NEW PEOPLES BANKSHARES INC
Form 10-K
March 25, 2014
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United States

Securities and Exchange Commission

Washington, D.C. 20549

FORM 10-K

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

For fiscal year ended December 31, 2013

Commission File Number 000-33411

New Peoples Bankshares, Inc.

(Exact name of registrant as specified in its charter)

Virginia	**31-1804543**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**

67 Commerce Drive

Honaker, VA	**24260**
(Address of principal executive offices)	**(Zip Code)**

Registrant s telephone number, including area code (276) 873-7000

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

None

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

Common Stock - $2 Par Value

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

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

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

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

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

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. (Check one):

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

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

The aggregate market value of the common stock held by non-affiliates, based on the last reported sales prices of $1.30 per share on the last business day of the second quarter of 2013 was $10,894,351.

The number of shares outstanding of the registrant s common stock was 21,872,293 as of March 21, 2014.

DOCUMENTS INCORPORATED BY REFERENCE:

The Proxy Statement for New Peoples Bankshares, Inc s 2014 Annual Meeting to Shareholders, is incorporated into Items 10 through 14 of this form 10-K.

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PART I

Item 1. Business

General

New Peoples Bankshares, Inc. (New Peoples) is a Virginia bank holding company headquartered in Honaker, Virginia. Prior to January 1, 2009, New Peoples was a financial holding company. Our business is conducted primarily through New Peoples Bank, Inc., a Virginia banking corporation (the Bank). The Bank has a division doing business as New Peoples Financial Services which offers investment services through its broker dealer relationship with LPL Financial Services, Inc. NPB Insurance Services, Inc. (NPB Insurance) is a subsidiary of the Bank and offers insurance services only.

The Bank offers a range of banking and related financial services focused primarily on serving individuals, small to medium size businesses, and the professional community. We strive to serve the banking needs of our customers while developing personal, hometown relationships with them. Our board of directors believes that marketing customized banking services enables us to establish a niche in the financial services marketplace where we do business.

The Bank is headquartered in Honaker, Virginia and operates 23 full service offices in the southwestern Virginia counties of Russell, Scott, Washington, Tazewell, Buchanan, Dickenson, Wise, Lee, Smyth, and Bland; Mercer County in southern West Virginia and the eastern Tennessee county of Sullivan. The close proximity and mobile nature of individuals and businesses in adjoining counties and nearby cities in Virginia, West Virginia and Tennessee places these markets within our Bank s targeted trade area, as well.

We provide professionals and small and medium size businesses in our market area with responsive and technologically enabled banking services. These services include loans that are priced on a deposit relationship basis, easy access to our decision makers, and quick and innovative action necessary to meet a customer s banking needs. Our capitalization and lending limit enable us to satisfy the credit needs of a large portion of the targeted market segment. When a customer needs a loan that exceeds our lending limit, we try to find other financial institutions to participate in the loan with us.

Our History

The Bank was incorporated under the laws of the Commonwealth of Virginia on December 9, 1997 and began operations on October 28, 1998. On September 27, 2001, the shareholders of the Bank approved a plan of reorganization under which they exchanged their shares of Bank common stock for shares of New Peoples common stock. On November 30, 2001, the reorganization was completed and the Bank became New Peoples wholly owned subsidiary.

In June 2003, New Peoples formed two new wholly-owned subsidiaries, NPB Financial Services, Inc. (currently named NPB Insurance Services, Inc.) and NPB Web Services, Inc. (NPB Web), a web design and hosting company.

NPB Insurance is a full-service insurance agency, selling property, general and professional liability, bonds, life and health products, and credit life and accident insurance to individual and commercial clients. However, the Bank, through its division New Peoples Financial services, offers fixed and variable annuities, fee based asset management and other investment products through a broker/dealer relationship with LPL Financial Services, Inc.

NPB Web is inactive.

In July 2004, NPB Capital Trust I was formed to issue $11.3 million in trust preferred securities.

In September 2006, NPB Capital Trust 2 was formed to issue $5.2 million in trust preferred securities.

Branch Locations

After a period of significant branch expansion between 2000 and 2008, we have consolidated some of our branch operations to improve efficiency. Currently, in addition to our headquarters in Honaker, Virginia we have 22 branches located in Abingdon, Virginia; Big Stone Gap, Virginia; Bland, Virginia; Bluefield, Virginia; Bristol, Virginia; Castlewood, Virginia; Chilhowie, Virginia; Clintwood, Virginia; Gate City, Virginia; Grundy, Virginia; Haysi, Virginia; Jonesville, Virginia; Lebanon, Virginia; Norton, Virginia; Pound, Virginia; Pounding Mill, Virginia; Tazewell, Virginia; Weber City, Virginia; Wise, Virginia; Bluewell, West Virginia; Princeton, West Virginia; and Kingsport, Tennessee.

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Our Market Areas

Our primary market area consists of southwestern Virginia, southern West Virginia and northeastern Tennessee. Specifically, we operate in the southwestern Virginia counties of Russell, Scott, Washington, Tazewell, Buchanan, Dickenson, Wise, Lee, Smyth, and Bland; Mercer County in southern West Virginia and the northeastern Tennessee county of Sullivan (collectively, the Tri-State Area). The close proximity and mobile nature of individuals and businesses in adjoining counties and nearby cities in Virginia, West Virginia and Tennessee place these markets within our Bank s targeted trade area, as well.

Accessibility to Interstates I-77, I-81, I-26, I-64 and I-75, as well as major state and U.S. highways including US 19, US 23, US 58, US 460 and US 421, make the area an ideal location for businesses to serve markets in the Mid-Atlantic, Southeast and Midwest. The area is strategically located midway between Atlanta-Pittsburgh, Charlotte-Cincinnati, and Richmond-Louisville, and is within a day s drive of more than half of the U.S. population. A regional airport located in Bristol, Tennessee serves the area with commercial flights to and from major cities in the United States. Commercial rail service providers include CSX Transportation and Norfolk Southern Railways.

The Tri-State Area has a diversified economy supported by natural resources, which include coal, natural gas, limestone, and timber; agriculture; healthcare; education; technology; manufacturing and services industries. Predominantly, the market is comprised of locally-owned and operated small businesses. Considerable investments in high-technology communications, high-speed broadband network and infrastructure have been made which has opened the area to large technology companies and future business development potential for new and existing businesses. Industries are taking advantage of the low cost of doing business, training opportunities, available workforce and an exceptional quality of life experience for employers and employees alike.

Internet Site

We have our internet banking site at www.newpeoplesbank.com. The site includes a customer service area that contains branch and ATM locations, product descriptions and current interest rates offered on deposit accounts. Customers with internet access can access account balances, make transfers between accounts, enter stop payment orders, order checks, and use an optional bill paying service.

Available Information

We file annual, quarterly, and current reports, proxy statements and other information with the Securities and Exchange Commission (the SEC). Our SEC filings are filed electronically and are available to the public over the internet at the SEC s web site at www.sec.gov. In addition, any document we file with the SEC can be read and copied at the SEC s public reference facilities at 100 F Street, N.E., Washington, D.C. 20549. Copies of documents can be obtained at prescribed rates by writing to the Public Reference Section of the SEC at 100 F Street, N.E., Washington, D.C. 20549. The public may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. We also provide a link to our filings on the SEC website, free of charge, through our internet website www.npbankshares.com under Investor Relations.

Banking Services

General. We accept deposits, make consumer and commercial loans, issue drafts, and provide other services customarily offered by a commercial bank, such as business and personal checking and savings accounts, walk-up tellers, drive-in windows, and 24-hour automated teller machines. The Bank is a member of the Federal Reserve System and its deposits are insured under the Federal Deposit Insurance Act to the maximum limit.

Loans. Generally, we offer a full range of short-to-medium term commercial, 1-4 family residential mortgages and personal loans. Commercial loans include both secured and unsecured loans for working capital (including inventory and receivables), business expansion (including acquisition of real estate and improvements) and purchase of equipment and machinery. Consumer loans may include secured and unsecured loans for financing automobiles, home improvements, education, personal investments and other purposes.

Our lending activities are subject to a variety of lending limits imposed by state law. While differing limits apply in certain circumstances based on the type of loan or the nature of the borrower (including the borrower s relationship to the Bank), in general, the Bank is subject to a loan-to-one borrower limit of an amount equal to 15% of its capital and surplus in the case of loans which are not fully secured by readily marketable or other permissible types of collateral. The Bank voluntarily may choose to impose a policy limit on loans to a single borrower that is less than the legal lending limit.

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We obtain short-to-medium term commercial and personal loans through direct solicitation of business owners and continued business from existing customers. Completed loan applications are reviewed by our loan officers. As part of the application process, information is obtained concerning the income, financial condition, employment and credit history of the applicant. If commercial real estate is involved, information is also obtained concerning cash flow after debt service. Loan quality is analyzed based on the Bank s experience and its credit underwriting guidelines.

Loans by type as a percentage of total loans are as follows:

	December 31,				
	2013	2012	2011	2010	2009
Commercial, financial and agricultural	11.70%	12.61%	14.35%	15.48%	15.56%
Real estate construction	4.55%	4.66%	5.42%	7.39%	9.41%
Real estate mortgage	78.46%	77.09%	73.79%	69.13%	66.02%
Installment loans to individuals	5.29%	5.64%	6.44%	8.00%	9.01%
Total	100.00%	100.00%	100.00%	100.00%	100.00%

In the above table the category Real estate mortgage includes both commercial loans secured by real estate and residential mortgage loans secured by real estate. At December 31, 2013 we had $126.2 million in loans secured by commercial real estate, or 25.59% of total loans, and $260.7 million secured by residential real estate, or 52.87% of total loans.

Commercial Loans. We make commercial loans to qualified businesses in our market area. Our commercial lending consists primarily of commercial and industrial loans to finance accounts receivable, inventory, property, plant and equipment. Commercial business loans generally have a higher degree of risk than residential mortgage loans, but have commensurately higher yields. Residential mortgage loans are generally made on the basis of the borrower s ability to make repayment from employment and other income and are secured by real estate whose value tends to be easily ascertainable. In contrast, commercial business loans typically are made on the basis of the borrower s ability to make repayment from cash flow from its business and are secured by business assets, such as commercial real estate, accounts receivable, equipment and inventory. As a result, the availability of funds for the repayment of commercial business loans may be substantially dependent on the success of the business itself.

Further, the collateral for commercial business loans may depreciate over time and cannot be appraised with as much precision as residential real estate. To manage these risks, our underwriting guidelines require us to secure commercial loans with both the assets of the borrowing business and other additional collateral and guarantees that may be available. In addition, we actively monitor certain measures of the borrower, including advance rate, cash flow, collateral value and other appropriate credit factors.

Residential Mortgage Loans. Our residential mortgage loans consist of residential first and second mortgage loans, residential construction loans, home equity lines of credit and term loans secured by first and second mortgages on the residences of borrowers for home improvements, education and other personal expenditures. We make mortgage loans with a variety of terms, including fixed and floating or variable rates and a variety of maturities.

Under our underwriting guidelines, residential mortgage loans are generally made on the basis of the borrower s ability to make repayment from employment and other income and are secured by real estate whose value tends to be easily ascertainable. These loans are made consistent with our appraisal policies and real estate lending policies, which detail maximum loan-to-value ratios and maturities. New requirements arising out of the response to the recent financial crisis for extending residential mortgage loans may impact our ability to make these types of loans in the same volume as in the past.

Construction Loans. Construction lending entails significant additional risks, compared to residential mortgage lending. Construction loans often involve larger loan balances concentrated with single borrowers or groups of related borrowers. Construction loans also involve additional risks attributable to the fact that loan funds are advanced upon the security of property under construction, which is of uncertain value prior to the completion of construction. Thus, it is more difficult to evaluate the total loan funds required to complete a project and related loan-to-value ratios accurately. To minimize the risks associated with construction lending, loan-to-value limitations for residential, multi-family and non-residential construction loans are in place. These are in addition to the usual credit analysis of borrowers. Management feels that the loan-to-value ratios help to minimize the risk of loss and to compensate for normal fluctuations in the real estate market. Maturities for construction loans generally range from 4 to 12 months for residential property and from 6 to 18 months for non-residential and multi-family properties.

Consumer Loans. Our consumer loans consist primarily of installment loans to individuals for personal, family and household purposes. The specific types of consumer loans that we make include home improvement loans, debt consolidation loans and general consumer lending. Consumer loans entail greater risk than residential mortgage loans do, particularly in the case of consumer loans that are unsecured, such as lines of credit, or secured by rapidly depreciating assets such as automobiles. In such cases, any repossessed collateral for a defaulted consumer loan may not provide an adequate source of repayment of the outstanding loan balance as a result of the greater likelihood of damage, loss or depreciation. The remaining deficiency often does not warrant further substantial collection efforts against the borrower. In addition, consumer loan collections are dependent on the borrower s continuing financial stability, and thus are more likely to be adversely affected by job loss, divorce, illness or personal bankruptcy. Furthermore, the application of various federal and state laws, including federal and state bankruptcy and insolvency laws, may limit the amount which can be recovered on such loans. A borrower may also be able to assert against the Bank as an assignee any claims and defenses that it has against the seller of the underlying collateral.

Our underwriting policy for consumer loans seeks to limit risk and minimize losses, primarily through a careful analysis of the borrower. In evaluating consumer loans, we require our lending officers to review the borrower s level and stability of income, past credit history and the impact of these factors on the ability of the borrower to repay the loan in a timely manner. In addition, we maintain an appropriate margin between the loan amount and collateral value.

Deposits. We offer a variety of deposit products for both individual and business customers. These include demand deposit, interest-bearing demand deposit, savings deposit, and money market deposit accounts. In addition, we offer certificates of deposit with terms ranging from 7 days to 60 months and individual retirement accounts with terms ranging from 12 months to 60 months.

Investment Services. We offer a variety of investment services for both individual and business customers. These services include fixed income products, variable annuities, mutual funds, indexed certificates of deposit, individual retirement accounts, long term care insurance, employee group benefit plans, college savings plans, financial planning, managed money accounts, and estate planning. We offer these services through our broker-dealer relationship with LPL Financial Services, Inc.

Other Bank Services. Other bank services include safe deposit boxes, cashier s checks, certain cash management services, direct deposit of payroll and social security checks and automatic drafts for various accounts. We offer ATM card services that can be used by our customers throughout Virginia and other regions. We also offer MasterCard and VISA credit card services through an intermediary. Electronic banking services include debit cards, internet banking, telephone banking and wire transfers.

We do not presently anticipate obtaining trust powers, but we are able to provide similar services through our affiliation with LPL Financial Services, Inc.

Competition

The banking business is highly competitive. We compete as a financial intermediary with other commercial banks, savings and loan associations, credit unions, mortgage banking firms, consumer finance companies, securities brokerage firms, insurance companies, money market mutual funds and other financial institutions operating in the southwestern Virginia, southern West Virginia, and eastern Tennessee market area and elsewhere. Our market area is a highly competitive, highly branched banking market.

Competition in the market area for loans to small businesses and professionals, the Bank s target market, is intense, and pricing is important. Many of our larger competitors have substantially greater resources and lending limits than we have. They offer certain services, such as extensive and established branch networks and trust services that we do not expect to provide or will not provide in the near future. Moreover, larger institutions operating in the market area have access to borrowed funds at lower costs than are available to us. Deposit competition among institutions in the market area also is strong. As a result, it is possible that we may have to pay above-market rates to attract deposits.

While pricing is important, our principal method of competition is service. As a community banking organization, we strive to serve the banking needs of our customers while developing personal, hometown relationships with them. As a result, we provide a significant amount of service and a range of products without the fees that customers can expect from larger banking institutions.

According to a market share report prepared by the Federal Deposit Insurance Corporation (the FDIC), as of June 30, 2013, the most recent date for which market share information is available, the Bank s deposits as a percentage of total deposits in its major market areas were as follows: Russell County, VA 25.55%, Scott County, VA 35.64%, Dickenson County, VA 27.54%, Tazewell County, VA 7.65%, Smyth County, VA 2.78%, Lee County, VA 3.89%, Buchanan County, VA 9.62%, Wise County, VA 7.96%, City of Norton, VA 10.59%, Bland County, VA 23.78%, Washington County, VA 2.68%, and the City of Bristol, VA 2.25%, Mercer County, WV 8.91%, and City of Kingsport, TN 1.39%.

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Employees

As of December 31, 2013, we had 277 total employees, of which 252 were full-time employees. None of our employees are covered by a collective bargaining agreement, and we consider relations with employees to be excellent.

Supervision and Regulation

General. As a bank holding company, we are subject to regulation under the Bank Holding Company Act of 1956, as amended (BHCA), and the examination and reporting requirements of the Board of Governors of the Federal Reserve System (the Federal Reserve). We are also subject to Chapter 13 of the Virginia Banking Act, as amended (Virginia Act). As a state-chartered commercial bank, the Bank is subject to regulation, supervision and examination by the Virginia State Corporation Commission s Bureau of Financial Institutions (BFI). As a member of the Federal Reserve system, the Bank is also subject to regulation, supervision and examination by the Federal Reserve. Other federal and state laws, including various consumer protection and compliance laws, govern the activities of the Bank, such as the investments that it makes and the aggregate amount of loans that it may grant to one borrower.

The following description summarizes the most significant federal and state laws applicable to New Peoples and its subsidiaries. To the extent that statutory or regulatory provisions are described, the description is qualified in its entirety by reference to that particular statutory or regulatory provision.

The Bank Holding Company Act. Under the BHCA, the Federal Reserve examines New Peoples periodically. New Peoples is also required to file periodic reports and provide any additional information that the Federal Reserve may require. Activities at the bank holding company level are generally limited to:

- banking, managing or controlling banks;
- furnishing services to or performing services for its subsidiaries; and
- engaging in other activities that the Federal Reserve has determined by regulation or order to be so closely related to banking as to be a proper incident to these activities.

Thus, the activities we can engage in are restricted as a matter of law.

With some limited exceptions, the BHCA requires every bank holding company to obtain the prior approval of the Federal Reserve before:

- acquiring substantially all the assets of any bank;
- acquiring direct or indirect ownership or control of any voting shares of any bank if after such acquisition it would own or control more than 5% of the voting shares of such bank (unless it already owns or controls the majority of such shares); or

merging or consolidating with another bank holding company.

As a result, our ability to engage in certain strategic activities is conditioned on regulatory approval.

