

C & F FINANCIAL CORP  
Form 10-K  
March 11, 2015  
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

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FORM 10-K

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(Mark One)

Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the fiscal year ended December 31, 2014

or

Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the transition period from to \_\_\_\_\_

Commission file number 000-23423

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C&F FINANCIAL CORPORATION

(Exact name of registrant as specified in its charter)

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Virginia 54-1680165  
(State or other jurisdiction of incorporation or organization) (I.R.S. Employer Identification No.)

802 Main Street

West Point, VA 23181

(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code: (804) 843-2360

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

Common Stock, \$1.00 par value per share	The NASDAQ Stock Market LLC
Title of each class	Name of each exchange on which registered

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

NONE

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

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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

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

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 during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

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

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

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

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

The aggregate market value of common stock held by non-affiliates of the registrant as of June 30, 2014 was \$114,598,638.

There were 3,393,935 shares of common stock outstanding as of March 6, 2015.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the definitive Proxy Statement to be delivered to shareholders in connection with the Annual Meeting of Shareholders to be held April 21, 2015 are incorporated by reference in Part III of this report.

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SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT  
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PART I

ITEM 1. BUSINESS

General

C&F Financial Corporation (the Corporation) is a bank holding company that was incorporated in March 1994 under the laws of the Commonwealth of Virginia. The Corporation owns all of the stock of Citizens and Farmers Bank (the Bank or C&F Bank), which is an independent commercial bank chartered under the laws of the Commonwealth of Virginia. C&F Bank originally opened for business under the name Farmers and Mechanics Bank on January 22, 1927. C&F Bank has the following five wholly-owned active subsidiaries, all incorporated under the laws of the Commonwealth of Virginia:

- C&F Mortgage Corporation and its wholly-owned subsidiary Certified Appraisals LLC
- C&F Finance Company and its wholly-owned subsidiary C&F Remarketing LLC
- C&F Investment Services, Inc.
- C&F Insurance Services, Inc.
- CVB Title Services, Inc.

On October 1, 2013, the Corporation acquired all of the outstanding common stock of Central Virginia Bankshares, Inc. (CVBK) in an all-cash transaction in which CVBK shareholders received \$0.32 for each share of CVBK common stock they owned, or approximately \$846,000 in the aggregate. In addition, the Corporation purchased from the U.S. Treasury for \$3.4 million all of CVBK's preferred stock and warrants issued to the U.S. Treasury under the Capital Purchase Program (CPP). CVBK was a one-bank holding company incorporated under the laws of the Commonwealth of Virginia. CVBK owned all of the stock of Central Virginia Bank (CVB), which was an independent commercial bank chartered under the laws of the Commonwealth of Virginia. On March 22, 2014, CVBK was merged with and into C&F Financial Corporation and CVB was merged with and into C&F Bank.

The Corporation operates in a decentralized manner in three principal business activities: (1) retail banking through C&F Bank, (2) mortgage banking through C&F Mortgage Corporation (C&F Mortgage) and (3) consumer finance through C&F Finance Company (C&F Finance). The following general business discussion focuses on the activities within each of these segments.

In addition, the Corporation conducts brokerage activities through C&F Investment Services, Inc., insurance activities through C&F Insurance Services, Inc. and title insurance service through CVB Title Services, Inc. The financial position and operating results of any one of these subsidiaries are not significant to the Corporation as a whole and are not considered principal activities of the Corporation at this time.

The Corporation also owns three non-operating subsidiaries, C&F Financial Statutory Trust II (Trust II) formed in December 2007, C&F Financial Statutory Trust I (Trust I) formed in July 2005, and Central Virginia Bankshares Statutory Trust I (CVBK Trust I) formed in December 2003. These trusts were formed for the purpose of issuing \$10.0 million each for Trust II and Trust I of the Corporation's junior subordinated debt securities and \$5.0 million for CVBK Trust I of junior subordinated debt securities originally issued by CVBK, but assumed by the Corporation when CVBK was merged into the Corporation on March 22, 2014, with all such issuances occurring in private placements to institutional investors. All three trusts are unconsolidated subsidiaries of the Corporation. The principal assets of these trusts are \$10.3 million each for Trust II and Trust I and \$5.2 million for CVBK Trust I of the Corporation's junior subordinated debt securities (such securities of the Corporation referred to herein as "trust preferred capital notes") that are reported as liabilities of the consolidated Corporation.



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### Retail Banking

We provide retail banking services through C&F Bank. C&F Bank provides retail banking services at its main office in West Point, Virginia, and 24 Virginia branches located one each in Cartersville, Chester, Cumberland, Hampton, Mechanicsville, Newport News, Norge, Powhatan, Providence Forge, Quinton, Saluda, Sandston, Varina, West Point and Yorktown, two in Williamsburg, three in Richmond and four in Midlothian. These branches provide a wide range of banking services to individuals and businesses. These services include various types of checking and savings deposit accounts, as well as business, real estate, development, mortgage, home equity and installment loans. The Bank also offers ATMs, internet banking and debit and credit cards, as well as travelers' checks, safe deposit box rentals, collection, notary public, wire service and other customary bank services to its customers. Revenues from retail banking operations consist primarily of interest earned on loans and investment securities and fees related to deposit services. At December 31, 2014, assets of the Retail Banking segment totaled \$1.18 billion. For the year ended December 31, 2014, the net income for this segment totaled \$5.6 million.

### Mortgage Banking

We conduct mortgage banking activities through C&F Mortgage, which was organized in September 1995. C&F Mortgage provides mortgage loan origination services through 12 locations in Virginia, two in Maryland and two in North Carolina. The Virginia offices are located one each in Charlottesville, Fishersville, Fredericksburg, Glen Allen, Harrisonburg, Lynchburg, Newport News, Roanoke, Virginia Beach and Williamsburg, and two in Midlothian. The Maryland offices are located in Annapolis and Waldorf. The North Carolina offices are located in Gastonia and Raleigh. C&F Mortgage offers a wide variety of residential mortgage loans, which are originated for sale generally to the following investors: Wells Fargo Home Mortgage; Franklin American Mortgage Company; Penny Mac Corporation; and the Virginia Housing Development Authority (VHDA). C&F Mortgage does not securitize loans. C&F Bank may also purchase permanent loans from C&F Mortgage. C&F Mortgage originates conventional mortgage loans, mortgage loans insured by the Federal Housing Administration (the FHA), mortgage loans guaranteed by the United States Department of Agriculture (the USDA) and the Veterans Administration (the VA). A majority of the conventional loans are conforming loans that qualify for purchase by the Federal National Mortgage Association (Fannie Mae) or the Federal Home Loan Mortgage Corporation (Freddie Mac). The remainder of the conventional loans are non-conforming in that they do not meet Fannie Mae or Freddie Mac guidelines, but are eligible for sale to various other investors. Through its subsidiary, C&F Mortgage also provides ancillary mortgage loan origination services for residential appraisals. Revenues from mortgage banking operations consist principally of gains on sales of loans to investors in the secondary mortgage market, loan origination fee income and interest earned on mortgage loans held for sale. At December 31, 2014, assets of the Mortgage Banking segment totaled \$42.4 million. For the year ended December 31, 2014, net income for this segment totaled \$411,000.

### Consumer Finance

We conduct consumer finance activities through C&F Finance. C&F Finance is a regional finance company providing automobile loans throughout Virginia and in portions of Alabama, Florida, Georgia, Illinois, Indiana, Kentucky, Maryland, Missouri, New Hampshire, New Jersey, North Carolina, Ohio, Pennsylvania, Tennessee, Texas and West Virginia through its offices in Richmond and Hampton, Virginia, in Nashville, Tennessee and in Hunt Valley, Maryland. C&F Finance is an indirect lender that provides automobile financing through lending programs that are designed to serve customers in the “non-prime” market who have limited access to traditional automobile financing. C&F Finance generally purchases automobile retail installment sales contracts from manufacturer-franchised dealerships with used-car operations and through selected independent dealerships. C&F Finance selects these dealers based on the types of vehicles sold. Specifically, C&F Finance prefers to finance later model, low mileage used vehicles because the initial depreciation on new vehicles is extremely high. The typical borrowers on the retail installment sales contracts purchased have experienced prior credit difficulties. Because C&F Finance serves customers who are unable to meet the credit standards imposed by most traditional automobile financing sources, C&F Finance typically charges interest at higher rates than those charged by traditional financing sources. As C&F Finance provides financing in a relatively high-risk market, it expects to experience a higher level of credit losses than traditional automobile financing sources. Revenues from consumer finance operations consist principally of interest earned on automobile loans. At December 31, 2014, assets of the Consumer Finance segment totaled \$283.9 million. For the year ended December 31, 2014, net income for this segment totaled \$6.9 million.

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Employees

At December 31, 2014, we employed 616 full-time equivalent employees. We consider relations with our employees to be excellent.

Competition

Retail Banking

In the Bank's market area, we compete with large national and regional financial institutions, savings associations and other independent community banks, as well as credit unions, mutual funds, brokerage firms and insurance companies. Increased competition has come from out-of-state banks through their acquisition of Virginia-based banks and interstate branching, and expansion of community and regional banks into our service areas.

The banking business in Virginia, and in the Bank's primary service area in the Hampton to Richmond corridor, is highly competitive for both loans and deposits, and is dominated by a relatively small number of large banks with many offices operating over a wide geographic area. Among the advantages such large banks have are their ability to finance wide-ranging advertising campaigns, efficiencies through economies of scale and, by virtue of their greater total capitalization, substantially higher lending limits than the Bank.

