Disclosures.</u>	<u>40</u>
Item 5.	<u>Other Information.</u>	<u>40</u>
Item 6.	<u>Exhibits.</u>	<u>40</u>
	<u>Signatures</u>	<u>41</u>
	EX-31.1 SECTION 302 CERTIFICATION OF THE CEO	
	EX-31.2 SECTION 302 CERTIFICATION OF THE CFO	
	EX-32.1 SECTION 906 CERTIFICATION OF THE CEO	
	EX-32.2 SECTION 906 CERTIFICATION OF THE CFO	
	EX -101 INTERACTIVE DATA FILE	



Table of Contents

## Part I. Financial Information

## Item 1. Financial Statements

## WILSON BANK HOLDING COMPANY

## Consolidated Balance Sheets

September 30, 2015 and December 31, 2014

(Unaudited)

	September 30, 2015	December 31, 2014
	(Dollars in Thousands Except Share Amounts)	
Assets		
Loans	\$ 1,467,036	\$ 1,352,437
Less: Allowance for loan losses	(22,702)	(22,572)
Net loans	1,444,334	1,329,865
Securities:		
Held to maturity, at cost (market value \$25,958 and \$28,400, respectively)	25,790	28,123
Available-for-sale, at market (amortized cost \$292,613 and \$347,520, respectively)	293,051	346,420
Total securities	318,841	374,543
Loans held for sale	13,437	9,466
Restricted equity securities	3,012	3,012
Federal funds sold	15,405	16,005
Total earning assets	1,795,029	1,732,891
Cash and due from banks	66,191	52,002
Bank premises and equipment, net	41,307	40,123
Accrued interest receivable	5,340	5,463
Deferred income tax asset	9,169	9,171
Other real estate	6,533	7,298
Bank owned life insurance and annuity contracts	26,560	17,331
Other assets	4,442	4,158
Goodwill	4,805	4,805
Total assets	\$ 1,959,376	\$ 1,873,242
Liabilities and Stockholders' Equity		
Deposits	\$ 1,723,827	\$ 1,660,270
Securities sold under repurchase agreements	2,854	3,437
Accrued interest and other liabilities	14,153	8,643
Total liabilities	1,740,834	1,672,350
Stockholders' equity:		
Common stock, \$2.00 par value; authorized 15,000,000 shares, issued and outstanding 7,650,645 and 7,571,968 shares, respectively	15,301	15,144
Additional paid-in capital	61,283	57,709
Retained earnings	141,688	128,718
Net unrealized gains (losses) on available-for-sale securities, net of income taxes of \$168 and \$421, respectively	270	(679)
Total stockholders' equity	218,542	200,892
Total liabilities and stockholders' equity	\$ 1,959,376	\$ 1,873,242

See accompanying notes to consolidated financial statements (unaudited)



Table of Contents

## WILSON BANK HOLDING COMPANY

## Consolidated Statements of Earnings

Three Months and Nine Months Ended September 30, 2015 and 2014

(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014
	(Dollars in Thousands Except Per Share Amounts)			
Interest income:				
Interest and fees on loans	\$18,262	\$17,069	\$53,123	\$49,456
Interest and dividends on securities:				
Taxable securities	1,356	1,592	4,492	4,832
Exempt from Federal income taxes	208	173	551	505
Interest on loans held for sale	104	83	269	196
Interest on Federal funds sold	22	33	100	120
Interest and dividends on restricted securities	30	30	91	91
Total interest income	19,982	18,980	58,626	55,200
Interest expense:				
Interest on negotiable order of withdrawal accounts	389	406	1,143	1,197
Interest on money market and savings accounts	449	588	1,447	1,756
Interest on time deposits	1,275	1,426	3,925	4,398
Interest on federal funds purchased	—	1	1	1
Interest on securities sold under repurchase agreements	1	5	5	19
Total interest expense	2,114	2,426	6,521	7,371
Net interest income before provision for loan losses	17,868	16,554	52,105	47,829
Provision for loan losses	109	87	265	364
Net interest income after provision for loan losses	17,759	16,467	51,840	47,465
Non-interest income:				
Service charges on deposit accounts	1,401	1,174	3,755	3,139
Other fees and commissions	2,768	2,314	7,758	6,693
Gain on sale of loans	1,061	796	3,057	1,926
Gain on sale of premises and equipment	—	—	—	7
Gain on sale of other real estate	259	—	305	—
Gain on sale of securities	19	5	185	293
Total non-interest income	5,508	4,289	15,060	12,058
Non-interest expense:				
Salaries and employee benefits	7,802	6,926	23,348	20,462
Occupancy expenses, net	944	858	2,542	2,250
Furniture and equipment expense	538	447	1,535	1,286
Data processing expense	685	574	1,773	1,713
Directors' fees	169	166	526	512
Other operating expenses	3,245	2,979	8,239	8,908
Loss on the sale of premises and equipment	22	—	30	—
Loss on sale of other assets	—	—	2	3
Loss on sale of other real estate	—	34	—	190
Total non-interest expense	13,405	11,984	37,995	35,324
Earnings before income taxes	9,862	8,772	28,905	24,199

Edgar Filing: WILSON BANK HOLDING CO - Form 10-Q

Income taxes	3,774	3,421	11,000	9,522
Net earnings	\$6,088	\$5,351	\$17,905	\$14,677
Weighted average number of shares outstanding-basic	7,637,448	7,559,136	7,615,096	7,538,860
Weighted average number of shares outstanding-diluted	7,640,796	7,563,354	7,618,530	7,543,210
Basic earnings per common share	\$0.80	\$0.71	\$2.35	\$1.95
Diluted earnings per common share	\$0.80	\$0.71	\$2.35	\$1.95
Dividends per share	\$0.35	\$0.30	\$0.65	\$0.60
See accompanying notes to consolidated financial statements (unaudited)				

4

---



Table of Contents

## WILSON BANK HOLDING COMPANY

## Consolidated Statements of Comprehensive Earnings

Three Months and Nine Months Ended September 30, 2015 and 2014

(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014
	(In Thousands)			
Net earnings	\$6,088	\$5,351	\$17,905	\$14,677
Other comprehensive earnings (loss), net of tax:				
Unrealized gains (losses) on available-for-sale securities arising during period, net of taxes of \$623,1,005 \$417, \$660 and \$1,320, respectively		(674	) 1,063	2,126
Reclassification adjustment for net gains included in net earnings, net of taxes of \$7, \$2, \$71, and \$112, respectively	(12	) (3	) (114	) (181
Other comprehensive earnings (loss)	993	(677	) 949	1,945
Comprehensive earnings	\$7,081	\$4,674	\$18,854	\$16,622

See accompanying notes to consolidated financial statements (unaudited)

Table of Contents

## WILSON BANK HOLDING COMPANY

## Consolidated Statements of Cash Flows

Nine Months Ended September 30, 2015 and 2014

Increase (Decrease) in Cash and Cash Equivalents

(Unaudited)

	Nine Months Ended September 30,	
	2015	2014
	(In Thousands)	
Cash flows from operating activities:		
Interest received	\$60,239	\$56,628
Fees and commissions received	11,513	9,832
Proceeds from sale of loans held for sale	120,450	74,251
Origination of loans held for sale	(121,364)	(74,084)
Interest paid	(6,755)	(7,666)
Cash paid to suppliers and employees	(31,432)	(29,076)
Income taxes paid	(11,499)	(10,132)
Net cash provided by operating activities	21,152	19,753
Cash flows from investing activities:		
Proceeds from maturities, calls, and principal payments of held-to-maturity securities	2,663	1,452
Proceeds from maturities, calls, and principal payments of available-for-sale securities	64,972	51,317
Proceeds from the sale of available-for-sale securities	42,844	49,021
Purchase of held-to-maturity securities	(527)	(3,609)
Purchase of available-for-sale securities	(54,017)	(107,535)
Loans made to customers, net of repayments	(114,875)	(101,315)
Purchase of Bank owned life insurance	(8,464)	(5,000)
Purchase of premises and equipment	(3,118)	(3,024)
Proceeds from sale of premises and equipment	—	7
Proceeds from sale of other real estate	1,207	2,419
Proceeds from sale of other assets	12	1
Net cash used in investing activities	(69,303)	(116,266)
Cash flows from financing activities:		
Net increase in non-interest bearing, savings and NOW deposit accounts	83,403	103,666
Net decrease in time deposits	(19,846)	(33,649)
Net decrease in securities sold under repurchase agreements	(583)	(4,230)
Dividends paid	(4,935)	(4,510)
Proceeds from sale of common stock pursuant to dividend reinvestment	3,511	3,204
Repurchase of common stock	—	(94)
Proceeds from exercise of stock options	190	156
Net cash provided by financing activities	61,740	64,543
Net increase (decrease) in cash and cash equivalents	13,589	(31,970)
Cash and cash equivalents at beginning of period	68,007	111,504
Cash and cash equivalents at end of period	\$81,596	\$79,534

See accompanying notes to consolidated financial statements (unaudited)



Table of Contents

## WILSON BANK HOLDING COMPANY

Consolidated Statements of Cash Flows, Continued

Nine Months Ended September 30, 2015 and 2014

Increase (Decrease) in Cash and Cash Equivalents

(Unaudited)

	Nine Months Ended September 30,	
	2015	2014
	(In Thousands)	
Reconciliation of net earnings to net cash provided by operating activities:		
Net earnings	\$17,905	\$14,677
Adjustments to reconcile net earnings to net cash provided by operating activities:		
Depreciation, amortization, and accretion	3,394	3,159
Provision for loan losses	265	364
Loss (gain) on sale and writedown of other real estate	(305	) 190
Security gains	(185	) (293
Stock option compensation	30	32
Increase in taxes payable	88	89
Loss on the sale of other assets	2	3
Loss (gain) on the sale of premises and equipment	30	(7
Increase in loans held for sale	(3,971	) (1,759
Increase in deferred tax assets	(587	) (699
Increase in other assets, net	(1,059	) (1,191
Decrease (increase) in interest receivable	123	(123
Increase in other liabilities	5,656	5,606
Decrease in interest payable	(234	) (295
Total adjustments	\$3,247	\$5,076
Net cash provided by operating activities	\$21,152	\$19,753
Supplemental schedule of non-cash activities:		
Unrealized gain (loss) in values of securities available-for-sale, net of taxes of \$589 and \$1,208 for the nine months ended September 30, 2015 and 2014, respectively	\$949	\$1,945
Non-cash transfers from loans to other real estate	\$1,317	\$424
Non-cash transfers from other real estate to loans	\$1,180	\$1,080
Non-cash transfers from loans to other assets	\$4	\$8
See accompanying notes to consolidated financial statements (unaudited)		

Table of Contents

WILSON BANK HOLDING COMPANY

Notes to Consolidated Financial Statements

(Unaudited)

Note 1. Summary of Significant Accounting Policies

Nature of Business — Wilson Bank Holding Company (the “Company”) is a bank holding company whose primary business is conducted by its wholly-owned subsidiary, Wilson Bank & Trust (the “Bank”). The Bank is a commercial bank headquartered in Lebanon, Tennessee. The Bank provides a full range of banking services in its primary market areas of Wilson, Davidson, Rutherford, Trousdale, Sumner, Dekalb, Putnam and Smith Counties, Tennessee.

Basis of Presentation — The accompanying unaudited, consolidated financial statements have been prepared in accordance with instructions to Form 10-Q and therefore do not include all information and footnotes necessary for a fair presentation of financial position, results of operations, and cash flows in conformity with U.S. generally accepted accounting principles. All adjustments consisting of normally recurring accruals that, in the opinion of management, are necessary for a fair presentation of the financial position and results of operations for the periods covered by the report have been included. The accompanying unaudited consolidated financial statements should be read in conjunction with the Company’s consolidated financial statements and related notes appearing in the 2014 Annual Report previously filed on Form 10-K.

These consolidated financial statements include the accounts of the Company and its wholly-owned subsidiary.

Significant intercompany transactions and accounts are eliminated in consolidation.

Use of Estimates — The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities as of the balance sheet date and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term include the determination of the allowance for loan losses, the valuation of deferred tax assets, determination of any impairment of intangibles, other-than-temporary impairment of securities, the valuation of other real estate, and the fair value of financial instruments. These financial statements should be read in conjunction with the Company’s Annual Report on Form 10-K for the year ended December 31, 2014. There have been no significant changes to the Company’s significant accounting policies as disclosed in the Company’s Annual Report on Form 10-K for the year ended December 31, 2014.

