UNITED BANCSHARES INC/OH
Form 10-K/A
September 05, 2014

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM 10-K/A

(Amendment No. 1)

Annual report pursuant to Section 13 or 15(d) of the

Securities Exchange Act of 1934, as amended

For the fiscal year ended December 31, 2013

Commission File No.: 000-29283

UNITED BANCSHARES, INC.

(exact name of registrant as specified in its charter)

OHIO	**34-1516518**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer I.D. No.)

100 S. High Street, Columbus Grove, Ohio 45830

(Address of principal executive offices)

Registrant's telephone number, including area code: **(419) 659-2141**

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

Common Stock, no par value – NASDAQ Global Market

(Title of class)

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

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes ____ No _X_

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.

Yes ___ 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 (§229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ____

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

Large accelerated filer ____ Accelerated filer ____ Non-accelerated filer ____ 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 voting stock held by non-affiliates of the registrant was $39,785,746, based upon the last sales price as quoted on the NASDAQ Global Market as of June 30, 2013.

The number of shares of Common Stock, no par value outstanding as of January 31, 2014: 3,442,364.

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DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Annual Report to Shareholders for the fiscal year ended December 31, 2013 are incorporated by reference into Part II. Portions of the Proxy Statement dated March 19, 2014 for the 2014 Annual Meeting of Shareholders to be held on April 23, 2014 are incorporated by reference into Part III.

EXPLANATORY NOTE

United Bancshares, Inc. (the "Corporation") is filing this Amendment No. 1 on Form 10-K/A to amend our Annual Report on Form 10-K for the year ended December 31, 2013, originally filed with the Securities and Exchange Commission (the "SEC") on March 19, 2014 ("the Original Filing"), to include the Annual Report to Shareholders as Exhibit 13 inadvertently omitted pages due to a clerical error. The Annual Report to Shareholders includes information incorporated by reference into the Form 10-K/A. This Form 10-K/A does not attempt to modify or update any other information in the Original Filing, except as required to reflect the additional information included in Part IV of this Form 10-K/A.

The information that was inadvertently omitted was published and posted to the Corporation's website at www.theubank.com on March 20, 2014, and was also mailed to the shareholders of record with the Corporation's definitive proxy statement dated March 19, 2014.

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PART I

Item 1. Business

General

United Bancshares, Inc. (the “Corporation”), an Ohio corporation, is a bank holding company registered under the Bank Holding Company Act of 1956, as amended, and is subject to regulation by the Board of Governors of the Federal Reserve System (the “Federal Reserve Board”). The Corporation was incorporated and organized in 1985. The executive offices of the Corporation are located at 100 S. High Street, Columbus Grove, Ohio 45830. The Corporation is a one-bank holding company, through its wholly-owned subsidiary, The Union Bank Company, Columbus Grove, Ohio (“Bank”) as that term is defined by the Federal Reserve Board. As of December 31, 2013, the Corporation employed approximately 137 full-time equivalent employees.

United Bancshares, Inc’s. common stock has traded on the NASDAQ Global Market under the symbol “UBOH” since March 2001.

The Corporation is registered as a Securities Exchange Act of 1934 (the “1934 Act”) reporting company.

Forward Looking Statements

Certain matters disclosed herein may be deemed to be forward-looking statements that involve risks and uncertainties, including regulatory policy changes, interest rate fluctuations, loan demand, loan delinquencies and losses, general economic conditions, and other risks. Forward-looking statements are often characterized by the use of qualifying words and their derivatives such as “expects,” “anticipates,” “believes,” “estimates,” “plans,” “projects,” and other words and statements concerning opinions or judgments of the Corporation and its management about future events. Actual strategies and results in future time periods may differ materially from those currently expected. Such forward-looking statements represent management’s judgment as of the current date. The Corporation disclaims, however, any intent or obligation to update such forward-looking statements.

This report contains forward-looking statements that are based on management's beliefs, assumptions, current expectations, estimates and projections about the financial services industry, the economy, and the Corporation.