In addition, and subject to some exceptions, the BHCA and the Change in Bank Control Act require Federal Reserve approval prior to any person or company acquiring control of a bank holding company as defined in the statutes and regulations. These requirements make it more difficult for control of our company to change or for us to acquire substantial investments.

The Virginia Act. As a bank holding company registered with the BFI, we must provide the BFI with information concerning our financial condition, operations and management, among other reports required by the BFI. New Peoples is also examined by the BFI in addition to its Federal Reserve examinations. Similar to the BHCA, the Virginia Act requires that the BFI approve the acquisition of direct or indirect ownership or control of more than 5% of the voting shares of any Virginia bank or bank holding company like us.

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Payment of Dividends. New Peoples is a separate legal entity that derives the majority of its revenues from dividends paid to it by its subsidiaries. The Bank is subject to laws and regulations that limit the amount of dividends it can pay. In addition, both New Peoples and the Bank are subject to various regulatory restrictions relating to the payment of dividends, including requirements to maintain capital at or above regulatory minimums. Banking regulators have indicated that banking organizations should generally pay dividends only if the organization s net income available to common shareholders over the past year has been sufficient to fully fund the dividends and the prospective rate of earnings retention appears consistent with the organization s capital needs, asset quality and overall financial condition. The FDIC has the general authority to limit the dividends paid by FDIC insured banks if the FDIC deems the payment to be an unsafe and unsound practice. The FDIC has indicated that paying dividends that deplete a bank s capital base to an inadequate level would be an unsound and unsafe banking practice. In October 2009, the Federal Reserve Bank of Richmond (Richmond FRB) restricted the Company from paying dividends without prior approval. It is therefore highly unlikely that the Company will pay any dividends at least until the Richmond FRB s restriction is removed and this can impact the company s ability to attract capital investment and its share price.

As the recession continues to impact asset quality and earnings at financial institutions as the above discussion states, the regulatory authorities have broad discretion to, and may, further restrict the payment of dividends by affected financial institutions and this could impact us.

Capital Requirements. The Federal Reserve has issued risk-based and leverage capital guidelines applicable to banking organizations that it supervises. Under the risk-based capital requirements, the Bank and the Company are each generally required to maintain a minimum ratio of total capital to risk-weighted assets (including certain off-balance sheet activities, such as standby letters of credit) of 8%. At least half of the total capital must be composed of Tier 1 Capital , which is defined as common equity, retained earnings and qualifying perpetual preferred stock, less certain intangibles. The remainder may consist of Tier 2 Capital , which is defined as specific subordinated debt, some hybrid capital instruments and other qualifying preferred stock and a limited amount of the loan loss allowance. These risk-based capital standards attempt to measure capital adequacy relative to the institution s risk profiles. In addition, each of the federal banking regulatory agencies has established minimum leverage capital requirements for banking organizations. Under these requirements, banking organizations must maintain a minimum ratio of Tier 1 capital to adjusted average quarterly assets of between 3% and 5%, subject to federal bank regulatory evaluation of an organization s overall safety and soundness. The principal objective of the leverage ratio is to constrain the degree to which an institution may leverage its equity capital base. In sum, the capital measures used by the federal banking regulators are:

- the Total Capital ratio, which is the total of Tier 1 Capital and Tier 2 Capital;
- the Tier 1 Capital ratio; and
- the leverage ratio.

Under these regulations, a bank will be:

- well capitalized if it has a Total Capital ratio of 10% or greater, a Tier 1 Capital ratio of 6% or greater, a leverage ratio of 5% or greater, and is not subject to any written agreement, order, capital directive, or prompt corrective action directive by a federal bank regulatory agency to meet and maintain a specific capital level for any capital measure;

adequately capitalized if it has a Total Capital ratio of 8% or greater, a Tier 1 Capital ratio of 4% or greater, and a leverage ratio of 4% or greater or 3% in certain circumstances and is not well capitalized;

undercapitalized if it has a Total Capital ratio of less than 8%, a Tier 1 Capital ratio of less than 4% - or 3% in certain circumstances;

significantly undercapitalized if it has a Total Capital ratio of less than 6%, a Tier 1 Capital ratio of less than 3%, or a leverage ratio of less than 3%; or

critically undercapitalized if its tangible equity is equal to or less than 2% of average quarterly tangible assets,

The risk-based capital standards of the Federal Reserve explicitly identify concentrations of credit risk and the risk arising from non-traditional activities, as well as an institution s ability to manage these risks, as important factors to be taken into account by the agency in assessing an institution s overall capital adequacy. The capital guidelines also provide that an institution s exposure to a decline in the economic value of its capital due to changes in interest rates be considered as a factor in evaluating a banking organization s capital adequacy. Thus, the capital level of a bank can be of regulatory concern even if it is well-capitalized under the regulatory formula and a well-capitalized bank can be required to maintain even higher capital levels based on its asset quality or other regulatory concerns.

The regulators may take various corrective actions with respect to a financial institution considered to be capital deficient. These powers include, but are not limited to, requiring the institution to be recapitalized, prohibiting asset growth, restricting interest rates paid or dividends, requiring prior approval of capital distributions by any bank holding company that controls the institution, requiring divestiture by the institution of its subsidiaries or by the holding company of the institution itself, requiring new election of directors, and requiring the dismissal of directors and officers. As discussed above, in October 2009 the Richmond FRB imposed a prohibition on the Bank paying dividends to preserve capital. Bank holding companies can be called upon to boost their subsidiary bank s capital and to partially guarantee the institution s performance under its capital restoration plan. If this occurs, capital which otherwise would be available for holding company purposes, including possible distributions to shareholders, would be required to be downstreamed to the subsidiary bank. In this respect, the Richmond FRB also notified New Peoples that we must defer dividends on our trust preferred issuances, which we did as of October 2009. As of December 31, 2013, the Bank was well capitalized, with a Total Capital ratio of 13.96%; a Tier 1 Capital ratio of 12.69%; and a leverage ratio of 7.49%.

In addition, under the terms of the Written Agreement (See, Management s Discussion and Analysis of Financial Condition and Results of Operations), both the Company and the Bank have agreed to submit capital plans to maintain sufficient capital at the Company, on a consolidated basis, and the Bank, on a stand-alone basis, and to refrain from declaring or paying dividends without prior regulatory approval. The Company has agreed that it will not take any other form of payment representing a reduction in the Bank s capital or make any distributions of interest, principal, or other sums on subordinated debentures or trust preferred securities without prior regulatory approval. The Company may not incur, increase or guarantee any debt without prior regulatory approval and has agreed not to purchase or redeem any shares of its stock without prior regulatory approval.

On July 2, 2013, the Federal Reserve voted to adopt final Basel III capital rules for U.S. banking organizations. The final rules establish an integrated regulatory capital framework and will implement in the United States the Basel III regulatory capital reforms from the Basel Committee on Banking Supervision and certain changes required by the Dodd-Frank Act. Under the final rule, minimum requirements will increase for both the quantity and quality of capital held by banking organizations. Consistent with the international Basel framework, the final rule includes a new minimum ratio of common equity tier 1 capital (Tier I Common) to risk-weighted assets and a common equity tier 1 capital conservation buffer of 2.5% of risk-weighted assets that will apply to all supervised financial institutions. The rule also raises the minimum ratio of tier 1 capital to risk-weighted assets and includes a minimum leverage ratio of 4% for all banking organizations. These new minimum capital ratios will become effective for the Company on January 1, 2015 and will be fully phased-in on January 1, 2019.

The final rule emphasizes common equity tier 1 capital, the most loss-absorbing form of capital, and implements strict eligibility criteria for regulatory capital instruments. The final rule also improves the methodology for calculating risk-weighted assets to enhance risk sensitivity. Banks and regulators use risk weighting to assign different levels of risk to different classes of assets. We are in the process of evaluating the impact of the Basel III final rule on the Company s regulatory capital ratios.

Other Safety and Soundness Regulations. There are a number of obligations and restrictions imposed on bank holding companies and their bank subsidiaries by federal law and regulatory policy that are designed to reduce potential loss exposure to the depositors of such depository institutions and to the FDIC insurance funds in the event that the depository institution is insolvent or is in danger of becoming insolvent. For example, the Federal Reserve requires a bank holding company to serve as a source of financial strength to its subsidiary depository institutions and to commit resources to support such institutions in circumstances where it might not do so otherwise. These requirements can restrict the ability of bank holding companies to deploy their capital as they otherwise might.

Interstate Banking and Branching. Banks in Virginia may branch without geographic restriction. Current federal law authorizes interstate acquisitions of banks and bank holding companies without geographic limitation. Bank holding companies may acquire banks in any state without regard to state law except for state laws requiring a minimum time a bank must be in existence to be acquired. The Virginia Act generally permits out of state bank holding companies or banks to acquire Virginia banks or bank holding companies subject to regulatory approval. These laws have the effect of increasing competition in banking markets.

Monetary Policy. The commercial banking business is affected not only by general economic conditions but also by the monetary policies of the Federal Reserve. The Federal Reserve s monetary policies have had a significant effect on the operating results of commercial banks in the past and are expected to continue to do so in the future. In view of unsettled conditions in the national and international economy and money markets, as well as governmental fiscal and monetary policies their impact on interest rates, deposit levels, loan demand or the business and earnings of the Bank is unpredictable.

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Federal Reserve System. Depository institutions that maintain transaction accounts or nonpersonal time deposits are subject to reserve requirements. These reserve requirements are subject to adjustment by the Federal Reserve. Because required reserves must be maintained in the form of vault cash or in a non-interest-bearing account at, or on behalf of, a Federal Reserve Bank, the effect of the reserve requirement is to reduce the amount of the institution s interest-earning assets.

Transactions with Affiliates. Transactions between banks and their affiliates are governed by Sections 23A and 23B of the Federal Reserve Act. These provisions restrict the amount and provide conditions with respect to loans, investments, transfers of assets and other transactions between New Peoples and the Bank.

Loans to Insiders. The Bank is subject to rules on the amount, terms and risks associated with loans to executive officers, directors, principal shareholders and their related interests.

Community Reinvestment Act. Under the Community Reinvestment Act, depository institutions have an affirmative obligation to assist in meeting the credit needs of their market areas, including low and moderate-income areas, consistent with safe and sound banking practice. The Community Reinvestment Act emphasizes the delivery of bank products and services through branch locations in its market areas and requires banks to keep data reflecting their efforts to assist in its community s credit needs. Depository institutions are periodically examined for compliance with the Community Reinvestment Act and are periodically assigned ratings in this regard. Banking regulators consider a depository institution s Community Reinvestment Act rating when reviewing applications to establish new branches, undertake new lines of business, and/or acquire part or all of another depository institution. An unsatisfactory rating can significantly delay or even prohibit regulatory approval of a proposed transaction by a bank holding company or its depository institution subsidiaries. A bank holding company will not be permitted to become a financial holding company and no new activities authorized under the GLBA (see below) may be commenced by a holding company or by a bank financial subsidiary if any of its bank subsidiaries received less than a satisfactory rating in its latest Community Reinvestment Act examination. The Bank received a rating of Satisfactory at its last Community Reinvestment Act performance evaluation, as of August 12, 2013.

Other Laws. Banks and other depository institutions also are subject to numerous consumer-oriented laws and regulations. These laws, which include the Truth in Lending Act, the Truth in Savings Act, the Real Estate Settlement Procedures Act, the Electronic Funds Transfer Act, the Equal Credit Opportunity Act, the Fair and Accurate Credit Transactions Act of 2003 and the Fair Housing Act, require compliance by depository institutions with various disclosure and consumer information handling requirements. These and other similar laws result in significant costs to financial institutions and create potential liability for financial institutions, including the imposition of regulatory penalties for inadequate compliance.

Gramm-Leach-Bliley Act of 1999. The Gramm-Leach-Bliley Act of 1999 (GLBA) covers a broad range of issues, including a repeal of most of the restrictions on affiliations among depository institutions, securities firms and insurance companies.

For example, the GLBA permits unrestricted affiliations between banks and securities firms. It also permits bank holding companies to elect to become financial holding companies, which can engage in a broad range of financial services, including securities activities such as underwriting, dealing, investment, merchant banking, insurance underwriting, sales and brokerage activities. In order to become a financial holding company, a bank holding company and all of its affiliated depository institutions must be well-capitalized, well-managed and have at least a satisfactory Community Reinvestment Act rating. We converted to bank holding company status on January 1, 2009 from financial holding company. We believe we adequately provide the products and services our customers currently need or want as a bank holding company.

Essentially GLBA removed many of the limitations on affiliations between commercial banks and their holding companies and other financially related business that had been in place since the Depression. Recently, this effect of GLBA has been the subject of controversy and cited as one of the causes of the financial services crisis. As a result, The Dodd-Frank Act (as discussed later) addressed some of the criticized aspects of GLBA, but not in a way that would materially affect us.

The GLBA also provides that the states continue to have the authority to regulate insurance activities, but prohibits the states in most instances from preventing or significantly interfering with the ability of a bank, directly or through an affiliate, to engage in insurance sales, solicitations or cross-marketing activities.

USA Patriot Act. The USA Patriot Act provides for the facilitation of information sharing among governmental entities and financial institutions for the purpose of combating terrorism and money laundering. Regulatory authorities must consider the effectiveness of a financial institution s anti-money laundering activities, for example, its procedures for effective customer identification, when reviewing bank mergers and acquisitions. Various other laws and regulations require the Bank to cooperate with governmental authorities in respect to counter-terrorism activities. Although it does create a reporting obligation and cost of compliance for the Bank, the USA Patriot Act has not materially affected New Peoples products, services or other business activities.

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Privacy and Fair Credit Reporting. Financial institutions, such as the Bank, are required to disclose their privacy policies to customers and consumers and require that such customers or consumers be given a choice (through an opt-out notice) to forbid the sharing of nonpublic personal information about them with nonaffiliated third persons. The Bank also requires business partners with whom it shares such information to assure the Bank that they have adequate security safeguards and to abide by the redisclosure and reuse provisions of applicable law. In addition to adopting federal requirements regarding privacy, individual states are authorized to enact more stringent laws relating to the use of customer information. To date, Virginia has not done so. These privacy laws create compliance obligations and potential liability for the Bank.

Sarbanes-Oxley Act. The Sarbanes-Oxley Act of 2002 (the Sarbanes-Oxley Act) is intended to increase corporate responsibility, provide enhanced penalties for accounting and auditing improprieties by publicly traded companies and to protect investors by improving the accuracy and reliability of corporate disclosures made pursuant to the securities law. The changes required by the Sarbanes-Oxley Act and its implementing regulations are intended to allow shareholders to monitor the performance of companies and their directors more easily and effectively.

The Sarbanes-Oxley Act generally applies to all domestic companies, such as New Peoples, that file periodic reports with the Securities and Exchange Commission (SEC) under the Securities Exchange Act of 1934, as amended. The Sarbanes-Oxley Act includes significant additional disclosure requirements and expanded corporate governance rules and the SEC has adopted extensive additional disclosures, corporate governance provisions and other related rules pursuant to it. New Peoples has expended, and will continue to expend, considerable time and money in complying with the Sarbanes-Oxley Act.

Emergency Economic Stabilization Act of 2008. EESA was enacted in response to the financial crises affecting the banking system and financial markets.

Pursuant to EESA, the Department of the Treasury implemented the Troubled Asset Relief Program Capital Purchase Program (the TARP Capital Purchase Program) under which the Treasury agreed to make $250 billion of capital available to U.S. financial institutions in the form of preferred stock (from the $700 billion authorized by the EESA). Numerous requirements have been imposed on TARP participating financial institutions, particularly requirements related to executive compensation. We did not elect to apply to participate in TARP.

Federal Deposit Insurance Corporation. The Bank s deposits are insured by the Deposit insurance Fund, as administered by the FDIC, to the maximum amount permitted by law, now $250,000 per depositor. Due to the increased number of bank failures resulting from the credit crisis and severe recession, FDIC premiums have materially increased and may increase further. This is a significant expense for us and is likely to continue to be.

Dodd-Frank Wall Street Reform and Consumer Protection Act. The Dodd-Frank Act was signed into law on July 21, 2010. Its wide ranging provisions affect all federal financial regulatory agencies and nearly every aspect of the American financial services industry. Among the provisions of the Dodd-Frank Act that directly impact the Company is the creation of an independent Consumer Financial Protection Bureau (CFPB), which has the ability to write rules for consumer protections governing all financial institutions. All consumer protection responsibility formerly handled by other banking regulators is consolidated in the CFPB. It will also oversee the enforcement of all federal laws intended to ensure fair access to credit. For smaller financial institutions such as the Company and the Bank, the CFPB will coordinate its examination activities through their primary regulators.

The Dodd-Frank Act contains provisions designed to reform mortgage lending, which includes the requirement of additional disclosures for consumer mortgages. The CFPB has begun implementing mortgage lending regulations to carry out its mandate. In addition, the Federal Reserve has issued new rules, effective October 1, 2011, which had the effect of limiting the fees charged to merchants by credit card companies for debit card transactions. The result of these rules will be to limit the amount of interchange fee income available explicitly to larger banks and indirectly to us. The Dodd-Frank Act also contains provisions that affect corporate governance and executive compensation.

Although the Dodd-Frank Act provisions themselves are extensive, the ultimate impact on the Company of this massive legislation is unknown. The Act provides that several federal agencies, including the Federal Reserve, the CFPB and the Securities and Exchange Commission, shall issue regulations implementing major portions of the legislation, and this process is ongoing.

Future Regulatory Uncertainty. Because federal and state regulation of financial institutions changes regularly and is the subject of constant legislative debate, New Peoples cannot forecast how regulation of financial institutions may change in the future and impact its operations. New Peoples fully expects that the financial institution industry will remain heavily regulated and that additional laws or regulations may be adopted further regulating specific banking practices.

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Subsequent Events

We have considered subsequent events through the date of the financial statements in this Form 10-K.

Item 1A. Risk Factors

Not applicable.

Item 1B. Unresolved Staff Comments

Not applicable.

Item 2. Properties

At December 31, 2013, the Company s net investment in premises and equipment in service was $30.0 million. Our main office and operations center is located in Honaker, Virginia. This location contains a full service branch, and our administration and operations center.

The Bank owns all of its 23 full service branches, including its headquarter office. The location of these branches are described in Item 1.