Factors such as interest rates offered, the number and location of branches and the types of products offered, as well as the reputation of the institution, affect competition for deposits and loans. We compete by emphasizing customer service and technology, establishing long-term customer relationships, building customer loyalty, and providing products and services to address the specific needs of our customers. We target individual and small-to-medium size business customers.

No material part of the Bank's business is dependent upon a single or a few customers, and the loss of any single customer would not have a materially adverse effect upon the Bank's business.

## Mortgage Banking

C&F Mortgage competes with large national and regional banks, credit unions, smaller regional mortgage lenders and small local broker operations. Due to the increased regulatory and compliance burden, the industry has seen a consolidation in the number of competitors in the marketplace. The agency guidelines for sales of mortgages in the secondary market business continue to be stringent. Interest rates, low housing inventory, cash buyers, new mortgage lending regulations and other market conditions have resulted in reduced originations across the industry during 2014. C&F Mortgage was not immune to these factors, as its production declined as well.

The competitive factors faced by C&F Mortgage have changed and may continue to change due to the Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act). The Dodd-Frank Act affects many aspects of mortgage finance regulation, which has changed and may continue to result in changes to the competitive landscape in the future. The many modifications introduced have required or will require extensive rulemaking, and the full effect of the Dodd-Frank Act and the full effect of the related compliance burden will not be known for some time to come. The reforms to mortgage lending encompass broad new restrictions on lending practices and loan terms, amend price thresholds for certain lending segments, add new disclosure forms and procedures for all mortgages, and mandate stronger legal liabilities in connection with real estate finance. In addition, the Dodd-Frank Act authorizes the Consumer Financial Protection Bureau (the CFPB) to establish certain minimum standards for the origination of residential mortgages, including a determination of the borrower's ability to repay (for which the finalized rules became effective in January 2014), and allows borrowers to raise certain defenses to foreclosure if they receive any loan other than a "qualified mortgage" as defined by the Dodd-Frank Act and CFPB regulations. While C&F Mortgage is continuing to evaluate all aspects of the Dodd-Frank Act and regulations issued pursuant thereto and by the CFPB, such legislation and regulations could materially and adversely affect the manner in which it conducts its mortgage business, result in heightened federal regulation and oversight of its business activities, and result in increased costs and potential litigation associated with its business activities. Given the far-reaching effect of the Dodd-Frank Act and CFPB regulations on mortgage finance, compliance with the

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requirements of the Dodd-Frank Act and CFPB regulations may require substantial changes to mortgage lending systems and processes and other implementation efforts.

To operate profitably in this environment, lenders must have a high level of operational and risk management skills and be able to attract and retain top mortgage origination talent. C&F Mortgage competes by attracting the top people in sales and operations in the industry, providing an infrastructure that manages regulatory changes efficiently and effectively, offering a product menu that is both competitive in loan parameters as well as price, and providing consistently high quality customer service.

No material part of C&F Mortgage's business is dependent upon a single customer and the loss of any single customer would not have a materially adverse effect upon C&F Mortgage's business. Further, C&F Mortgage has implemented strategies to mitigate potential disruption in C&F Mortgage's direct or indirect access to the secondary market for residential mortgage loans. C&F Mortgage, like all residential mortgage lenders, would be affected by the inability of Fannie Mae, Freddie Mac, the FHA or the VA to purchase or guarantee loans. Although C&F Mortgage sells loans to various intermediaries, the ability of these aggregators to purchase or guarantee loans would be limited if these government-sponsored entities cease to exist or materially limit their purchases or guarantees of mortgage loans or suffer deteriorations in their financial condition.

## Consumer Finance

The non-prime automobile finance business is highly competitive. The automobile finance market is highly fragmented and is served by a variety of financial entities, including the captive finance affiliates of major automotive manufacturers, banks, savings associations, credit unions and independent finance companies. Many of these competitors have substantially greater financial resources and lower costs of funds than our finance subsidiary. In addition, competitors often provide financing on terms that are more favorable to automobile purchasers or dealers than the terms C&F Finance offers. Many of these competitors also have long-standing relationships with automobile dealerships and may offer dealerships or their customers other forms of financing, including dealer floor plan financing and leasing, which we do not.

During 2013 and 2014, a number of financial institutions and other lenders have increased focus on operations in the non-prime automobile finance markets resulting in intensified competition for loans and qualified personnel and, to a lesser extent thus far, credit easing. To continue to operate profitably, lenders must have a high level of operational and risk management skills and access to competitive costs of funds.

Providers of automobile financing traditionally have competed on the basis of interest rates charged, the quality of credit accepted, the flexibility of loan terms offered and the quality of service provided to dealers and customers. To establish C&F Finance as one of the principal financing sources at the dealers it serves, we compete predominately by providing a high level of dealer service, building strong dealer relationships, offering flexible loan terms, and quickly funding loans purchased from dealers.

No material part of C&F Finance's business is dependent upon any single dealer relationship, and the loss of any single dealer relationship would not have a materially adverse effect upon C&F Finance's business.

## Regulation and Supervision

### General

Bank holding companies and banks are extensively regulated under both federal and state law. The following summary briefly describes significant provisions of currently applicable federal and state laws and certain regulations and the potential impact of such provisions. This summary is not complete, and we refer you to the particular statutory or regulatory provisions or proposals for more information. Because regulation of financial institutions changes regularly and is the subject of constant legislative and regulatory debate, we cannot forecast how federal and state regulation and supervision of financial institutions may change in the future and affect the Corporation's and the Bank's operations.

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### Regulatory Reform

The financial crisis of 2008, including the downturn of global economic, financial and money markets and the threat of collapse of numerous financial institutions, and other events led to the adoption of numerous laws and regulations that apply to, and focus on, financial institutions. The most significant of these laws is the Dodd-Frank Act, which was adopted on July 21, 2010 and, in part, is intended to implement significant structural reforms to the financial services industry. The Dodd-Frank Act is discussed in more detail below.

As a result of the Dodd-Frank Act and other regulatory reforms, the Corporation continues to experience a period of rapidly changing regulations. These regulatory changes could have a significant effect on how the Corporation conducts its business. The specific implications of the Dodd-Frank Act and other proposed regulatory reforms cannot yet be fully predicted and will depend to a large extent on the specific regulations that are adopted in the coming months and years to implement regulatory reform initiatives.

### Regulation of the Corporation

As a bank holding company, the Corporation is subject to the Bank Holding Company Act of 1956 (the BHCA) and regulation and supervision by the Board of Governors of the Federal Reserve System (the Federal Reserve Board). Pursuant to the BHCA the Federal Reserve Board has the power to order any bank holding company or its subsidiaries to terminate any activity or to terminate its ownership or control of any subsidiary when the Federal Reserve Board has reasonable grounds to believe that continuation of such activity or ownership constitutes a serious risk to the financial soundness, safety or stability of any bank subsidiary of the bank holding company.

The BHCA generally limits the activities of a bank holding company and its subsidiaries to that of banking, managing or controlling banks, or any other activity that is closely related to banking or to managing or controlling banks, and permits interstate banking acquisitions subject to certain conditions, including national and state concentration limits. The Federal Reserve Board has jurisdiction under the BHCA to approve any bank or non-bank acquisition, merger or consolidation proposed by a bank holding company. A bank holding company must be well capitalized and well managed to engage in an interstate bank acquisition or merger, and Banks may branch across state lines provided that the law of the state in which the branch is to be located would permit establishment of the branch if the bank were a state bank chartered by such state.

Each of the Bank's depository accounts is insured by the Federal Deposit Insurance Corporation (the FDIC) against loss to the depositor to the maximum extent permitted by applicable law, and federal law and regulatory policy impose a number of obligations and restrictions on the Corporation and the Bank to reduce potential loss exposure to

depositors and to the FDIC Deposit Insurance Fund (DIF). For example, pursuant to the Dodd-Frank Act and Federal Reserve Board policy, a bank holding company must commit resources to support its subsidiary depository institutions, which is referred to as serving as a "source of strength." In addition, insured depository institutions under common control must reimburse the FDIC for any loss suffered or reasonably anticipated by the DIF as a result of the default of a commonly controlled insured depository institution. The FDIC may decline to enforce the provisions if it determines that a waiver is in the best interest of the DIF. An FDIC claim for damages is superior to claims of stockholders of an insured depository institution or its holding company but is subordinate to claims of depositors, secured creditors and holders of subordinated debt, other than affiliates, of the commonly controlled insured depository institution.

The Federal Deposit Insurance Act (the FDIA) provides that amounts received from the liquidation or other resolution of any insured depository institution must be distributed, after payment of secured claims, to pay the deposit liabilities of the institution before payment of any other general creditor or stockholder. This provision would give depositors a preference over general and subordinated creditors and stockholders if a receiver is appointed to distribute the assets of a bank.

The Corporation also is subject to regulation and supervision by the State Corporation Commission of Virginia. The Corporation also must file annual, quarterly and other periodic reports with, and comply with other regulations of, the Securities and Exchange Commission (the SEC).