Forward-looking statements are identifiable by words or phrases such as “outlook”, “plan” or “strategy”; that an event or trend “may”, “should”, “will”, “is likely”, or is “probably” to occur or “continue”, has “begun” or “is scheduled” or “on track” Corporation or its management “anticipates”, “believes”, “estimates”, “plans”, “forecasts”, “intends”, “predicts”, “projects”, or a particular result, or is “committed”, “confident”, “optimistic” or has an “opinion” that an event will occur, or other words or phrases such as “ongoing”, “future”, “signs”, “efforts”, “tend”, “exploring”, “appearing”, “until”, “near term”, “going forward” variations of such words and similar expressions. Such statements are based upon current beliefs and expectations and involve substantial risks and uncertainties which could cause actual results to differ materially from those expressed or implied by such forward-looking statements. These statements include, among others, statements related to real estate valuation, future levels of non-performing loans, the rate of asset dispositions, dividends, future growth and funding sources, future liquidity levels, future profitability levels, the effects on earnings of changes in interest rates and the future level of other revenue sources. Management's determination of the provision and allowance for loan losses, the appropriate carrying value of intangible assets (including goodwill and mortgage servicing rights), deferred tax assets, other real estate owned, and the fair value of investment securities (including whether any impairment on any investment security is temporary or other-than-temporary and the amount of any impairment) and other financial instruments, involves judgments that are inherently forward-looking. All statements with references to future time periods are forward-looking. All of the information concerning interest rate sensitivity is forward-looking. Management's assumptions regarding pension and other post retirement plans involve judgments that are inherently forward-looking. Our ability to successfully implement new programs and initiatives, increase efficiencies, respond to declines in collateral values and credit quality, maintain our current level of deposits and other sources of funding, and improve profitability is not entirely within our control and is not assured. The future effect of changes in the real estate, financial and credit markets and the national and regional economy on the banking industry, generally, and the Corporation, specifically, are also inherently uncertain. These statements are not guarantees of future performance and involve certain risks, uncertainties and assumptions (“risk factors”) that are difficult to predict with regard to timing, extent, likelihood and degree of occurrence. Therefore, actual results and outcomes may materially differ from what may be expressed or forecasted in such forward-looking statements.

General Description of Bank Subsidiary

The Bank is engaged in the business of commercial banking. The Bank is an Ohio state-chartered bank, which serves the Ohio counties of Allen, Hancock, Putnam, Sandusky, Van Wert and Wood, with office locations in Bowling Green, Columbus Grove, Delphos, Findlay, Gibsonburg, Kalida, Leipsic, Lima, Ottawa, and Pemberville, Ohio.

The Bank offers a full range of commercial banking services, including checking accounts, savings and money market accounts; certificates of deposit; automatic teller machines; commercial, consumer, agricultural, residential mortgage and home equity loans; safe deposit box rentals; and other personalized banking services.

Competition

The Corporation competes for deposits with other commercial banks, savings associations and credit unions and issuers of commercial paper and other securities, such as shares in money market mutual funds. Primary factors in competing for deposits include customer service, interest rates and convenience. In making loans, the Corporation competes with other commercial banks, savings associations, consumer finance companies, credit unions, leasing companies, mortgage companies and other lenders. Competition is affected by, among other things, the general availability of lendable funds, general and local economic conditions, current interest rate levels and other factors that are not readily predictable. The number of financial institutions competing with the Corporation may increase as a result of changes in statutes and regulations eliminating various restrictions on interstate and inter-industry branching and acquisitions. Such increased competition may have an adverse effect upon the Corporation.

Effect of Environmental Regulation

Compliance with federal, state and local provisions regulating the discharge of material into the environment, or otherwise relating to the protection of the environment, have not had a material effect upon the capital expenditures, earnings or competitive position of the Corporation and its subsidiary. The Corporation believes that the nature of the operations of its subsidiary has little, if any, environmental impact. The Corporation, therefore, anticipates no material capital expenditures for environmental control facilities for its current fiscal year or for the foreseeable future. The Corporation’s subsidiary may be required to make capital expenditures for environmental control facilities related to properties, which they may acquire through foreclosure proceedings in the future; however, the amount of such capital expenditures, if any, is not currently determinable.