The Bank owns a location in Dungannon, Virginia that half of the location was used for a branch location until its closure during 2010. This half and the other half of the location is currently being leased. The Bank owns additional property in Princeton, West Virginia that is being developed for a future full service branch location, and currently serves as a loan administration office. The Princeton location is anticipated to operate as a full service branch in the distant future. During 2012, the Bank closed offices in Bristol, Pennington Gap, and Richlands, Virginia and Jonesborough, Tennessee. The Bristol office was leased to the Bank s subsidiary NPB Insurance Services, Inc. in 2013 and this lease will continue in 2014. The Pennington Gap property was sold in January 2013. The other two offices are vacant and may be used for future banking offices again when the economy recovers.

We believe that all of our properties are maintained in good operating condition and are suitable and adequate for our operational needs.

Item 3. Legal Proceedings

In the course of operations, we may become a party to legal proceedings. We became aware of a lawsuit against the Bank in April 2010. This case involves a claim against the Bank by a joint venture between Bank customers, some of whom are former members of senior management, and three investors. The allegation is that the joint venture, VFI, should have priority over the Bank s deed of trust in order for VFI s unrecorded and unrecordable ground lease to be enforceable for its full ten year term. There are also additional claims for damages resulting from allegations that the Bank s representatives imputed liability to the Bank based upon breach of fiduciary duty, fraud, and collaboration. The parties agreed to litigate the ground lease issue first and are now in negotiations to resolve all pending issues due to the fact that the business associated with the building has ceased and the building is vacant. Attempts to mediate this matter have been unsuccessful and a pretrial hearing was held in April 2013. On January 24, 2014 a hearing was held and in March 2014 the Judge ruled in the Bank s favor regarding VFI s claim of unjust enrichment and a hearing has been scheduled to enter an order to this effect and release the lis pendens recorded against the property. Two of the three plaintiffs have withdrawn their claim in this matter. Management and Bank s counsel believe VFI s position is not supported by law or the facts presented.

Item 4. Mine Safety Disclosures

Not applicable.

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PART II

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

(a) Market Information

Registrar and Transfer Company is the stock transfer agent for New Peoples Bankshares, Inc. The common stock of New Peoples is quoted on the Over The Counter Bulletin Board (OTCBB) under the symbol NWPP . The volume of trading of shares of common stock is very limited. Trades in our common stock occur sporadically on a local basis and typically small volumes of stock is traded.

The high and low prices at which our common stock has traded known to us for each quarter in the past two years are set forth in the table below. These prices are obtained through inquiry of shareholders transferring stock and by our listing on the OTCBB. Other transactions may have occurred at prices about which we are not aware.

	2013		2012	
	High	Low	High	Low
1st quarter	$ 1.75	$ 1.25	$ 3.00	$ 1.50
2nd quarter	1.56	1.30	1.50	1.05
3rd quarter	2.20	1.30	5.00	1.07
4th quarter	1.70	1.00	1.50	1.07

The most recent sales price of which management is aware was $1.34 per share on March 12, 2014.

(b) Holders

On March 21, 2014, there were approximately 4,453 shareholders of record.

(c) Dividends

In order to preserve capital to support our growth in the past we have not paid cash dividends. The declaration of dividends in the future will depend on our earnings and capital requirements and compliance with regulatory mandates. We are subject to certain restrictions imposed by the reserve and capital requirements of federal and Virginia banking statutes and regulations. Moreover, the Written Agreement we have with the banking regulators prohibits the Company from paying any cash dividends and the Bank s ability to pay dividends to the Company. So long as these restrictions remain in place the Company will not pay any cash dividends. Thereafter, the Company may or may not pay cash dividends depending on various factors including capital needs, earnings, and other factors our Board of Directors deems relevant. As a result, we do not anticipate paying a dividend on our common stock in 2014. See Note 3, Note 16 and Note 22 of the Notes to the Consolidated Financial Statements for further discussion of dividend limitations and capital requirements.

Item 6. Selected Financial Data

Not applicable.

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

Caution About Forward Looking Statements

We make forward looking statements in this annual report that are subject to risks and uncertainties. These forward looking statements include statements regarding our profitability, liquidity, allowance for loan losses, interest rate sensitivity, market risk, growth strategy, and financial and other goals. The words believes, expects, may, will, sh projects, contemplates, anticipates, forecasts, intends, or other similar words or terms are intended to identify fo looking statements. The forward-looking information is based on various factors and was derived using numerous assumptions. Important factors that may cause actual results to differ from projections include:

- the success or failure of our efforts to implement our business plan;
- achieving and maintaining compliance with the Written Agreement between us and the banking regulators;
- any required increase in our regulatory capital ratios;
- satisfying other regulatory requirements that may arise from examinations, changes in the law and other similar factors;
- any substantial increase in nonperforming loans;
- our ability to attract additional talent that we may need;
- any required increase to our loan loss reserve;
- the difficult market conditions in our industry;
- the unprecedented levels of market volatility;
- the effects of soundness of other financial institutions;
- the uncertain outcome of recently enacted legislation to stabilize the U.S. financial system;
- the potential impact on us of recently enacted legislation;

- the lack of a market for our common stock;
- the ability to successfully manage our growth or implement our growth strategies if we are unable to identify attractive markets, locations or opportunities to expand in the future;
- success in increasing capital to support our financial condition resulting from the recession;
- in the near future, achieving the cost savings we project without customer rejection as we close unprofitable branches, and, in the longer term maintaining cost controls and asset qualities as we open or acquire new branches;
- the successful management of interest rate risk;
- changes in interest rates and interest rate policies;
- reliance on our management team, including our ability to attract and retain key personnel;
- changes in general economic and business conditions in our market area;
- risks inherent in making loans such as repayment risks and fluctuating collateral values;
- competition with other banks and financial institutions, and companies outside of the banking industry, including those companies that have substantially greater access to capital and other resources;
- demand, development and acceptance of new products and services;
- problems with technology utilized by us;
- changing trends in customer profiles and behavior;
- changes in governmental regulations, tax rates and similar matters; and
- other risks which may be described in our future filings with the SEC.

Because of these uncertainties, our actual future results may be materially different from the results indicated by these forward looking statements. In addition, our past results of operations do not necessarily indicate our future results.

We expressly disclaim any obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise, except as required by law.

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General

The following commentary discusses major components of our business and presents an overview of our consolidated financial position at December 31, 2013 and 2012 as well as results of operations for the years ended December 31, 2013 and 2012. This discussion should be reviewed in conjunction with the consolidated financial statements and accompanying notes and other statistical information presented elsewhere in this Form 10-K.

New Peoples generates a significant amount of its income from the net interest income earned by the Bank. Net interest income is the difference between interest income and interest expense. Interest income depends on the amount of interest-earning assets outstanding during the period and the interest rates earned thereon. The Bank s interest expense is a function of the average amount of deposits and borrowed money outstanding during the period and the interest rates paid thereon. The quality of the assets further influences the amount of interest income lost on nonaccrual loans and the amount of additions to the allowance for loan losses. The Bank also generates noninterest income from service charges on deposit accounts and commissions on insurance and investment products sold.

Written Agreement

The Company and the Bank entered into a written agreement (the Written Agreement) with the Federal Reserve Bank of Richmond and the Virginia Bureau of Financial Institutions. Under the Written Agreement, the Bank has agreed to develop and submit for approval within specified time periods written plans to: (a) strengthen board oversight of management and the Bank s operation; (b) if appropriate after review, to strengthen the Bank s management and board governance; (c) strengthen credit risk management policies; (d) enhance lending and credit administration; (e) enhance the Bank s management of commercial real estate concentrations; (f) conduct ongoing review and grading of the Bank s loan portfolio; (g) improve the Bank s position with respect to loans, relationships, or other assets in excess of $1 million which are now or in the future become past due more than 90 days, which are on the Bank s problem loan list, or which are adversely classified in any report of examination of the Bank; (h) review and revise, as appropriate, current policy and maintain sound processes for maintaining an adequate allowance for loan and lease losses; (i) enhance management of the Bank s liquidity position and funds management practices; (j) revise its contingency funding plan; (k) revise its strategic plan; and (l) enhance the Bank s anti-money laundering and related activities.

In addition, the Bank has agreed that it will: (a) not extend, renew, or restructure any credit that has been criticized by the Reserve Bank or the Bureau absent prior board of directors approval in accordance with the restrictions in the Agreement; (b) eliminate all assets or portions of assets classified as loss and thereafter charge off all assets classified as loss in a federal or state report of examination, which has been done.

The Company and the Bank have agreed to submit capital plans to maintain sufficient capital at the Company, on a consolidated basis, and the Bank, on a stand-alone basis, and to refrain from declaring or paying dividends without prior regulatory approval. The Company has agreed that it will not take any other form of payment representing a reduction in the Bank s capital or make any distributions of interest, principal, or other sums on subordinated debentures or trust preferred securities without prior regulatory approval. The Company may not incur, increase or guarantee any debt without prior regulatory approval and has agreed not to purchase or redeem any shares of its stock without prior regulatory approval.

Under the terms of the Written Agreement, the Company and the Bank have appointed a committee to monitor compliance. The directors of the Company and the Bank have recognized and unanimously agree with the common goal of financial soundness represented by the Written Agreement and have confirmed the intent of the directors and executive management to diligently seek to comply with all requirements of the Written Agreement.

Written Agreement Progress Report

At December 31, 2013, we believe we have not yet achieved full compliance with the Written Agreement but we have made progress in our compliance efforts under the Written Agreement. We are aggressively working to comply with the Written Agreement and have timely submitted each required plan by its respective deadline. We have hired an independent consultant to assist us in these efforts and the following actions have taken place:

1. With regard to corporate governance, we have established a weekly Director s Loan Committee to oversee all loan approvals and all loan renewals, extensions and approvals for loans risk rated Special Mention or worse, as well as, exposures exceeding the Chief Credit Officer s lending authority. This has enabled the Board to increase its oversight of the Bank s largest credit exposures and problem credits, and enhanced the monitoring and compliance with all loan policies and procedures. Secondly, we have enhanced our reporting of credit quality to the board. Furthermore, we have adopted formal charters for our Nominating, Compliance, Compensation, and Loan Committees. A corporate governance policy was adopted by the Board of Directors on April 23, 2012.

2. The requirement to assess the Board and management has been completed by an independent party. A report has been issued to the Board and recommendations are being followed. In September 2010, our President and CEO was added as a member of the Board and in November 2010, Eugene Hearl was added as a member of the Board. Mr. Hearl has over 40 years banking experience as President and CEO for two community banks and Regional President of a large regional financial institution.

In addition, training is a key initiative of both the Board of Directors and employees. Further training of the Board and employees has been implemented and will be ongoing.

A formal management succession plan has been developed and approved by the Board of Directors.

3. In the month of September 2010, a newly revised strategic plan and a capital plan were completed and submitted to our regulators. The 2011 Budget was submitted to our regulators in the fourth quarter of 2010. The 2012 Budget was submitted to our regulators also in the fourth quarter of 2011. The 2013 Budget was submitted to our regulators in January 2013. A revised 2013 Budget was submitted to our regulators in the third quarter of 2013.

A revised strategic plan for the years 2013 through 2015 was completed and submitted to the regulators in January 2013.

A new strategic plan for the years 2014 through 2016 and the 2014 Budget were submitted to our regulators in the fourth quarter of 2013. A newly revised 2014-2016 capital plan has been submitted for regulatory review and is pending approval.

In September 2012, we converted notes payable to two of our directors totaling $5.5 million plus accrued interest of $272 thousand to common stock. As a result of the conversion, New Peoples returned to well capitalized status at September 30, 2012.

In accordance with our capital plan, we began a common stock offering in July 2012 to existing shareholders followed by an offering to the public during the third and fourth quarters of 2012. The offering was closed on December 20, 2012 and proceeds of $12,061,257 were received on December 28, 2012. Upon receipt of the proceeds we injected $7.0 million of capital into the Bank. The remaining net proceeds are held at the Company and will be used for payment of operating expenses and, when permitted by regulatory authorities, the payment of deferred trust preferred interest. The remaining additional cash may be used for future capital injections, if needed; thus, providing a source of strength at the holding company level for the Bank. In addition, the conversion of the director notes to common stock and the recent stock offering included common stock warrants that may be exercised in the next five years and potentially provide additional capital if, and when, they are exercised. A total of 2,364,142 common stock warrants were outstanding as of December 31, 2013 with an exercise price of $1.75. Assuming all of these warrants are exercised before expiration, then an additional $4.1 million in capital would be provided by their exercise.

4. Loan policies have been revised; an online approval and underwriting system for loans has been implemented; underwriting, monitoring and management of credits and collections have been enhanced; frequency of external loan reviews increased; and the focus on problem loans intensified at all levels in the organization. As a result, we are more timely in identifying problem loans. In the future, continuing these procedures should strengthen asset quality substantially. Further training of lending personnel is ongoing regarding proper risk grading of credits and identification of problem credits.

5. Enhanced loan concentration identification and new procedures for monitoring and managing concentrations have been implemented. Loan concentration targets have been established and efforts continue to reduce higher risk concentrations. In particular, construction and development loans and commercial real estate loans have been reduced and continue to decrease toward acceptable levels as determined by the new policies.

6. To strengthen management of credit quality and loan production, we added a new Chief Credit Officer, Stephen Trescot, in the first quarter of 2011 who has brought vast credit administration experience to our management team. Sharon Borich, our former Chief Credit Officer, assumed the role of Senior Lending Officer with oversight of loan production and business development which is her area of expertise. On February 28, 2014, Stephen Trescot retired as Executive Vice President and Chief Credit Officer of the Bank. Karen Wimmer was appointed as Executive Vice President and Chief Credit Officer of the Bank effective March 1, 2014. Ms. Wimmer previously served as Senior Vice President and Senior Credit Officer

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of the Bank since the fourth quarter of 2012 in which she reported directly to Mr. Trescot. Ms. Wimmer has a total of 26 years of banking experience. Mr. Trescot will continue to provide consulting services to the Bank on a contractual basis.

In addition to new lending policies and procedures, the management of all real estate development projects and draws has been centralized. We have segregated the duties of lenders for greater specialization of commercial and retail lending responsibilities. As a result we have formed a Commercial Loan division that is supervised by the Senior Vice President and Senior Lending Officer. The retail loans are primarily the responsibility of branch personnel who report to branch managers and respective area managers.

The credit analysis function has been restructured and is a part of credit administration. The credit analysis function is led by a Vice President/Senior Analyst, who supervises two analysts, of which, one analyst is a CPA. The function reports directly to the Executive Vice President and Chief Credit Officer and is responsible for analyzing new and renewed loan relationships of $250 thousand or more prior to approval and conducting annual financial reviews of loan relationships of $500 thousand or more.

The appraisal review function, consisting of two Vice Presidents, one of which is an experienced licensed appraiser, and one administrative assistant, also reports directly to the Chief Credit Officer. The appraisal review function reviews the quality of appraisals on behalf of the Bank by reviewing the methods, assumptions, and value conclusions of internal and external appraisals. In addition, this data is used to determine whether an external appraiser should be utilized for future work.

7. We have retained an independent third party to perform loan reviews on a quarterly basis in 2010 and 2011 and engaged them to perform this function in June 2012 and December 2012. We engaged them to perform this function in June 2013, December 2013, June 2014 and December 2014. The third party loan review company has also conducted two loan portfolio stress tests for the Bank to obtain a better understanding of potential loan losses over a two year period. In 2013, we began conducting our own loan portfolio stress test.

8. To support the focus on problem credit management the Bank further developed, in March, 2011, a Special Assets department which reports to the Chief Credit Officer. Presently, the department has one workout specialist/Vice President, one Vice President managing other real estate owned properties, an analyst, and two support personnel. Substantially all the credits in the Bank which are risk rated Special Mention or worse are assigned to this department once all efforts to return the credit to a satisfactory rating have been exhausted. This department is organizationally structured to manage workout situations, collections, other real estate owned, nonperforming assets, watch list credits, and the Bank s legal department. New reporting and monitoring is conducted monthly by this division. Material changes to Special Asset credits are reported to the Board at the time of occurrence and, quarterly, the Board receives written action plans and status updates on all problem credits in excess of $1.0 million. A quarterly management watch list committee has been established to actively manage and monitor these credits.

9. A new allowance for loan loss model was implemented and reviewed independently during 2010. The Board has approved a new allowance for loan loss policy. We have shifted duties for maintaining the allowance for loan loss model and credit reporting to a more experienced employee. The allowance for loan loss and the methodology supporting the results are approved quarterly by the Audit Committee of the Board of Directors, and ratified by the Board.

10. We have significantly increased our asset based liquidity sources throughout 2010, 2011, 2012 and 2013 to meet financial obligations. A new liquidity risk management policy has been adopted and a revised contingency funding plan has been created. We have lost all of our federal funds lines of credit, but we have added an internet certificate of deposit funding source to increase contingent funding sources. We believe that we have adequate liquidity in normal and stressed situations. We are further developing an investment portfolio, as well. The investment portfolio has grown to $79.1 million at December 31, 2013 from $4.7 million at December 31, 2010.

11. In the fourth quarter of 2009, we ceased the declaration of dividends from the Bank to the Company. We also deferred interest payments on our trust preferred securities issuances.

12. Anti-money laundering and bank secrecy act programs and training have been enhanced.

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Overview

At December 31, 2013, total assets were $684.7 million, total loans were $493.0 million, and total deposits were $619.0 million at December 31, 2013. The Company returned to profitability in 2013 and reports a total net income after tax of $1.5 million or $0.07 per basic share and per diluted share for the year ended December 31, 2013 as compared to a net loss of $6.3 million, or $0.57 per basic and per diluted share for the year ended December 31, 2012. The annualized return on average assets for the fiscal year 2013 was 0.21% as compared to (0.86)% for the same period in 2012. The annualized return on average equity was 3.71% for the fiscal year 2013 and (23.62)% for the same period in 2012.

During the years 2013 and 2012, we strategically decreased total assets, total loans and higher cost deposits to improve our capital position and manage our net interest margin by reducing higher cost funding. Total assets decreased $34.3 million in 2013, or 4.77%, from $719.0 million at December 31, 2012. We currently expect total assets to remain around current levels in the near future as we manage to maintain the level of earning assets and continue to improve net income. In December 2012, the Company successfully completed a public offering of its common stock, which resulted in net proceeds of $11.4 million after $624 thousand of expenses related to the offering. Upon completion of the offering and receipt of proceeds, $7.0 million was injected in the Bank s capital. As a result of this asset shrinkage and capital injection, the Bank improved its capital position and maintained a well-capitalized status throughout 2012 and 2013. The following Bank ratios existed at December 31, 2013 as compared to December 31, 2012, respectively: Tier 1 leverage ratio of 7.49% versus 7.08%; Tier 1 risk based capital ratio of 12.69% versus 11.60%; and total risk based capital ratio of 13.96% versus 12.88%.