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Capital Requirements

The Federal Reserve Board and the FDIC have adopted rules to implement the Basel III capital framework as outlined by the Basel Committee on Banking Supervision and standards for calculating risk-weighted assets and risk-based capital measurements (collectively, the Basel III Final Rules) that apply to banking organizations they supervise. For the purposes of these capital rules, (i) common equity tier 1 capital (CET1) consists principally of common stock (including surplus) and retained earnings; (ii) Tier 1 capital consists principally of CET1 plus non-cumulative preferred stock and related surplus, and certain grandfathered cumulative preferred stocks and trust preferred securities; and (iii) Tier 2 capital consists principally of Tier 1 capital plus qualifying subordinated debt and preferred stock, and limited amounts of the allowance for loan losses. Each regulatory capital classification is subject to certain adjustments and limitations, as implemented by the Basel III Final Rules. The Basel III Final Rules also establish risk weightings that are applied to many classes of assets held by community banks, importantly including applying higher risk weightings to certain commercial real estate loans.

The Basel III Final Rules were effective January 1, 2015, and the Basel III Final Rules capital conservation buffer will be phased in from 2015 to 2019.

When fully phased in, the Basel III Final Rules require banks to maintain (i) a minimum ratio of CET1 to risk-weighted assets of at least 4.5%, plus a 2.5% “capital conservation buffer” (which is added to the 4.5% CET1 ratio as that buffer is phased in, effectively resulting in a minimum ratio of CET1 to risk-weighted assets of at least 7%), (ii) a minimum ratio of Tier 1 capital to risk-weighted assets of at least 6.0%, plus the capital conservation buffer (which is added to the 6.0% Tier 1 capital ratio as that buffer is phased in, effectively resulting in a minimum Tier 1 capital ratio of 8.5% upon full implementation), (iii) a minimum ratio of total (that is, Tier 1 plus Tier 2) capital to risk-weighted assets of at least 8.0%, plus the capital conservation buffer (which is added to the 8.0% total capital ratio as that buffer is phased in, effectively resulting in a minimum total capital ratio of 10.5% upon full implementation) and (iv) a minimum leverage ratio of 4%, calculated as the ratio of Tier 1 capital to balance sheet exposures plus certain off-balance sheet exposures (computed as the average for each quarter of the month-end ratios for the quarter).

The Basel III Final Rules provide deductions from and adjustments to regulatory capital measures, primarily to CET1, including deductions and adjustments that were not applied to reduce CET1 under historical regulatory capital rules. For example, mortgage servicing rights, deferred tax assets, dependent upon future taxable income, and significant investments in non-consolidated financial entities must be deducted from CET1 to the extent that any one such category exceeds 10% of CET1 or all such categories in the aggregate exceed 15% of CET1. These deductions from and adjustments to regulatory capital will generally be phased in beginning in 2015 through 2018.

The Basel III Final Rules permanently includes in Tier 1 capital trust preferred securities issued prior to May 19, 2010 by bank holding companies with less than \$15 billion in total assets, subject to a limit of 25% of Tier 1 capital. The Corporation expects that its trust preferred securities will be included in the Corporation's Tier 1 capital until their maturity.

The Basel III Final Rules also implement a "countercyclical capital buffer," generally designed to absorb losses during periods of economic stress and to be imposed when national regulators determine that excess aggregate credit growth becomes associated with a buildup of systemic risk. This buffer is a CET1 add-on to the capital conservation buffer in the range of 0% to 2.5% when fully implemented (potentially resulting in total buffers of between 2.5% and 5%).

#### Limits on Dividends

The Corporation is a legal entity that is separate and distinct from the Bank. A significant portion of the revenues of the Corporation result from dividends paid to it by the Bank. Both the Corporation and C&F Bank are subject to laws and regulations that limit the payment of dividends, including limits on the sources of dividends and requirements to maintain capital at or above regulatory minimums. Banking regulators have indicated that Virginia banking organizations should generally pay dividends only (1) from net undivided profits of the bank, after providing for all expenses, losses, interest and taxes accrued or due by the bank and (2) if the prospective rate of earnings retention appears consistent with

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the organization's capital needs, asset quality and overall financial condition. In addition, the FDIA prohibits insured depository institutions such as C&F Bank from making capital distributions, including paying dividends, if, after making such distribution, the institution would become undercapitalized as defined in the statute. We do not expect that any of these laws, regulations or policies will materially affect the ability of the Corporation or C&F Bank to pay dividends.

The Dodd-Frank Act

The Dodd-Frank Act implements far-reaching changes across the financial regulatory landscape, including changes that will affect all bank holding companies and banks, including the Corporation and the Bank. Provisions that significantly affect the business of the Corporation and the Bank include the following:

- Insurance of Deposit Accounts. The Dodd-Frank Act changed the assessment base for federal deposit insurance from the amount of insured deposits to consolidated assets less tangible capital. The Dodd-Frank Act also made permanent the \$250,000 limit for federal deposit insurance and increased the cash limit of Securities Investor Protection Corporation protection from \$100,000 to \$250,000.
- Payment of Interest on Demand Deposits. The Dodd-Frank Act repealed the federal prohibitions on the payment of interest on demand deposits, thereby permitting depository institutions to pay interest on business transaction and other accounts.
- Creation of the Consumer Financial Protection Bureau. The Dodd-Frank Act centralized significant aspects of consumer financial protection by creating a new agency, the CFPB, which is discussed in more detail below.
- Debit Card Interchange Fees. The Dodd-Frank Act amended the Electronic Fund Transfer Act (EFTA) to, among other things, require that debit card interchange fees be reasonable and proportional to the actual cost incurred by the issuer with respect to the transaction. In June 2011, the Federal Reserve Board adopted regulations setting the maximum permissible interchange fee as the sum of 21 cents per transaction and 5 basis points multiplied by the value of the transaction, with an additional adjustment of up to one cent per transaction if the issuer implements additional fraud-prevention standards. Although issuers that have assets of less than \$10 billion are exempt from the Federal Reserve Board's regulations that set maximum interchange fees, these regulations could significantly affect the interchange fees that financial institutions with less than \$10 billion in assets are able to collect.

In addition, the Dodd-Frank Act implements other far-reaching changes to the financial regulatory landscape, including provisions that:

- Restrict the preemption of state law by federal law and disallow subsidiaries and affiliates of national banks from availing themselves of such preemption.
- Impose comprehensive regulation of the over-the-counter derivatives market, subject to significant rulemaking processes, which would include certain provisions that would effectively prohibit insured depository institutions from conducting certain derivatives businesses in the institution itself.
- Require depository institutions with total consolidated assets of more than \$10 billion to conduct regular stress tests and require large, publicly traded bank holding companies to create a risk committee responsible for the oversight of enterprise risk management.
- Require loan originators to retain 5 percent of any loan sold or securitized, unless it is a “qualified residential mortgage,” subject to certain exceptions.
- Prohibit banks and their affiliates from engaging in proprietary trading and investing in and sponsoring certain unregistered investment companies (the Volcker Rule).
- Implement corporate governance revisions that apply to all public companies not just financial institutions.

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Many aspects of the Dodd-Frank Act remain subject to future rulemaking, making it difficult to anticipate the overall financial impact on the Corporation, its subsidiaries, its customers or the financial industry more generally. Some of the rules that have been proposed and, in some cases, adopted to comply with the Dodd-Frank Act's mandates are discussed further below.

Insurance of Accounts, Assessments and Regulation by the FDIC

The Bank's deposits are insured by the DIF of the FDIC up to the standard maximum insurance amount for each deposit insurance ownership category. The basic limit on FDIC deposit insurance coverage is \$250,000 per depositor. Under the FDIA, the FDIC may terminate deposit insurance upon a finding that the institution has engaged in unsafe and unsound practices, is in an unsafe or unsound condition to continue operations, or has violated any applicable law, regulation, rule, order or condition imposed by the FDIC, subject to administrative and potential judicial hearing and review processes.

Deposit Insurance Assessments. The DIF is funded by assessments on banks and other depository institutions calculated based on average consolidated total assets minus average tangible equity (defined as Tier 1 capital). As required by the Dodd-Frank Act, the FDIC has adopted a large-bank pricing assessment scheme, set a target "designated reserve ratio" (described in more detail below) of 2 percent for the DIF and established a lower assessment rate schedule when the reserve ratio reaches 1.15 percent and, in lieu of dividends, provides for a lower assessment rate schedule, when the reserve ratio reaches 2 percent and 2.5 percent. An institution's assessment rate depends upon the institution's assigned risk category, which is based on supervisory evaluations, regulatory capital levels and certain other factors. Initial base assessment rates ranges from 2.5 to 45 basis points. The FDIC may make the following further adjustments to an institution's initial base assessment rates: decreases for long-term unsecured debt including most senior unsecured debt and subordinated debt; increases for holding long-term unsecured debt or subordinated debt issued by other insured depository institutions; and increases for broker deposits in excess of 10 percent of domestic deposits for institutions not well rated and well capitalized.

The Dodd-Frank Act transferred to the FDIC increased discretion with regard to managing the required amount of reserves for the DIF, or the "designated reserve ratio." Among other changes, the Dodd-Frank Act (i) raised the minimum designated reserve ratio to 1.35 percent and removed the upper limit on the designated reserve ratio, (ii) requires that the designated reserve ratio reach 1.35 percent by September 2020, and (iii) requires the FDIC to offset the effect on institutions with total consolidated assets of less than \$10 billion of raising the designated reserve ratio from 1.15 percent to 1.35 percent – which requirement will be met by rules that will be proposed by the FDIC when the reserve ratio approaches 1.15 percent. The FDIA requires that the FDIC consider the appropriate level for the designated reserve ratio on at least an annual basis. The FDIC has adopted a DIF restoration plan to ensure that the fund reserve ratio reaches 1.35 percent by September 30, 2020, as required by the Dodd-Frank Act.