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Supervision and Regulation

Other Statutes and Regulations

The following is a summary of certain other statutes and regulations affecting the Corporation and its subsidiary. This summary is qualified in its entirety by reference to such statutes and regulations.

The Corporation is a bank holding company under the Bank Holding Company Act of 1956, as amended, which restricts the activities of the Corporation and the acquisition by the Corporation of voting shares or assets of any bank, savings association or other company. The Corporation is also subject to the reporting requirements of, and examination and regulation by, the Federal Reserve Board. Subsidiary banks of a bank holding company are subject to certain restrictions imposed by the Federal Reserve Act on transactions with affiliates, including any loans or extensions of credit to the bank holding company or any of its subsidiaries, investments in the stock or other securities thereof and the taking of such stock or securities as collateral for loans or extensions of credit to any borrower; the issuance of guarantees, acceptances or letters of credit on behalf of the bank holding company and its subsidiary; purchases or sales of securities or other assets; and the payment of money or furnishing of services to the bank holding company and other subsidiaries. Bank holding companies are prohibited from acquiring direct or indirect control of more than 5% of any class of voting stock or substantially all of the assets of any bank holding company without the prior approval of the Federal Reserve Board. A bank holding company and its subsidiaries are prohibited from engaging in certain tying arrangements in connection with extensions of credit and/or the provision of other property or services to a customer by the bank holding company or its subsidiaries.

As an Ohio state-chartered bank, the Bank is supervised and regulated by the Ohio Division of Financial Institutions and the Federal Deposit Insurance Corporation (“FDIC”). The deposits of the Bank are insured by the FDIC and the Bank is subject to the applicable provisions of the Federal Deposit Insurance Act. A subsidiary of a bank holding company can be liable to reimburse the FDIC if the FDIC incurs or anticipates a loss because of a default of another FDIC-insured subsidiary of the bank holding company or in connection with FDIC assistance provided to such subsidiary in danger of default. In addition, the holding company of any insured financial institution that submits a capital plan under the federal banking agencies’ regulations on prompt corrective action guarantees a portion of the institution’s capital shortfall, as discussed below.

Various requirements and restrictions under the laws of the United States and the State of Ohio affect the operations of the Bank, including requirements to maintain reserves against deposits, restrictions on the nature and amount of loans which may be made and the interest that may be charged thereon, restrictions relating to investments and other activities, limitations on credit exposure to correspondent banks, limitations on activities based on capital and surplus, limitations on payment of dividends, and limitations on branching.

The Federal Reserve Board has adopted risk-based capital guidelines for bank holding companies. The risk-based capital guidelines include both a definition and a framework for calculating risk weighted assets by assigning assets and off-balance sheet items to broad risk categories. The minimum ratio of total capital to risk weighted assets (including certain off-balance sheet items, such as standby letters of credit) is 8%. At least 4% is to be comprised of common shareholders' equity (including retained earnings but excluding treasury stock), noncumulative perpetual preferred stock, a limited amount of cumulative perpetual preferred stock, and minority interest in equity accounts of consolidated subsidiaries, less goodwill and certain other intangible assets ("Tier 1 capital"). The remainder ("Tier 2 capital") may consist, among other things, of mandatory convertible debt securities, a limited amount of subordinated debt, other preferred stock and a limited amount of allowance for loan losses. The Federal Reserve Board also imposes a minimum leverage ratio (Tier 1 capital to total assets) of 3% for bank holding companies and state member banks that meet certain specified conditions, including having the highest regulatory rating. The minimum leverage ratio is 1%-2% higher for other bank holding companies and state member banks based on their particular circumstances and risk profiles and for those banks experiencing or anticipating significant growth. State non-member bank subsidiaries, such as the Bank are subject to similar capital requirements adopted by the FDIC.

The Corporation and its subsidiary currently satisfy all regulatory capital requirements. Failure to meet applicable capital guidelines could subject a banking institution to a variety of enforcement remedies available to federal and state regulatory authorities, including the termination of deposit insurance by the FDIC. The junior subordinated deferrable interest debentures issued in 2003, as described in Note 9 to the consolidated financial statements contained in the Corporation's Annual Report, qualify as Tier I capital under current regulations.