For the year ending December 31, 2013, we had net income of $1.5 million as compared to a $6.3 million loss for the same period in 2012, an increase of $7.8 million, or 123.47%. This increase in earnings was primarily related to three areas: reduced provisions for loan losses, reduced other real estate related expenses, no federal income tax expense as it was applied to the net operating loss carryforward, and no valuation allowance was needed on our deferred tax asset. We maintained a strong net interest margin of 4.03% in 2013 as compared to 4.13% in 2012. However, the decreased volume of earning assets in 2013 and high levels of nonperforming assets decreased net interest income to $25.3 million in 2013 from $27.3 million in 2012. In 2013, we made $550 thousand in provisions for loan losses compared to $4.8 million in 2012, a decrease of $4.3 million, or 88.54%. Expenses related to other real estate owned properties were $2.3 million in 2013 compared to $4.5 million in 2012. During 2013 we had to record writedowns on other real estate owned properties in the amount of $562 thousand compared to $2.6 million in 2012. During 2013 we reversed $428 thousand of our deferred tax valuation allowance as compared to a $4.1 million deferred tax asset valuation allowance recorded in 2012. We may be able to continue reversing the valuation allowance in the future as earnings improve resulting in taxable income to offset net loss tax carryforwards.

Total deposits decreased $33.9 million, or 5.19%, from $652.9 million at December 31, 2012. The largest decrease in deposits has taken place in time deposits which have decreased from $372.5 million at December 31, 2012 to $347.0 million at December 31, 2013. This $25.5 million decrease in time deposits, or 6.84%, is the result of decreased interest rates offered in this very low interest rate environment, which is helping us lower our cost of funds and improve capital ratios through increased earnings and decreased assets.

Total loans decreased $29.4 million in 2013, or 5.62%, from $522.4 million at December 31, 2012 primarily in adversely classified loans. Loans rated substandard decreased $17.2 million, or 27.77%, to $44.9 million at December 31, 2013 from $62.1 million at December 31, 2012. The remaining loan portfolio remained relatively unchanged. The reduction in the adversely classified loans is the result of charge offs of $6.0 million during 2013, foreclosures, and the resolution of problem loans. The remaining portfolio maintained levels as we continue to serve our customers by renewing existing credits and pursuing new loans to qualified borrowers. We anticipate some further decrease in the loan portfolio in the future as we decrease nonperforming loans. However, lending personnel are focused on developing new and existing lending relationships which should continue to slow the pace of the reduction and maintain current levels in total loans subject, of course, to the impact of the underperforming economy and heightened competition in the banking industry.

Although asset quality is improving, nonperforming assets are higher than we desire as a result of the prolonged deterioration of the residential and commercial real estate markets, as well as the recessionary period. The ratio of nonperforming assets to total assets lowered to 6.45% at December 31, 2013 as compared to 6.67% at December 31, 2012. Nonperforming assets, which include nonaccrual loans, other real estate owned and past due loans greater than 90 days still accruing interest, decreased to $44.2 million at December 31, 2013 from $48.0 million at December 31, 2012, a reduction of $3.8 million, or 7.91%. The majority of these assets are loans secured by commercial real estate, residential mortgages, and farmland and other real estate owned properties. We are undertaking extensive efforts to work out these credits and liquidate foreclosed properties. This will take some time, but overall we believe we are making progress. In 2013, net charge offs were $4.3 million as compared to $6.4 million for 2012. Net charge offs for the year were related to real estate residential and commercial loans with collateral values that are dependent upon current market and economic conditions when these are ascertainable. Delinquencies also showed improvement in 2013 as total past dues decreased to $30.7 million at December 31, 2013 from $39.5 million at December 31, 2012, an improvement of $8.8 million, or 22.19% decrease.

During 2013, we have continued our progress in identifying the risks in our loan portfolio and strengthening asset quality. In addition, we have continued to improve our lending policies and train our lending staff on these policies and procedures. Each of these steps are critical to minimize future losses and to strengthen asset quality of the Bank. Our allowance for loan loss at December 31, 2013 is $13.1 million, or 2.65% of total loans as compared to $16.8 million, or 3.22% of total loans at December 31, 2012. The provision for loan losses decreased to $550 thousand in 2013 as compared to $4.8 million in 2012. The allowance for loan losses is being maintained at a level that management deems appropriate to absorb any potential future losses and known impairments within the loan portfolio whether or not the losses are actually ever realized. We continue to modify the allowance for loan loss model to best reflect the risks in the portfolio and the improvements made in our internal policies and procedures; however, future provisions may be deemed necessary. Net charge-offs year-to-date for 2013 as a percentage of total average loans improved to 0.84% as compared to 1.14% in 2012. Impaired loans decreased $24.0 million, or 36.83%, in 2013 to $41.2 million with an estimated allowance of $4.2 million for potential losses at December 31, 2013 as compared to $65.2 million in impaired loans with an estimated allowance of $5.9 million at the end of 2012.

Critical Accounting Policies

Certain critical accounting policies affect the more significant judgments and estimates used in the preparation of our financial statements. Our most critical accounting policies relate to our provision for loan losses and the calculation of our deferred tax asset and valuation allowance.

The provision for loan losses reflects the estimated losses resulting from the inability of our customers to make required payments. If the financial condition of our borrowers were to further deteriorate, resulting in an impairment of their ability to make payments, our estimates would be updated, and additional provisions could be required. For further discussion of the estimates used in determining the allowance for loan losses, we refer you to the section on Provision for Loan Losses in this discussion.

Our deferred income tax assets and liabilities are determined using the liability (or balance sheet) method. Under this method, the net deferred tax asset or liability is determined based on the tax effects of the temporary differences between the book and tax bases of the various balance sheet assets and liabilities and gives current recognition to changes in tax rates and laws. If all or a portion of the net deferred tax asset is determined to be unlikely to be realized, a valuation allowance is established to reduce the net deferred tax asset to the amount that is more likely than not to be realized. For further discussion of the deferred tax asset and valuation allowance, we refer you to the section on Deferred Tax Asset and Income Taxes in this discussion.

For further discussion of our other critical accounting policies, see Note 2, Summary of Significant Accounting Policies, to our Consolidated Financial Statements, found in Item 8 to this annual report on Form 10-K.

Net Interest Income and Net Interest Margin

The Company s primary source of income, net interest income, decreased $2.0 million, or 7.11% from 2012 to 2013. The decrease in net interest income is due primarily to a reduction in loans during 2013, decreased interest income from new and renewed loans recorded at lower interest rates, and the level of nonearning assets, i.e. nonaccrual loans and other real estate owned properties. Nonaccrual loans were $28.3 million at December 31, 2013, which negatively affects the net interest margin as these loans are nonearning assets. Loan interest income decreased $3.8 million, or

11.56%, from $32.6 million in 2013 to $28.8 million in 2012. Interest expense decreased $1.8 million, or 26.58%, from $6.5 million for the year ending 2012 to $4.7 million in 2013 as a result of deposits re-pricing at lower interest rates at maturity, and a shift in the deposit mix whereby our higher cost time deposits were replaced with lower cost deposit products. The net interest margin for the year ending December 31, 2013 was 4.03% as compared to 4.13% for the same period in 2012. We are trying to preserve the net interest margin, but we may experience some decrease in the net interest margin as new and renewed loans are sometimes priced at lower market interest rates and as opportunities decrease to lower our cost of funds since repricing of deposits will be close to existing interest rates in the future. Because of the tightening of our underwriting, loan pricing may be lower than historically; however, typically more conservative underwriting reduces the likelihood of future loan losses. Loan losses negatively impact earnings through various related expenses, for example, loan loss provisions, collection expenses, etc.

With regard to recognition of interest income on impaired loans, interest income and cash receipts on impaired loans are handled differently depending on whether or not the loan is on nonaccrual status. If the impaired loan is not on nonaccrual status, then the interest income on the loan is computed using the effective interest method. If there is serious doubt about the collectability of an impaired loan, it is the Bank s policy to stop accruing interest on a loan and classify that loan as nonaccrual under the following circumstances: (a) whenever we are advised by the borrower that scheduled payment or interest payments cannot be met, (b) when our best judgment indicates that payment in full of principal and interest can no longer be expected, or (c) when any such loan or obligation becomes delinquent for 90 days unless it is both well secured and in the process of collection. All interest accrued but not collected for loans that are placed on nonaccrual or charged off are reversed against interest income. The interest on these loans is accounted for on the cash basis or cost-recovery method, until qualifying for return to accrual. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and prospects for future contractual payments are reasonably assured. In addition, funds generated from a shrinking loan portfolio are reinvested at lower interest rates in both overnight deposits for liquidity purposes and in investment securities. If nonaccruing loans increase, it may reduce our net interest margin further. We continue to manage our yields on assets and our costs of funds to attempt to improve the net interest margin. As mentioned earlier, our loan portfolio has decreased and as a result the interest income generated by these higher earning assets has been redeployed into investment securities, a lower yielding asset. The overall effect is a decrease in the interest income of the Bank.

Although our cost of funds has decreased due to deposits repricing at lower interest rates, the rate of this decrease in interest costs is not consistent with the rate of decrease in interest income; consequently, this is causing net interest income to decrease overall During the fourth quarter of 2013, we changed an interest bearing demand deposit product totaling $40.5 million to become a non-interest bearing demand deposit. This modification will result in a lower average balance in the future for interest bearing demand deposits and related interest expense, however, we expect this change to have little or no effect on total deposits as a whole. The following table shows the rates paid on earning assets and deposit liabilities for the periods indicated.

Net Interest Margin Analysis

Average Balances, Income and Expense, and Yields and Rates

(Dollars in thousands)

	For the Year Ended December 31, 2013			For the Year Ended December 31, 2012			For the Year Ended December 31, 2011		
	Average Balance	Income/ Expense	Yields/ Rates	Average Balance	Income/ Expense	Yields/ Rates	Average Balance	Income/ Expense	Yields/ Rates
ASSETS									
Loans (1), (2), (3)	$ 506,697	$ 28,824	5.69%	$ 556,504	$ 32,592	5.86%	$ 659,298	$ 41,176	6.25%
Federal funds sold	960	2	0.21%	1,216	3	0.25%	6,202	9	0.15%
Interest bearing deposits	58,515	188	0.32%	58,677	173	0.29%	74,000	184	0.25%
Other investments (3)	62,804	1,062	1.69%	44,307	965	2.18%	10,952	400	3.65%
Total Earning Assets	628,976	30,076	4.78%	660,704	33,733	5.11%	750,452	41,769	5.57%
	(14,905)			(18,475)			(20,805)		

Less: Allowance for loans losses									
Non-earning assets	85,910			92,494			101,972		
Total Assets	$ 699,981			$ 734,723			$ 831,619		
LIABILITIES AND STOCKHOLDERS EQUITY									
Deposits									
Demand Interest bearing	$ 65,227	$ 82	0.13%	$ 61,842	$ 110	0.18%	$ 57,675	$ 155	0.27%
Savings	103,086	205	0.20%	96,764	242	0.25%	103,346	460	0.45%
Time deposits	359,402	3,743	1.04%	406,669	5,018	1.23%	485,072	7,717	1.59%
Other Borrowings	5,968	242	4.05%	15,487	600	3.87%	24,151	838	3.47%
Trust Preferred Securities	16,496	471	2.86%	16,496	490	2.97%	16,496	436	2.64%
Total interest bearing liabilities	550,179	4,743	0.86%	597,258	6,460	1.08%	686,740	9,606	1.40%
Non-interest bearing deposits	105,614			106,780			102,957		
Other liabilities	4,202			3,913			5,338		
Total Liabilities	659,995			707,951			795,035		
Stockholders Equity	39,986			26,772			36,584		
Total Liabilities and Stockholders Equity	$ 699,981			$ 734,723			$ 831,619		
Net Interest Income		$ 25,333			$ 27,273			$ 32,163	
Net Interest Margin			4.03%			4.13%			4.29%
Net Interest Spread			3.92%			4.03%			4.17%

(1) Non-accrual loans have been included in the average balance of loans outstanding.
(2) Loan fees have been included in interest income on loans.
(3) Tax exempt income is not significant and has been treated as fully taxable.

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Net interest income is affected by changes in both average interest rates and average volumes of interest-earning assets and interest-bearing liabilities. The following table sets forth the amounts of the total changes in interest income and expense which can be attributed to rate (change in rate multiplied by old volume) and volume (change in volume multiplied by old rate) for the periods indicated.

Volume and Rate Analysis
(Dollars in thousands)

	2013 Compared to 2012 Increase (Decrease)			2012 Compared to 2011 Increase (Decrease)		
	Volume Effect	Rate Effect	Change in Interest Income/ Expense	Volume Effect	Rate Effect	Change in Interest Income/ Expense
Interest Income:						
Loans	$ (2,917)	$ (851)	$ (3,768)	$ (6,420)	$ (2,164)	$ (8,584)
Federal funds sold	(1)		(1)	(7)	1	(6)
Interest bearing deposits		15	15	(38)	27	(11)
Other investments	403	(306)	97	1,218	(653)	565
Total Earning Assets	(2,515)	(1,142)	(3,657)	(5,247)	(2,789)	(8,036)
Interest Bearing Liabilities:						
Demand	6	(34)	(28)	11	(56)	(45)
Savings	16	(53)	(37)	(29)	(189)	(218)
All other time deposits	(583)	(692)	(1,275)	(1,247)	(1,452)	(2,699)
Other borrowings	(369)	11	(358)	(301)	63	(238)
Trust Preferred Securities		(19)	(19)		54	54
Total Interest Bearing Liabilities	(930)	(787)	(1,717)	(1,566)	(1,580)	(3,146)
Change in Net Interest Income	$ (1,585)	$ (355)	$ (1,940)	$ (3,681)	$ (1,209)	$ (4,890)

Loans

Our primary source of income comes from interest earned on loans. Total loans decreased in 2013 by $29.4 million, or 5.62%, from $522.4 million at year end 2012 primarily by reducing adversely classified loans as the result of charge offs of $6.0 million in 2013, foreclosures and effectively working with our borrowers. We plan to maintain the level of the loan portfolio as we reduce certain risks to various industry sectors that have posed higher risks in recent times and resolve nonperforming loans, while we increase lower risk loan production that offsets the reductions as mentioned. We remain committed to serving our customers and as a result we promote various loan products to meet lending needs in our market area. Our lending personnel continue to receive training to meet the needs of our customers and to develop new business with qualified borrowers that will ensure a stronger portfolio in the future.

Total loans decreased $75.4 million in 2012 from 2011. A schedule of loans by type is set forth immediately below. Approximately 83.01% of the loan portfolio is secured by real estate at the end of 2013.

Loans receivable outstanding are summarized as follows:

	Loan Portfolio				
	December 31,				
(Dollars in thousands)	2013	2012	2011	2010	2009
Commercial, financial and agricultural	$ 57,704	$ 65,888	$ 85,798	$ 109,418	$ 118,844
Real estate construction	22,421	24,327	32,389	52,307	71,854
Real estate mortgage	386,843	402,703	441,107	489,314	504,071
Installment loans to individuals	26,055	29,445	38,522	56,755	68,801
Total	$ 493,023	$ 522,363	$ 597,816	$ 707,794	$ 763,570

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Our loan maturities as of December 31, 2013 are shown in the following table:

	Maturities of Loans			
(Dollars in thousands)	Less than One Year	One to Five Years	After Five Years	Total
Commercial, financial and agricultural	$ 24,845	$ 27,321	$ 5,538	$ 57,704
Real estate construction	5,341	9,171	7,909	22,421
Real estate mortgage	75,516	167,437	143,890	386,843
Installment loans to individuals	6,039	17,663	2,353	26,055
Total	$ 111,741	$ 221,592	$ 159,690	$ 493,023
Loans with fixed rates	$ 40,154	$ 103,307	$ 153,066	$ 296,527
Loans with variable rates	71,587	118,285	6,624	196,496
Total	$ 111,741	$ 221,592	$ 159,690	$ 493,023

The above table reflects the earlier of the maturity or re-pricing dates for loans at December 31, 2013. In preparing this table, no assumptions are made with respect to loan prepayments. Loan principal payments are included in the earliest period in which the loan matures or can be re-priced. Principal payments on installment loans scheduled prior to maturity are included in the period of maturity or re-pricing.

Provision for Loan Losses

The calculation of the allowance for loan losses is considered a critical accounting policy. The adequacy of the allowance for loan losses is based upon management s judgment and analysis. The following factors are included in our evaluation of determining the adequacy of the allowance: risk characteristics of the loan portfolio, current and historical loss experience, concentrations and internal and external factors such as general economic conditions.

The allowance for loan losses decreased to $13.1 million at December 31, 2013 as compared to $16.8 million at December 31, 2012. The allowance for loan losses at the end of 2013 was approximately 2.65% of total loans as compared to 3.22% at the end of 2012. Net loans charged off decreased in 2013 as they were $4.3 million, or 0.84% of average loans, compared to $6.4 million, or 1.14% of average loans, in 2012. The provision for loan losses also decreased to $550 thousand for 2013 as compared with $4.8 million for 2012, a reduction of $4.3 million, or 88.54%.

We have experienced a decrease in loan delinquencies and nonaccrual loans in 2013. Loans delinquent greater than 90 days still accruing interest and loans in non-accrual status present higher risks of default and loan losses. At December 31, 2013, there were 129 loans in non-accrual status totaling $28.3 million, or 5.74% of total loans. At December 31, 2012, there were 112 loans in non-accrual status totaling $33.5 million, or 6.42% of total loans. The amounts of interest that would have been recognized on these loans were $969 thousand and $1.4 million in the years 2013 and 2012, respectively. There were 5 loans past due 90 days or greater and still accruing interest totaling $1 thousand at December 31, 2013, which consisted entirely of overdrawn demand deposit accounts, down from 15 loans past due 90 days or greater and still accruing interest totaling $551 thousand at year end 2012, which consisted entirely of past due loan accounts. There were $12.3 million in loans classified as troubled debt restructurings as of

December 31, 2013, also an improvement, as compared to $20.0 million in loans classified as troubled debt restructurings as of December 31, 2012. Of the loans classified as troubled debt restructurings at December 31, 2013, $6.8 million were in non-accrual status, compared to $5.4 million at December 31, 2012. We do not have any commitments to lend additional funds to non-performing debtors.