Loans — Loans are reported at their outstanding principal balances less unearned income, the allowance for loan losses and any deferred fees or costs on originated loans. Interest income on loans is accrued based on the principal balance outstanding. Loan origination fees, net of certain loan origination costs, are deferred and recognized as an adjustment to the related loan yield using a method which approximates the interest method.

Loans are charged off when management believes that the full collectability of the loan is unlikely. As such, a loan may be partially charged-off after a “confirming event” has occurred which serves to validate that full repayment pursuant to the terms of the loan is unlikely.

Loans are placed on nonaccrual status when there is a significant deterioration in the financial condition of the borrower, which often is determined when the principal or interest is more than 90 days past due, unless the loan is both well-secured and in the process of collection. Generally, all interest accrued but not collected for loans that are placed on nonaccrual status, is reversed against current income. Interest income is subsequently recognized only to the extent cash payments are received while the loan is classified as nonaccrual, but interest income recognition is reviewed on a case-by-case basis. A nonaccrual loan is returned to accruing status once the loan has been brought current and collection is reasonably assured or the loan has been “well-secured” through other techniques. Past due status is determined based on the contractual due date per the underlying loan agreement.

All loans that are placed on nonaccrual are further analyzed to determine if they should be classified as impaired loans. At December 31, 2014 and at September 30, 2015, there were no loans classified as nonaccrual that were not also deemed to be impaired except for those loans not individually evaluated for impairment as described below. A loan is considered to be impaired when it is probable the Company will be unable to collect all principal and interest payments due in accordance with the contractual terms of the loan. This determination is made using a variety of

techniques, which include a review of the borrower's financial condition, debt-service coverage ratios, global cash flow analysis, guarantor support, other loan file information, meetings with borrowers, inspection or reappraisal of collateral and/or consultation with legal counsel as well as results of reviews of other similar industry credits (e.g. builder loans, development loans, church loans, etc). Prior to January 1, 2015, loans with an identified weakness and principal balance of \$100,000 or more were subject to individual identification for impairment. During the first quarter of 2015, the Company increased the threshold for identification of individually impaired loans to \$500,000, based on regulatory developments, continued improvement in loan quality

8

---

Table of Contents

trends and ratios and strengthening local economies in which the Company operates. Management believes that increasing the threshold will not materially impact the calculation of the allowance for loan losses. Individually identified impaired loans are measured based on the present value of expected payments using the loan's original effective rate as the discount rate, the loan's observable market price, or the fair value of the collateral if the loan is collateral dependent. If the recorded investment in the impaired loan exceeds the measure of fair value, a specific valuation allowance is established as a component of the allowance for loan losses or, in the case of collateral dependent loans, the excess may be charged off. Changes to the valuation allowance are recorded as a component of the provision for loan losses. Any subsequent adjustments to present value calculations for impaired loan valuations as a result of the passage of time, such as changes in the anticipated payback period for repayment, are recorded as a component of the provision for loan losses. For loans less than \$500,000, the Company assigns a valuation allowance to these loans utilizing an allocation rate equal to the allocation rate calculated for non-impaired loans of a similar type.

**Allowance for Loan Losses** — The allowance for loan losses is maintained at a level that management believes to be adequate to absorb probable losses in the loan portfolio. Loan losses are charged against the allowance when they are known. Subsequent recoveries are credited to the allowance. Management's determination of the adequacy of the allowance is based on an evaluation of the portfolio, current economic conditions, volume, growth, composition of the loan portfolio, homogeneous pools of loans, risk ratings of specific loans, historical loan loss factors, loss experience of various loan segments, identified impaired loans and other factors related to the portfolio. This evaluation is performed quarterly and is inherently subjective, as it requires material estimates that are susceptible to significant change including the amounts and timing of future cash flows expected to be received on any impaired loans. In assessing the adequacy of the allowance, we also consider the results of our ongoing independent loan review process. We undertake this process both to ascertain whether there are loans in the portfolio whose credit quality has weakened over time and to assist in our overall evaluation of the risk characteristics of the entire loan portfolio. Our loan review process includes the judgment of management, independent loan reviewers, and reviews that may have been conducted by third-party reviewers. We incorporate relevant loan review results in the loan impairment determination. In addition, regulatory agencies, as an integral part of their examination process, will periodically review the Company's allowance for loan losses, and may require the Company to record adjustments to the allowance based on their judgment about information available to them at the time of their examinations.

**Recently Adopted Accounting Pronouncements**

There were no recently issued accounting pronouncements that are expected to materially impact the Company.

Table of Contents

## Note 2. Loans and Allowance for Loan Losses

For financial reporting purposes, the Company classifies its loan portfolio based on the underlying collateral utilized to secure each loan. This classification is consistent with those utilized in the Quarterly Report of Condition and Income filed by the Bank with the Federal Deposit Insurance Corporation ("FDIC").

The following schedule details the loans of the Company at September 30, 2015 and December 31, 2014:

	(In Thousands)	
	September 30, 2015	December 31, 2014
Mortgage loans on real estate		
Residential 1-4 family	\$357,360	\$350,758
Multifamily	53,956	31,242
Commercial	603,283	564,965
Construction and land development	286,381	245,830
Farmland	34,911	30,236
Second mortgages	8,053	9,026
Equity lines of credit	47,958	41,496
Total mortgage loans on real estate	1,391,902	1,273,553
Commercial loans	27,278	30,000
Agricultural loans	1,524	1,670
Consumer installment loans		
Personal	38,768	37,745
Credit cards	3,002	3,280
Total consumer installment loans	41,770	41,025
Other loans	9,700	10,530
	1,472,174	1,356,778
Net deferred loan fees	(5,138)	(4,341)
Total loans	1,467,036	1,352,437
Less: Allowance for loan losses	(22,702)	(22,572)
Net Loans	\$1,444,334	\$1,329,865

The adequacy of the allowance for loan losses is assessed at the end of each calendar quarter. The level of the allowance is based upon evaluation of the loan portfolio, past loan loss experience, current asset quality trends, known and inherent risks in the portfolio, adverse situations that may affect the borrowers' ability to repay (including the timing of future payment), the estimated value of any underlying collateral, composition of the loan portfolio, economic conditions, historical loss experience, industry and peer bank loan quality indications and other pertinent factors, including regulatory recommendations.



Table of Contents

Transactions in the allowance for loan losses for the nine months ended September 30, 2015 and year ended December 31, 2014 are summarized as follows:

	(In Thousands)										
	Residential 1-4 Family	Multifamily	Commercial Real Estate	Commercial Construction	Farm/land	Second Mortgages	Equity Lines of Credit	Commercial	Agricultural	Installment Other	Total
September 30, 2015											
Allowance for loan losses:											
Beginning balance	\$5,582	172	9,578	5,578	795	61	304	176	2	324	22,572
Provision	225	125	(1,259)	900	(185)	72	49	32	4	302	265
Charge-offs	(156)	—	(43)	(1)	—	(45)	(6)	—	(2)	(465)	(718)
Recoveries	37	—	315	32	1	—	1	6	2	189	583
Ending balance	\$5,688	297	8,591	6,509	611	88	348	214	6	350	22,702
Ending balance individually evaluated for impairment	\$208	—	711	—	—	—	—	—	—	—	919
Ending balance collectively evaluated for impairment	\$5,480	297	7,880	6,509	611	88	348	214	6	350	21,783
Ending balance loans acquired with deteriorated credit quality	\$—	—	—	—	—	—	—	—	—	—	—
Loans:											
Ending balance	\$357,360	53,956	603,283	286,381	34,911	8,053	47,958	27,278	1,524	51,470	1,472,174
Ending balance individually evaluated for impairment	\$1,378	—	8,703	—	575	—	—	—	—	—	10,656
Ending balance collectively evaluated for	\$355,982	53,956	594,580	286,381	34,336	8,053	47,958	27,278	1,524	51,470	1,461,518

impairment  
Ending  
balance  
loans  
acquired  
with  
deteriorated  
credit  
quality

\$— — — — — — — — — —

11

---

Table of Contents

	Residential 1-4 Family	Multifamily	Commercial Real Estate	Construction	Farmland	Second Mortgages	Equity Lines of Credit	Commercial	Agricultural	Installment and Other	Total
December 31, 2014											
Allowance for loan losses:											
Beginning balance	\$4,935	77	10,918	5,159	618	205	300	395	7	321	22,935
Provision	1,059	95	(378 )	102	176	(164 )	3	(641 )	(10 )	256	498
Charge-offs	(468 )	—	(968 )	(7 )	—	—	—	(37 )	—	(387 )	(1,867 )
Recoveries	56	—	6	324	1	20	1	459	5	134	1,006
Ending balance	\$5,582	172	9,578	5,578	795	61	304	176	2	324	22,572
Ending balance individually evaluated for impairment	\$376	—	1,135	—	120	—	—	—	—	—	1,631
Ending balance collectively evaluated for impairment	\$5,206	172	8,443	5,578	675	61	304	176	2	324	20,941
Ending balance loans acquired with deteriorated credit quality	\$—	—	—	—	—	—	—	—	—	—	—
Loans:											
Ending balance	\$350,758	31,242	564,965	245,830	30,236	9,026	41,496	30,000	1,670	51,555	1,356,778
Ending balance individually evaluated for impairment	\$3,061	—	6,455	—	701	280	—	—	—	—	10,497
Ending balance collectively evaluated for impairment	\$347,697	31,242	558,510	245,830	29,535	8,746	41,496	30,000	1,670	51,555	1,346,281
Ending balance loans	\$—	—	—	—	—	—	—	—	—	—	—

acquired  
with  
deteriorated  
credit  
quality

**Impaired Loans**

At September 30, 2015, the Company had certain impaired loans of \$4,868,000 which were on non-accruing interest status. At December 31, 2014, the Company had certain impaired loans of \$574,000 which were on non-accruing interest status. In each case, at the date such loans were placed on nonaccrual status, the Company reversed all previously accrued interest income against current year earnings. The following table presents the Company's impaired loans at September 30, 2015 and December 31, 2014.

Table of Contents

	In Thousands				
	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
September 30, 2015					
With no related allowance recorded:					
Residential 1-4 family	\$629	622	—	754	29
Multifamily	—	—	—	—	—
Commercial real estate	4,293	4,293	—	5,183	5
Construction	—	—	—	—	—
Farmland	575	575	—	383	—
Second mortgages	—	—	—	—	—
Equity lines of credit	—	—	—	—	—
Commercial	—	—	—	—	—
Agricultural	—	—	—	—	—
	\$5,497	5,490	—	6,320	34
With allowance recorded:					
Residential 1-4 family	\$764	756	208	768	32
Multifamily	—	—	—	—	—
Commercial real estate	4,420	6,113	711	4,558	147
Construction	—	—	—	—	—
Farmland	—	—	—	191	—
Second mortgages	—	—	—	—	—
Equity lines of credit	—	—	—	—	—
Commercial	—	—	—	—	—
Agricultural	—	—	—	—	—
	\$5,184	6,869	919	5,517	179
Total					
Residential 1-4 family	\$1,393	1,378	208	1,522	61
Multifamily	—	—	—	—	—
Commercial real estate	8,713	10,406	711	9,741	152
Construction	—	—	—	—	—
Farmland	575	575	—	574	—
Second mortgages	—	—	—	—	—
Equity lines of credit	—	—	—	—	—
Commercial	—	—	—	—	—
Agricultural	—	—	—	—	—
	\$10,681	12,359	919	11,837	213

Table of Contents

	In Thousands				
	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
December 31, 2014					
With no related allowance recorded:					
Residential 1-4 family	\$ 1,891	1,854	—	1,081	114
Multifamily	—	—	—	—	—
Commercial real estate	1,352	2,188	—	5,984	95
Construction	—	—	—	673	—
Farmland	—	—	—	—	—
Second mortgages	281	280	—	222	3
Equity lines of credit	—	—	—	—	—
Commercial	—	—	—	—	—
Agricultural, installment and other	—	—	—	—	—
	\$3,524	4,322	—	7,960	212
With allowance recorded:					
Residential 1-4 family	\$ 1,219	1,207	376	1,363	61
Multifamily	—	—	—	—	—
Commercial real estate	5,131	6,811	1,135	5,755	202
Construction	—	—	—	1,815	—
Farmland	702	701	120	767	7
Second mortgages	—	—	—	—	—
Equity lines of credit	—	—	—	—	—
Commercial	—	—	—	—	—
Agricultural, installment and other	—	—	—	—	—
	\$7,052	8,719	1,631	9,700	270
Total:					
Residential 1-4 family	\$3,110	3,061	376	2,444	175
Multifamily	—	—	—	—	—
Commercial real estate	6,483	8,999	1,135	11,739	297
Construction	—	—	—	2,488	—
Farmland	702	701	120	767	7
Second mortgages	281	280	—	222	3
Equity lines of credit	—	—	—	—	—
Commercial	—	—	—	—	—
Agricultural, installment and other	—	—	—	—	—
	\$10,576	13,041	1,631	17,660	482

Table of Contents

Impaired loans also include loans that the Company may elect to formally restructure due to the weakening credit status of a borrower such that the restructuring may facilitate a repayment plan that minimizes the potential losses that the Company may have to otherwise incur. These loans are classified as impaired loans and, if on non-accruing status as of the date of restructuring, the loans are included in the nonperforming loan balances. Not included in nonperforming loans are loans that have been restructured that were performing as of the restructure date.