The federal banking regulators have established regulations governing prompt corrective action to resolve capital deficient banks. Under these regulations, institutions, which become undercapitalized, become subject to mandatory regulatory scrutiny and limitations that increase as capital decreases. Such institutions are also required to file capital plans with their primary federal regulator, and their holding companies must guarantee the capital shortfall up to 5% of the assets of the capital deficient institution at the time it becomes undercapitalized.

The ability of a bank holding company to obtain funds for the payment of dividends and for other cash requirements is largely dependent on the amount of dividends that may be declared by its subsidiary bank and other subsidiaries. However, the Federal Reserve Board expects the Corporation to serve as a source of strength to its subsidiary bank, which may require it to retain capital for further investment in the subsidiary, rather than for dividends for shareholders of the Corporation. The Bank may not pay dividends to the Corporation if, after paying such dividends, it would fail to meet the required minimum levels under the risk-based capital guidelines and the minimum leverage ratio requirements. The Bank must have the approval of its regulatory authorities if a dividend in any year would cause the total dividends for that year to exceed the sum of the current year's net income and the retained net income for the preceding two years, less required transfers to surplus. Payment of dividends by a bank subsidiary may be restricted at any time at the discretion of the regulatory authorities, if they deem such dividends to constitute an unsafe and/or unsound banking practice. These provisions could have the effect of limiting the Corporation's ability to pay dividends on its outstanding common shares.

Deposit Insurance Assessments and Recent Legislation

The Federal Deposit Insurance Reform Act of 2005 and the Federal Deposit Insurance Reform Conforming Amendments Act of 2005 (collectively, the "Deposit Insurance Reform Acts") were both signed into law during February, 2006. The provisions of the Deposit Insurance Reform Acts included, among other things, merging the Bank Insurance Fund and the Savings Association Insurance Fund into a new fund called the Deposit Insurance Fund, which merger was effective March 31, 2006; increasing insurance coverage for retirement accounts from $100,000 to $250,000, effective April 1, 2006; adjusting deposit insurance levels of $100,000 for non-retirement accounts and $250,000 for retirement accounts every five years based on an inflation index, with the first adjustment to be effective on January 1, 2011; eliminating a 1.25% hard target Designated Reserve Ratio, as defined, and giving the FDIC discretion to set the Designated Reserve Ratio within a range of 1.15% to 1.50% for any given year; eliminating certain restrictions on premium rates the FDIC charges covered institutions and establishing a risk-based premium system; and providing for a one-time credit for institutions that paid premiums to the Bank Insurance Fund or the Savings Association Insurance Fund prior to December 31, 1996.

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Current economic conditions have increased bank failures and expectations for further failures, in which case the FDIC insures payment of deposits up to insured limits from the Deposit Insurance Fund. In late 2008, the FDIC announced an increase in insurance premium rates of seven basis points for the first quarter of 2009. On February 27, 2009, the FDIC announced its adoption of an interim final rule imposing a one-time special assessment of up to 20 basis points and a final rule adjusting the risk-based calculation used to determine the premiums due from each financial institution. On March 5, 2009, the FDIC announced its plan to reduce the special assessment to 10 basis points. The special assessment and the changes in the premium calculation significantly increased the Corporation's FDIC insurance expense in 2009. On September 29, 2009, the FDIC adopted a Notice of Proposed Rule making it mandatory that insured depository institutions prepay their quarterly risk-based assessments to the FDIC on December 30, 2009 for the fourth quarter of 2009 and for the years 2010 through 2012. The FDIC applied the Bank's first two quarterly assessments in 2013 against the remaining prepaid balance and refunded $171,034 to the Bank at the end of the second quarter of 2013.