## Regulation of the Bank and Other Subsidiaries

The Bank is subject to supervision, regulation and examination by the Virginia State Corporation Commission Bureau of Financial Institutions (VBFI) and its primary federal regulator, the FDIC. The various laws and regulations issued and administered by the regulatory agencies (including the CFPB) affect corporate practices, such as the payment of dividends, the incurrence of debt and the acquisition of financial institutions and other companies, and affect business practices and operations, such as the payment of interest on deposits, the charging of interest on loans, the types of business conducted, the products and terms offered to customers and the location of offices. Prior approval of the applicable primary federal regulator and the VBFI is required for a Virginia chartered bank or bank holding company to merge with another bank or bank holding company, or purchase the assets or assume the deposits of another bank or bank holding company, or acquire control of another bank or bank holding company. In reviewing applications seeking approval of merger and acquisition transactions, the bank regulatory authorities will consider, among other things, the competitive effect and public benefits of the transactions, the capital position of the combined organization, the risks to the stability of the U.S. banking or financial system, the applicant's performance record under the Community Reinvestment Act (CRA) and fair housing initiatives, and the applicant's compliance with and the effectiveness of the subject organizations in combating money laundering activities and complying with Bank Secrecy Act requirements.

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Community Reinvestment Act. The CRA imposes on financial institutions an affirmative and ongoing obligation to meet the credit needs of their local communities, including low and moderate-income neighborhoods, consistent with the safe and sound operation of those institutions. A financial institution's efforts in meeting community credit needs are assessed based on specified factors. These factors also are considered in evaluating mergers, acquisitions and applications to open a branch or facility. In 2014, the Bank received a "Satisfactory" CRA rating.

Federal Home Loan Bank of Atlanta. The Bank is a member of the Federal Home Loan Bank (FHLB) of Atlanta, which is one of 12 regional FHLBs that provide funding to their members for making housing loans as well as for affordable housing and community development loans. Each FHLB serves as a reserve, or central bank, for the members within its assigned region. Each FHLB makes loans to members in accordance with policies and procedures established by the Board of Directors of the FHLB. As a member, the Bank must purchase and maintain stock in the FHLB. At December 31, 2014, the Bank owned \$3.3 million of FHLB stock.

Consumer Protection. The Dodd-Frank Act created the CFPB, a federal regulatory agency that is responsible for implementing, examining and enforcing compliance with federal consumer financial laws for institutions with more than \$10 billion of assets and, to a lesser extent, smaller institutions. The Dodd-Frank Act gives the CFPB authority to supervise and regulate providers of consumer financial products and services, and establishes the CFPB's power to act against unfair, deceptive or abusive practices, and gives the CFPB rulemaking authority in connection with numerous federal consumer financial protection laws (for example, but not limited to, the Truth-in-Lending Act (TILA) and the Real Estate Settlement Procedures Act (RESPA)).

As a smaller institution (i.e., with assets of \$10 billion or less), most consumer protection aspects of the Dodd-Frank Act will continue to be applied to the Corporation by the Federal Reserve Board and to the Bank by the FDIC. However, the CFPB may include its own examiners in regulatory examinations by a small institution's principal regulators and may require smaller institutions to comply with certain CFPB reporting requirements. In addition, regulatory positions taken by the CFPB and administrative and legal precedents established by CFPB enforcement activities, including in connection with supervision of larger bank holding companies, could influence how the Federal Reserve Board and FDIC apply consumer protection laws and regulations to financial institutions that are not directly supervised by the CFPB. The precise effect of the CFPB's consumer protection activities on the Corporation and the Bank cannot be determined with certainty.

Mortgage Banking Regulation. In connection with making mortgage loans, the Bank is subject to rules and regulations that, among other things, establish standards for loan origination, prohibit discrimination, provide for inspections and appraisals of property, require credit reports on prospective borrowers, in some cases, restrict certain loan features and fix maximum interest rates and fees, require the disclosure of certain basic information to mortgagors concerning credit and settlement costs, limit payment for settlement services to the reasonable value of the services rendered and require the maintenance and disclosure of information regarding the disposition of mortgage applications based on

race, gender, geographical distribution and income level. The Bank's mortgage origination activities are subject to the Equal Credit Opportunity Act (ECOA), TILA, Home Mortgage Disclosure Act, RESPA, and Home Ownership Equity Protection Act, and the regulations promulgated under these acts, among other additional state and federal laws, regulations and rules.

The Bank's mortgage origination activities are also subject to Regulation Z, which implements TILA. Certain provisions of Regulation Z require mortgage lenders 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. Alternatively, a mortgage lender can originate "qualified mortgages", which are generally defined as mortgage loans without negative amortization, interest-only payments, balloon payments, terms exceeding 30 years, and points and fees paid by a consumer equal to or less than 3% of the total loan amount. Higher-priced qualified mortgages (e.g., subprime loans) receive a rebuttable presumption of compliance with ability-to-repay rules, and other qualified mortgages (e.g., prime loans) are deemed to comply with the ability-to-repay rules. The Corporation's Mortgage Banking segment predominately originates mortgage loans that comply with Regulation Z's "qualified mortgage" rules.

In addition to certain regulations applicable to the Bank, the Corporation's Mortgage Banking segment is subject to the rules and regulations of, and examination by, the Department of Housing and Urban Development (HUD), the FHA,



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the USDA, the VA and state regulatory authorities with respect to originating, processing and selling mortgage loans. Those rules and regulations, among other things, establish standards for loan origination, prohibit discrimination, provide for inspections and appraisals of property, require credit reports on prospective borrowers and, in some cases, restrict certain loan features and fix maximum interest rates and fees.

**Consumer Financing Regulation.** The Corporation's Consumer Finance segment also is regulated by the VBFI and the states and jurisdictions in which it operates, and the segment's lending operations are subject to numerous federal regulations over which the CFPB has rulemaking authority and regarding which enforcement authority is shared by the Federal Reserve Board, the FDIC, the Department of Justice and the Federal Trade Commission. The VBFI regulates and enforces laws relating to consumer lenders and sales finance agencies such as C&F Finance. Such rules and regulations generally provide for licensing of sales finance agencies; limitations on amounts, duration and charges, including interest rates, for various categories of loans; requirements as to the form and content of finance contracts and other documentation; and restrictions on collection practices and creditors' rights.

Certain federal regulatory agencies, and in particular, the CFPB, the Federal Trade Commission, and the Federal Reserve Board, have recently become more active in investigating the products, services and operations of banks and other finance companies engaged in auto finance activities. These investigations have extended to banks that engage in indirect automobile lending, and the CFPB has released regulatory guidance that deems automobile lenders within the CFPB's jurisdiction responsible for ECOA noncompliance even if such noncompliance is a result of dealer lending practices. As of January 1, 2015, the Corporation and C&F Finance are not subject to supervision by the CFPB.

## Other Regulations

**Prompt Correction Action.** The federal banking agencies have broad powers under current federal law to take prompt corrective action to resolve problems of insured depository institutions. The extent of these powers depends upon whether the institution in question is "well capitalized," "adequately capitalized," "undercapitalized," "significantly undercapitalized" or "critically undercapitalized." These terms are defined under uniform regulations issued by each of the federal banking agencies regulating these institutions. An insured depository institution which is less than adequately capitalized must adopt an acceptable capital restoration plan, is subject to increased regulatory oversight and is increasingly restricted in the scope of its permissible activities. As of December 31, 2014, the Bank was considered "well capitalized."

**Incentive Compensation.** The Federal Reserve Board, the Office of the Comptroller of the Currency (OCC) and the FDIC have issued regulatory guidance (the Incentive Compensation Guidance) intended to ensure that the incentive compensation policies of banking organizations do not undermine the safety and soundness of such organizations by encouraging excessive risk-taking. The Federal Reserve will review, as part of the regular, risk-focused examination process, the incentive compensation arrangements of banking organizations, such as the Corporation, that are not

"large, complex banking organizations." The findings will be included in reports of examination, and deficiencies will be incorporated into the organization's supervisory ratings. Enforcement actions may be taken against a banking organization if its incentive compensation arrangements, or related risk-management control or governance processes, pose a risk to the organization's safety and soundness and the organization is not taking prompt and effective measures to correct the deficiencies.

As required by the Dodd-Frank Act, in March 2011 the SEC and the federal bank regulatory agencies proposed regulations that would prohibit financial institutions with assets of at least \$1 billion from maintaining executive compensation arrangements that encourage inappropriate risk taking by providing excessive compensation or that could lead to material financial loss. If the regulations are adopted in the form initially proposed, they will impose limitations on the manner in which the Corporation may structure compensation for its executives and will require the Corporation to submit annual reports to the Federal Reserve Board regarding the Corporation's incentive compensation. These proposed regulations incorporate the principles discussed in the Incentive Compensation Guidance. The comment period for these proposed regulations has closed and a final rule has not yet been published.

Financial Holding Company Status. As provided by the Gramm-Leach-Bliley Act of 1999 (GLBA), a bank holding company may become eligible to engage in activities that are financial in nature or incident or complimentary to financial activities by qualifying as a financial holding company. To qualify as a financial holding company, each insured depository

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institution controlled by the bank holding company must be well-capitalized, well-managed and have at least a satisfactory rating under the CRA. In addition, the bank holding company must file with the Federal Reserve Board a declaration of its intention to become a financial holding company. To date, the Corporation has not filed a declaration to become a financial holding company, and qualification as such by other bank holding companies has not had a material effect on the Corporation's or the Bank's business.