Certain risks exist in the Bank s loan portfolio. A majority of our loans are collateralized by real estate located in our market area. It is our policy to sufficiently collateralize loans to help minimize loss exposures in case of default. With the exception of real estate development type properties which have experienced more deterioration in market values, the local residential and commercial real estate market values have shown some deterioration but remain relatively stable. It is uncertain as to when or if local real estate values will be more significantly impacted. We do not believe that there will be a severely negative effect in our market area, but because of the uncertainty we deem it prudent to assign more of the allowance to these types of loans. Our market area is somewhat diverse, but certain areas are more reliant upon agriculture, coal mining and natural gas. As a result, increased risk of loan impairments is possible as the coal mining and natural gas industry have been negatively affected in the past couple of years due to layoffs and environmental legislation. We do not foresee a major impact upon the Bank unless an additional severe downturn occurs which we believe is not highly likely. We are monitoring these industries. We consider these factors to be the primary higher risk characteristics of the loan portfolio.

Commercial loans are initially risk rated by the originating loan officer. If deteriorations in the financial condition of the borrower and the capacity to repay the debt occur, along with other factors, the loan may be downgraded. This is to be determined by the loan officer. Guidance for the evaluation is established by the regulatory authorities who periodically review the Bank s loan portfolio for compliance. Classifications used by the Bank are exceptional, very good, standard, acceptable, transitory risk, other assets especially mentioned, substandard, doubtful and loss. For the year 2013, we engaged a third party loan review firm to conduct semiannual loan reviews and have engaged them to perform this function in 2014 on a semiannual basis. Our most recent loan review was conducted in December 2013. Upon their review, loans risk ratings may change from the rating assigned by the respective lender. We have experienced fewer rating changes in more recent reviews indicating better risk identification for the loan portfolio in light of the experience from the severe recession.

In regards to our consumer loans and consumer real estate loan portfolio, the Company uses the guidance found in the Uniform Retail Credit Classification and Account Management Policy and as a result affects our estimate of the allowance for loan losses. Under this approach when a consumer loan or consumer real estate loan is originated, it must possess qualities of a credit risk grade of Pass for approval and will remain with the initial risk rating through maturity unless there is a deterioration in the credit quality of the loan. Subsequently, if the loan becomes contractually 90 days past due or the borrower files for bankruptcy protection, it is downgraded to Substandard and placed in nonaccrual status. If the loan is unsecured, upon being deemed Substandard, the entire loan amount is charged off.

At 90 days past due, or earlier if the customer has filed bankruptcy, for non 1-4 family residential secured loans, the collateral value less estimated liquidation costs is compared to the loan balance to calculate any potential deficiency. If there is sufficient collateral, no charge-off is necessary. If there is a deficiency, then prior to the loan becoming contractually 120 days past due, the deficiency is charged-off against the allowance for loan loss. In the case of 1-4 family residential or home equity loans, upon the loan becoming 120 days past due, a current value is obtained and after application of an estimated liquidation discount, a comparison is made to the loan balance to calculate any deficiency. Subsequently, any noted deficiency is then charged-off against the allowance for loan loss when the loan becomes contractually 180 days past due. If the customer has filed bankruptcy, then within 60 days of the bankruptcy notice, any calculated deficiency is charged-off against the allowance for loan loss. Collection efforts continue by means of repossessions or foreclosures, and upon bank ownership, liquidation ensues.

All loans classified as substandard, doubtful and loss are individually reviewed for impairment. In determining impairment, collateral for loans classified as substandard, doubtful and loss is reviewed to determine if the collateral is sufficient for each of these credits, generally through the review of the appraisal. If the appraisal is current, less than twelve months old, and has been reviewed, then if no negative information regarding the appraised value is obtained, the value is accepted, and impairment, if required is made. If the appraisal is not current, we perform a useful life review of the appraisal to determine if it is reasonable. If this review determines that the appraisal is not reasonable, then a new appraisal is ordered, in most cases. Impaired loans decreased to $41.2 million with $25.2 million requiring a valuation allowance of $4.2 million at December 31, 2013 as compared to $65.2 million with $28.1 million requiring a valuation allowance of $5.9 million at December 31, 2012. Of the $41.2 million recorded as impaired loans, $23.7 million were nonperforming loans, which includes nonaccrual loans and past due 90 days or more. Management is aggressively working to reduce the impaired credits at minimal loss.

In determining the component of our allowance in accordance with the Contingencies topic of the Accounting Standards Codification (ASC 450), we do not directly consider the potential for outdated appraisals since that portion of our allowance is based on the analysis of the performance of loans with similar characteristics, external and internal risk factors. We consider the overall quality of our underwriting process in our internal risk factors, but the need to update appraisals is associated with loans identified as impaired under the Receivables topic of the Accounting Standards Codification (ASC 310). If an appraisal is older than one year, a new external certified appraisal may be obtained and used to determine impairment. If an exposure exists, a specific allowance is directly made for the amount of the potential loss in addition to estimated liquidation and disposal costs. The evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available.

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Following is a summary of non-accrual, past due loans greater than 90 days still accruing interest, and restructured loans:

Non-Accrual, Past Due, and Restructured Loans

(Dollars in thousands)

			December 31,		
	2013	2012	2011	2010	2009
Non-accruing loans					
Commercial, financial and agricultural	$ 6,307	$ 10,962	$ 10,633	$ 5,970	$ 1,027
Real estate construction	775	2,412	5,583	15,460	13,727
Real estate mortgage	21,121	20,153	26,099	22,986	9,670
Installment loans to individuals	104	9	1	1,365	289
Total Non-accruing loans	28,307	33,536	42,316	45,781	24,713
Loans past due 90 days or more and still accruing	1	551	1,504	1,693	3,875
Troubled debt restructurings (accruing)	5,563	14,567	20,959	5,647	
Total	$ 33,871	$ 48,654	$ 64,779	$ 53,121	$ 28,588
Percent of total loans	6.87%	9.31%	10.84%	7.51%	3.74%

The above table includes $6.8 million and $5.4 million in nonaccrual loans as of December 31, 2013 and 2012, respectively, that have been classified as troubled debt restructurings. No troubled debt restructurings were past due 90 days or more and still accruing as of December 31, 2013 and 2012. There were $12.3 million in loans classified as troubled debt restructurings as of December 31, 2013, as compared to $20.0 million in loans classified as troubled debt restructurings as of December 31, 2012.

In addition to impaired loans, the remaining loan portfolio is evaluated based on past due history, economic conditions, and internal processes. For past due history, we use an average of our past 12 quarters historical net charge off history in the years 2013, 2012 and a portion of 2011. Prior to this methodology, in earlier periods we based the loss factor on the greater of Virginia peers or our own historical loss rates since previously we did not have historical losses in some categories of loans. Loss trends have now developed and provide better support than previous data. Economic data currently used includes national and local regional unemployment information, local housing price changes, gross domestic product growth, and interest rates are external factors. Lastly, we also evaluate our internal processes of underwriting and consider the inherent risks present in the portfolio due to past and present lending practices. In the past, these factors were not directly allocated to a particular loan category and were considered unallocated in the breakdown data in the table below. During 2011, however, we further analyzed our loan portfolio and the various unallocated internal and external factors. From our analysis, we determined that certain unallocated factors were relevant to certain sectors of the loan portfolio and allocated accordingly. As economic conditions, performance of our loans and internal processes change, it is possible that future increases or possible decreases may be needed to the allowance for loan losses. The following table provides a summary of the activity in the allowance for loan losses.

Analysis of the Allowance for Loan Losses

(Dollars in thousands)

	For the Years Ended December 31,				
Activity	2013	2012	2011	2010	2009
Beginning Balance	$ 16,810	$ 18,380	$ 25,014	$ 18,588	$ 6,904
Provision charged to expense	550	4,800	7,959	22,328	12,841
Advances made on loans with off balance sheet provision			153		
Loan Losses:					
Commercial, financial and agricultural	(1,625)	(1,523)	(4,022)	(1,911)	(129)
Real estate - construction	(312)	(357)	(7,245)	(10,002)	(446)
Real estate - mortgage	(3,954)	(4,535)	(5,446)	(3,867)	(367)
Installment loans to individuals	(153)	(336)	(694)	(728)	(334)
Total loan losses	(6,044)	(6,751)	(17,407)	(16,508)	(1,276)
Recoveries:					
Commercial, financial and agricultural	169	97	224	530	37
Real estate construction	452	73	1,296		8
Real estate - mortgage	1,015	148	1,018	6	21
Installment loans to individuals	128	63	123	70	53
Total recoveries	1,764	381	2,661	606	119
Net charge offs	(4,280)	(6,370)	(14,746)	(15,902)	(1,157)
Balance at End of Period	$ 13,080	$ 16,810	$ 18,380	$ 25,014	$ 18,588
Net charge offs as a % of average loans	0.84%	1.14%	2.24%	2.14%	0.15%

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We have allocated the allowance according to the amount deemed to be reasonably necessary to provide for the possibility of losses being incurred within each of the categories of loans. The allocation of the allowance as shown in the following table should not be interpreted as an indication that loan losses in future years will occur in the same proportions or that the allocation indicates future loan loss trends. Furthermore, the portion allocated to each loan category is not the total amount available for future losses that might occur within such categories since the total allowance is a general allowance applicable to the entire portfolio.

The allocation of the allowance for loan losses is based on our judgment of the relative risk associated with each type of loan. We have allocated 66% of the allowance to real estate loans, which constituted 78.46% of our loan portfolio at December 31, 2013. Real estate mortgages consist of both residential and commercial real estate loans. Mortgage loans are secured by real estate whose value tends to be easily ascertainable. These loans are made consistent with appraisal policies and real estate lending policies, which detail maximum loan-to-value ratios and maturities.

We have allocated 9% of the allowance to real estate construction loans, which constituted 4.55% of our loan portfolio at December 31, 2013. Construction loans are secured by real estate with values that are dependent upon market and economic conditions. Values may not always be easily ascertainable as evidenced by the current market conditions. These loans are made consistent with appraisal policies and real estate lending policies which detail maximum loan-to-value ratios and maturities. Our allocation decreased as a percentage of the allowance for loan losses due to the $1.9 million decrease in construction real estate loans during 2013.

We have allocated 21% of the allowance to commercial loans, which constituted 11.70% of our loan portfolio at December 31, 2013. This allocation remained comparable to the 20% in 2012 despite the fact commercial loans decreased $8.2 million from 2012 to 2013 due to the $1.6 million in charge offs during 2013 that impacts our historical loss rate.

We have allocated 1% of the allowance to consumer installment loans, which constituted 5.29% of our loan portfolio at December 31, 2013. The reason for the decrease in the allocation was the result of the $3.3 million decrease in these loans during 2013.

The following table shows the balance and percentage of our allowance for loan losses (or ALLL) allocated to each major category of loans.

Allocation of the Allowance for Loan Losses

December 31, 2009 through December 31, 2013

(Dollars in thousands)

	December 31, 2013			December 31, 2012			December 31, 2011		
	Amount	% of ALLL	% of Loans	Amount	% of ALLL	% of Loans	Amount	% of ALLL	% of Loans
Commercial	$ 2,710	21%	11.70%	$ 3,383	20%	12.61%	$ 3,322	18%	14.35%
R/E const.	1,184	9%	4.55%	2,166	13%	4.66%	3,848	21%	5.42%
R/E-mortg.	8,652	66%	78.46%	10,322	62%	77.09%	9,578	52%	73.79%
Installment	153	1%	5.29%	388	2%	5.64%	781	4%	6.44%
Unallocated	381	3%		551	3%		851	5%	

Total	$ 13,080	100%	100.00%	$ 16,810	100%	100.00%	$ 18,380	100%	100.00%

	December 31, 2010			December 31, 2009		
	Amount	% of ALLL	% of Loans	Amount	% of ALLL	% of Loans
Commercial	$ 5,323	21%	15.48%	$ 1,710	9%	15.56%
R/E- const.	4,913	20%	7.39%	8,036	43%	9.41%
R/E mortg.	6,882	27%	69.13%	3,525	19%	66.02%
Installment	1,733	7%	8.00%	1,501	8%	9.01%
Unallocated	6,163	25%		3,816	21%	
Total	$ 25,014	100%	100.00%	18,588	100%	100.00%

Other Real Estate Owned

Other real estate owned increased $2.0 million, or 14.31%, to $15.9 million at December 31, 2013 from $13.9 million at December 31, 2012. We anticipate total other real estate owned to increase in the near future as we foreclose on real estate collateralized loans. All properties are being marketed for sale by commercial and residential realtors under the direction of our Special Assets division. During 2013, we were able to sell $5.1 million of our properties as compared to sales of $8.1 million in 2012. As a result we incurred net losses on the sales of these properties in the amounts of $570 thousand and $480 thousand for the years 2013 and 2012, respectively. During 2013 we had to record net writedowns on other real estate owned properties in the amount of $562 thousand compared to $2.6

million in 2012. This was due to the receipt of updated valuations on the other real estate owned properties, which showed a lower fair value than our carrying amount of the properties, and accordingly we recorded a writedown on the properties. In some instances, real estate values increased from prior period writedowns and are netted against current year devaluations in other properties. Future sales of these properties are contingent upon an economic recovery; consequently, it is difficult to estimate the duration of our ownership of these assets. We have designated employees to monitor other real estate owned properties to ensure proper fair market values of these assets and to ensure that maintenance and improvements are made to make these properties more marketable.

Investment Securities

Total investment securities increased to $79.1 million at December 31, 2013 from $49.6 million at December 31, 2012 as we have intentionally increased the investment portfolio of the Bank. All securities are classified as available-for-sale for liquidity purposes. Investment securities with a carrying value of $17.0 million and $18.4 million at December 31, 2013 and 2012, were pledged to secure public deposits, overnight payment processing and for other purposes required by law.

As we curtail loans, we continue to build an investment portfolio. We anticipate slightly increasing the size of the portfolio during 2014. The portfolio will be comprised of short to mid-term investments. The carrying values of investment securities and the different types of investments are shown in the following table:

Investment Securities Portfolio

(Dollars in thousands)

December 31,	2013		2012	
	Amortized	Fair	Amortized	Fair
Available for Sale	Cost	Value	Cost	Value
U.S. Government Agencies	$ 39,296	$ 38,601	$ 23,177	$ 23,637
Mortgage backed securities	41,284	40,525	25,822	25,978
Total Securities AFS	$ 80,580	$ 79,126	$ 48,999	$ 49,615

At December 31, 2013, we had an unrealized loss in our investment portfolio totaling $1.5 million as compared to a $616 thousand unrealized gain at December 31, 2012. The $2.1 million decrease in fair value is due to increased long term interest rates during 2013. We believe this may be a continued trend when interest rates increase; therefore, our strategy is to reduce the overall portfolio interest rate risk as interest rates may rise in the future. We foresee purchasing additional securities in the near future as opportunities arise, and selling securities when it improves the portfolio strategies in a rising interest rate environment that may occur in the future. We have, however, reviewed our investment portfolio and no investment security is deemed to have a permanent impairment. We monitor our portfolio regularly and are actively managing it to maintain liquidity, reduce interest rate risk and enhance earnings.

The amortized cost, fair value and weighted average yield of investment securities at December 31, 2013 are shown by contractual maturity and do not reflect principal paydowns for amortizing securities, in the following schedule. Expected maturities will differ from contractual maturities because issuers may have the right to call or prepay obligations with or without call or prepayment penalties.

Maturities of Securities

(Dollars are in thousands) Securities Available for Sale	Amortized Cost	Fair Value	Weighted Average Yield
Due in one year or less	$	$	%
Due after one year through five years	2,660	2,651	1.02%
Due after five years through fifteen years	26,552	26,213	1.69%
Due after fifteen years	51,368	50,262	1.97%
Total	$ 80,580	$ 79,126	1.84%

Deposits

Total deposits were $619.0 million at December 31, 2013, a decrease of $33.9 million, or 5.19%, from $652.9 million at December 31, 2012. This decrease is attributed to our plan to decrease higher cost deposits in order to improve earnings and increase capital ratios. Most of the decrease has been in time deposits which are our highest cost deposit funding source. During 2013, we experienced a decrease in time deposits of $25.5 million. This is the result of decreased interest rates offered in this very low interest rate environment. During 2013, interest rate sensitive deposits have withdrawn to seek other investment opportunities.

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Demand deposits remained substantially at the same level as they slightly increased 0.47%, or $786 thousand, from $167.1 million at December 31, 2012 to $167.9 million at December 31, 2013. We continue to maintain demand deposits through attractive consumer and commercial deposit products and strong ties with our customer base and communities. Savings deposits decreased $9.2 million, or 8.08%, to $104.1 million at December 31, 2013 as compared to $113.3 million at December 31, 2012.

We are working to increase demand and savings deposits as we further optimize our branch network and develop our customer relationships. We believe there are opportunities for this segment of deposit growth.

We also expect to continue to lose higher cost deposits in the near future, but at a decreased pace than in the past. However, we monitor deposits to ensure that we maintain adequate liquidity levels. We believe despite the deposit decrease, we have adequate liquidity.

Time deposits of $100,000 or more equaled approximately 21.08% of deposits at the end of 2013 and 21.37% of deposits at the end of 2012.

We have brokered deposits totaling $2.7 million with a term of 10 years. These deposits were used to fund a particular 10 year balloon mortgage product. Internet accounts are limited to customers located in the surrounding geographical area. The average balance of and the average rate paid on deposits is shown in the net interest margin analysis above. Total CDARs time deposits increased to $7.6 million in 2013 as compared to $7.2 million in 2012.

Maturities of time deposits of $100,000 or more outstanding are summarized as follows:

Maturities of Time Deposits of $100 Thousand and More

(Dollars in thousands)

December 31, 2013

Three months or less	$ 25,808
Over three months through six months	23,240
Over six months through twelve months	28,077
Over one year	53,342
Total	$ 130,467

Noninterest Income

Noninterest income was $5.5 million in 2013 which was comparable to the $5.6 million in 2012. During 2013 we had $99 thousand in realized gains on the sale of investment securities as compared to $537 thousand in 2012. The ratio of noninterest income as a percentage of average assets increased to 0.79% in 2013 as compared to 0.76% in 2012. We anticipate this percentage to slightly increase during 2014 as we continue to seek opportunities to improve noninterest income. As a part of these efforts, NPB Insurance Services, Inc., the Bank s subsidiary, a full service insurance agency, began operations in the first quarter of 2013, dealing in personal and group life, property and casualty, health, and disability products.