**Troubled Debt Restructuring**

The Bank's loan portfolio includes certain loans that have been modified in a troubled debt restructuring (TDR), where economic concessions have been granted to borrowers who have experienced or are expected to experience financial difficulties. These concessions typically result from the Bank's loss mitigation activities and could include reductions in the interest rate, payment extensions, forgiveness of principal, forbearance or other actions. Certain TDRs are classified as nonperforming at the time of restructure and may only be returned to performing status after considering the borrower's sustained repayment performance for a reasonable period, generally six months.

The following table summarizes the carrying balances of TDR's at September 30, 2015 and December 31, 2014.

	September 30, 2015	December 31, 2014
	(In thousands)	
Performing TDRs	\$4,246	\$4,443
Nonperforming TDRs	1,968	3,597
Total TDRS	\$6,214	\$8,040

The following table outlines the amount of each troubled debt restructuring categorized by loan classification for the nine months ended September 30, 2015 and the year ended December 31, 2014 (in thousands, except for number of contracts):

	September 30, 2015			December 31, 2014		
	Number of Contracts	Pre Modification Recorded Investment	Post Modification Recorded Investment, Net of Related Allowance	Number of Contracts	Pre Modification Recorded Investment	Post Modification Recorded Investment, Net of Related Allowance
Residential 1-4 family	1	\$ 56	\$ 56	6	\$ 1,346	\$ 1,218
Multifamily	—	—	—	—	—	—
Commercial real estate	—	—	—	2	1,020	1,020
Construction	—	—	—	—	—	—
Farmland	—	—	—	—	—	—
Second mortgages	—	—	—	—	—	—
Equity lines of credit	—	—	—	—	—	—
Commercial	—	—	—	1	3	3
Agricultural, installment and other	1	2	2	1	1	1
Total	2	\$ 58	\$ 58	10	\$ 2,370	\$ 2,242

Table of Contents

As of September 30, 2015, the Company had one large loan relationship in the amount of \$1.0 million that had been previously classified as troubled debt restructuring subsequently default within twelve months of restructuring. As of December 31, 2014, the Company did not have any loans previously classified as troubled debt restructuring subsequently default within twelve months of restructuring. A default is defined as an occurrence which violates the terms of the receivable's contract.

As of September 30, 2015 and December 31, 2014, the Company's recorded investment in consumer mortgage loans in the process of foreclosure amounted to \$432,000 and \$639,000, respectively.

Potential problem loans, which include nonperforming loans, amounted to approximately \$28.6 million at September 30, 2015 compared to \$35.8 million at December 31, 2014. Potential problem loans represent those loans with a well-defined weakness and where information about possible credit problems of borrowers has caused management to have serious doubts about the borrower's ability to comply with present repayment terms. This definition is believed to be substantially consistent with the standards established by the FDIC, the Bank's primary federal regulator, for loans classified as special mention, substandard, or doubtful.

The following summary presents our loan balances by primary loan classification and the amount classified within each risk rating category. Pass rated loans include all credits other than those included in special mention, substandard and doubtful which are defined as follows:

Special mention loans have potential weaknesses that deserve management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the asset or in the Bank's credit position at some future date.

Substandard loans are inadequately protected by the current sound worth and paying capacity of the obligor or of the collateral pledged, if any. Assets so classified must have a well-defined weakness or weaknesses that jeopardize liquidation of the debt. Substandard loans are characterized by the distinct possibility that the Bank will sustain some loss if the deficiencies are not corrected.

Doubtful loans have all the characteristics of substandard loans with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions and values, highly questionable and improbable. The Bank considers all doubtful loans to be impaired and places the loan on nonaccrual status.

The following table is a summary of the Bank's loan portfolio by risk rating:



Table of Contents

	(In Thousands)										Total
	Residential 1-4 Family	Multifam	Commercial Real Estate	Commercial Construction	Farmland	Second Mortgages	Equity Lines of Credit	Commercial	Agricultural	Installment and Other	
September 30, 2015											
Credit Risk Profile by Internally Assigned Rating											
Pass	\$347,897	53,956	586,317	285,934	33,888	7,488	47,949	27,267	1,524	51,372	1,443,592
Special Mention	5,500	—	7,721	401	32	290	—	11	—	6	13,961
Substandard	3,963	—	9,245	46	991	275	9	—	—	92	14,621
Doubtful	—	—	—	—	—	—	—	—	—	—	—
Total	\$357,360	53,956	603,283	286,381	34,911	8,053	47,958	27,278	1,524	51,470	1,472,174
December 31, 2014											
Credit Risk Profile by Internally Assigned Rating											
Pass	\$339,529	31,242	545,301	243,416	29,260	8,007	41,274	29,893	1,661	51,387	1,320,970
Special Mention	7,681	—	13,313	2,362	57	347	176	18	2	14	23,970
Substandard	3,548	—	6,351	52	919	672	46	89	7	154	11,838
Doubtful	—	—	—	—	—	—	—	—	—	—	—
Total	\$350,758	31,242	564,965	245,830	30,236	9,026	41,496	30,000	1,670	51,555	1,356,778

Table of Contents

## Note 3. Debt and Equity Securities

Debt and equity securities have been classified in the consolidated balance sheet according to management's intent. Debt and equity securities at September 30, 2015 and December 31, 2014 are summarized as follows:

	September 30, 2015 Securities Available-For-Sale In Thousands			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Market Value
U.S. Government-sponsored enterprises (GSEs)*	\$94,160	\$403	\$276	\$94,287
Mortgage-backed:				
GSE residential and SBA Pools	147,488	629	471	147,646
Asset-backed:				
SBAP	27,723	137	37	27,823
Obligations of states and political subdivisions	23,242	167	114	23,295
	\$292,613	\$1,336	\$898	\$293,051
	September 30, 2015 Securities Held-to-Maturity In Thousands			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Market Value
Mortgage-backed:				
Government-sponsored enterprises (GSEs)* residential	\$6,745	\$62	\$135	\$6,672
Obligations of states and political subdivisions	19,045	270	29	19,286
	\$25,790	\$332	\$164	\$25,958

\* Such as Federal National Mortgage Association, Federal Home Loan Mortgage Corporation, Federal Home Loan Bank, and Federal Farm Credit Bank.

	December 31, 2014 Securities Available-For-Sale In Thousands			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Market Value
U.S. Government-sponsored enterprises (GSEs)*	\$131,767	129	1,329	130,567
Mortgage-backed:				
GSE residential	170,802	731	464	171,069
Asset-backed:				
SBAP	30,627	98	205	30,520
Obligations of states and political subdivisions	14,324	98	158	14,264
	\$347,520	1,056	2,156	346,420



Table of Contents

	December 31, 2014			
	Securities Held-To-Maturity			
	In Thousands			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Market Value
Mortgage-backed:				
Government-sponsored enterprises (GSEs)* residential	\$7,398	76	147	7,327
Obligations of states and political subdivisions	20,725	389	41	21,073
	\$28,123	465	188	28,400

\* Such as Federal National Mortgage Association, Federal Home Loan Mortgage Corporation, Federal Home Loan Bank, and Federal Farm Credit Bank.

The amortized cost and estimated market value of debt securities at September 30, 2015, by contractual maturity, are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Held-to-Maturity		Available-for-sale	
	In Thousands			
	Amortized Cost	Estimated Market Value	Amortized Cost	Estimated Market Value
Due in one year or less	\$2,573	\$2,592	\$—	\$—
Due after one year through five years	9,955	10,093	44,258	44,487
Due after five years through ten years	3,372	3,432	120,979	121,173
Due after ten years	9,890	9,841	127,376	127,391
	\$25,790	\$25,958	\$292,613	\$293,051

The following table shows the gross unrealized losses and fair value of the Company's investments with unrealized losses that are not deemed to be other-than-temporarily impaired, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position at September 30, 2015 and December 31, 2014.

Table of Contents

September 30, 2015	In Thousands, Except Number of Securities						Total	
	Less than 12 Months			12 Months or More			Fair Value	Unrealized Losses
	Fair Value	Unrealized Losses	Number of Securities Included	Fair Value	Unrealized Losses	Number of Securities Included	Fair Value	Unrealized Losses
Held to Maturity Securities:								
Mortgage-backed: Government-sponsored enterprises (GSEs) residential	\$1,576	\$14	1	\$2,748	\$121	3	\$4,324	\$135
Obligations of states and political subdivisions	5,449	27	15	298	2	1	5,747	29
	\$7,025	\$41	16	\$3,046	\$123	4	\$10,071	\$164
Available-for-Sale Securities:								
GSEs	\$—	\$—	—	\$34,967	\$276	11	\$34,967	\$276
Mortgage-backed: GSE residential	62,178	386	32	4,198	85	8	66,376	471
Asset-backed: SBAP	8,701	36	5	2,513	1	1	11,214	37
Obligations of states and political subdivisions	4,077	33	11	3,309	81	9	7,386	114
	\$74,956	\$455	48	\$44,987	\$443	29	\$119,943	\$898

Table of Contents

	In Thousands, Except Number of Securities							
	Less than 12 Months			12 Months or More			Total	
	Fair Value	Unrealized Losses	Number of Securities Included	Fair Value	Unrealized Losses	Number of Securities Included	Fair Value	Unrealized Losses
December 31, 2014								
Held to Maturity Securities:								
Mortgage-backed: Government-sponsored enterprises (GSEs) residential	\$—	\$—	—	\$4,674	\$147	4	\$4,674	\$147
Obligations of states and political subdivisions	—	—	—	2,577	41	6	2,577	41
	\$—	\$—	—	\$7,251	\$188	10	\$7,251	\$188
Available-for-Sale Securities:								
GSEs	\$34,753	\$143	10	\$74,250	\$1,186	24	\$109,003	\$1,329
Mortgage-backed: GSE residential	66,504	279	36	22,172	185	13	88,676	464
Asset-backed: SBAP	16,114	205	9	—	—	—	16,114	205
Obligations of states and political subdivisions	2,078	8	4	4,699	150	13	6,777	158
	\$119,449	\$635	59	\$101,121	\$1,521	50	\$220,570	\$2,156

Unrealized losses on securities have not been recognized into income because the issuers' securities are of high credit quality, management does not intend to sell the securities and it is likely that management will not be required to sell the securities prior to their anticipated recovery, and the decline in fair value is largely due to changes in interest rates and other market conditions. The issuers continue to make timely principal and interest payment on the securities. The fair value is expected to recover as the securities approach maturity. The Company does not consider these securities to be other-than-temporarily impaired at September 30, 2015.

The carrying values of the Company's investment securities could decline in the future if the financial condition of issuers deteriorate and management determines it is probable that the Company will not recover the entire amortized cost bases of the securities. As a result, there is a risk that other-than-temporary impairment charges may occur in the future given the current economic environment.

#### Note 4. Earnings Per Share

The computation of basic earnings per share is based on the weighted average number of common shares outstanding during the period. The computation of diluted earnings per share for the Company begins with the basic earnings per share plus the effect of common shares contingently issuable from stock options.