Confidentiality and Required Disclosures of Customer Information. The Corporation is subject to various laws and regulations that address the privacy of nonpublic personal financial information of consumers. The GLBA and certain regulations issued thereunder protect against the transfer and use by financial institutions of consumer nonpublic personal information. A financial institution must provide to its customers, at the beginning of the customer relationship and annually thereafter, the institution's policies and procedures regarding the handling of customers' nonpublic personal financial information. These privacy provisions generally prohibit a financial institution from providing a customer's personal financial information to unaffiliated third parties unless the institution discloses to the customer that the information may be so provided and the customer is given the opportunity to opt out of such disclosure.

The Corporation is also subject to various laws and regulations that attempt to combat money laundering and terrorist financing. The Bank Secrecy Act requires all financial institutions to, among other things, create a system of controls designed to prevent money laundering and the financing of terrorism, and imposes recordkeeping and reporting requirements. The USA Patriot Act facilitates information sharing among governmental entities and financial institutions for the purpose of combating terrorism and money laundering, and requires financial institutions to establish anti-money laundering programs. The Federal Bureau of Investigation (FBI) sends banking regulatory agencies lists of the names of persons suspected of involvement in terrorist activities, and requests banks to search their records for any relationships or transactions with persons on those lists. If the Bank finds any relationships or transactions, it must file a suspicious activity report with the U.S. Department of the Treasury (the Treasury) and contact the FBI. The Office of Foreign Assets Control (OFAC), which is a division of the Treasury, is responsible for helping to ensure that United States entities do not engage in transactions with "enemies" of the United States, as defined by various Executive Orders and Acts of Congress. If the Bank finds a name of an "enemy" of the United States on any transaction, account or wire transfer that is on an OFAC list, it must freeze such account or place transferred funds into a blocked account, file a suspicious activity report with the Treasury and notify the FBI.

Although these laws and programs impose compliance costs and create privacy obligations and, in some cases, reporting obligations, and compliance with all of the laws, programs, and privacy and reporting obligations may require significant resources of the Corporation and the Bank, these laws and programs do not materially affect the Bank's products, services or other business activities.

Stress Testing. As required by the Dodd-Frank Act, the federal banking agencies have implemented stress testing requirements for certain financial institutions, including bank holding companies and state chartered banks, with more than \$10 billion in total consolidated assets. Although these requirements do not apply to institutions with less than

\$10 billion in total consolidated assets, the federal banking agencies emphasize that all banking organizations, regardless of size, should have the capacity to analyze the potential effect of adverse market conditions or outcomes on the organization's financial condition. Based on existing regulatory guidance, the Corporation and the Bank will be expected to consider the institution's interest rate risk management, commercial real estate loan concentrations and other credit-related information, and funding and liquidity management during this analysis of adverse market conditions or outcomes.

**Volcker Rule.** The Dodd-Frank Act prohibits bank holding companies and their subsidiary banks from engaging in proprietary trading except in limited circumstances, and places limits on ownership of equity investments in private equity and hedge funds (the Volcker Rule). On December 10, 2013, the U.S. financial regulatory agencies (including the Federal Reserve Board, the FDIC and the SEC) adopted final rules to implement the Volcker Rule. Among other things, these final rules would have prohibited banking entities from owning collateralized debt obligations (CDOs) backed by trust preferred securities (TruPS), effective July 21, 2015. However, subsequent to these final rules the U.S. financial regulatory agencies issued an interim rule effective April 1, 2014 to exempt CDOs backed by TruPS from the final rule implementing the Volcker Rule, provided that (a) the CDO was established prior to May 19, 2010, (b) the banking entity reasonably believes that the CDO's offering proceeds were used to invest primarily in TruPS issued by banks with less than \$15 billion in assets, and (c) the banking entity acquired the CDO investment on or before December 10, 2013. Neither the Corporation

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nor the Bank currently has any CDO investments, and the Corporation believes that its financial condition will not be significantly affected by the Volcker Rule, the final rule or the interim rule. Several portions of the Volcker Rule remain subject to regulatory rulemaking and legislative activity, including to further delay effectiveness of some provisions of the Volcker Rule. The Corporation and the Bank do not expect that any delays in the effectiveness of a portion of the Volcker Rule will significantly affect the Corporation's or the Bank's financial condition.

Future Regulation

From time to time, various legislative and regulatory initiatives are introduced in Congress and state legislatures, as well as by regulatory agencies. Such initiatives may include proposals to expand or contract the powers of bank holding companies and depository institutions or proposals to substantially change the financial institution regulatory system. Such legislation could change banking statutes and the operating environment of the Corporation in substantial and unpredictable ways. If enacted, such legislation could increase or decrease the cost of doing business, limit or expand permissible activities or affect the competitive balance among banks, savings associations, credit unions, and other financial institutions. The Corporation cannot predict whether any such legislation will be enacted, and, if enacted, the effect that it, or any implementing regulations, would have on the financial condition or results of operations of the Corporation. A change in statutes, regulations or regulatory policies applicable to the Corporation or any of its subsidiaries could have a material effect on the business of the Corporation.

Available Information

The Corporation's SEC filings are filed electronically and are available to the public over the Internet at the SEC's web site at <http://www.sec.gov>. In addition, any document filed by the Corporation with the SEC can be read and copied at the SEC's public reference facilities at 100 F Street, N.E., Room 1580, 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. The Corporation's SEC filings also are available through our web site at <http://www.cffc.com> under "Investor Relations/SEC Filings" as of the day they are filed with the SEC. Copies of documents also can be obtained free of charge by writing to the Corporation's secretary at P.O. Box 391, West Point, VA 23181 or by calling 804-843-2360.

ITEM 1A.RISK FACTORS

Deterioration in the soundness of our counterparties or disruptions to credit markets could adversely affect us.

Our ability to engage in routine funding transactions could be adversely affected by the actions and commercial soundness of other financial institutions. Financial services institutions are interrelated as a result of trading, clearing, counterparty or other relationships, and we routinely execute transactions with counterparties in the financial industry, including brokers and dealers, commercial banks, and other institutional clients. As a result, defaults by, or even rumors or questions about, one or more financial services institutions, or the financial services industry generally, could create another market-wide liquidity crisis similar to that experienced in late 2008 and early 2009 and could lead to losses or defaults by us or by other institutions. In addition, over the last several years, developments in the global or national economies or financial markets have caused temporary disruptions in the credit and liquidity markets, which at times has restricted the flow of capital to credit markets and financial institutions, and future disruptions could restrict our ability to engage in routine funding transactions and adversely affect our liquidity. There is no assurance that the failure of our counterparties would not materially adversely affect the Corporation's results of operations.

Compliance with laws, regulations and supervisory guidance, both new and existing, may adversely affect our business, financial condition and results of operations.

We are subject to numerous laws, regulations and supervision from both federal and state agencies. During the past few years, there has been an increase in legislation related to and regulation of the financial services industry. We expect this increased level of oversight to continue. Failure to comply with these laws and regulations could result in financial, structural and operational penalties, including receivership. In addition, establishing systems and processes to achieve

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compliance with these laws and regulations may increase our costs and/or limit our ability to pursue certain business opportunities.

Laws and regulations, and any interpretations and applications with respect thereto, generally are intended to benefit consumers, borrowers and depositors, not stockholders. The legislative and regulatory environment is beyond our control, may change rapidly and unpredictably and may negatively influence our revenues, costs, earnings, and capital levels. Our success depends on our ability to maintain compliance with both existing and new laws and regulations.

The Dodd-Frank Act could continue to increase our regulatory compliance burden and associated costs, place restrictions on certain products and services, and limit our future capital raising strategies.

A wide range of regulatory initiatives directed at the financial services industry have been proposed in recent years. One of those initiatives, the Dodd-Frank Act, represents a sweeping overhaul of the financial services industry regulatory environment within the United States and mandates significant changes in the financial regulatory landscape that will affect all financial institutions, including the Corporation. The Dodd-Frank Act has increased and will likely continue to increase our regulatory compliance burden and may have a material adverse effect on us, by increasing the costs associated with our regulatory examinations and compliance measures. The federal regulatory agencies, and particularly bank regulatory agencies, have been given significant discretion in drafting the Dodd-Frank Act's implementing rules and regulations, many of which have not been finalized. Consequently, many of the details and much of the impact of the Dodd-Frank Act will depend on the final implementing rules and regulations, and it remains too early to fully assess the complete effect of the Dodd-Frank Act and related regulatory rulemaking processes on our business, financial condition or results of operations.

The Dodd-Frank Act increases regulatory supervision and examination of bank holding companies and their banking and non-banking subsidiaries, which could increase our regulatory compliance burden and costs and restrict our ability to generate revenues from non-banking operations. The Dodd-Frank Act imposes more stringent capital requirements on bank holding companies, which when considered in connection with the Basel III Final Rules and related regulatory capital rules and proposals could significantly limit our future capital strategies. The Dodd-Frank Act also increases regulation of derivatives and hedging transactions, which could limit our ability to enter into, or increase the costs associated with, interest rate hedging transactions.

The Consumer Financial Protection Bureau may increase our regulatory compliance burden and could affect the consumer financial products and services that we offer.