Noninterest Expense

Noninterest expenses decreased $3.1 million, or 9.65%, to $28.9 million in 2013 from $32.0 million in 2012. The following are explanations of the decrease in non-interest expenses during 2013.

Salaries and employee benefits decreased from $13.9 million in 2012 to $13.4 million in 2013. This was a decrease of $517 thousand, or 3.71%. Total full time equivalent employees have decreased to 264 at December 31, 2013 from 286 at December 31, 2012, a reduction of 22, or 7.69%.

Other real estate owned and repossessed asset expenses decreased $2.2 million, or 48.63%, to $2.3 million in 2013 from $4.5 million in 2012. This decrease is related to a decrease in writedowns on other real estate owned during 2013 of $2.1 million, or 78.55%. We re-assessed the values of the properties in other real estate owned in 2013 and wrote down these assets by $562 thousand to reflect fair market value changes in the properties since the original date that the assets were acquired in 2013 or the prior year balance for properties that continue to be held. During 2012 we wrote down these assets by $2.6 million. In the year 2013, we had a net loss on the sale of other real estate owned property of $570 thousand compared to a net loss of $480 thousand in 2012.

In 2013, FDIC assessment expense decreased $145 thousand, or 8.74%, from $1.7 million in 2012 to $1.5 million in 2013. This is the result of the reduction of total deposits during 2013.

The ratio of noninterest expense as a percentage of average assets decreased in 2013 to 4.13% as compared to 4.35% in 2012. We expect greater efficiencies to result as we maximize the performance of our branches and as the economy improves.

Our efficiency ratio, which is defined as noninterest expense divided by the sum of net interest income plus noninterest income, was 93.64% in 2013 as compared to 97.32% for 2012. Included in this calculation are the other real estate owned write-downs and related expenses which significantly and negatively impact the ratio. During the third quarter of 2013, we engaged an outside consultant to evaluate our operational efficiencies. Based on the recommendations we plan to implement, we anticipate the efficiency ratio to improve in the future as we realize cost savings from operational improvements.

Life Insurance

We have life insurance policies on the life of one key officer and three former key officers. The Bank is the beneficiary under each policy. In addition, we own a policy in which the Bank is the beneficiary which was collateral for a defaulted loan. The aggregate total cash surrender value of the policies was $12.1 million and $12.0 million at December 31, 2013 and December 31, 2012, respectively. Total income for the policies during 2013 was $89 thousand as compared to $309 thousand for the year ending 2012. The policies owned on current and former officers are separate account life insurance policies and the income is based on a short term investment portfolio managed by the insurance provider which should increase in earnings when and if interest rates increase in the future. The other policy is a general account policy with a minimum earning rate.

Deferred Tax Asset and Income Taxes

Due to timing differences between book and tax treatment of several income and expense items, a deferred tax asset of $5.4 million existed at December 31, 2013 as compared to a deferred tax asset of $4.7 million at December 31, 2012. During 2013 we reversed $428 thousand of our deferred tax valuation allowance as compared to a $4.1 million deferred tax asset valuation allowance recorded in 2012, which decreased the total valuation allowance to $6.4 million at December 31, 2013, compared to $6.8 million at December 31, 2012. Management reviewed the deferred tax calculation to determine the need for a valuation allowance. Based on the trend of reduced levels of earning assets and net interest income, we modified the projections of taxable income over the next three years and determined that no additional deferred tax asset valuation allowance was required during 2013. A valuation allowance is provided when it is more likely than not that some portion of the deferred tax asset will not be realized. In management s opinion, based on a three year taxable income projection, tax strategies which would result in potential securities gains and the effects of off-setting deferred tax liabilities, it is more likely than not that all the deferred tax assets, net of the $6.4 million allowance, would be realizable. As of December 31, 2013, the Company had $16.1 million of net operating loss carryforwards which will expire in 2031 thru 2033. Management expects to utilize all of these carryforwards prior to expiration. Direct charge-offs contributed to a reduction of the tax asset and are permitted as tax deductions. In addition, writedowns on other real estate owned property are expensed for book purposes but are not deductible for tax purposes until disposition of the property. Goodwill expense also was realized for book purposes in 2011 but continues to only be tax deductible based on the statutory requirements; thus, creating a deferred tax asset. When, and if, taxable income increases in the future and during the net operating loss carryforward period, this valuation allowance may be reversed and used to decrease tax obligations in the future. Our income tax expense was computed at the normal corporate income tax rate of 34% of taxable income included in net income. We do not have significant nontaxable income or nondeductible expenses.

The Company s tax filings for years ended 2010 through 2013 are currently open to audit under statutes of limitations by the Internal Revenue Service (IRS) and the Virginia Department of Taxation. Our tax filings for the years ended

2010, 2011, and 2012 are currently under examination by the IRS. The results of the examination could impact the amount of our deferred tax asset, but we do not anticipate a material change if any change at all.

After the common stock offering was concluded in December 2012, the Company evaluated whether a change of control as defined in Internal Revenue Code (IRC) section 382 had occurred. A change of control for purposes of IRC section 382 would have occurred if 50% or more of the ownership of the Company had changed as a result of the offering and stock transactions occurring in the preceding 3 years. In that case IRC section 382 would impose certain limitations which would restrict the ability of the Company to utilize the current amount of tax loss carryforwards among other future tax deductions. We concluded that a change of control did not occur under the IRC section 382. We must, however, continue to monitor any increase in the ownership of any 5% owner in the Company, of any new investors participating in the common stock offering that were not investors before the offering, and of any new 5% owner acquiring common stock from existing shareholders excluding the two aforementioned groups. If the combined additional ownership of these three groups ever causes their total ownership to exceed 50% in the next three years, the limitations of Internal Revenue Code 382 would apply. The Company is considering implementing a tax preservation plan in the near future to protect the ability to realize the future tax loss carryforwards that would help protect current investors from any such change of control under IRC section 382, if one should occur.

Capital Resources

Our total capital at the end of 2013 was $40.0 million compared to $39.9 million in 2012. The increase was $94 thousand, or 0.24%. The Bank and the Company were both well capitalized as of December 31, 2013, as defined by the regulatory capital guidelines. New Peoples equity as a percentage of total assets was 5.84% at December 31, 2013 compared to 5.54% at December 31, 2012. The annualized return on average assets for the fiscal year 2013 was 0.21% as compared to (0.86)% for the same period in 2012. The annualized return on average equity was 3.71% for the fiscal year 2013 and (23.62)% for the same period in 2012. The book value per common share was $1.83 at December 31, 2013 compared to $1.82 at December 31, 2012.

Total assets decreased in 2013 and we anticipate assets to remain relatively the same in 2014. Our primary source of capital comes from retained earnings. We developed a new strategic plan and capital plan in 2013. Under current economic conditions, we believe it is prudent to continue to increase capital to absorb potential losses that may occur if asset quality deteriorates further. We are aware that capital needs and requirements are affected by the level of problem assets, growth, earnings and other factors. Based upon projections, we believe retained earnings will be sufficient to provide for this economic cycle to increase capital levels. As part of our initiative to improve regulatory capital ratios, we are further reducing our nonperforming assets, and focusing on replacing this reduction with high quality loans resulting in a slight increase in the loan portfolio. Deposit growth is primarily focused on growing core deposits, which are mainly transaction accounts, commercial relationships and savings products. We are focused on improving earnings by maintaining a strong net interest margin and decreasing overhead expenses. We are fully implementing this strategy to increase capital. However, these efforts alone may not provide us adequate capital if further loan losses are realized.

No cash dividends have been paid historically and none are anticipated in the foreseeable future. Earnings will continue to be retained to build capital.

Liquidity

We closely monitor our liquidity and our liquid assets in the form of cash, due from banks, federal funds sold, and unpledged available for sale investments were $116.8 million at December 31, 2013, down from $125.3 million at December 31, 2012. We plan to maintain surplus short-term assets at levels adequate to meet potential liquidity needs during 2014.

At December 31, 2013, all of our investments are classified as available-for-sale, providing an additional source of liquidity in the amount of $62.1 million, which is net of those securities pledged as collateral. This will primarily serve as a source of liquidity while yielding a higher return than other short term investment options, such as federal funds sold and overnight deposits with the Federal Reserve Bank. We have increased our investment portfolio from $49.6 million at December 31, 2012 to $79.1 million at December 31, 2013. Our strategy is to manage the portfolio with future purchases that reduce price risk in a rising interest rate environment and shorten the duration of these securities to be able to invest in higher yielding loans and investments when interest rates do rise again. This decrease in fair market value resulting in a net unrealized loss of $1.5 million, a $2.1 million decrease from the net unrealized gain at December 31, 2012, which was $616 thousand, could negatively impact earnings if the investment portfolio had to be quickly liquidated.

Our loan to deposit ratio was 79.65% at December 31, 2013 and 80.01% at year end 2012. We anticipate this ratio to remain below 80% in the future. We can further lower the ratio as management deems appropriate by managing the rate of growth in our loan portfolio and by offering special promotions to entice new deposits. This can be done by changing interest rates charged or limiting the amount of new loans approved.

Available third party sources of liquidity remain intact at December 31, 2013 which includes the following: our line of credit with the Federal Home Loan Bank of Atlanta, the brokered certificates of deposit markets, internet certificates of deposit, and the discount window at the Federal Reserve Bank of Richmond.

At December 31, 2013, we had borrowings from the Federal Home Loan Bank totaling $5.4 million as compared to $6.6 million at December 31, 2012. None are overnight and subject to daily interest rate changes. The borrowings have a maturity date in the year 2018, but reduce in principal amounts monthly. The decrease of $1.2 million was due to regularly scheduled principal payments. We also used our line of credit with the Federal Home Loan Bank to issue a letter of credit for $3.0 million in 2010 and $7.0 million in 2013 to the Treasury Board of Virginia for collateral on public funds. An additional $72.7 million was available on December 31, 2013 on the $88.0 million line of credit, which is secured by a blanket lien on our residential real estate loans.

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We have access to the brokered deposits market. Currently we have $2.7 million in 10 year term time deposits comprised of $3 thousand incremental deposits which yield an interest rate of 4.10%. With the exception of CDARS time deposits, we have no other brokered deposits. Though this has not been a strategy in the past, we may utilize this source in the future as a lower cost source of funds.

We are a member of an internet certificate of deposit network whereby we may obtain funds from other financial institutions at auction. We may invest funds through this network as well. Currently, we only intend to use this source of liquidity in a liquidity crisis event.

The Bank has access to additional liquidity through the Federal Reserve Bank discount window for overnight funding needs. We may collateralize this line with investment securities and loans at our discretion; however, we do not anticipate using this funding source except as a last resort.

Additional liquidity is expected to be provided by loan repayments and core deposit growth that will result from an increase in market share in our targeted trade area.

With the increased asset liquidity and other external sources of funding, we believe at the Bank level we have adequate liquidity and capital resources to meet our requirements and needs for the foreseeable future. However, liquidity can be further affected by a number of factors such as counterparty willingness or ability to extend credit, regulatory actions and customer preferences, some of which are beyond our control.

Concerning the Company s liquidity, we have $4.4 million in cash as of December 31, 2013. These funds will be used to pay operating expense, trust preferred interest payments (upon regulatory approval), and provide additional capital injections to the Bank, if needed. As of now, all interest payments to the trust preferred securities is deferred. In the event, trust preferred interest payments are no longer deferred, then the Company has the cash to meet this obligation without any reliance on the Bank. The current deferred liability totals $2.0 million and is anticipated to be paid in the first quarter of 2015 subject to regulatory approval.

As a result of the conversion of director notes and the common stock offering, a total of 2,370,900 common stock warrants were issued. The warrants are immediately exercisable over the next five years at a price of $1.75 per share. During 2013, 6,758 warrants were exercised, which reduced the number of warrants outstanding at December 31, 2013 to 2,364,142. When, and if, these warrants are exercised, additional funds may be received by the Company, which provides potentially up to $4.1 million in additional liquidity and capital at the Company level. Additional contingent funding sources will be explored as available.

Financial Instruments with Off-Balance-Sheet Risk

The Bank is a party to financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit and standby letters of credit. Those instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the balance sheet. The contract or notional amounts of those instruments reflect the extent of involvement the Bank has in particular classes of financial instruments.

The Bank s exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit and standby letters of credit is represented by the contractual amount of those instruments. The Bank uses the same credit policies in making commitments and conditional obligations as it does for on-balance-sheet instruments.

A summary of the contract amount of the Bank s exposure to off-balance-sheet risk as of December 31, 2013 and 2012 is as follows:

(Dollars in thousands)	2013	2012
Financial instruments whose contract amounts represent credit risk:		
Commitments to extend credit	$ 29,039	$ 27,877
Standby letters of credit	2,907	2,721

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Bank evaluates each customer s credit worthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Bank upon extension of credit, is based on management s credit evaluation of the counterparty. Collateral held varies but may include accounts receivable, inventory, property and equipment, and income-producing commercial properties.

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Unfunded commitments under lines of credit are commitments for possible future extensions of credit to existing customers. Those lines of credit may not actually be drawn upon to the total extent to which the Bank is committed.

Standby letters of credit are conditional commitments issued by the Bank to guarantee the performance of a customer to a third party. Those guarantees are primarily issued to support public and private borrowing arrangements, including commercial paper, bond financing, and similar transactions. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. The Bank holds certificates of deposit, deposit accounts, and real estate as collateral supporting those commitments for which collateral is deemed necessary.

Interest Sensitivity

At December 31, 2013 we had a negative cumulative gap rate sensitivity ratio of 31.88% for the one year re-pricing period, compared to 31.67% at December 31, 2012. A negative cumulative gap generally indicates that net interest income would improve in a declining interest rate environment as liabilities re-price more quickly than assets. Conversely, net interest income would probably decrease in periods during which interest rates are increasing. We are closely monitoring our position and implementing adjustments periodically to strategically position ourselves to enhance earnings in current and anticipated interest rate environments. This table based on contractual maturities and does not take into consideration prepayment speeds of investment securities and loans nor does it factor decay rates for non maturity deposits. Based on these behavioral factors, we are in a position to increase interest income in a rising interest rate environment. Management reviews our interest rate risk profile quarterly and believes that the current position is an acceptable risk.

Interest Sensitivity Analysis

December 31, 2013

(Dollars in thousands)

	1- 90 Days	91-365 Days	1-3 Years	4-5 Years	6-15 Years	Over 15 Years	Total
Uses of funds:							
Loans	$ 48,755	$ 62,764	$ 122,483	$ 99,330	$ 114,146	$ 45,545	$ 493,023
Federal funds sold	2						2
Deposits with banks	35,908						35,908
Investments	13,616	3,082	11,035	4,114	20,303	26,976	79,126
Bank owned life insurance	12,118						12,118
Total earning assets	$ 110,399	65,846	$ 133,518	$ 103,444	$ 134,449	$ 72,521	$ 620,177

Sources of funds:							
Interest Bearing DDA	$ 30,138	$	$	$	$	$	30,138
Savings & MMDA	104,123						104,123
Time Deposits	80,687	142,532	95,723	25,325	2,724		346,991
Trust preferred securities	16,496						16,496
Other borrowings				5,358			5,358
Total interest bearing liabilities	$ 231,444	$ 142,532	$ 95,723	$ 30,683	$ 2,724	$	$ 503,106
Discrete Gap	$ (121,045)	$ (76,686)	$ 37,795	$ 72,761	$ 131,725	$ 72,521	$ 117,071
Cumulative Gap	$ (121,045)	$ (197,731)	$ (159,936)	$ (87,175)	$ 44,550	$ 117,071	
Cumulative Gap as % of Total Earning Assets	(19.52%)	(31.88%)	(25.79%)	(14.06%)	7.18%	18.88%	

Item 7A. Quantitative and Qualitative Disclosures About Market Risk

Not applicable.

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Item 8. Financial Statements and Supplementary Data

FINANCIAL STATEMENTS

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Report of Independent Registered Public Accounting Firm

To the Board of Directors and Stockholders

New Peoples Bankshares, Inc.

Honaker, Virginia

We have audited the accompanying consolidated balance sheets of New Peoples Bankshares, Inc. and subsidiaries (the Company) as of December 31, 2013 and 2012, and the related consolidated statements of income (loss), comprehensive income (loss), stockholders equity, and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Company s management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company s internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of New Peoples Bankshares, Inc. and subsidiaries as of December 31, 2013 and 2012, and the results of their operations and their cash flows for the years then ended, in conformity with U.S. generally accepted accounting principles.

/s/ Elliott Davis, LLC

Richmond, Virginia

March 24, 2014

Elliott Davis LLC | Elliott Davis PLLC | www.elliottdavis.com

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NEW PEOPLES BANKSHARES, INC.

CONSOLIDATED BALANCE SHEETS

DECEMBER 31, 2013 AND 2012

(IN THOUSANDS EXCEPT SHARE DATA)

	2013	2012
ASSETS		
Cash and due from banks	$ 18,770	$ 17,517
Interest-bearing deposits with banks	35,908	76,590
Federal funds sold	2	2
Total Cash and Cash Equivalents	54,680	94,109
Investment securities available-for-sale	79,126	49,615
Loans receivable	493,023	522,363
Allowance for loan losses	(13,080)	(16,810)
Net Loans	479,943	505,553
Bank premises and equipment, net	29,976	31,190
Equity securities (restricted)	2,704	2,803
Other real estate owned	15,853	13,869
Accrued interest receivable	2,286	2,374
Life insurance investments	12,118	11,964
Intangible assets	8	53
Deferred taxes, net	5,446	4,686
Other assets	2,571	2,799
Total Assets	$ 684,711	$ 719,015
LIABILITIES		
Deposits		
Demand deposits		
Noninterest bearing	$ 137,745	$ 98,432
Interest-bearing	30,138	68,665
Savings deposits	104,123	113,280
Time deposits	346,991	372,473
Total Deposits	618,997	652,850
FHLB advances	5,358	6,558
Accrued interest payable	2,287	1,880

Accrued expenses and other liabilities	1,613	1,365
Trust preferred securities	16,496	16,496
Total Liabilities	644,751	679,149
STOCKHOLDERS EQUITY		
Common stock - $2.00 par value; 50,000,000 shares authorized; 21,872,293 and 21,865,535 shares issued and outstanding at December 31, 2013 and 2012, respectively	43,745	43,731
Common stock warrants	2,050	2,056
Additional paid-in capital	13,050	13,081
Retained deficit	(17,925)	(19,409)
Accumulated other comprehensive income (loss)	(960)	407
Total Stockholders Equity	39,960	39,866
Total Liabilities and Stockholders Equity	$ 684,711	$ 719,015

The accompanying notes are an integral part of this statement.