The following is a summary of components comprising basic and diluted earnings per share ("EPS") for the three and nine months ended September 30, 2015 and 2014:

Table of Contents

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014
	(Dollars in Thousands Except Per Share Amounts)		(Dollars in Thousands Except Per Share Amounts)	
Basic EPS Computation:				
Numerator – Earnings available to common stockholders	\$6,088	\$5,351	\$17,905	\$14,677
Denominator – Weighted average number of common shares outstanding	7,637,448	7,559,136	7,615,096	7,538,860
Basic earnings per common share	\$0.80	\$0.71	\$2.35	\$1.95
Diluted EPS Computation:				
Numerator – Earnings available to common stockholders	\$6,088	\$5,351	\$17,905	\$14,677
Denominator – Weighted average number of common shares outstanding	7,637,448	7,559,136	7,615,096	7,538,860
Dilutive effect of stock options	3,348	4,218	3,434	4,350
	7,640,796	7,563,354	7,618,530	7,543,210
Diluted earnings per common share	\$0.80	\$0.71	\$2.35	\$1.95

## Note 5. Income Taxes

Accounting Standards Codification (“ASC”) 740, Income Taxes, defines the threshold for recognizing the benefits of tax return positions in the financial statements as “more-likely-than-not” to be sustained by the taxing authority. This section also provides guidance on the derecognition, measurement and classification of income tax uncertainties, along with any related interest and penalties, and includes guidance concerning accounting for income tax uncertainties in interim periods. As of September 30, 2015, the Company had no unrecognized tax benefits related to Federal or State income tax matters and does not anticipate any material increase or decrease in unrecognized tax benefits relative to any tax positions taken prior to September 30, 2015.

As of September 30, 2015, the Company has accrued no interest and no penalties related to uncertain tax positions. The Company’s policy is to recognize interest and/or penalties related to income tax matters in income tax expense. The Company and its subsidiaries file consolidated U.S. Federal and state of Tennessee income tax returns. The Company is currently open to audit under the statute of limitations by the state of Tennessee for the years ended December 31, 2011 through 2014 and the IRS for the years ended December 31, 2012 through 2014.

## Note 6. Commitments and Contingent Liabilities

In the normal course of business, the Bank has entered into off-balance sheet financial instruments which include commitments to extend credit (i.e., including unfunded lines of credit) and standby letters of credit. Commitments to extend credit are usually the result of lines of credit granted to existing borrowers under agreements that the total outstanding indebtedness will not exceed a specific amount during the term of the indebtedness. Typical borrowers are commercial concerns that use lines of credit to supplement their treasury management functions, thus their total outstanding indebtedness may fluctuate during any time period based on the seasonality of their business and the resultant timing of their cash flows. Other typical lines of credit are related to home equity loans granted to consumers. Commitments to extend credit generally have fixed expiration dates or other termination clauses and may require payment of a fee.

Standby letters of credit are generally issued on behalf of an applicant (our customer) to a specifically named beneficiary and are the result of a particular business arrangement that exists between the applicant and the beneficiary. Standby letters of credit have fixed expiration dates and are usually for terms of two years or less unless terminated beforehand due to criteria specified in the standby letter of credit. A typical arrangement involves the applicant routinely being indebted to the beneficiary for such items as inventory purchases, insurance, utilities, lease guarantees or other third party commercial transactions. The standby letter of credit would permit the beneficiary to obtain payment from the Company under certain prescribed circumstances. Subsequently, the Company would then

seek reimbursement from the applicant pursuant to the terms of the standby letter of credit.

The Company follows the same credit policies and underwriting practices when making these commitments as it does for on-balance sheet instruments. Each customer's creditworthiness is evaluated on a case-by-case basis, and the amount of

22

---



Table of Contents

collateral obtained, if any, is based on management's credit evaluation of the customer. Collateral held varies but may include cash, real estate and improvements, marketable securities, accounts receivable, inventory, equipment, and personal property.

The contractual amounts of these commitments are not reflected in the consolidated financial statements and would only be reflected if drawn upon. Since many of the commitments are expected to expire without being drawn upon, the contractual amounts do not necessarily represent future cash requirements. However, should the commitments be drawn upon and should our customers default on their resulting obligation to us, the Company's maximum exposure to credit loss, without consideration of collateral, is represented by the contractual amount of those instruments.

A summary of the Company's total contractual amount for all off-balance sheet commitments at September 30, 2015 is as follows:

Commitments to extend credit	\$397,729,000
Standby letters of credit	\$34,323,000

The Company originates residential mortgage loans, sells them to third-party purchasers, and does not retain the servicing rights. These loans are originated internally and are primarily to borrowers in the Company's geographic market footprint. These sales are on a best efforts basis to investors that follow conventional government sponsored entities (GSE) and the Department of Housing and Urban Development/U.S. Department of Veterans Affairs (HUD/VA) guidelines. Generally, loans held for sale are underwritten by the Company, including HUD/VA loans. Each purchaser has specific guidelines and criteria for sellers of loans, and the risk of credit loss with regard to the principal amount of the loans sold is generally transferred to the purchasers upon sale. While the loans are sold without recourse, the purchase agreements require the Company to make certain representations and warranties regarding the existence and sufficiency of file documentation and the absence of fraud by borrowers or other third parties such as appraisers in connection with obtaining the loan. If it is determined that the loans sold were in breach of these representations or warranties or the loan had an early payoff or payment default, the Company has obligations to either repurchase the loan for the unpaid principal balance and related investor fees or make the purchaser whole for the economic benefits of the loan.

To date, repurchase activity pursuant to the terms of these representations and warranties has been insignificant and has resulted in insignificant losses to the Company.

Based on information currently available, management believes that it does not have significant exposure to contingent losses that may arise relating to the representations and warranties that it has made in connection with its mortgage loan sales.

Various legal claims also arise from time to time in the normal course of business. In the opinion of management, the resolution of these claims outstanding at September 30, 2015 will not have a material impact on the Company's financial statements.

#### Note 7. Fair Value Measurements

FASB ASC 820, Fair Value Measurements and Disclosures, which defines fair value, establishes a framework for measuring fair value in U.S. GAAP and expands disclosures about fair value measurements. The definition of fair value focuses on the exit price, i.e., the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date, not the entry price, i.e., the price that would be paid to acquire the asset or received to assume the liability at the measurement date. The statement emphasizes that fair value is a market-based measurement; not an entity-specific measurement. Therefore, the fair value measurement should be determined based on the assumptions that market participants would use in pricing the asset or liability.

#### Valuation Hierarchy

FASB ASC 820 establishes a three-level valuation hierarchy for disclosure of fair value measurements. The valuation hierarchy is based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date. The three levels are defined as follows:

Level 1 — inputs to the valuation methodology are quoted prices (unadjusted) for identical assets or liabilities in active markets.

23

---

Table of Contents

Level 2 — inputs to the valuation methodology include quoted prices for similar assets and liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument.

Level 3 — inputs to the valuation methodology are unobservable and significant to the fair value measurement.

A financial instrument's categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement. Following is a description of the valuation methodologies used for assets and liabilities measured at fair value, as well as the general classification of such assets and liabilities pursuant to the valuation hierarchy.

#### Assets

**Securities available-for-sale** — Where quoted prices are available for identical securities in an active market, securities are classified within Level 1 of the valuation hierarchy. Level 1 securities include highly liquid government securities and certain other financial products. If quoted market prices are not available, then fair values are estimated by using pricing models that use observable inputs or quoted prices of securities with similar characteristics and are classified within Level 2 of the valuation hierarchy. In certain cases where there is limited activity or less transparency around inputs to the valuation and more complex pricing models or discounted cash flows are used, securities are classified within Level 3 of the valuation hierarchy.

**Impaired loans** — A loan is considered to be impaired when it is probable the Company will be unable to collect all principal and interest payments due in accordance with the contractual terms of the loan agreement. Impaired loans are measured based on the present value of expected payments using the loan's original effective rate as the discount rate, the loan's observable market price, or the fair value of the collateral less selling costs if the loan is collateral dependent. If the recorded investment in the impaired loan exceeds the measure of fair value, a valuation allowance may be established as a component of the allowance for loan losses or the expense is recognized as a charge-off. Impaired loans are classified within Level 3 of the valuation hierarchy due to the unobservable inputs used in determining their fair value such as collateral values and the borrower's underlying financial condition.

**Other real estate owned** — Other real estate owned ("OREO") represents real estate foreclosed upon by the Company through loan defaults by customers or acquired in lieu of foreclosure. Substantially all of these amounts relate to construction and land development, other loans secured by land, and commercial real estate loans for which the Company believes it has adequate collateral. Upon foreclosure, the property is recorded at the lower of cost or fair value, based on appraised value, less selling costs estimated as of the date acquired with any loss recognized as a charge-off through the allowance for loan losses. Additional OREO losses for subsequent valuation downward adjustments are determined on a specific property basis and are included as a component of noninterest expense along with holding costs. Any gains or losses realized at the time of disposal are also reflected in noninterest expense, as applicable. OREO is included in Level 3 of the valuation hierarchy due to the lack of observable market inputs into the determination of fair value. Appraisal values are property-specific and sensitive to the changes in the overall economic environment.

**Mortgage loans held-for-sale** — Mortgage loans held-for-sale are carried at the fair value. The fair value of loans held-for-sale is determined using quoted prices for similar assets, adjusted for specific attributes of that loan (Level 2).

**Other assets** — Included in other assets are certain assets carried at fair value, including the cash surrender value of bank owned life insurance policies and annuity contracts. The Company uses financial information received from insurance carriers indicating the performance of the insurance policies, cash surrender values, and annuity contracts in determining the carrying value. The Company reflects these assets within Level 3 of the valuation hierarchy due to the unobservable inputs included in the valuation of these items. The Company does not consider the fair values of these policies and contracts to be materially sensitive to changes in these unobservable inputs.

The following tables present the financial instruments carried at fair value as of September 30, 2015 and December 31, 2014, by caption on the consolidated balance sheet and by FASB ASC 820 valuation hierarchy (as described above) (in thousands):



Table of Contents

	Assets and Liabilities Measured at Fair Value on a Recurring Basis			
	Total Carrying Value in the Consolidated Balance Sheet	Quoted Market Prices in an Active Market (Level 1)	Models with Significant Observable Market Parameters (Level 2)	Models with Significant Unobservable Market Parameters (Level 3)
September 30, 2015				
Investment securities available-for-sale:				
U.S. Government sponsored enterprises	\$94,287	—	94,287	—
Mortgage-backed securities	147,646	—	147,646	—
Asset-backed securities	27,823	—	27,823	—
State and municipal securities	23,295	—	23,295	—
Total investment securities available-for-sale	293,051	—	293,051	—
Loans held for sale	13,437	—	13,437	—
Other assets	26,560	—	—	26,560
Total assets at fair value	\$333,048	—	306,488	26,560
December 31, 2014				
Investment securities available-for-sale:				
U.S. Government sponsored enterprises	\$130,567	—	130,567	—
Mortgage-backed securities	171,069	—	171,069	—
Asset-backed securities	30,520	—	30,520	—
State and municipal securities	14,264	—	14,264	—
Total investment securities available-for-sale	346,420	—	346,420	—
Loans held for sale	9,466	—	9,466	—
Other assets	17,331	—	—	17,331
Total assets at fair value	\$373,217	—	355,886	17,331
Assets and Liabilities Measured at Fair Value on a Non-Recurring Basis				
	Total Carrying Value in the Consolidated Balance Sheet	Quoted Market Prices in an Active Market (Level 1)	Models with Significant Observable Market Parameters (Level 2)	Models with Significant Unobservable Market Parameters (Level 3)
September 30, 2015				
Other real estate owned	\$6,533	—	—	6,533
Impaired loans, net <sup>(1)</sup>	9,737	—	—	9,737
Total	\$16,270	—	—	16,270
December 31, 2014				
Other real estate owned	\$7,298	—	—	7,298
Impaired loans, net <sup>(1)</sup>	8,866	—	—	8,866
Total	\$16,164	—	—	16,164

<sup>(1)</sup> Amount is net of a valuation allowance of \$0.9 million at September 30, 2015 and \$1.6 million at December 31, 2014 as required by ASC 310, "Receivables."

In the case of the bond portfolio, the Company monitors the valuation technique utilized by various pricing agencies to ascertain when transfers between levels have been affected. The nature of the remaining assets and liabilities is such

that transfers in and out of any level are expected to be rare. For the nine months ended September 30, 2015, there were no transfers between Levels 1, 2 or 3.