Pursuant to the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act"), the FDIC has established 2.0% as the designated reserve ratio (DRR), that is, the ratio of the Deposit Insurance Fund to insured deposits. The Dodd-Frank Act directs the FDIC to amend its assessment regulations so that future assessments will generally be based upon a depository institution's average total consolidated assets minus the average tangible equity of the insured depository institution during the assessment period, whereas assessments were previously based on the amount of an institution's insured deposits. The minimum deposit insurance fund rate will increase from 1.15% to 1.35% by September 30, 2020, and the cost of the increase will be borne by depository institutions with assets of $10 billion or more. At least semi-annually, the FDIC will update its loss and income projections for the fund and, if needed, will increase or decrease assessment rates, following notice-and-comment rulemaking if required.

The Consumer Financial Protection Bureau ("CFPB"), pursuant to the Dodd-Frank Act, issued a final rule on January 10, 2013 (effective on January 10, 2014), amending Regulation Z as implemented by the Truth in Lending Act, requiring creditors to make a reasonable and good faith determination based on verified and documented information that a consumer applying for a mortgage loan has a reasonable ability to repay the loan according to its terms. Creditors are required to determine consumers' ability to repay in one of two ways. The first alternative requires the creditor to consider the following eight underwriting factors when making the credit decision: (i) current or reasonably expected income or assets; (ii) current employment status; (iii) the monthly payment on the covered transaction; (iv) the monthly payment on any simultaneous loan; (v) the monthly payment for mortgage-related obligations; (vi) current debt obligations, alimony, and child support; (vii) the monthly debt-to-income ratio or residual income; and (viii) credit history. Alternatively, the creditor can originate "qualified mortgages," which are entitled to a presumption that the creditor making the loan satisfied the ability-to-repay requirements. In general, a "qualified mortgage" is a mortgage loan without negative amortization, interest-only payments, balloon payments, or terms exceeding 30 years. In addition, to be a qualified mortgage the points and fees paid by a consumer cannot exceed 3% of the total loan amount. Qualified mortgages that are "higher-priced" (e.g. subprime loans) garner a rebuttable presumption of compliance with the ability-to-repay rules, while qualified mortgages that are not "higher-priced" (e.g. prime loans) are given a safe harbor of compliance. To meet the mortgage credit needs of a broader customer base, the Corporation and its subsidiary are predominantly an originator of mortgages that are in compliance with the Ability-to-Pay rules.

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Uncertainty remains as to the ultimate impact of the Dodd-Frank Act, which could have a material adverse impact either on the financial services industry as a whole, or on the Corporation's business, results of operations and financial condition. Provisions in the legislation that affect deposit insurance assessments, payment of interest on demand deposits and interchange fees could increase the costs associated with deposits as well as place limitations on certain revenues those deposits may generate. Provisions in the legislation that require revisions to the capital requirements of the Corporation and the Bank could require the Corporation and the Bank to seek other sources of capital in the future.

In July 2013, the federal banking agencies issued a final rule that will revise the leverage and risk-based capital requirements and the method for calculating risk-weighted assets to make them consistent with the agreements that were reached by the international Basel Committee on Banking Supervision and the Dodd-Frank Act. Among other things, the rule establishes a new common equity Tier 1 minimum capital requirement (4.5% of risk-weighted assets), adopts a uniform minimum leverage requirement of 4% of total assets, increases the minimum tier 1 capital to risk-weighted assets requirement (from 4% to 6% of risk-weighted assets) and assigns a higher risk weighting (150%) to exposures that are more than 90 days past due or are on nonaccrual status and to certain commercial real estate facilities that finance the acquisition, development or construction of real property. The final rule also requires unrealized gains and losses on certain "available for sale" securities holdings to be included for purposes of calculating regulatory capital unless a one-time opt-out is exercised. Additional restraints will also be imposed on the inclusion in regulatory capital of mortgage-servicing assets, defined tax assets and minority interests. The rule limits a banking organization's capital distributions and certain discretionary bonus payments to executives if the banking organization does not hold a "capital conservation buffer" consisting of 2.5% of common equity Tier 1 capital to risk-weighted assets in addition to the amount necessary to meet its minimum risk-based capital requirements. The final rule becomes effective on January 1, 2015. The capital conservation buffer requirements will be phased in beginning January 1, 2016 and ending January 1, 2019, when the full capital conservation buffer requirement will be effective.