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NEW PEOPLES BANKSHARES, INC.

CONSOLIDATED STATEMENTS OF INCOME (LOSS)

FOR THE YEARS ENDED DECEMBER 31, 2013 AND 2012

(IN THOUSANDS EXCEPT SHARE AND PER SHARE DATA)

	2013	2012
INTEREST AND DIVIDEND INCOME		
Loans including fees	$ 28,824	$ 32,592
Federal funds sold	2	3
Interest-earning deposits with banks	188	173
Investments	934	851
Dividends on equity securities (restricted)	128	114
Total Interest and Dividend Income	30,076	33,733
INTEREST EXPENSE		
Deposits		
Demand	82	110
Savings	205	242
Time deposits below $100,000	2,196	2,994
Time deposits above $100,000	1,547	2,024
FHLB advances	242	472
Other borrowings		128
Trust Preferred Securities	471	490
Total Interest Expense	4,743	6,460
NET INTEREST INCOME	25,333	27,273
PROVISION FOR LOAN LOSSES	550	4,800
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	24,783	22,473
NONINTEREST INCOME		
Service charges	2,258	2,482
Fees, commission and other income	2,763	1,949
Insurance and investment fees	322	319
Net realized gains on sale of investment securities	99	537
Life insurance investment income	89	309
Total Noninterest Income	5,531	5,596

NONINTEREST EXPENSES		
Salaries and employee benefits	13,430	13,947
Occupancy and equipment expenses	4,001	4,104
Advertising and public relations	411	472
Data processing and telecommunications	1,956	1,743
FDIC insurance premiums	1,514	1,659
Other real estate owned and repossessed assets, net	2,290	4,458
Other operating expenses	5,299	5,605
Total Noninterest Expenses	28,901	31,988
INCOME (LOSS) BEFORE INCOME TAXES	1,413	(3,919)
INCOME TAX EXPENSE (BENEFIT)	(71)	2,405
NET INCOME (LOSS)	$ 1,484	$ (6,324)
Income (Loss) Per Share		
Basic and Fully Diluted	$ 0.07	$ (0.57)
Average Weighted Shares of Common Stock		
Basic and Fully Diluted	21,870,758	11,181,963

The accompanying notes are an integral part of this statement.

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NEW PEOPLES BANKSHARES, INC.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

FOR THE YEARS ENDED DECEMBER 31, 2013 AND 2012

(IN THOUSANDS)

	2013	2012
NET INCOME (LOSS)	$ 1,484	$ (6,324)
Other comprehensive income (loss):		
Investment securities activity:		
Unrealized gains (losses) arising during the year	(1,971)	777
Tax related to unrealized gains (losses)	670	(264)
Reclassification of realized gains during the year	(99)	(537)
Tax related to realized gains	33	182
TOTAL OTHER COMPREHENSIVE INCOME (LOSS)	(1,367)	158
TOTAL COMPREHENSIVE INCOME (LOSS)	$ 117	$ (6,166)

The accompanying notes are an integral part of this statement.

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NEW PEOPLES BANKSHARES, INC.

CONSOLIDATED STATEMENTS OF STOCKHOLDERS EQUITY

FOR THE YEARS ENDED DECEMBER 31, 2013 AND 2012

(IN THOUSANDS INCLUDING SHARE DATA)

	Shares of Common Stock	Common Stock	Common Stock Warrants	Additional Paid in Capital	Retained Deficit	Accumulated Other Comprehensive Income (Loss)	Total Stockholders Equity
Balance, December 31, 2011	10,010	$ 20,020	$	$ 21,689	$ (13,085)	$ 249	$ 28,873
Net loss					(6,324)		(6,324)
Conversion of Director notes plus accrued interest	3,815	7,629	663	(2,570)			5,722
Common stock and common stock warrants issuance, net of costs of $624	8,041	16,082	1,393	(6,038)			11,437
Other comprehensive income, net of tax						158	158
Balance, December 31, 2012	21,866	43,731	2,056	13,081	(19,409)	407	39,866
Net income					1,484		1,484
Exercise of common stock warrants	6	14	(6)	6			14
Stock offering costs				(37)			(37)
Other comprehensive loss, net of tax						(1,367)	(1,367)
Balance, December 31, 2013	21,872	$ 43,745	$ 2,050	$ 13,050	$ (17,925)	$ (960)	$ 39,960

The accompanying notes are an integral part of this statement.

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NEW PEOPLES BANKSHARES, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

FOR THE YEARS ENDED DECEMBER 31, 2013 AND 2012

(IN THOUSANDS)

	2013	2012
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income (loss)	$ 1,484	$ (6,324)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation	2,338	2,500
Provision of loan losses	550	4,800
Income (less expenses) on life insurance	(154)	(613)
Gain on sale of securities available-for-sale	(99)	(537)
Loss on sale of fixed assets	23	357
Loss on sale of foreclosed real estate	570	480
Adjustment of carrying value of foreclosed real estate	562	2,620
Accretion of bond premiums/discounts	922	572
Deferred tax expense (benefit)	(57)	2,453
Amortization of core deposit intangible	45	70
Net change in:		
Interest receivable	88	693
Other assets	228	1,595
Accrued interest payable	407	356
Accrued expenses and other liabilities	248	(106)
Net Cash Provided by Operating Activities	7,155	8,916
CASH FLOWS FROM INVESTING ACTIVITIES		
Net decrease in loans	16,847	59,108
Purchase of securities available-for-sale	(48,280)	(40,828)
Proceeds from sale and maturities of securities available-for-sale	15,876	23,851
Sale of Federal Home Loan Bank stock	309	770
Purchase of Federal Reserve Bank stock	(210)	
Payments for the purchase of premises and equipment	(1,552)	(1,333)
Proceeds from sale of premises and equipment	405	427
Proceeds from sales of other real estate owned	5,097	8,098
Net Cash Provided by (Used in) Investing Activities	(11,508)	50,093
CASH FLOWS FROM FINANCING ACTIVITIES		
Issuance of common stock and common stock warrants		12,061
Stock offering costs	(37)	(624)

Exercise of common stock warrants	14	
Repayments to Federal Home Loan Bank	(1,200)	(11,425)
Net change in:		
Demand deposits	786	(991)
Savings deposits	(9,157)	18,711
Time deposits	(25,482)	(73,185)
Net Cash Used in Financing Activities	(35,076)	(55,453)
Net increase (decrease) in cash and cash equivalents	(39,429)	3,556
Cash and Cash Equivalents, Beginning of the Year	94,109	90,553
Cash and Cash Equivalents, End of the Year	$ 54,680	$ 94,109
Supplemental Disclosure of Cash Paid During the Year for:		
Interest	$ 4,336	$ 6,544
Taxes	$	$
Supplemental Disclosure of Non Cash Transactions:		
Other real estate acquired in settlement of foreclosed loans	$ 9,001	$ 9,975
Loans made to finance sale of foreclosed real estate	$ 787	$
Conversion of Director notes in other borrowings to common stock	$	$ 5,450
Conversion of accrued interest payable on Director notes to common stock	$	$ 272
Common stock issued as a result of the conversion of Director notes	$	$ 5,722

The accompanying notes are an integral part of this statement.

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NEW PEOPLES BANKSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 NATURE OF OPERATIONS:

Nature of Operations New Peoples Bankshares, Inc. (The Company) is a bank holding company whose principal activity is the ownership and management of a community bank. New Peoples Bank, Inc. (The Bank) was organized and incorporated under the laws of the Commonwealth of Virginia on December 9, 1997. The Bank commenced operations on October 28, 1998, after receiving regulatory approval. As a state chartered member bank, the Bank is subject to regulation by the Virginia Bureau of Financial Institutions, the Federal Deposit Insurance Corporation and the Federal Reserve Bank. The Bank provides general banking services to individuals, small and medium size businesses and the professional community of southwestern Virginia, southern West Virginia, and eastern Tennessee. On June 9, 2003, the Company formed two wholly owned subsidiaries, NPB Financial Services, Inc. and NPB Web Services, Inc. On July 7, 2004 the Company established NPB Capital Trust I for the purpose of issuing trust preferred securities. On September 27, 2006, the Company established NPB Capital Trust 2 for the purpose of issuing additional trust preferred securities. NPB Financial Services, Inc. was a subsidiary of the Company until January 1, 2009 when it became a subsidiary of the Bank. The name of NPB Financial Services, Inc. was changed in June 2012 to NPB Insurance Services, Inc. which operates solely as an insurance agency.

NOTE 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

Consolidation Policy - The consolidated financial statements include the Company, the Bank, NPB Insurance Services, Inc., and NPB Web Services, Inc. (Hereinafter, collectively referred to as The Company.) All significant intercompany balances and transactions have been eliminated. In accordance with ASC 942, NPB Capital Trust I and 2 are not included in the consolidated financial statements.

Use of Estimates - The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. The determination of the adequacy of the allowance for loan losses is based on estimates that are particularly susceptible to significant changes in the economic environment and market conditions.

Cash and Cash Equivalents Cash and cash equivalents as used in the cash flow statements include cash and due from banks, interest-bearing deposits with banks, and federal funds sold.

Investment Securities Management determines the appropriate classification of securities at the time of purchase. If management has the intent and the Company has the ability at the time of purchase to hold securities until maturity, they are classified as held to maturity and carried at amortized historical cost. Securities not intended to be held to maturity are classified as available for sale and carried at fair value. Securities available for sale are intended to be used as part of the Company s asset and liability management strategy and may be sold in response to changes in interest rates, prepayment risk or other similar factors.

The amortization of premiums and accretion of discounts are recognized in interest income using the effective interest method over the period to maturity. Realized gains and losses on dispositions are based on the net proceeds and the adjusted book value of the securities sold, using the specific identification method. Realized gains (losses) on securities available-for-sale are included in noninterest income and, when applicable, are reported as a reclassification adjustment, net of tax, in other comprehensive income. Unrealized gains and losses on investment securities available for sale are based on the difference between book value and fair value of each security. These gains and losses are credited or charged to other comprehensive income, net of tax, whereas realized gains and losses flow through the statement of operations.

Loans Loans are carried on the balance sheet at unpaid principal balance, net of any unearned interest and the allowance for loan losses. Interest income on loans is computed using the effective interest method, except where serious doubt exists as to the collectibility of the loan, in which case accrual of the income is discontinued.

It is the Company s policy to stop accruing interest on a loan, and classify that loan as non-accrual under the following circumstances: (a) whenever we are advised by the borrower that scheduled payment or interest payments cannot be met, (b) when our best judgment indicates that payment in full of principal and interest can no longer be expected, or (c) when any such loan or obligation becomes delinquent for 90 days unless it is both well secured and in the process of collection. All interest accrued but not collected for loans that are place on nonaccrual or charged off is reversed against interest income. The interest on these loans is accounted for on the cash basis or cost-recovery method, until qualifying for return to accrual. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and prospects for future contractual payments are reasonably assured.

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

Significant Group Concentrations of Credit Risk The Company identifies a concentration as any obligation, direct or indirect, of the same or affiliated interests which represent 25% or more of the Company s capital structure, or $10.0 million as of December 31, 2013. Most of the Company s activities are with customers located within the southwest Virginia, southern West Virginia, and northeastern Tennessee region. Certain concentrations may pose credit risk. The Company does not have any significant concentrations to any one industry or customer.

Allowance for Loan Losses The allowance for loan losses is maintained at a level that, in management s judgment, is adequate to absorb credit losses inherent in the loan portfolio. The loan portfolio is analyzed periodically and loans are assigned a risk rating. Allowances for impaired loans are generally determined based on collateral values or the present value of expected cash flows. A general allowance is made for all other loans not considered impaired as deemed appropriate by management. In determining the adequacy of the allowance, management considers the following factors: the nature of the portfolio, credit concentrations, trends in historical loss experience, specific impaired loans, the estimated value of any underlying collateral, prevailing environmental factors and economic conditions, and other inherent risks. While management uses available information to recognize losses on loans, further reductions in the carrying amounts of loans may be necessary based on changes in collateral values and changes in estimates of cash flows on impaired loans. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available.

The allowance is increased by a provision for loan losses, which is charged to expense and reduced by charge-offs, net of recoveries. Loans are charged against the allowance for loan losses when management believes that collectability of all or part of the principal is unlikely. Past due status is determined based on contractual terms.

In regards to its consumer loans and consumer real estate loan portfolio, the Company uses the guidance found in the Uniform Retail Credit Classification and Account Management Policy and as a result affects our estimate of the allowance for loan losses. Under this approach when a consumer loan or consumer real estate loan is originated, it must possess qualities of a credit risk grade of Pass for approval and will remain with the initial risk rating through maturity unless there is a deterioration in the credit quality of the loan. Subsequently, if the loan becomes contractually 90 days past due or the borrower files for bankruptcy protection, it is downgraded to Substandard and placed in nonaccrual status. If the loan is unsecured, upon being deemed Substandard, the entire loan amount is charged off.

At 90 days past due, or earlier if the customer has filed bankruptcy, for non 1-4 family residential secured loans, the collateral value less estimated liquidation costs is compared to the loan balance to calculate any potential deficiency. If there is sufficient collateral, no charge-off is necessary. If there is a deficiency, then prior to the loan becoming contractually 120 days past due, the deficiency is charged-off against the allowance for loan loss. In the case of 1-4 family residential or a home equity loans, upon the loan becoming 120 days past due, a current value is obtained and after application of an estimated liquidation discount, a comparison is made to the loan balance to calculate any deficiency. Subsequently, any noted deficiency is then charged-off against the allowance for loan loss when the loan becomes contractually 180 days past due. If the customer has filed bankruptcy, then within 60 days of the bankruptcy notice, any calculated deficiency is charged-off against the allowance for loan loss. Collection efforts continue by means of repossessions or foreclosures, and upon bank ownership, liquidation ensues.

Other Real Estate Owned Other real estate owned represents properties acquired through foreclosure or deed taken in lieu of foreclosure. At the time of acquisition, these properties are recorded at fair value less estimated costs to sell. Expenses incurred in connection with operating these properties and subsequent write-downs, if any, are charged to expense. Subsequent to foreclosure, management periodically considers the adequacy of the reserve for losses on the property. Gains and losses on the sales of these properties are credited or charged to income in the year of the sale.

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Bank Premises and Equipment Land, buildings and equipment are recorded at cost less accumulated depreciation. Depreciation is computed using the straight-line method over the following estimated useful lives:

Type	Estimated useful life
Buildings	39 years
Paving and landscaping	15 years
Computer equipment and software	3 to 5 years
Vehicles	5 years
Furniture and other equipment	5 to 7 years

Stock Options - The Company records compensation related to stock options pursuant to ASC 718 which requires the estimated fair market value of the expense to be reflected over the period the award is earned which is presumed to be the vesting period. For additional discussion concerning stock options see Note 15, Stock Option Plan.

Common Stock Warrants - The company issued common stock warrants as a result of its conversion of Director notes and the completion of its common stock offering in 2012. For additional discussion concerning these transactions including the terms and value of the warrants, see Note 22, Capital.

Income Taxes Deferred income tax assets and liabilities are determined using the liability (or balance sheet) method. Under this method, the net deferred tax asset or liability is determined based on the tax effects of the temporary differences between the book and tax bases of the various balance sheet assets and liabilities and gives current recognition to changes in tax rates and laws. If all or a portion of the net deferred tax asset is determined to be unlikely to be realized, a valuation allowance is established to reduce the net deferred tax asset to the amount that is more likely than not to be realized.

In the event the Company has unrecognized tax expense in future accounting periods, the Company will recognize interest in interest expense and penalties in operating expenses. There were no interest or penalties related to an unrecognized tax position for the years ended December 31, 2013 and 2012. Because of the impact of deferred tax accounting, other than interest and penalties, the reversal of the Company s treatment by taxing authorities would not affect the annual effective tax rate but would defer or accelerate the payment of cash to the taxing authority. The Company s tax filings for years ended 2010 through 2013 are currently open to audit under statutes of limitations by the Internal Revenue Service (IRS) and the Virginia Department of Taxation. Our tax filings for the years ended 2010, 2011, and 2012 are currently under examination by the IRS.

Financial Instruments **Off-balance-sheet instruments** - In the ordinary course of business, the Company has entered into commitments to extend credit. Such financial instruments are recorded in the financial statements when they are funded.

Earnings Per Share Basic earnings per share computations are based on the weighted average number of shares outstanding during each year. Dilutive earnings per share reflects the additional common shares that would have been outstanding if dilutive potential common shares had been issued. Potential common shares that may be issued relate to outstanding options and common stock warrants and are determined by the Treasury Method. For the years ending December 31, 2013 and 2012, potential common shares of 2,648,871 and 2,742,766, respectively, were anti-dilutive and were not included in the calculation. Basic and diluted net income (loss) per common share calculations follows:

(Amounts in Thousands, Except Share and Per Share Data)	For the years ended December 31, 2013	2012
Net income (loss)	$ 1,484	$ (6,324)
Weighted average shares outstanding	21,870,758	11,181,963
Weighted average dilutive shares outstanding	21,870,758	11,181,963
Basic and diluted income (loss) per share	$ 0.07	$ (0.57)

Comprehensive Income (Loss) Generally accepted accounting principles require that recognized revenue, expenses, gains and losses be included in net income. Although certain changes in assets and liabilities, such as

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unrealized gains and losses on available-for-sale securities, are reported as a separate component of the equity section of the balance sheet, such items, along with net income, are components of comprehensive income. The change in unrealized gains and losses on available-for-sale securities is our only component of other comprehensive income.

Advertising Cost Advertising costs are expensed in the period incurred.