Among the Dodd-Frank Act's significant regulatory changes, the Dodd-Frank Act creates a new financial consumer protection agency that could impose new regulations on us and include its examiners in our routine regulatory examinations conducted by the FDIC, which could increase our regulatory compliance burden and costs and restrict the financial products and services we can offer to our customers. This agency, named the Consumer Financial Protection Bureau (CFPB), may reshape the consumer financial laws through rulemaking and enforcement of the Dodd-Frank Act's prohibitions against unfair, deceptive and abusive consumer finance products or practices, which may directly affect the business operations of financial institutions offering consumer financial products or services, including the Corporation. This agency's broad rulemaking authority includes identifying practices or acts that are unfair, deceptive or abusive in connection with any consumer financial transaction or consumer financial product or service. Although the CFPB has jurisdiction over banks with \$10 billion or greater in assets, rules, regulations and policies issued by the CFPB may also apply to the Corporation or its subsidiaries by virtue of the adoption of such policies and best practices by the Federal Reserve and the FDIC. Further, the CFPB may include its own examiners in regulatory examinations by the Corporation's primary regulators. The costs and limitations related to this additional regulatory agency and the limitations and restrictions that will be placed upon the Corporation with respect to its consumer product and service offerings have yet to be determined. However, these costs, limitations and restrictions may produce significant, material effects on our business, financial condition and results of operations.



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The Basel III Final Rules will require higher levels of capital and liquid assets, which could adversely affect the Corporation's net income and return on equity.

The Basel III Final Rules represent the most comprehensive overhaul of the U.S. banking capital framework in over two decades. This new capital framework and related changes to the standardized calculations of risk-weighted assets are complex and create additional compliance burdens, especially for community banks. The Basel III Final Rules require bank holding companies and their subsidiaries, such as the Corporation and C&F Bank, to maintain significantly more capital as a result of higher required capital levels and more demanding regulatory capital risk weightings and calculations. As a result of the Basel III Final Rules, many community banks could be forced to limit banking operations and activities, and growth of loan portfolios, in order to focus on retention of earnings to improve capital levels. The Corporation believes that it maintains sufficient levels of Tier 1 and Common Equity Tier 1 capital to comply with the Basel III Final Rules. However, the Corporation can offer no assurances with regard to the ultimate effect of the Basel III Final Rules, and satisfying increased capital requirements imposed by the Basel III Final Rules may require the Corporation to limit its banking operations, retain net income or reduce dividends to improve regulatory capital levels, which could negatively affect our business, financial condition and results of operations.

Our deposit insurance premiums could increase in the future, which may adversely affect our future financial performance.

The FDIC insures deposits at FDIC insured financial institutions, including the Bank. The FDIC charges insured financial institutions premiums to maintain the DIF at a certain level. Economic conditions since 2008 have increased the rate of bank failures and expectations for further bank failures, requiring the FDIC to make payments for insured deposits from the DIF and prepare for future payments from the DIF.

On February 7, 2011, the FDIC adopted final rules to implement changes required by the Dodd-Frank Act with respect to the FDIC assessment rules, which became effective April 1, 2011. A depository institution's deposit insurance assessment is now calculated based on the institution's total assets less tangible equity, rather than the previous base of total deposits. While the Corporation's FDIC insurance assessments have declined as a result of this change, the Bank's FDIC insurance premiums could increase if the Bank's asset size increases, if the FDIC raises base assessment rates, or if the FDIC takes other actions to replenish the DIF.

Our earnings are significantly affected by the fiscal and monetary policies of the federal government and its agencies.

The policies of the Federal Reserve affect us significantly. The Federal Reserve regulates the supply of money and credit in the United States. Its policies directly and indirectly influence the rate of interest earned on loans and paid on

borrowings and interest-bearing deposits and can also affect the value of financial instruments we hold. Those policies determine to a significant extent our cost of funds for lending and investing. Changes in those policies are beyond our control and are difficult to predict. Federal Reserve policies can also affect our borrowers, potentially increasing the risk that they may fail to repay their loans. For example, a tightening of the money supply by the Federal Reserve could reduce the demand for a borrower's products and services. This could adversely affect the borrower's earnings and ability to repay a loan, which could have a material adverse effect on our financial condition and results of operations.

We are subject to interest rate risk and fluctuations in interest rates may negatively affect our financial performance.

Our profitability depends in substantial part on our net interest margin, which is the difference between the interest earned on loans, securities and other interest-earning assets, and interest paid on deposits and borrowings divided by total interest-earning assets. Changes in interest rates will affect our net interest margin in diverse ways, including the pricing of loans and deposits, the levels of prepayments and asset quality. We are unable to predict actual fluctuations of market interest rates because many factors influencing interest rates are beyond our control. We attempt to minimize our exposure to interest rate risk, but we are unable to eliminate it. We believe that our current interest rate exposure is manageable and does not indicate any significant exposure to interest rate changes. The Federal Reserve's Federal Open Market Committee has stated it will keep the federal funds target rate at 0%-0.25% until economic, inflation and labor conditions improve. While such a continuance of accommodative monetary policy could allow us to continue to reprice a portion of our fixed-rate deposits at lower rates, sustained low interest rates could put further pressure on the yields generated by our loan

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portfolio and on our net interest margin. There is no guarantee we will continue to be able to reprice deposits at favorable rates as competition for deposits from both local and national financial institutions is intense, and continued pressure on our asset yields and net interest margin could adversely affect our results of operations.

In addition, a significant portion of C&F Finance's funding is indexed to short-term interest rates and reprices as short-term interest rates change. An upward movement in interest rates may result in an unfavorable pricing disparity between C&F Finance's fixed rate loan portfolio and its adjustable-rate borrowings.

Our business is subject to various lending and other economic risks that could adversely affect our results of operations and financial condition.

Deterioration in economic conditions, such as the recent recession could hurt our business. Our business is directly affected by general economic and market conditions; broad trends in industry and finance; legislative and regulatory changes; changes in governmental monetary and fiscal policies; and inflation, all of which are beyond our control. A deterioration in economic conditions, in particular a prolonged economic slowdown within our geographic region, could result in the following consequences, any of which could hurt our business materially: an increase in loan delinquencies; an increase in problem assets and foreclosures; a decline in demand for our products and services; and a deterioration in the value of collateral for loans made by our various business segments.

Our level of credit risk is higher due to the concentration of our loan portfolio in commercial loans and in consumer finance loans.

At December 31, 2014, 37 percent of our loan portfolio consisted of commercial, financial and agricultural loans, which include loans secured by real estate for builder lines, acquisition and development and commercial development, as well as commercial loans secured by personal property. These loans generally carry larger loan balances and involve a greater degree of financial and credit risk than home equity and residential loans. The increased financial and credit risk associated with these types of loans is a result of several factors, including the concentration of principal in a limited number of loans and to borrowers in similar lines of business, the size of loan balances, the effects of general economic conditions on income-producing properties and the increased difficulty of evaluating and monitoring these types of loans.

At December 31, 2014, 34 percent of our loan portfolio consisted of consumer finance loans that provide automobile financing for customers in the non-prime market. During periods of economic slowdown or recession, delinquencies, defaults, repossessions and losses may increase in this portfolio. Significant increases in the inventory of used automobiles during periods of economic recession may also depress the prices at which we may sell repossessed

automobiles or delay the timing of these sales. Because we focus on non-prime borrowers, the actual rates of delinquencies, defaults, repossessions and losses on these loans are higher than those experienced in the general automobile finance industry and could be dramatically affected by a general economic downturn. In addition, our servicing costs may increase without a corresponding increase in our finance charge income. While we manage the higher risk inherent in loans made to non-prime borrowers through our underwriting criteria for installment sales contracts we purchase and collection methods, we cannot guarantee that these criteria or methods will ultimately provide adequate protection against these risks.

Competition from other financial institutions and financial intermediaries may adversely affect our profitability.

We face substantial competition in originating loans and in attracting deposits. Our competition in originating loans and attracting deposits comes principally from other banks, mortgage banking companies, consumer finance companies, savings associations, credit unions, brokerage firms, insurance companies and other institutional lenders and purchasers of loans. Additionally, banks and other financial institutions with larger capitalization and financial intermediaries not subject to bank regulatory restrictions have larger lending limits and are thereby able to serve the credit needs of larger clients. These institutions may be able to offer the same loan products and services that we offer at more competitive rates and prices. Increased competition could require us to increase the rates we pay on deposits or lower the rates we offer on loans, which could adversely affect our profitability.

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Weakness in the secondary residential mortgage loan markets will adversely affect income from our mortgage company.

One of the components of our strategic plan is to generate significant noninterest income from C&F Mortgage, which originates a variety of residential loan products for sale into the secondary market to investors. Interest rates, low housing inventory, cash buyers, new mortgage lending regulations and other market conditions have resulted in reduced originations across the industry during 2014. C&F Mortgage was not immune to these factors, as its production declined as well.

In addition, credit markets have continued to experience difficult conditions and volatility. While payment defaults by borrowers and mortgage loan foreclosures may have abated, the agencies and investors continue to submit claims in an attempt to minimize their losses. This may result in potential repurchase or indemnification liability to C&F Mortgage on residential mortgage loans originated and sold into the secondary market in the event of claims by investors of borrower misrepresentation, fraud, early-payment default, or underwriting error, as investors attempt to minimize their losses. We cannot be assured that a prolonged period of payment defaults and foreclosures will not result in an increase in requests for repurchases or indemnifications, or that established reserves will be adequate, which could adversely affect the Corporation's net income.

Our home lending profitability could be significantly reduced if we are not able to originate and sell a high volume of mortgage loans.