Monetary Policy and Economic Conditions

The commercial banking business is affected not only by general economic conditions, but also by the policies of various governmental regulatory authorities, including the Federal Reserve Board. The Federal Reserve Board regulates money and credit conditions and interest rates in order to influence general economic conditions primarily through open market operations in U.S. Government securities, changes in the discount rate on bank borrowings and changes in reserve requirements against bank deposits. These policies and regulations significantly affect the overall growth and distribution of bank loans, investments and deposits, and the interest rates charged on loans as well as the interest rates paid on deposits and accounts.

The monetary policies of the Federal Reserve Board have had a significant effect on the operating results of commercial banks in the past and are expected to continue to have significant effects in the future. In view of the changing conditions in the economy and the money market and the activities of monetary and fiscal authorities, no definitive predictions can be made as to future changes in interest rates, credit availability or deposit level.

Statistical Financial Information Regarding the Corporation

The following schedules and table analyze certain elements of the consolidated balance sheets and statements of income of the Corporation and its subsidiary, as required under Securities Act Industry Guide 3 promulgated by the Securities and Exchange Commission, and should be read in conjunction with the narrative analysis presented in ITEM 7, MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATION and the Consolidated Financial Statements of the Corporation, both of which are included in the 2013 Annual Report.

Available Information

The Corporation files various reports with the SEC, including Forms 10-Q, 10-K, 11-K and 8-K as required. The public may read and copy any filed materials with the SEC at the SEC's Public Reference Room at 100 F Street, N.E., Washington, DC 20549. The public may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. The SEC maintains an Internet site (http://www.sec.gov) that contains reports, proxy and information statements, and other information that the Corporation electronically files with the SEC.

Various information on the Corporation may also be obtained from the Corporation's maintained website at http://www.theubank.com.

I. DISTRIBUTION OF ASSETS, LIABILITIES AND SHAREHOLDERS' EQUITY; INTEREST RATES AND INTEREST DIFFERENTIAL

A. The following are the average balance sheets for the years ended December 31:

	2013	2012	2011
	(dollars in thousands)		
ASSETS			
Interest-earning assets			
Securities (1)			
Taxable	$132,471	$121,376	$104,755
Non-taxable	60,107	46,390	46,981
Interest bearing deposits	29,770	37,625	41,802
Federal funds sold	23	46	82
Loans (2)	299,379	325,114	360,669
Total interest-earning assets	521,750	530,551	554,289
Non-interest-earning assets			
Cash and due from banks	8,487	7,242	6,944
Premises and equipment, net	9,174	9,385	9,728
Accrued interest receivable and other assets	28,027	28,773	31,266
Allowance for loan losses	(5,681)	(7,485)	(8,762)
	$561,757	$568,466	$593,465
LIABILITIES AND SHAREHOLDERS' EQUITY			
Interest-bearing liabilities			
Deposits			
Savings and interest-bearing demand deposits	$212,464	$194,590	$171,142
Time deposits	180,110	208,982	256,953
Junior subordinated deferrable interest debentures	10,300	10,300	10,300
Other borrowings	21,589	27,488	41,058
Total interest-bearing liabilities	424,463	441,360	479,453
Non-interest-bearing liabilities			
Demand deposits	69,794	60,876	53,505
Accrued interest payable and other Liabilities	4,136	4,196	3,078
Shareholders' equity (3)	63,364	62,034	57,429
	$561,757	$568,466	$593,465

(1) Securities include securities available-for-sale, which are carried at fair value, and Federal Home Loan Bank (FHLB) stock carried at cost. The average balance includes monthly average balances of fair value adjustments and daily average balances for the amortized cost of securities.

(2) Loan balances include principal balances of non-accrual loans and loans held for sale.

(3)

Shareholders' equity includes average net unrealized appreciation (depreciation) on securities available-for-sale, net of tax.