The table below includes a rollforward of the balance sheet amounts for the nine months ended September 30, 2015 and 2014 (including the change in fair value) for financial instruments classified by the Company within Level 3 of the valuation hierarchy for assets and liabilities measured at fair value on a recurring basis. When a determination is made to classify a financial instrument within Level 3 of the valuation hierarchy, the determination is based upon the significance of the unobservable factors

25

---

Table of Contents

to the overall fair value measurement. However, since Level 3 financial instruments typically include, in addition to the unobservable or Level 3 components, observable components (that is, components that are actively quoted and can be validated to external sources), the gains and losses in the table below include changes in fair value due in part to observable factors that are part of the valuation methodology (in thousands):

	For the Nine Months Ended September 30,			
	2015		2014	
	Other	Other	Other	Other
	Assets	Liabilities	Assets	Liabilities
Fair value, January 1	\$17,331	—	\$11,390	—
Total realized gains included in income	765	—	306	—
Change in unrealized gains/losses included in other comprehensive income for assets and liabilities still held at June 30	—	—	—	—
Purchases, issuances and settlements, net	8,464	—	5,000	—
Transfers out of Level 3	—	—	—	—
Fair Value September 30,	\$26,560	—	\$16,696	—
Total realized gains included in income related to financial assets and liabilities still on the consolidated balance sheet at June 30	\$765	—	306	—

The following methods and assumptions were used by the Company in estimating its fair value disclosures for financial instruments that are not measured at fair value. In cases where quoted market prices or observable components are not available, fair values are based on estimates using discounted cash flow models. Those models are significantly affected by the assumptions used, including the discount rates, estimates of future cash flows and borrower creditworthiness. The fair value estimates presented herein are based on pertinent information available to management as of September 30, 2015 and December 31, 2014. Such amounts have not been revalued for purposes of these consolidated financial statements since those dates and, therefore, current estimates of fair value may differ significantly from the amounts presented herein.

**Held-to-maturity securities** — Estimated fair values for investment securities are based on quoted market prices where available. If quoted market prices are not available, then fair values are estimated by using pricing models that use observable inputs or quoted prices of securities with similar characteristics.

**Loans** — The fair value of our loan portfolio includes a credit risk factor in the determination of the fair value of our loans. This credit risk assumption is intended to approximate the fair value that a market participant would realize in a hypothetical orderly transaction. Our loan portfolio is initially fair valued using a segmented approach. We divide our loan portfolio into the following categories: variable rate loans, impaired loans and all other loans. The results are then adjusted to account for credit risk.

For variable-rate loans that reprice frequently and have no significant change in credit risk, fair values approximate carrying values. Fair values for impaired loans are estimated using discounted cash flow models or based on the fair value of the underlying collateral. For other loans, fair values are estimated using discounted cash flow models, using current market interest rates offered for loans with similar terms to borrowers of similar credit quality. The values derived from the discounted cash flow approach for each of the above portfolios are then further discounted to incorporate credit risk to determine the exit price.

**Deposits and Securities sold under agreements to repurchase** — Fair values for deposits are estimated using discounted cash flow models, using current market interest rates offered on deposits with similar remaining maturities.

**Off-Balance Sheet Instruments** — The fair values of the Company's off-balance-sheet financial instruments are based on fees charged to enter into similar agreements. However, commitments to extend credit do not represent a significant value to the Company until such commitments are funded.

The following table presents the carrying amounts, estimated fair value and placement in the fair valuation hierarchy of the Company's financial instruments at September 30, 2015 and December 31, 2014. This table excludes financial

instruments for which the carrying amount approximates fair value. For short-term financial assets such as cash and cash equivalents, the carrying amount is a reasonable estimate of fair value due to the relatively short time between the origination of the instrument and its expected realization.

26

---



Table of Contents

(in Thousands)	Carrying/ Notional Amount	Estimated Fair Value <sup>(1)</sup>	Quoted Market Prices in an Active Market (Level 1)	Models with Significant Observable Market Parameters (Level 2)	Models with Significant Unobservable Market Parameters (Level 3)
September 30, 2015					
Financial assets:					
Securities held-to-maturity	\$25,790	25,958	—	25,958	—
Loans, net	1,444,334	1,457,511	—	—	1,457,511
Financial liabilities:					
Deposits and securities sold under agreements to repurchase	1,726,861	1,506,229	—	—	1,506,229
Off-balance sheet instruments:					
Commitments to extend credit	—	—	—	—	—
Standby letters of credit	—	—	—	—	—
December 31, 2014					
Financial assets:					
Securities held-to-maturity	\$28,123	28,400	—	28,400	—
Loans, net	1,329,865	1,346,569	—	—	1,346,569
Financial liabilities:					
Deposits and securities sold under agreements to repurchase	1,663,707	1,530,607	—	—	1,530,607
Off-balance sheet instruments:					
Commitments to extend credit	—	—	—	—	—
Standby letters of credit	—	—	—	—	—

(1) Estimated fair values are consistent with an exit-price concept. The assumptions used to estimate the fair values are intended to approximate those that a market-participant would realize in a hypothetical orderly transaction.

## Part I. Financial Information

## Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

The purpose of this discussion is to provide insight into the financial condition and results of operations of the Company and its bank subsidiary. This discussion should be read in conjunction with the consolidated financial statements appearing elsewhere in this report. Reference should also be made to the Company's Annual Report on Form 10-K for the year ended December 31, 2014 and the Company's Quarterly Report on Form 10-Q for the quarters ended June 30, 2015 and March 31, 2015 for a more complete discussion of factors that impact liquidity, capital and the results of operations.

## Forward-Looking Statements

This Form 10-Q contains certain forward-looking statements regarding, among other things, the anticipated financial and operating results of the Company. Investors are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date hereof. The Company undertakes no obligation to publicly release any modifications or revisions to these forward-looking statements to reflect events or circumstances occurring after the date hereof or to reflect the occurrence of unanticipated events.

In connection with the "safe harbor" provisions of the Private Securities Litigation Reform Act of 1995, the Company cautions investors that future financial and operating results may differ materially from those projected in forward-looking statements made by, or on behalf of, the Company. The words "expect," "intend," "should," "may," "could," "believe," "suspect," "anticipate," "seek," "plan," "estimate" and similar expressions are intended to identify such forward-looking statements, but other statements not based on historical fact may also be considered forward-looking. Such forward-looking statements involve known and unknown risks and uncertainties, including, but not limited to those

described in the Company's Annual Report on Form 10-K for the year ended December 31, 2014, and also include, without limitation, (i) deterioration in the financial condition of borrowers resulting in significant increases in loan losses and provisions for these losses, (ii) renewed deterioration in the real estate market conditions in the Company's market areas, (iii) increased competition with other financial institutions, (iv) the deterioration of the economy in the Company's market areas, (v) continuation of the extremely low short-term interest rate

27

---

Table of Contents

environment or rapid fluctuations in short-term interest rates, (vi) significant downturns in the business of one or more large customers, (vii) the inability of the Company to comply with regulatory capital requirements, including those resulting from recently effective changes to capital calculation methodologies and required capital maintenance levels; (viii) changes in state or Federal regulations, policies, or legislation applicable to banks and other financial service providers, including regulatory or legislative developments arising out of current unsettled conditions in the economy, including implementation of the Dodd Frank Wall Street Reform and Consumer Protection Act, (ix) changes in capital levels and loan underwriting, credit review or loss reserve policies associated with economic conditions, examination conclusions, or regulatory developments, (x) inadequate allowance for loan losses, (xi) the effectiveness of the Company's activities in improving, resolving or liquidating lower quality assets, (xii) results of regulatory examinations, (xiii) the vulnerability of our network and online banking portals to unauthorized access, computer viruses, phishing schemes, spam attacks, human error, natural disasters, power loss and other security breaches; (xiv) the possibility of additional increases to compliance costs as a result of increased regulatory oversight; and (xv) loss of key personnel. These risks and uncertainties may cause the actual results or performance of the Company to be materially different from any future results or performance expressed or implied by such forward-looking statements. The Company's future operating results depend on a number of factors which were derived utilizing numerous assumptions that could cause actual results to differ materially from those projected in forward-looking statements.

**Critical Accounting Estimates**

The accounting principles we follow and our methods of applying these principles conform with U.S. generally accepted accounting principles and with general practices within the banking industry. In connection with the application of those principles, we have made judgments and estimates which, in the case of the determination of our allowance for loan losses have been critical to the determination of our financial position and results of operations. There have been no significant changes to our critical accounting policies as discussed in our Annual Report on Form 10-K for the year ended December 31, 2014.

**Allowance for Loan Losses ("allowance").** Our management assesses the adequacy of the allowance prior to the end of each calendar quarter. This assessment includes procedures to estimate the allowance and test the adequacy and appropriateness of the resulting balance. The level of the allowance is based upon management's evaluation of the loan portfolio, past loan loss experience, current asset quality trends, known and inherent risks in the portfolio, adverse situations that may affect the borrower's ability to repay (including the timing of future payment), the estimated value of any underlying collateral, composition of the loan portfolio, economic conditions, industry and peer bank loan quality indications and other pertinent factors, including regulatory recommendations. This evaluation is inherently subjective as it requires material estimates including the amounts and timing of future cash flows expected to be received on impaired loans that may be susceptible to significant change. Loan losses are charged off when management believes that the full collectability of the loan is unlikely. A loan may be partially charged-off after a "confirming event" has occurred which serves to validate that full repayment pursuant to the terms of the loan is unlikely. Allocation of the allowance may be made for specific loans, but the entire allowance is available for any loan that, in management's judgment, is deemed to be uncollectible.

A loan is impaired when, based on current information and events, it is probable that we will be unable to collect all amounts due according to the contractual terms of the loan agreement. Collection of all amounts due according to the contractual terms means that both the interest and principal payments of a loan will be collected as scheduled in the loan agreement.

An impairment allowance is recognized if the fair value of the loan is less than the recorded investment in the loan (recorded investment in the loan is the principal balance plus any accrued interest, net of deferred loan fees or costs and unamortized premium or discount). The impairment is recognized through the allowance. Loans that are impaired are recorded at the present value of expected future cash flows discounted at the loan's effective interest rate, or if the loan is collateral dependent, impairment measurement is based on the fair value of the collateral, less estimated disposal costs. If the measure of the impaired loan is less than the recorded investment in the loan, the Company recognizes an impairment by creating a valuation allowance with a corresponding charge to the provision for loan losses or by adjusting an existing valuation allowance for the impaired loan with a corresponding charge or credit to

the provision for loan losses. Management believes it follows appropriate accounting and regulatory guidance in determining impairment and accrual status of impaired loans.

The level of allowance maintained is believed by management to be adequate to absorb probable losses inherent in the portfolio at the balance sheet date. The allowance is increased by provisions charged to expense and decreased by charge-offs, net of recoveries of amounts previously charged-off.

In assessing the adequacy of the allowance, we also consider the results of our ongoing loan review process. We undertake this process both to ascertain whether there are loans in the portfolio whose credit quality has weakened over time and to assist in our overall evaluation of the risk characteristics of the entire loan portfolio. Our loan review process includes the

28

---

## Table of Contents

judgment of management, the input from our independent loan reviewers, and reviews that may have been conducted by bank regulatory agencies as part of their usual examination process. We incorporate loan review results in the determination of whether or not it is probable that we will be able to collect all amounts due according to the contractual terms of a loan.

As part of management's quarterly assessment of the allowance, management divides the loan portfolio into twelve segments based on bank call reporting requirements. Each segment is then analyzed such that an allocation of the allowance is estimated for each loan segment.

The allowance allocation begins with a process of estimating the probable losses in each of the twelve loan segments. The estimates for these loans are based on our historical loss data for that category over the last twenty quarters. During the first quarter of 2015, management increased the number of quarters of loss data that it reviews from twelve quarters to the last twenty quarters. Management believes that twenty quarters is a more accurate representation of an economic business cycle.

The estimated loan loss allocation for all twelve loan portfolio segments is then adjusted for several "environmental" factors. The allocation for environmental factors is particularly subjective and does not lend itself to exact mathematical calculation. This amount represents estimated probable inherent credit losses which exist, but have not yet been identified, as of the balance sheet date, and are based upon quarterly trend assessments in delinquent and nonaccrual loans, unanticipated charge-offs, credit concentration changes, prevailing economic conditions, changes in lending personnel experience, changes in lending policies or procedures and other influencing factors. These environmental factors are considered for each of the twelve loan segments and the allowance allocation, as determined by the processes noted above for each component, is increased or decreased based on the incremental assessment of these various environmental factors.

We then test the resulting allowance by comparing the balance in the allowance to industry and peer information. Our management then evaluates the result of the procedures performed, including the result of our testing, and concludes on the appropriateness of the balance of the allowance in its entirety. The board of directors reviews and approves the assessment prior to the filing of quarterly and annual financial information.

**Impairment of Intangible Assets.** Long-lived assets, including purchased intangible assets subject to amortization, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized by the amount by which the carrying amount of the asset exceeds the fair value of the asset. Assets to be disposed of would be separately presented in the balance sheet and reported at the lower of the carrying amount or fair value less costs to sell, and are no longer depreciated.