One of the components of our strategic plan is to generate significant noninterest income from C&F Mortgage, which originates a variety of single-family residential loan products for sale to investors in the secondary market. The existence of an active secondary market is dependent upon the continuation of programs currently offered by government-sponsored enterprises (GSEs) (such as Fannie Mae and Freddie Mac), the FHA, the VA, the USDA, and state bond programs, which account for a substantial portion of the secondary market in residential mortgage loans. Because the largest participants in the secondary market are GSEs whose activities are governed by federal law, any future changes in laws that significantly affect the activity of the GSEs could adversely affect our mortgage company's operations. Further, in September 2008, Fannie Mae and Freddie Mac were placed into conservatorship by the U.S. government. Although to date, the conservatorship has not had a significant or adverse effect on our operations, it is unclear whether further changes or reforms would adversely affect our operations. Although we sell loans to various intermediaries, the ability of these aggregators to purchase loans would be limited if the GSEs cease to exist or materially limit their purchases of mortgage loans.

Pursuant to the Dodd-Frank Act and the subsequent final rules issued by the CFPB in January 2013 amending Regulation Z, as implemented by the Truth in Lending Act, effective January 2014 mortgage lenders are responsible for making 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. These CFPB rules require a mortgage lender to either (i) originate "qualified mortgages," defined as loans that do not include negative amortization, interest-only payments, balloon payments, or terms longer than 30 years; or (ii) originate loans that consider eight separate underwriting factors that are identified in the CFPB rules to evaluate each borrower's ability to repay. These CFPB rules, in addition to other previously-issued and to-be-issued CFPB regulations, could materially affect our ability to originate and sell a high volume of mortgage loans, which could adversely affect our financial condition and results of operations.

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An increase in interest rates may reduce our mortgage revenues, which would negatively impact our noninterest income.

Our Mortgage Banking segment provides a significant portion of our noninterest income. We generate gains on sales of mortgage loans primarily from sales of mortgage loans that we originate to investors. In a rising or higher interest rate environment, our originations of mortgage loans may decrease, resulting in fewer loans that are available to be sold to investors. This would result in a decrease in noninterest income. In addition, our results of operations are affected by the amount of noninterest expenses associated with mortgage banking activities, such as salaries and employee benefits. During periods of reduced loan demand, our results of operations may be adversely affected to the extent that we are unable to reduce expenses commensurate with the decline in mortgage loan origination activity.

If our allowance for loan losses becomes inadequate, our results of operations may be adversely affected.

Making loans is an essential element of our business. The risk of nonpayment is affected by a number of factors, including but not limited to: the duration of the credit; credit risks of a particular customer; changes in economic and industry conditions; and, in the case of a collateralized loan, risks resulting from uncertainties about the future value of the collateral. Although we seek to mitigate risks inherent in lending by adhering to specific underwriting practices, our loans may not be repaid. We attempt to maintain an appropriate allowance for loan losses to provide for losses in our loan portfolio. Our allowance for loan losses is determined by analyzing historical loan losses for relevant periods of time, current trends in delinquencies and charge-offs, current economic conditions that may affect a borrower's ability to repay and the value of collateral, changes in the size and composition of the loan portfolio and industry information. Also included in our estimates for loan losses are considerations with respect to the effect of economic events, the outcome of which are uncertain. Because any estimate of loan losses is necessarily subjective and the accuracy of any estimate depends on the outcome of future events, we face the risk that charge-offs in future periods will exceed our allowance for loan losses and that additional increases in the allowance for loan losses will be required. Additions to the allowance for loan losses would result in a decrease of our net income. Although we believe our allowance for loan losses is adequate to absorb probable losses in our loan portfolio, we cannot predict such losses or that our allowance will be adequate in the future.

Our real estate lending business can result in increased costs associated with foreclosed properties.

Because we originate loans secured by real estate, we may have to foreclose on the collateral property to protect our investment and may thereafter own and operate such property, in which case we are exposed to the risks inherent in the ownership of real estate. The amount that we, as a mortgagee, may realize after a default is dependent upon factors outside of our control, included, but not limited to general or local economic conditions, environmental cleanup liability, neighborhood values, interest rates, real estate tax rates, operating expenses of the mortgaged properties, and supply of and demand for properties. Certain expenditures associated with the ownership of income-producing real

estate, principally real estate taxes and maintenance costs, may adversely affect the net cash flows generated by the real estate. Therefore, the cost of operating income-producing real property may exceed the rental income earned from such property, and we may have to advance funds in order to protect our investment or we may be required to dispose of the real property at a loss.

We may incur losses on purchased loans that are materially greater than reflected in our fair value adjustments.

We accounted for the CVBK acquisition under the acquisition method of accounting, recording the acquired assets and liabilities of CVBK at fair value based on acquisition accounting adjustments. We recorded at fair value all purchased credit-impaired loans acquired based on the present value of their expected cash flows. We estimated cash flows using specific credit reviews of certain loans, quantitative credit risk, interest rate risk and prepayment risk models, and qualitative economic and environmental assessments, each of which uses assumptions about matters that are inherently uncertain, and involves the exercise of our best judgment in making those assumptions. We may not realize the estimated cash flows or fair value of these loans. In addition, although the difference between the pre-acquisition carrying value of purchased credit-impaired loans and their expected cash flows - the nonaccretable difference - is available to absorb future charge-offs, we may be required to increase our allowance for loan losses and related provision expense due to subsequent additional credit deterioration in these loans.

For more information see, "Critical Accounting Policies - Purchased Credit-Impaired Loans" in Item 7. "Management's Discussion and Analysis of Financial Condition and Results of Operations" in this report.



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Acquisition of CVBK's assets and assumption of CVBK's liabilities may expose us to intangible asset risk, which could affect our result of operations and financial condition.

In connection with accounting for the acquisition of CVBK, we recorded assets acquired and liabilities assumed at their fair value, which resulted in us recording certain intangible assets, including goodwill. Adverse conditions in our business climate, including a significant decline in future operating cash flows, a significant change in our stock price or market capitalization, or a deviation from our expected growth rate and performance, may significantly affect the fair value of any goodwill (including goodwill related to the CVBK acquisition) and may trigger impairment losses, which could be materially adverse to our results of operations, financial condition and stock price.

We are subject to security and operational risks relating to our use of technology that could damage our reputation and our business.

In the ordinary course of business, the Corporation collects and stores sensitive data, including proprietary business information and personally identifiable information of our customers and employees, in systems and on networks. The secure processing, maintenance and use of this information is critical to operations and the Corporation's business strategy. The Corporation has invested in information security technologies and continually reviews processes and practices that are designed to protect its networks, computers and data from damage or unauthorized access. Despite these security measures, the Corporation's computer systems and infrastructure may be vulnerable to attacks by hackers or breached due to employee error, malfeasance or other disruptions. Security breaches, including cyber incidents and hacking events, have been experienced by several of the world's largest financial institutions that utilize sophisticated security tools to prevent such breaches, incidents and events. Any security breach that we experience could expose us to possible liability and damage our reputation. We rely on standard security systems and procedures to provide the security and authentication necessary to effect secure collection, transmission and storage of sensitive data. These systems and procedures include but are not limited to (i) regular penetration testing of our network perimeter, (ii) regular employee training programs on sound security practices, (iii) deployment of tools to monitor our network including intrusion prevention and detection systems, electronic mail spam filters, anti-virus and anti-malware, resource logging and patch management, (iv) multifactor authentication for customers using treasury management tools, and (v) enforcement of security policies and procedures for the additions and maintenance of user access and rights to resources.

While most of our core data processing is conducted internally, certain key applications are outsourced to third party providers. If our third party providers encounter difficulties or if we have difficulty in communicating with such third parties, it will significantly affect our ability to adequately process and account for customer transactions, which would significantly affect our business operations. Additionally, in recent years banking regulators have focused on the responsibilities of financial institutions to supervise vendors and other third-party service providers. We may have to dedicate significant resources to manage risks and regulatory burdens presented by our relationship with vendors and third-party service providers, including our data processing and cybersecurity service providers.

Our business is technology dependent and an inability to invest in technological improvements may adversely affect results of operations and financial condition.

The financial services industry is undergoing rapid technological changes with frequent introductions of new technology-driven products and services, which may require substantial capital expenditures to modify or adapt existing products and services. In addition to better customer service, the effective use of technology increases efficiency and results in reduced costs. Our future success will depend in part upon our ability to create synergies in our operations through the use of technology. Many competitors have substantially greater resources to invest in technological improvements. We cannot assure that technological improvements will increase operational efficiency or that we will be able to effectively implement new technology-driven products and services or be successful in marketing these products and services to our customers.

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Changes in accounting standards and management's selection of accounting methods, including assumptions and estimates, could materially affect our financial statements.

From time to time, the SEC and the Financial Accounting Standards Board (FASB) change the financial accounting and reporting standards that govern the preparation of the Corporation's financial statements. These changes can be hard to predict and can materially affect how the Corporation records and reports its financial condition and results of operations. In some cases, the Corporation could be required to apply a new or revised standard retroactively, resulting in changes to previously reported financial results, or a cumulative charge to retained earnings. In addition, management is required to use certain assumptions and estimates in preparing our financial statements, including determining the fair value of certain assets and liabilities, among other items. If the assumptions or estimates are incorrect, the Corporation may experience unexpected material consequences.

We rely heavily on our management team and the unexpected loss of key officers may adversely affect our operations.

We believe that our growth and future success will depend in large part on the skills of our executive officers. We also depend upon the experience of the officers of our subsidiaries and on their relationships with the communities they serve. The loss of the services of one or more of these officers could disrupt our operations and impair our ability to implement our business strategy, which could adversely affect our business, financial condition and results of operations.