I. DISTRIBUTION OF ASSETS, LIABILITIES AND SHAREHOLDERS' EQUITY; INTEREST RATES AND INTEREST DIFFERENTIAL (CONTINUED)

B. The following tables set forth, for the years indicated, the condensed average balances of interest-earning assets and interest-bearing liabilities, the interest earned or paid on such amounts, and the average interest rates earned or paid thereon.

	2013		
	Average Balance (dollars in thousands)	Interest	Average Rate
INTEREST-EARNING ASSETS			
Securities (1)			
Taxable	$132,471	$2,690	2.03 %
Non-taxable (2)	60,107	2,816	4.68 %
Loans (3, 4)	299,379	15,248	5.09 %
Other	29,793	102	0.34 %
Total interest-earning assets	$521,750	20,856	4.00 %
INTEREST-BEARING LIABILITIES			
Deposits			
Savings and interest-bearing demand deposits	$212,464	304	0.14 %
Time deposits	180,110	1,838	1.02 %
Junior subordinated deferrable interest debentures	10,300	353	3.43 %
Other borrowings	21,589	754	3.49 %
Total interest-bearing liabilities	$424,463	3,249	0.77 %
Net interest income, tax equivalent basis		$17,607	
Net interest income as a percent of average interest-earning assets			3.38 %

(1) Securities include securities available-for-sale, which are carried at fair value, and FHLB stock carried at cost. The average balance includes monthly average balances of fair value adjustments and daily average balances for the amortized cost of securities.
(2) Computed on tax equivalent basis for non-taxable securities (34% statutory rate).
(3) Loan balances include principal balance of non-accrual loans.
(4) Interest income on loans includes fees of $798,786.

I. DISTRIBUTION OF ASSETS, LIABILITIES AND SHAREHOLDERS' EQUITY; INTEREST RATES AND INTEREST DIFFERENTIAL (CONTINUED)

	2012			
	Average Balance (dollars in thousands)	Interest	Average Rate	
INTEREST-EARNING ASSETS				
Securities (1)				
Taxable	$121,376	$2,777	2.29	%
Non-taxable (2)	46,390	2,708	5.84	%
Loans (3, 4)	325,114	17,922	5.51	%
Other	37,671	114	0.30	%
Total interest-earning assets	$530,551	23,521	4.43	%
INTEREST-BEARING LIABILITIES				
Deposits				
Savings and interest-bearing demand deposits	$194,590	286	0.15	%
Time deposits	208,982	3,062	1.47	%
Junior subordinated deferrable interest debentures	10,300	368	3.57	%
Other borrowings	27,488	960	3.49	%
Total interest-bearing liabilities	$441,360	4,676	1.06	%
Net interest income, tax equivalent basis		$18,845		
Net interest income as a percent of average interest-earning assets			3.55	%

(1) Securities include securities available-for-sale, which are carried at fair value, and FHLB stock carried at cost. The average balance includes monthly average balances of market value adjustments and daily average balances for the amortized cost of securities.
(2) Computed on tax equivalent basis for non-taxable securities (34% statutory rate).
(3) Loan balances include principal balance of non-accrual loans.
(4) Interest income on loans includes fees of $1,213,462.

I. DISTRIBUTION OF ASSETS, LIABILITIES AND SHAREHOLDERS' EQUITY; INTEREST RATES AND INTEREST DIFFERENTIAL (CONTINUED)

	2011		
	Average Balance	Interest	Average Rate
	(dollars in thousands)		
INTEREST-EARNING ASSETS			
Securities available-for-sale (1)			
Taxable	$104,755	$3,257	3.11 %
Non-taxable (2)	46,981	2,933	6.24 %
Loans (3, 4)	360,669	21,198	5.88 %
Other	41,884	99	0.24 %
Total interest-earning assets	$554,289	27,487	4.96 %
INTEREST-BEARING LIABILITIES			
Deposits			
Savings and interest-bearing demand deposits	$171,142	249	0.15 %
Time deposits	256,953	5,291	2.06 %
Junior subordinated deferrable interest debentures	10,300	350	3.40 %
Other borrowings	41,058	1,436	3.50 %
Total interest-bearing liabilities	$479,453	7,326	1.53 %
Net interest income, tax equivalent basis		$20,161	
Net interest income as a percent of average interest-earning assets			3.64 %

(1) Securities include securities available-for-sale, which are carried at fair value, and FHLB stock carried at cost. The average balance includes monthly average balances of market value adjustments and daily average balances for the amortized cost of securities.
(2) Computed on tax equivalent basis for non-taxable securities (34% statutory rate).
(3) Loan balances include principal balance of non-accrual loans and loans held for sale.
(4) Interest income on loans includes fees of $922,947.