Goodwill and intangible assets that have indefinite useful lives are evaluated for impairment annually and are evaluated for impairment more frequently if events and circumstances indicate that the asset might be impaired. That annual assessment date is December 31. An impairment loss is recognized to the extent that the carrying amount exceeds the asset's fair value. The Company first has the option to perform a qualitative assessment of goodwill to determine if impairment has occurred. Based upon the qualitative assessment, if the fair value of goodwill exceeds the carrying value, the evaluation of goodwill is complete. If the qualitative assessment indicates that impairment is present, the goodwill impairment analysis continues with a two-step test. The first step, used to identify potential impairment, involves comparing each reporting unit's estimated fair value to its carrying value, including goodwill. If the estimated fair value of a reporting unit exceeds its carrying value, goodwill is considered not to be impaired. If the carrying value exceeds estimated fair value, there is an indication of potential impairment and the second step is performed to measure the amount of impairment.

If required, the second step involves calculating an implied fair value of goodwill for each reporting unit for which the first step indicated potential impairment. The implied fair value of goodwill is determined in a manner similar to the amount of goodwill calculated in a business combination, by measuring the excess of the estimated fair value of the reporting unit, as determined in the first step, over the aggregate estimated fair values of the individual assets,

liabilities and identifiable intangibles as if the reporting unit was being acquired in a business combination. If the implied fair value of goodwill exceeds the carrying value of goodwill assigned to the reporting unit, there is no impairment. If the carrying value of goodwill assigned to a reporting unit exceeds the implied fair value of the goodwill, an impairment charge is recorded for the excess. An impairment loss cannot exceed the carrying value of goodwill assigned to a reporting unit, and the loss establishes a new basis in the goodwill.

Other-than-temporary Impairment. A decline in the fair value of any available-for-sale or held-to-maturity security below cost that is deemed to be other-than-temporary results in a reduction in the carrying amount of the security. To determine whether impairment is other-than-temporary, management considers whether the entity expects to recover the entire amortized cost basis of the security by reviewing the present value of the future cash flows associated with the security. The shortfall of the

Table of Contents

present value of the cash flows expected to be collected in relation to the amortized cost basis is referred to as a credit loss and is deemed to be other-than temporary impairment. If a credit loss is identified, the credit loss is recognized as a charge to earnings and a new cost basis for the security is established. If management concludes that no credit loss exists and it is not more-likely-than-not that the Company will be required to sell the security before maturity, then the security is not other-than-temporarily impaired and the shortfall is recorded as a component of equity.

**Results of Operations**

Net earnings increased 21.99% to \$17,905,000 for the nine months ended September 30, 2015 from \$14,677,000 in the first nine months of 2014. Net earnings were \$6,088,000 for the quarter ended September 30, 2015, an increase of \$737,000, or 13.77%, from \$5,351,000 for the three months ended September 30, 2014 and a decrease of \$113,000, or 1.82%, over the quarter ended June 30, 2015. The increase in net earnings during the nine months ended September 30, 2015 as compared to the prior year comparable period was primarily due to an increase in net interest income and an increase in noninterest income, slightly offset by an increase in noninterest expense. Net yield on earning assets for the nine months ended September 30, 2015 was 3.80% compared to 3.75% for the first nine months of 2014, and the net interest spread was 3.69% and 3.64%, respectively, for the nine months ended September 30, 2015 and the nine months ended September 30, 2014. Despite the increase in the net yield on earning assets, the yield on loans decreased in the first nine months of 2015 when compared to the comparable period in 2014 as a result of increased competition for loans in all market areas.

The average balances, interest, and average rates for the nine-month periods ended September 30, 2015 and September 30, 2014 are presented in the following table:

	September 30, 2015			September 30, 2014		
	Average Balance	Interest Rate	Income/Expense	Average Balance	Interest Rate	Income/Expense
Loans, net of unearned interest (1)	\$1,405,095	5.04	% 53,123	\$1,242,785	5.31	% 49,456
Investment securities—taxable	318,793	1.88	4,492	343,709	1.87	4,832
Investment securities—tax exempt	16,359	2.02	551	32,377	2.08	505
Taxable equivalent adjustment	—	1.04	378	—	1.07	347
Total tax-exempt investment securities	36,359	3.06	929	32,377	3.15	852
Total investment securities	355,152	2.00	5,421	376,086	1.98	5,684
Loans held for sale	10,255	3.50	269	6,929	3.77	196
Federal funds sold	69,428	0.19	100	84,106	0.19	120
Restricted equity securities	3,012	4.03	91	3,012	4.03	91
Total earning assets	1,842,942	4.26	% 59,004	1,712,918	4.32	55,547
Cash and due from banks	9,374			10,925		
Allowance for loan losses	(22,519 )			(23,240 )		
Bank premises and equipment	40,488			39,204		
Other assets	54,725			50,801		
Total assets	\$1,925,010			\$1,790,608		

Table of Contents

	September 30, 2015			September 30, 2014		
	Average Balance	Interest Rate	Income/Expense	Average Balance	Interest Rate	Income/Expense
Deposits:						
Negotiable order of withdrawal accounts	\$391,033	0.39	% 1,143	\$345,559	0.46	% 1,197
Money market demand accounts	495,958	0.30	1,107	428,873	0.42	1,355
Individual retirement accounts	89,821	0.97	654	94,079	1.13	795
Other savings deposits	105,105	0.43	340	98,448	0.54	401
Certificates of deposit \$100,000 and over	227,814	1.06	1,808	246,893	1.06	1,956
Certificates of deposit under \$100,000	217,723	0.90	1,462	233,175	0.94	1,647
Total interest-bearing deposits	1,527,454	0.57	6,514	1,447,027	0.68	7,351
Securities sold under repurchase agreements	2,659	0.25	5	6,279	0.40	19
Federal funds purchased	119	—	1	164	0.81	1
Total interest-bearing liabilities	1,530,232	0.57	6,520	1,453,470	0.68	7,371
Demand deposits	174,879			141,662		
Other liabilities	12,086			11,212		
Stockholders' equity	207,813			184,264		
Total liabilities and stockholders' equity	\$1,925,010			\$1,790,608		
Net interest income, on a tax equivalent basis			\$52,484			\$48,176
Net yield on earning assets (2)		3.80	%		3.75	%
Net interest spread (3)		3.69	%		3.64	%

(1) Loan fees of \$4.3 million and \$3.7 million are included in interest income in 2015 and 2014, respectively.

(2) Net interest income divided by average interest-earning assets.

(3) Average interest rate on interest-earning assets less average interest rate on interest-bearing liabilities.

### Net Interest Income

Net interest income represents the amount by which interest earned on various earning assets exceeds interest paid on deposits and other interest-bearing liabilities and is the most significant component of the Company's earnings. Reflecting loan growth that outpaced the reduction in loan yields and an increase in the yields on taxable securities, the Company's total interest income, excluding tax equivalent adjustments relating to tax exempt securities, increased \$3,426,000, or 6.21%, during the nine months ended September 30, 2015 as compared to the same period in 2014. The increase in total interest income was \$1,002,000, or 5.28%, for the quarter ended September 30, 2015 as compared to the quarter ended September 30, 2014. Interest income for the third quarter of 2015 increased \$365,000, or 1.86%, over the second quarter of 2015. The increase in the first nine months of 2015 was primarily attributable to an overall increase in loans and the resulting increase in the interest and fees earned on loans that outpaced an overall reduction in loan yields resulting from competition in our market area. The ratio of average earning assets to total average assets was 95.7% and 95.7% for the nine months ended September 30, 2015 and September 30, 2014, respectively.

Interest expense decreased \$850,000, or 11.53%, for the nine months ended September 30, 2015 as compared to the same period in 2014. The decrease was \$312,000, or 12.86%, for the three months ended September 30, 2015 as compared to the same period in 2014. Interest expense decreased \$77,000, or 3.51%, for the quarter ended September 30, 2015 over the second quarter of 2015. The decrease for the nine months ended September 30, 2015 and



the quarter ended September 30, 2015 as compared to the prior year's comparable periods was primarily due to a decrease in the rates paid on deposits, particularly time deposits, reflecting the low interest rate environment and a shift in the mix of deposits from certificates of deposits to transaction and money market accounts.

Table of Contents

## Provision for Loan Losses

The allowance for loan losses totaled \$22,702,000 as of September 30, 2015 compared to \$22,572,000 as of December 31, 2014 and \$23,314,000 as of September 30, 2014. An analytical model based on historical loss experience, current trends and economic conditions as well as reasonably foreseeable events is used to determine the amount of provision to be recognized and to test the adequacy of the loan loss allowance. The volume of net loans charged off for the first nine months of 2015 totaled approximately \$135,000 compared to approximately \$15,000 in net recoveries during the first nine months of 2014 and \$3,980,000 of net chargeoffs for the first nine months of 2013. Overall, net charge offs were up for the nine month period ended September 30, 2015 when compared to the comparable periods in 2014 due to single large recovery that occurred in the first quarter of 2014. In general, the Bank has seen an overall improvement in its loan portfolio. Reflecting the improving asset quality trends experienced by the Bank in the first nine months of 2015, the provision for loan losses during the nine months ended September 30, 2015 was \$265,000, down \$99,000 from the \$364,000 incurred in the first nine months of 2014. Provision expense for the three months ended September 30, 2015 was \$109,000, up \$22,000 from the \$87,000 incurred in the third quarter of 2014 and up \$28,000 from the \$81,000 incurred in the second quarter of 2015.

The allowance for loan losses is based on past loan experience and other factors which, in management's judgment, deserve current recognition in estimating possible loan losses. Such factors include growth and composition of the loan portfolio, review of specific problem loans, review of updated appraisals and borrower financial information, the recommendations of the Company's regulators, and current economic conditions that may affect the borrower's ability to repay. Management has in place a system designed for monitoring its loan portfolio and identifying potential problem loans. Reflecting improving asset quality metrics, the allowance for loan losses was \$22,702,000 at September 30, 2015, an increase of 0.58% from \$22,572,000 at December 31, 2014 and a decrease of \$612,000, or 2.63%, from September 30, 2014. The allowance for loan losses was 1.55%, 1.67%, and 1.78% of total loans at September 30, 2015, December 31, 2014, and September 30, 2014, respectively.

Management believes the allowance for loan losses at September 30, 2015 to be adequate, but if economic conditions deteriorate beyond management's current expectations and additional charge-offs are incurred, the allowance for loan losses may require an increase through additional provision for loan losses which would negatively impact earnings.

## Non-Interest Income

The components of the Company's non-interest income include service charges on deposit accounts, other fees and commissions and gain on sale of loans. Total non-interest income for the nine months ended September 30, 2015 increased 24.90% to \$15,060,000 from \$12,058,000 for the same period in 2014. Total non-interest income increased \$1,219,000, or 28.42%, during the quarter ended September 30, 2015 compared to the third quarter in 2014 and there was an increase of \$477,000, or 9.48%, over the second quarter of 2015. The Company's non-interest income in the first nine months of 2015 increased from the first nine months of 2014 mainly due to an increase in other fees and commissions, an increase in service charges on deposit accounts, and an increase in gain on sale of loans. Gain on sale of loans increased \$1,131,000, or 58.72%, during the nine months ended September 30, 2015 compared to the same period in 2014. The increase in gain on sale of loans during the first nine months of 2015 related primarily to the increase in consumer demand for residential mortgages and the continued improvement in the real estate market in the bank's lending areas. Service charges on deposit accounts increased \$616,000, or 19.62%, to \$3,755,000 during the nine months ended September 30, 2015 compared to the same period in 2014 and increased \$227,000, or 19.34%, during the quarter ended September 30, 2015 compared to the third quarter of 2014 as a result of an increase in service charge on insufficient accounts as the result of an overdraft program implemented by the Bank in the third quarter of 2014 and an increase in consumer checking accounts. Other fees and commissions increased \$1,065,000, or 15.91%, to \$7,758,000 during the nine months ended September 30, 2015 compared to the same period in 2014. The increase was \$454,000 during the quarter ended September 30, 2015 compared to the third quarter of 2014, relating primarily to an increase in life insurance income that resulted from the \$8.5 million purchase of bank owned life insurance that occurred in the first nine months of 2015. Other fees and commissions include income on brokerage accounts, insurance policies sold, and various other fees.