Business Combinations - For purchase acquisitions accounted for as a business combination, the Company is required to record the assets acquired, including identified intangible assets and liabilities assumed at their fair value, which in many instances involves estimates based on third party valuations, such as appraisals, or internal valuations based on discounted cash flow analyses or other valuation techniques. The determination of the useful lives of intangible assets is subjective, as is the appropriate amortization method for such intangible assets. In addition, purchase acquisitions may result in goodwill, which is subject to ongoing periodic impairment testing based on the fair value of net assets acquired compared to the carrying value of goodwill. Changes in acquisition multiples, the overall interest rate environment, or the continuing operations of the assets acquired could have a significant impact on the periodic impairment testing. For additional discussion concerning our valuation of intangible assets, see Note 13, Intangible Assets.

Reclassification Certain reclassifications have been made to the prior years financial statements to place them on a comparable basis with the current year. Net income and stockholders equity previously reported were not affected by these reclassifications.

Subsequent Events The Company has evaluated subsequent events for potential recognition and/or disclosure through the date these consolidated financial statements were issued.

NOTE 3 FORMAL WRITTEN AGREEMENT:

Effective July 29, 2010, the Company and the Bank entered into a written agreement with the Federal Reserve Bank of Richmond (Reserve Bank) and the Virginia State Corporation Commission Bureau of Financial Institutions (the Bureau) called (the Written Agreement). At December 31, 2013, we believe we have not yet achieved full compliance with the Written Agreement but we have made progress in our compliance efforts under the Written Agreement and all of the written plans required to date, as discussed in the following paragraphs, have been submitted on a timely basis.

Under the terms of the Written Agreement, the Bank has agreed to develop and submit for approval within specified time periods written plans to: (a) strengthen board oversight of management and the Bank s operation; (b) if appropriate after review, to strengthen the Bank s management and board governance; (c) strengthen credit risk management policies; (d) enhance lending and credit administration; (e) enhance the Bank s management of commercial real estate concentrations; (f) conduct ongoing review and grading of the Bank s loan portfolio; (g) improve the Bank s position with respect to loans, relationships, or other assets in excess of $1 million which are now or in the future become past due more than 90 days, which are on the Bank s problem loan list, or which are adversely classified in any report of examination of the Bank; (h) review and revise, as appropriate, current policy and maintain sound processes for maintaining an adequate allowance for loan and lease losses; (i) enhance management of the Bank s liquidity position and funds management practices; (j) revise its contingency funding plan; (k) revise its strategic plan; and (l) enhance the Bank s anti-money laundering and related activities.

In addition, the Bank has agreed that it will: (a) not extend, renew, or restructure any credit that has been criticized by the Reserve Bank or the Bureau absent prior board of directors approval in accordance with the restrictions in the

Written Agreement; (b) eliminate all assets or portions of assets classified as loss and thereafter charge off all assets classified as loss in a federal or state report of examination, unless otherwise approved by the Reserve Bank.

Under the terms of the Written Agreement, both the Company and the Bank have agreed to submit capital plans to maintain sufficient capital at the Company, on a consolidated basis, and the Bank, on a stand-alone basis, and to refrain from declaring or paying dividends without prior regulatory approval. The Company has agreed that it will not take any other form of payment representing a reduction in the Bank s capital or make any distributions of interest, principal, or other sums on subordinated debentures or trust preferred securities without prior regulatory approval. The Company may not incur, increase or guarantee any debt without prior regulatory approval and has agreed not to purchase or redeem any shares of its stock without prior regulatory approval.

Under the terms of the Written Agreement, the Company and the Bank have appointed a committee to monitor compliance with the Written Agreement. The directors of the Company and the Bank have recognized and unanimously agree with the common goal of financial soundness represented by the Written Agreement and have confirmed the intent of the directors and executive management to diligently seek to comply with all requirements of the Written Agreement.

NOTE 4 DEPOSITS IN AND FEDERAL FUNDS SOLD TO BANKS:

The Bank had federal funds sold and cash on deposit with other commercial banks amounting to $35.9 million and $76.6 million at December 31, 2013 and 2012, respectively. Deposit amounts at other commercial banks may, at times, exceed federally insured limits.

The Bank is required to maintain average reserve balances, computed by applying prescribed percentages to its various types of deposits, either at the Bank or on deposit with the Federal Reserve Bank. At December 31, 2013 and 2012, all required reserves were met by the Bank s vault cash.

NOTE 5 INVESTMENT SECURITIES:

The amortized cost and estimated fair value of securities (all available-for-sale) are as follows:

(Dollars are in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Approximate Fair Value
December 31, 2013				
U.S. Government Agencies	$ 39,296	$ 246	$ 941	$ 38,601
Mortgage backed securities	41,284	60	819	40,525
Total Securities AFS	$ 80,580	$ 306	$ 1,760	$ 79,126
December 31, 2012				
U.S. Government Agencies	$ 23,177	$ 473	$ 13	$ 23,637
Mortgage backed securities	25,822	210	54	25,978
Total Securities AFS	$ 48,999	$ 683	$ 67	$ 49,615

The following table details unrealized losses and related fair values in the available-for-sale portfolio. This information is aggregated by the length of time that individual securities have been in a continuous unrealized loss position as of December 31, 2013 and December 31, 2012.

	Less than 12 Months		12 Months or More		Total	
(Dollars are in thousands)	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
December 31, 2013						

U.S. Government Agencies	$ 26,090	$ 936	$ 570	$ 5	$ 26,660	$ 941
Mtg. backed securities	27,461	693	5,046	126	32,507	819
Total Securities AFS	$ 53,551	$ 1,629	$ 5,616	$ 131	$ 59,167	$ 1,760
December 31, 2012						
U.S. Government Agencies	$ 2,931	$ 13	$	$	$ 2,931	$ 13
Mtg. backed securities	7,491	54			7,491	54
Total Securities AFS	$ 10,422	$ 67	$	$	$ 10,422	$ 67

At December 31, 2013, the available-for-sale portfolio included eighty investments for which the fair market value was less than amortized cost. At December 31, 2012, the available-for-sale portfolio included ten investments for which the fair market value was less than amortized cost. Management evaluates securities for other than temporary impairment at least on a quarterly basis, and more frequently when economic or market concerns warrant such evaluation. Consideration is given to (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial conditions and near-term prospects of the issuer, and (3) the intent and ability of the Company to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value. No securities had an other than temporary impairment.

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The amortized cost and fair value of investment securities at December 31, 2013, by contractual maturity, are shown in the following schedule. 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.

(Dollars are in thousands) Securities Available for Sale	Amortized Cost	Fair Value	Weighted Average Yield
Due in one year or less	$	$	%
Due after one year through five years	2,660	2,651	1.02%
Due after five years through fifteen years	26,552	26,213	1.69%
Due after fifteen years	51,368	50,262	1.97%
Total	$ 80,580	$ 79,126	1.84%

Investment securities with a carrying value of $17.0 million and $18.4 million at December 31, 2013 and 2012, were pledged to secure public deposits, overnight payment processing and for other purposes required by law.

The Bank, as a member of the Federal Reserve Bank and the Federal Home Loan Bank, is required to hold stock in each. These equity securities are restricted from trading and are recorded at a cost of $2.7 million and $2.8 million as of December 31, 2013 and 2012, respectively.

NOTE 6 LOANS:

Loans receivable outstanding at December 31, are summarized as follows:

(Dollars are in thousands)	2013	2012
Real estate secured:		
Commercial	$ 126,174	$ 149,935
Construction and land development	22,421	24,327
Residential 1-4 family	249,187	240,201
Multifamily	11,482	12,567
Farmland	28,892	33,068
Total real estate loans	438,156	460,098
Commercial	24,955	28,314
Agriculture	3,718	4,328
Consumer installment loans	26,055	29,445
All other loans	139	178
Total loans	$ 493,023	$ 522,363

Loans receivable on nonaccrual status at December 31, are summarized as follows:

(Dollars are in thousands)	2013	2012
Real estate secured:		
Commercial	$ 16,098	$ 16,308
Construction and land development	775	2,412
Residential 1-4 family	4,852	3,403
Multifamily	171	442
Farmland	5,315	7,750
Total real estate loans	27,211	30,315
Commercial	947	2,762
Agriculture	45	450
Consumer installment loans	104	9
All other loans		
Total loans receivable on nonaccrual status	$ 28,307	$ 33,536

Total interest income not recognized on nonaccrual loans for 2013 and 2012 was $969 thousand and $1.4 million, respectively. Total interest income recognized on nonaccrual loans for 2013 and 2012 was $1.4 million and $865 thousand, respectively.

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The following table presents information concerning the Company s investment in loans considered impaired as of December 31, 2013 and December 31, 2012:

As of December 31, 2013 (Dollars are in thousands)	Average Recorded Investment	Interest Income Recognized	Recorded Investment	Unpaid Principal Balance	Related Allowance
With no related allowance recorded:					
Real estate secured:					
Commercial	$ 16,270	$ 300	$ 9,807	$ 10,276	$
Construction and land development	2,246	26	336	345	
Residential 1-4 family	4,276	126	2,557	2,727	
Multifamily	652	16	326	326	
Farmland	4,260	166	2,533	2,670	
Commercial	717	7	315	423	
Agriculture	71	6	60	60	
Consumer installment loans	51	2	12	12	
All other loans					
With an allowance recorded:					
Real estate secured:					
Commercial	12,080	441	12,092	13,924	1,942
Construction and land development	492	9	554	640	138
Residential 1-4 family	3,980	260	5,458	5,824	1,180
Multifamily	561	17	268	268	39
Farmland	4,116	114	6,109	6,797	653
Commercial	1,012	3	672	740	208
Agriculture	138	4	55	71	43
Consumer installment loans	22	2	22	22	3
All other loans					
Total	$ 50,944	$ 1,499	$ 41,176	$ 45,125	$ 4,206

As of December 31, 2012 (Dollars are in thousands)	Average Recorded Investment	Interest Income Recognized	Recorded Investment	Unpaid Principal Balance	Related Allowance
With no related allowance recorded:					
Real estate secured:					
Commercial	$ 26,662	$ 829	$ 20,389	$ 21,434	$
Construction and land development	4,759	118	3,759	8,618	
Residential 1-4 family	7,824	227	6,308	6,567	
Multifamily	1,021	44	928	998	
Farmland	7,748	168	4,375	4,810	
Commercial	2,499	18	1,111	1,147	
Agriculture	463	7	109	109	
Consumer installment loans	83	10	98	98	

All other loans					
With an allowance recorded:					
Real estate secured:					
Commercial	14,770	347	13,495	14,014	3,196
Construction and land development	1,728	41	793	945	177
Residential 1-4 family	5,473	203	3,830	3,836	577
Multifamily	1,589	68	2,028	2,096	456
Farmland	4,972	(123)	5,702	5,714	635
Commercial	1,689	19	1,881	1,885	491
Agriculture	373	3	353	353	308
Consumer installment loans	69	3	27	27	16
All other loans					
Total	$ 81,722	$ 1,982	$ 65,186	$ 72,651	$ 5,856

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An age analysis of past due loans receivable was as follows:

As of December 31, 2013 (Dollars are in thousands)	Loans 30-59 Days Past Due	Loans 60-89 Days Past Due	Loans 90 or More Days Past Due	Total Past Due Loans	Current Loans	Total Loans	Accruing Loans 90 or More Days Past Due
Real estate secured:							
Commercial	$ 7,192	$ 1,713	$ 4,174	$ 13,079	$ 113,095	$ 126,174	$
Construction and land development	505	183	347	1,035	21,386	22,421	
Residential 1-4 family	6,391	1,067	1,271	8,729	240,458	249,187	
Multifamily		436		436	11,046	11,482	
Farmland	1,869	137	3,986	5,992	22,900	28,892	
Total real estate loans	15,957	3,536	9,778	29,271	408,885	438,156	
Commercial	135	14	902	1,051	23,904	24,955	
Agriculture	26	20	13	59	3,659	3,718	
Consumer installment Loans	241	48	8	297	25,758	26,055	
All other loans	11	7	1	19	120	139	1
Total loans	$ 16,370	$ 3,625	$ 10,702	$ 30,697	$ 462,326	$ 493,023	$ 1

As of December 31, 2012 (Dollars are in thousands)	Loans 30-59 Days Past Due	Loans 60-89 Days Past Due	Loans 90 or More Days Past Due	Total Past Due Loans	Current Loans	Total Loans	Accruing Loans 90 or More Days Past Due
Real estate secured:							
Commercial	$ 4,164	$ 998	$ 8,889	$ 14,051	$ 135,884	$ 149,935	$
Construction and land development	653		254	907	23,420	24,327	
Residential 1-4 family	9,031	861	3,027	12,919	227,282	240,201	304
Multifamily	90		442	532	12,035	12,567	
Farmland	1,777		5,871	7,648	25,420	33,068	191
Total real estate loans	15,715	1,859	18,483	36,057	424,041	460,098	495
Commercial	135	12	2,104	2,251	26,063	28,314	2
Agriculture	117	12	360	489	3,839	4,328	
Consumer installment Loans	506	66	55	627	28,818	29,445	54
All other loans	19	7		26	152	178	

Total loans	$ 16,492	$ 1,956	$ 21,002	$ 39,450	$ 482,913	$ 522,363	$ 551

The Company categorizes loans receivable into risk categories based on relevant information about the ability of borrowers to service their debt such as: current financial information, historical payment experience, credit documentation, public information, and current economic trends, among other factors. The Company analyzes loans and leases individually by classifying the loans receivable as to credit risk. The Company uses the following definitions for risk ratings:

Pass - Loans in this category are considered to have a low likelihood of loss based on relevant information analyzed about the ability of the borrowers to service their debt and other factors.

Special Mention - Loans in this category are currently protected but are potentially weak, including adverse trends in borrower s operations, credit quality or financial strength. Those loans constitute an undue and unwarranted credit risk but not to the point of justifying a substandard classification. The credit risk may be relatively minor yet constitute an unwarranted risk in light of the circumstances. Special mention loans have potential weaknesses which may, if not checked or corrected, weaken the loan or inadequately protect the Company s credit position at some future date.

Substandard - A substandard loan is inadequately protected by the current sound net worth and paying capacity of the obligor or of the collateral pledged, if any. Loans classified as substandard must have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt; they are characterized by the distinct possibility that the institution will sustain some loss if the deficiencies are not corrected.

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Doubtful - Loans classified Doubtful have all the weaknesses inherent in loans classified Substandard, plus 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.

Based on the most recent analysis performed, the risk category of loans receivable was as follows:

As of December 31, 2013

(Dollars are in thousands)	Pass	Special Mention	Substandard	Doubtful	Total
Real estate secured:					
Commercial	$ 100,403	$ 4,586	$ 21,185	$	$ 126,174
Construction and land development	19,138	2,107	1,176		22,421
Residential 1-4 family	234,857	1,916	12,213	201	249,187
Multifamily	10,777	266	439		11,482
Farmland	19,935	411	8,546		28,892
Total real estate loans	385,110	9,286	43,559	201	438,156
Commercial	23,258	634	1,034	29	24,955
Agriculture	3,583	11	124		3,718
Consumer installment loans	25,879		176		26,055
All other loans	139				139
Total	$ 437,969	$ 9,931	$ 44,893	$ 230	$ 493,023

As of December 31, 2012

(Dollars are in thousands)	Pass	Special Mention	Substandard	Doubtful	Total
Real estate secured:					
Commercial	$ 117,945	$ 5,782	$ 26,120	$ 88	$ 149,935
Construction and land development	18,502	1,067	4,758		24,327
Residential 1-4 family	220,534	4,739	14,437	491	240,201
Multifamily	9,765	178	2,624		12,567
Farmland	21,560	1,247	10,261		33,068
Total real estate loans	388,306	13,013	58,200	579	460,098
Commercial	21,793	3,227	3,254	40	28,314
Agriculture	3,841	53	434		4,328
Consumer installment loans	29,159	21	261	4	29,445
All other loans	178				178
Total	$ 443,277	$ 16,314	$ 62,149	$ 623	$ 522,363

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NOTE 7 ALLOWANCE FOR LOAN LOSSES:

The following table details activity in the allowance for loan losses by portfolio segment for the period ended December 31, 2013. Allocation of a portion of the allowance to one category of loans does not preclude its availability to absorb losses in other categories.

As of December 31, 2013

(Dollars are in thousands)	Beginning Balance	Charge Offs	Recoveries	Advances	Provisions	Ending Balance
Real estate secured:						
Commercial	$ 6,720	$ (2,811)	$ 439	$	$ 855	$ 5,203
Construction and land development	2,166	(312)	452		(1,122)	1,184
Residential 1-4 family	3,050	(1,143)	576		833	3,316
Multifamily	552				(419)	133
Farmland	1,074	(749)	68		831	1,224
Total real estate loans	13,562	(5,015)	1,535		978	11,060
Commercial	1,772	(513)	50		(162)	1,147
Agriculture	533	(363)	51		116	337
Consumer installment loans	388	(153)	128		(210)	153
All other loans	4				(2)	2
Unallocated	551				(170)	381
Total	$ 16,810	$ (6,044)	$ 1,764	$	$ 550	$ 13,080

As of December 31, 2013	Allowance for Loan Losses			Recorded Investment in Loans		
(Dollars are in thousands)	Individually Evaluated for Impairment	Collectively Evaluated for Impairment	Total	Individually Evaluated for Impairment	Collectively Evaluated for Impairment	Total
Real estate secured:						
Commercial	$ 1,942	$ 3,261	$ 5,203	$ 21,899	$ 104,275	$ 126,174
Construction and land development	138	1,046	1,184	890	21,531	22,421
Residential 1-4 family	1,180	2,136	3,316	8,015	241,172	249,187
Multifamily	39	94	133	594	10,888	11,482
Farmland	653	571	1,224	8,642	20,250	28,892
Total real estate loans	3,952	7,108	11,060	40,040	398,116	438,156
Commercial	208	939	1,147	987	23,968	24,955
Agriculture	43	294	337	115	3,603	3,718
Consumer installment loans	3	150	153	34	26,021	26,055
All other loans		2	2		139	139
Unallocated		381	381			
Total	$ 4,206	$ 8,874	$ 13,080	$ 41,176	$ 451,847	$ 493,023

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The following table details activity in the allowance for loan losses by portfolio segment for the period ended December 31, 2012. Allocation of a portion of the allowance to one category of loans does not preclude its availability to absorb losses in other categories.

As of December 31, 2012

(Dollars are in thousands)	Beginning Balance	Charge Offs	Recoveries	Advances	Provisions