I. DISTRIBUTION OF ASSETS, LIABILITIES AND SHAREHOLDERS' EQUITY; INTEREST RATES AND INTEREST DIFFERENTIAL (CONTINUED)

C. The following tables set forth the effect of volume and rate changes on interest income and expenses for the periods indicated. For purposes of these tables, changes in interest due to volume and rate were determined as follows:
Volume variance - change in volume multiplied by the previous year's rate.

Rate variance - change in rate multiplied by the previous year's volume.

Rate/volume variance - change in volume multiplied by the change in rate.

This variance was allocated to volume variances and rate variances in proportion to the relationship of the absolute dollar amount of the change in each.
Interest on non-taxable securities has been adjusted to a fully tax equivalent basis using a statutory tax rate of 34% in all years presented.

	2013/2012		
	Total	Variance Attributable To	
	Variance	Volume	Rate
	(dollars in thousands)		
INTEREST INCOME			
Securities -			
Taxable	$(87)	$241	$(328)
Non-taxable	108	706	(598)
Loans	(2,674)	(1,364)	(1,310)
Other	(12)	(26)	14
Subtotal	(2,665)	(443)	(2,222)
INTEREST EXPENSE			
Deposits -			
Savings and interest-bearing demand deposits	18	26	(8)
Time deposits	(1,223)	(383)	(840)
Junior subordinated deferrable interest debentures	(15)	-	(15)
Other borrowings	(206)	(206)	-
Subtotal	(1,426)	(563)	(863)

NET INTEREST INCOME	$(1,239)	$120	$(1,359)

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I. DISTRIBUTION OF ASSETS, LIABILITIES AND SHAREHOLDERS' EQUITY; INTEREST RATES AND INTEREST DIFFERENTIAL (CONTINUED)

	2012/2011		
	Total	Variance Attributable To	
	Variance	Volume	Rate
	(dollars in thousands)		
INTEREST INCOME			
Securities -			
Taxable	$(480)	$466	$(946)
Non-taxable	(225)	(37)	(188)
Loans	(3,276)	(2,010)	(1,266)
Other	15	(11)	26
Subtotal	(3,966)	(1,592)	(2,374)
INTEREST EXPENSE			
Deposits -			
Savings and interest-bearing demand deposits	37	34	3
Time deposits	(2,229)	(876)	(1,353)
Junior subordinated deferrable interest debentures	18	-	18
Other borrowings	(476)	(474)	(2)
Subtotal	(2,650)	(1,316)	(1,334)
NET INTEREST INCOME	$(1,316)	$(276)	$(1,040)

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II. INVESTMENT PORTFOLIO

A. The carrying amounts of securities available-for-sale as of December 31 are summarized as follows:

	2013	2012	2011
	(dollars in thousands)		
U.S. Government agency securities	$12,333	$15,554	$7,521
Obligations of states and political subdivisions	66,540	53,919	49,311
Mortgage-backed securities	117,472	107,607	94,599
Other	735	528	525
	$197,080	$177,608	$151,956

The above excludes Federal Home Loan Bank stock amounting to $4,893,800 in 2013, 2012, and 2011.

B. The maturity distribution and weighted average yield of securities available-for-sale at December 31, 2013 are as follows (1):

		Maturing		
	Within One Year	After One Year But Within Five Years	After Five Years But Within Ten Years	After Ten Years
	(dollars in thousands)			
Agencies	$-	$8,489	$3,844	$-
Obligations of states and political subdivisions	2,450	6,295	34,169	23,626
Mortgage-backed securities (2)	-	726		