## Non-Interest Expenses

Non-interest expenses consist primarily of employee costs, occupancy expenses, furniture and equipment expenses, advertising and marketing expenses, FDIC premiums, data processing expenses, director's fees, loss on sale of other real estate, and other operating expenses. Total non-interest expenses increased \$2,671,000, or 7.56%, during the first nine months of 2015 compared to the same period in 2014. The increase for the quarter ended September 30, 2015 was \$1,421,000, or 11.86%, as compared to the same quarter in 2014. The Company experienced an increase of \$918,000, or 7.35%, in non-interest expenses in the third quarter of 2015 as compared to the second quarter of 2015. The increase in non-interest expenses for the nine months ended September 30, 2015 when compared to the comparable period in 2014 is primarily attributable to an increase in salaries and employee bonuses associated with a one-time mid-year bonus that was paid to all employees in the second quarter of 2015

Table of Contents

in recognition of the Bank being named one of the 2015 Top Workplaces by the Tennessean newspaper. The increase in salaries was offset by a settlement of a claim during the second quarter of 2015 resulting in a \$1,325,000 reversal of an accrual for potential litigation losses due the settlement of a claim against the Company during the second quarter of 2015. Loss on the sale of other real estate decreased \$190,000 for the nine months ended September 30, 2015 as compared to the same period in 2014 due to a lower volume of foreclosures as well as improved economic conditions and an improved housing market.

**Income Taxes**

The Company's income tax expense was \$11,000,000 for the nine months ended September 30, 2015, an increase of \$1,478,000 over the comparable period in 2014. Income tax expense was \$3,774,000 for the quarter ended September 30, 2015, an increase of \$353,000 over the same period in 2014. The percentage of income tax expense to net income before taxes was 38.06% and 39.35% for the nine months ended September 30, 2015 and September 30, 2014, respectively, and 38.27% and 39.00% for the quarters ended September 30, 2015 and 2014, respectively. The percentage of income tax expense to net income before taxes was 37.29% for the second quarter of 2015.

**Financial Condition****Balance Sheet Summary**

The Company's total assets increased 4.60% to 1,959,376,000 during the nine months ended September 30, 2015 from 1,873,242,000 at December 31, 2014. Total assets increased \$19,948,000 during the three-month period ended September 30, 2015 and increased \$14,032,000, or 0.73%, during the three-month period ended June 30, 2015. Loans, net of allowance for loan losses, totaled \$1,444,334,000 at September 30, 2015, a 8.61% increase compared to \$1,329,865,000 at December 31, 2014. Net loans increased \$33,285,000, or 2.36%, during the three months ended September 30, 2015. The increase in loans resulted from an overall increase in loan demand in the housing market, as well other sectors in which we lend money, along with an increase in marketing efforts that concentrated on increasing the volume of loans. Reflecting increased loan demand, fed funds sold and securities decreased. Securities decreased \$55,702,000, or 14.87%, to \$318,841,000 at September 30, 2015 from \$374,543,000 at December 31, 2014. Securities decreased \$35,847,000, or 10.11%, during the three months ended September 30, 2015. Federal funds sold decreased to \$15,405,000 at September 30, 2015 from \$16,005,000 at December 31, 2014.

Total liabilities increased by 4.10% to \$1,740,834,000 at September 30, 2015 compared to \$1,672,350,000 at December 31, 2014. For the quarter ended September 30, 2015, total liabilities increased \$13,571,000, or 0.79%. The increase in total liabilities since December 31, 2014 was composed of a \$63,557,000, or 3.83%, increase in total deposits and a \$5,510,000, or 63.75%, increase in accrued interest and other liabilities, partially offset by a \$583,000, or 16.96%, decrease in securities sold under repurchase agreements. The increase in total deposits is attributable to expansion into new markets that resulted in the opening of new accounts. The increase in accrued interest and other liabilities is attributable to an increase in employee bonus payable as well as an increase in federal and state taxes payable.

**Non Performing Assets**

The following tables present the Company's non-accrual loans and past due loans as of September 30, 2015 and December 31, 2014.

Table of Contents

## Loans on Nonaccrual Status

	In Thousands	
	September 30, 2015	December 31, 2014
Residential 1-4 family	\$42	\$42
Multifamily	—	—
Commercial real estate	4,293	—
Construction	—	—
Farmland	575	574
Second mortgages	106	—
Equity lines of credit	—	—
Commercial	—	—
Agricultural, installment and other	—	—
Total	\$5,016	\$616

(In thousands)

	30-59 Days Past Due	60-89 Days Past Due	Non Accrual and Greater Than 90 Days	Total Non Accrual and Past Due	Current	Total Loans	Recorded Investment Greater Than 90 Days Past Due and Accruing
September 30, 2015							
Residential 1-4 family	\$2,685	910	956	4,551	352,809	357,360	\$ 914
Multifamily	—	—	—	—	53,956	53,956	—
Commercial real estate	82	—	4,316	4,398	598,885	603,283	23
Construction	137	83	—	220	286,161	286,381	—
Farmland	189	5	741	935	33,976	34,911	166
Second Mortgages	54	47	173	274	7,779	8,053	67
Equity Lines of Credit	24	—	9	33	47,925	47,958	9
Commercial	23	—	—	23	27,255	27,278	—
Agricultural, installment and other	362	71	33	466	52,529	52,995	33
Total	\$3,556	1,116	6,228	10,900	1,461,275	1,472,175	\$ 1,212
December 31, 2014							
Residential 1-4 family	\$6,166	1,275	1,352	8,793	341,965	350,758	\$ 1,310
Multifamily	—	—	—	—	31,242	31,242	—
Commercial real estate	2,151	242	19	2,412	562,553	564,965	19
Construction	125	91	73	289	245,541	245,830	73
Farmland	88	—	594	682	29,554	30,236	20
Second Mortgages	286	18	70	374	8,652	9,026	70
Equity Lines of Credit	346	—	5	351	41,145	41,496	5
Commercial	37	—	—	37	29,963	30,000	—
Agricultural, installment and other	301	126	44	471	52,754	53,225	44
Total	\$9,500	1,752	2,157	13,409	1,343,369	1,356,778	\$ 1,541

Generally, at the time a loan is placed on nonaccrual status, all interest accrued on the loan in the current fiscal year is reversed from income, and all interest accrued and uncollected from the prior year is charged off against the allowance for loan losses. Thereafter, interest on nonaccrual loans is recognized as interest income only to the extent that cash is

received and future

34

---

## Table of Contents

collection of principal is not in doubt. A nonaccrual loan may be restored to accruing status when principal and interest are no longer past due and unpaid and future collection of principal and interest on a timely basis is not in doubt.

Non-performing loans, which included non-accrual loans and loans 90 days past due, at September 30, 2015 totaled \$6,228,000 an increase from \$2,157,000 at December 31, 2014. The increase in non-performing loans during the nine months ended September 30, 2015 of \$4,071,000 is due primarily to an increase in non-performing commercial real estate mortgage loans of \$4,297,000 that resulted primarily from one large commercial real estate loan changing to non-performing status. Management believes that it is probable that it will incur losses on these loans but believes that these losses should not exceed the amount in the allowance for loan losses already allocated to these loans, unless there is renewed deterioration of local real estate values.

Other loans may be classified as impaired when the current net worth and financial capacity of the borrower or of the collateral pledged, if any, is viewed as inadequate. Such loans generally have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt, and if such deficiencies are not corrected, there is a probability that the Company will sustain some loss. In such cases, interest income continues to accrue as long as the loan does not meet the Company's criteria for nonaccrual status.

The increase in impaired loans during the nine months ended September 30, 2015 was primarily due to one loan relationship becoming impaired. Overall, the Company's market areas have seen improvements in the residential real estate market and the commercial real estate market remains steady. The allowance for loan loss related to collateral dependent impaired loans was measured based upon the estimated fair value of related collateral.

Loans are charged-off in the month when the determination is made that the loan is uncollectible. Net charge-offs for the nine months ended September 30, 2015 were \$135,000 as compared to \$15,000 in net recoveries for the same period in 2014 and \$861,000 in net charge-offs for the year ended December 31, 2014. The Bank has continued to experience a decrease in past dues and nonaccruals, with the exception of one large loan placed on non-accrual during the first quarter of 2015, and is experiencing fewer foreclosures which has resulted in fewer charge offs.

The collateral values securing potential problem loans, including impaired loans, based on estimates received by management, total approximately \$52.2 million. At September 30, 2015, the internally classified loans have decreased \$7,226,000, or 20.18%, to \$28,582,000 from \$35,808,000 at December 31, 2014. Loans are listed as classified when information obtained about possible credit problems of the borrower has prompted management to question the ability of the borrower to comply with the repayment terms of the loan agreement. The loan classifications do not represent or result from trends or uncertainties which management expects will materially impact future operating results, liquidity or capital resources.

The largest category of internally graded loans at September 30, 2015 was real estate mortgage loans. Included within this category are residential real estate construction and development loans, including loans to home builders and developers of land, as well as one-to-four family mortgage loans, and commercial real estate loans. Residential real estate loans, including construction and land development loans that are internally classified totaled \$11,507,000 and \$15,860,000 at September 30, 2015 and December 31, 2014, respectively. These loans have been graded accordingly due to bankruptcies, inadequate cash flows and delinquencies. The Bank continues to see an improvement in internally graded loans as the cash flows from home builders, land developers, and commercial real estate borrowers continue to improve. Management does not anticipate losses on the internally classified residential real estate construction and development loans at September 30, 2015 to exceed the amount already allocated to loan losses.

### Liquidity and Asset Management

The Company's management seeks to maximize net interest income by managing the Company's assets and liabilities within appropriate constraints on capital, liquidity and interest rate risk. Liquidity is the ability to maintain sufficient cash levels necessary to fund operations, meet the requirements of depositors and borrowers, and fund attractive investment opportunities. Higher levels of liquidity bear corresponding costs, measured in terms of lower yields on short-term, more liquid earning assets and higher interest expense involved in extending liability maturities.

Liquid assets include cash and cash equivalents and investment securities and money market instruments that will mature within one year. At September 30, 2015, the Company's liquid assets totaled \$208.8 million. Additionally, as of September 30, 2015, we had available to us approximately \$53.0 million in unused federal funds line of credit with

regional banks, subject to certain restrictions and collateral requirements, to meet short term funding needs. The Company maintains a formal asset and liability management process to quantify, monitor and control interest rate risk and to assist management in maintaining stability in the net interest margin under varying interest rate environments. The Company accomplishes this process through the development and implementation of lending, funding and pricing strategies designed to maximize net interest income under varying interest rate environments subject to specific liquidity and interest rate risk guidelines.

35

---



Table of Contents

Analysis of rate sensitivity and rate gap analysis are the primary tools used to assess the direction and magnitude of changes in net interest income resulting from changes in interest rates. Included in the analysis are cash flows and maturities of financial instruments held for purposes other than trading, changes in market conditions, loan volumes and pricing and deposit volume and mix. These assumptions are inherently uncertain, and, as a result, net interest income cannot be precisely estimated nor can the impact of higher or lower interest rates on net interest income be precisely predicted. Actual results will differ due to timing, magnitude and frequency of interest rate changes and changes in market conditions and management's strategies, among other factors.

The Company's primary source of liquidity is a stable core deposit base. In addition, short-term borrowings, loan payments and investment security maturities provide a secondary source. At September 30, 2015, the Company had a liability sensitive position (a negative gap). Liability sensitivity means that more of the Company's liabilities are capable of re-pricing over certain time frames than its assets. The interest rates associated with these liabilities may not actually change over this period but are capable of changing.

The Company also uses simulation modeling to evaluate both the level of interest rate sensitivity as well as potential balance sheet strategies. The Asset Liability Committee meets quarterly to analyze the interest rate shock simulation. The interest rate simulation model is based on a number of assumptions. These assumptions include, but are not limited to, prepayments on loans and securities, deposit decay rates, pricing decisions on loans and deposits, reinvestment and replacement of asset and liability cash flows and balance sheet management strategies. We model instantaneous change in interest rates using a growth in the balance sheet as well as a flat balance sheet to understand the impact to earnings and capital. The Company also uses Economic Value of Equity ("EVE") sensitivity analysis to understand the impact of changes in interest rates on long-term cash flows, income and capital. EVE is calculated by discounting the cash flows for all balance sheet instruments under different interest rate scenarios. The economic value of equity is a longer term view of interest rate risk because it measures the present value of the future cash flows. Presented below is the estimated impact on Wilson Bank's net interest income and EVE as of September 30, 2015, assuming an immediate shift in interest rates:

	% Change from Base Case for Immediate Parallel Changes in Rates		
	-100 BP <sup>(1)</sup>	+100 BP	+200 BP
Net interest income	(2.41	)% (3.41	) (6.73
EVE	(8.31	) 0.11	(0.68

(1) Because certain current interest rates are at or below 1.00%, the 100 basis points downward shock assumes that certain corresponding interest rates reflects a decrease of less than the full 100 basis point downward shock. Management believes that with present maturities, the anticipated growth in deposit base, and the efforts of management in its asset/liability management program, liquidity will not pose a problem in the near term future. At the present time there are no known trends or any known commitments, demands, events or uncertainties that will result in, or that are reasonably likely to result in, the Company's liquidity changing in a materially adverse way. Interest rate risk (sensitivity) management focuses on the earnings risk associated with changing interest rates. Management seeks to maintain profitability in both immediate and long-term earnings through funds management/interest rate risk management. The Company's rate sensitivity position has an important impact on earnings. Senior management of the Company analyzes the rate sensitivity position quarterly. Management focuses on the spread between the Company's cost of funds and interest yields generated primarily through loans and investments.

The Company's securities portfolio consists of earning assets that provide interest income. For those securities classified as held-to-maturity, the Company has the ability and intent to hold these securities to maturity or on a long-term basis. Securities classified as available-for-sale include securities intended to be used as part of the Company's asset/liability strategy and/or securities that may be sold in response to changes in interest rate, prepayment risk, the need or desire to increase capital and similar economic factors. At September 30, 2015, securities totaling

approximately \$17.6 million mature or will be subject to rate adjustments within the next twelve months. A secondary source of liquidity is the Company's loan portfolio. At September 30, 2015, loans totaling approximately \$360.4 million either will become due or will be subject to rate adjustments within twelve months from that date. Continued emphasis will be placed on structuring adjustable rate loans.

Table of Contents

As for liabilities, certificates of deposit of \$100,000 or greater totaling approximately \$113.3 million will become due or reprice during the next twelve months. Historically, there has been no significant reduction in immediately withdrawable accounts such as negotiable order of withdrawal accounts, money market demand accounts, demand deposit accounts and regular savings accounts. Management anticipates that there will be no significant withdrawals from these accounts in the future.

Management believes that with present maturities, the anticipated growth in deposit base, and the efforts of management in its asset/liability management program, liquidity will not pose a problem in the near term future. At the present time there are no known trends or any known commitments, demands, events or uncertainties that will result in or that are reasonably likely to result in the Company's liquidity changing in a materially adverse way.

Off Balance Sheet Arrangements

At September 30, 2015, we had unfunded loan commitments outstanding of \$397.7 million and outstanding standby letters of credit of \$34.3 million. Because these commitments generally have fixed expiration dates and many will expire without being drawn upon, the total commitment level does not necessarily represent future cash requirements. If needed to fund these outstanding commitments, the Bank has the ability to liquidate Federal funds sold or securities available-for-sale or on a short-term basis to borrow and purchase Federal funds from other financial institutions. Additionally, the Bank could sell participations in these or other loans to correspondent banks. As mentioned above, the Bank has been able to fund its ongoing liquidity needs through its stable core deposit base, loan payments, investment security maturities and short-term borrowings.

Capital Position and Dividends

At September 30, 2015, total stockholders' equity was \$218,542,000, or 11.15% of total assets, which compares with \$200,892,000, or 10.72% of total assets, at December 31, 2014. The dollar increase in stockholders' equity during the nine months ended September 30, 2015 results from the Company's net income of \$17,905,000, proceeds from the issuance of common stock related to exercise of stock options of \$190,000, the net effect of a \$1,538,000 unrealized gain on investment securities net of applicable income taxes of \$589,000, cash dividends declared of \$4,935,000 of which \$3,511,000 was reinvested under the Company's dividend reinvestment plan and \$30,000 related to stock option compensation.

The Company and the Bank are subject to regulatory capital requirements administered by the FDIC, the Federal Reserve and the Tennessee Department of Financial Institutions. Failure to meet minimum capital requirements can initiate certain mandatory and possibly additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the Company's and the Bank's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Company and the Bank must meet specific capital guidelines that involve quantitative measures of their assets, liabilities and certain off-balance sheet items as calculated under regulatory accounting practices. The capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors. Prompt corrective action provisions are not applicable to bank holding companies.

Quantitative measures established by regulation to ensure capital adequacy require the Company and the Bank to maintain minimum amounts and ratios (set forth in the following table) of total, common equity, and Tier 1 capital (as defined in the regulations) to risk-weighted assets (as defined) and of Tier 1 capital (as defined) to average assets (as defined). Management believes, as of September 30, 2015 and December 31, 2014, that the Company and Wilson Bank meet all capital adequacy requirements to which they are subject.

As of September 30, 2015, the most recent notification from the FDIC categorized Wilson Bank as well capitalized under the regulatory framework for prompt corrective action. There are no conditions or events since the notification that management believes have changed the Bank's category. To be categorized as well capitalized as of December 31, 2014, an institution must have maintained minimum total risk-based, Tier 1 risk-based, Common Equity Tier 1, and Tier 1 leverage ratios as set forth in the following tables and not have been subject to a written agreement, order or directive to maintain a higher capital level. The minimum capital levels required to be considered well-capitalized from and after January 1, 2015, are as follows: a Tier 1 leverage capital ratio of 5%, a common equity Tier 1 capital ratio of 6.5%, a Tier 1 risk-based capital ratio of 8% (up from 6.0% under the previous rules) and a total risk-based

capital ratio of 10%. The Company's and the Bank's actual capital amounts and ratios as of September 30, 2015 and December 31, 2014, are also presented in the table:

37

---

Table of Contents

	Actual		Minimum Capital Requirement		Minimum To Be Well Capitalized Under Applicable Regulatory Provisions			
	Amount	Ratio	Amount	Ratio	Amount	Ratio		
	(dollars in thousands)							
September 30, 2015								
Total capital to risk weighted assets:								
Consolidated	\$233,856	13.8	% \$135,569	8.0	% \$169,461	10.0	%	
Wilson Bank	232,749	13.8	134,927	8.0	168,659	10.0		
Tier 1 capital to risk weighted assets:								
Consolidated	213,466	12.6	101,650	6.0	135,534	8.0		
Wilson Bank	211,579	12.5	101,558	6.0	135,411	8.0		
Common equity tier 1 capital to average assets:								
Consolidated	213,466	12.6	76,238	4.5	110,121	6.5		
Wilson Bank	211,579	12.5	76,168	4.5	110,021	6.5		
Tier 1 capital to average assets:								
Consolidated	213,466	11.0	77,624	4.0	N/A	N/A		
Wilson Bank	211,579	10.9	77,644	4.0	97,055	5.0		
	Actual		Minimum Capital Requirement		Minimum To Be Well Capitalized Under Applicable Regulatory Provisions			
	Amount	Ratio	Amount	Ratio	Amount	Ratio		
	(dollars in thousands)							
December 31, 2014								
Total capital to risk weighted assets:								
Consolidated	\$214,779	15.0	% \$114,549	8.0	% \$143,186	10.0	%	
Wilson Bank	213,447	14.9	114,602	8.0	143,253	10.0		
Tier 1 capital to risk weighted assets:								
Consolidated	196,765	13.7	57,450	4.0	86,174	6.0		
Wilson Bank	195,433	13.6	57,480	4.0	86,220	6.0		
Tier 1 capital to average assets:								
Consolidated	196,765	10.6	74,251	4.0	N/A	N/A		
Wilson Bank	195,433	10.5	74,451	4.0	93,063	5.0		

In July 2013, the Federal banking regulators, in response to the statutory requirements of The Dodd-Frank Wall Street Reform and Consumer Protection Act, adopted new regulations implementing the Basel Capital Adequacy Accord (“Basel III”) and the related minimum capital ratios. The new capital requirements were effective January 1, 2015 and included a new “Common Equity Tier I Ratio”, which has stricter rules as to what qualifies as Common Equity Tier I Capital. Comparability between the ratios at December 31, 2014 and September 30, 2015 may be limited due to a change in the capital requirements and calculation of capital ratios. A summary of the changes to the Regulatory Capital Ratios are as follows:



Table of Contents

	Guideline in Effect At December 31, 2014		Basel III Requirements in Effect At September 30, 2015		
	Minimum	Well Capitalized	Minimum	Well Capitalized	
Common Equity Tier I Ratio (Common Equity to Risk Weighted Assets)	Not Applicable	Not Applicable	4.5	% 6.5	%
Tier I Capital to Risk Weighted Assets	4	% 6	% 6	% 8	%
Total Capital to Risk Weighted Assets	8	% 10	% 8	% 10	%
Tier I Leverage Ratio	4	% 5	% 4	% 5	%

The guidelines under Basel III establish a 2.5% capital conservation buffer requirement that is phased in over four years beginning January 1, 2016. The buffer is related to Risk Weighted Assets. The Basel III minimum requirements after giving effect to the buffer are as follow:

	2016	2017	2018	2019	
Common Equity Tier I Ratio	5.125	% 5.75	% 6.375	% 7.0	%
Tier I Capital to Risk Weighted Assets Ratio	6.625	% 7.25	% 7.875	% 8.5	%
Total Capital to Risk Weighted Assets Ratio	8.625	% 9.25	% 9.875	% 10.5	%

In order to avoid limitations on capital distributions such as dividends and certain discretionary bonus payments to executive officers, a banking organization must maintain capital ratios above the minimum ratios including the buffer.

**Impact of Inflation**

Although interest rates are significantly affected by inflation, the inflation rate is immaterial when reviewing the Company's results of operations.

**Part I. Financial Information****Item 3. Quantitative and Qualitative Disclosures About Market Risk**

The Company's primary component of market risk is interest rate volatility. Fluctuations in interest rates will ultimately impact both the level of income and expense recorded on a large portion of the Company's assets and liabilities, and the market value of all interest-earning assets and interest-bearing liabilities, other than those which possess a short term to maturity. Based upon the nature of the Company's operations, the Company is not subject to foreign currency exchange or commodity price risk.

Interest rate risk (sensitivity) management focuses on the earnings risk associated with changing interest rates.

Management seeks to maintain profitability in both short-term and long-term earnings through funds management/interest rate risk management. The Company's rate sensitivity position has an important impact on earnings. Senior management of the Company meets monthly to analyze the rate sensitivity position. These meetings focus on the spread between the cost of funds and interest yields generated primarily through loans and investments. There have been no material changes in reported market risks during the nine months ended September 30, 2015.

**Part I. Financial Information****Item 4. Controls and Procedures**

The Company maintains disclosure controls and procedures, as defined in Rule 13a-15(e) promulgated under the Securities Exchange Act of 1934 (the "Exchange Act"), that are designed to ensure that information required to be disclosed by the Company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms and that such information is accumulated and communicated to the Company's management, including its Chief Executive Officer and its Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. The Company carried out an evaluation, under the supervision and with the participation of its management, including its Chief Executive Officer and Chief Financial Officer,





Table of Contents

of the effectiveness of the design and operation of its disclosure controls and procedures as of the end of the period covered by this report. Based on the evaluation of these disclosure controls and procedures, its Chief Executive Officer and its Chief Financial Officer concluded that the Company's disclosure controls and procedures were effective.

There were no changes in the Company's internal control over financial reporting during the Company's fiscal quarter ended September 30, 2015 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

**PART II. OTHER INFORMATION**

**Item 1. LEGAL PROCEEDINGS**

Not applicable

**Item 1A. RISK FACTORS**

There were no material changes to the Company's risk factors as previously disclosed in Part I, Item 1A of the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2014.

**Item 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS**

(a) None

(b) Not applicable.

(c) None

**Item 3. DEFAULTS UPON SENIOR SECURITIES**

(a) None

(b) Not applicable

**Item 4. MINE SAFETY DISCLOSURES**

Not applicable

**Item 5. OTHER INFORMATION**

None

**Item 6. EXHIBITS**

31.1 Certification of the Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

31.2 Certification of the Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

32.1 Certification of the Chief Executive Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

32.2 Certification of the Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

101 Interactive Data File

\*Management compensatory plan or arrangement.

Table of Contents

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

WILSON BANK HOLDING COMPANY  
(Registrant)

DATE: November 9, 2015

/s/ Randall Clemons  
Randall Clemons  
President and Chief Executive Officer

DATE: November 9, 2015

/s/ Lisa Pominski  
Lisa Pominski  
Senior Vice President & Chief Financial Officer