The success of our business strategies depends on our ability to identify and recruit individuals with experience and relationships in our primary markets.

The successful implementation of our business strategy will require us to continue to attract, hire, motivate and retain skilled personnel to develop new customer relationships as well as new financial products and services. The market for qualified management personnel is competitive. In addition, the process of identifying and recruiting individuals with the combination of skills and attributes required to carry out our strategy is often lengthy. Our inability to identify, recruit and retain talented personnel to manage our operations effectively and in a timely manner could limit our growth, which could materially adversely affect our business.

Our corporate culture has contributed to our success, and if we cannot maintain this culture as we grow, we could lose the beneficial aspects fostered by our culture, which could harm our business.

We believe that a critical contributor to our success has been our corporate culture, which focuses on building personal relationships with our customers. As our organization grows, and we are required to implement more complex organizational management structures, we may find it increasingly difficult to maintain the beneficial aspects of our corporate culture. This could negatively affect our future success.

Our common stock price may be volatile, which could result in losses to our investors.

Our common stock price has been volatile in the past and several factors could cause the price to fluctuate in the future. These factors include, but are not limited to, actual or anticipated variations in earnings, changes in analysts' recommendations or projections with regard to our common stock or the markets and businesses in which we operate, operations and stock performance of other companies deemed to be peers, and reports of trends and concerns and other issues related to the financial services industry. Fluctuations in our common stock price may be unrelated to our performance. General market declines or market volatility in the future, especially in the financial institutions sector, could adversely affect the price of our common stock, and the current market price may not be indicative of future market prices.

Future sales of our common stock by shareholders or the perception that those sales could occur may cause our common stock price to decline.

Although our common stock is listed for trading on NASDAQ Global Select Market, the trading volume in our common stock may be lower than that of other larger financial institutions. A public trading market having the desired characteristics of depth, liquidity and orderliness depends on the presence in the marketplace of willing buyers and sellers of the common stock at any given time. This presence depends on the individual decisions of investors and general

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economic and market conditions over which we have no control. Given the potential for lower relative trading volume in our common stock, significant sales of the common stock in the public market, or the perception that those sales may occur, could cause the trading price of our common stock to decline or to be lower than it otherwise might be in the absence of these sales or perceptions.

ITEM 1B.UNRESOLVED STAFF COMMENTS

The Corporation has no unresolved comments from the SEC staff.

ITEM 2.PROPERTIES

The following describes the location and general character of the principal offices and other materially important physical properties of the Corporation.

C&F Bank owns a building located at Eighth and Main Streets in the business district of West Point, Virginia. The building, originally constructed in 1923, has three floors totaling 15,000 square feet. This building houses C&F Bank's Main Office and the main office of C&F Investment Services.

C&F Bank owns a building located at 3600 LaGrange Parkway in Toano, Virginia. The building was acquired in 2004 and has 85,000 square feet. Portions of the building were renovated in 2005 and 2014 in order to house the C&F Bank's operations center, which consists of C&F Bank's loan, deposit and administrative functions and staff.

The building owned by C&F Bank and previously used for the its loan operations at Sixth and Main Streets in West Point, Virginia, which is a 5,000 square foot building acquired and remodeled by the Corporation in 1998, has been retained as back-up facilities for the Toano operations center. Management has not yet determined the long-term utilization of this property.

C&F Bank owns a building located at 1400 Alverser Drive in Midlothian, Virginia. The building provides space for a branch office of C&F Bank and for a C&F Mortgage branch office, as well as C&F Mortgage's main administrative offices. This two-story building has 25,000 square feet and was constructed in 2001.

C&F Bank owns 23 other retail banking branch locations and leases one retail banking branch location and one regional commercial lending office in Virginia. Rental expense for leased locations totaled \$141,000 for the year ended December 31, 2014.

C&F Bank owns a building located at 2036 New Dorset Road in Powhatan, Virginia. The building was built in 1996 and has three floors totaling 14,000 square feet that had previously housed CVB's operations center. The building is currently utilized as an additional training and backup facility.

C&F Mortgage's Newport News loan production office is located on the second floor of C&F Bank's Newport News branch building. In addition, C&F Mortgage has 14 loan production offices leased from nonaffiliates including 10 in Virginia, two in Maryland, and two in North Carolina. Rental expense for leased locations totaled \$774,000 for the year ended December 31, 2014.

The Hampton office of C&F Finance is located on the second floor of C&F Bank's Hampton branch building. C&F Finance has a lease agreement with an unrelated third party for approximately 17,000 square feet of office space in Richmond, Virginia, which is being used for C&F Finance's headquarters and its loan and administrative functions and staff. C&F Finance has two leased offices, one each in Maryland and Tennessee. Rental expense for leased locations totaled \$325,000 for the year ended December 31, 2014.

All of the Corporation's properties are in good operating condition and are adequate for the Corporation's present and anticipated future needs.

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ITEM 3.LEGAL PROCEEDINGS

The Corporation and its subsidiaries may be involved in certain litigation matters arising in the ordinary course of business. Although the ultimate outcome of these matters cannot be ascertained at this time, and the results of legal proceedings cannot be predicted with certainty, we believe, based on current knowledge, that the resolution of any such matters arising in the ordinary course of business will not have a material adverse effect on the Corporation.

ITEM 4.MINE SAFETY DISCLOSURES

None.

EXECUTIVE OFFICERS OF THE REGISTRANT

Name (Age)	Business Experience
Present Position	During Past Five Years
<p>Larry G. Dillon (62) Chairman and Chief Executive Officer</p>	<p>Chairman and Chief Executive Officer of the Corporation and C&amp;F Bank since December 2014; Chairman, President and Chief Executive Officer of the Corporation and C&amp;F Bank from 1989 to December 2014; Chairman, President and Chief Executive Officer of CVBK and CVB from September 2013 through March 2014</p>
<p>Thomas F. Cherry (46) President, Chief Financial Officer and Secretary</p>	<p>Secretary of the Corporation and C&amp;F Bank since 2002; President and Chief Financial Officer of the Corporation and C&amp;F Bank since December 2014; Executive Vice President and Chief Financial Officer of the Corporation and C&amp;F Bank from December 2004 to December 2014; Executive Vice President and Chief Financial Officer of CVBK and CVB from September 2013 through March 2014</p>
<p>Bryan E. McKernon (58)  President and Chief Executive Officer,</p>	<p>President and Chief Executive Officer of C&amp;F Mortgage since 1995</p>

C&F Mortgage

John A. Seaman, III  
(57) Senior Vice President and Chief Credit Officer of C&F Bank since October 2011 and of CVB from September 2013 through March 2014; Director of Homebuilder Banking-Special Situations Group, Mid-Atlantic Region, Wells Fargo Bank, N.A., with particular responsibility for residential loan resolution and workouts from 2008 through September 2011

Senior Vice President  
and Chief Credit  
Officer,

C&F Bank

S. Dustin Crone (46) President of C&F Finance since 2010; Executive Vice President of C&F Finance from 2006 through 2009

President, C&F  
Finance

PART II

ITEM 5.MARKET FOR REGISTRANT’S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

The Corporation’s common stock is listed for trading on the NASDAQ Global Select Market of the NASDAQ Stock Market under the symbol “CFFI.” As of March 6, 2015, there were approximately 2,200 shareholders of record. As of that date, the closing price of our common stock on the NASDAQ Global Select Stock Market was \$35.80. Following are the



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high and low sales prices as reported by the NASDAQ Stock Market, along with the dividends that were declared quarterly in 2014 and 2013.

Quarter	2014			2013		
	High	Low	Dividends	High	Low	Dividends
First	\$ 45.88	\$ 32.13	\$ 0.29	\$ 42.00	\$ 36.80	\$ 0.29
Second	37.04	30.33	0.30	55.99	38.35	0.29
Third	36.99	32.61	0.30	59.59	48.06	0.29
Fourth	39.97	32.40	0.30	56.68	43.17	0.29

Payment of dividends is at the discretion of the Corporation's board of directors and is subject to various federal and state regulatory limitations. For further information regarding payment of dividends refer to Item 1, "Business," under the heading "Limits on Dividends."

#### Issuer Purchases of Equity Securities

The Corporation's Board of Directors has authorized a share repurchase program for the Corporation's outstanding common stock through May 2015 (the Repurchase Program). Repurchases under the Repurchase Program may be made through privately-negotiated transactions, or open-market transactions, including pursuant to a trading plan in accordance with Rule 10b5-1 of the Exchange Act and/or Rule 10b-18 of the Exchange Act. As of December 31, 2014, an additional \$4.9 million of the Corporation's common stock may be purchased under the Repurchase Program.

The following table summarizes repurchases of the Corporation's common stock that occurred during the three months ended December 31, 2014.

Total Number of Shares Purchased as Part of Publicly	Maximum (or Approximate) Dollar Value of Shares that May Be Purchased
------------------------------------------------------------	-----------------------------------------------------------------------------------

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(Dollars in thousands, except for per share amounts)	Total Number of Shares Purchased <sup>1</sup>	Average Price per Share	Under the Plans or Programs	Under the Plans or Programs
October 1, 2014 - October 31, 2014	234	\$ 33.01	—	\$ —
November 1, 2014 - November 30, 2014	—	—	—	—
December 1, 2014 - December 31, 2014	1,349	38.74	—	—
Total	1,583	\$ 37.89	—	\$ —

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<sup>1</sup> These shares were withheld from employees to satisfy tax withholding obligations arising upon the vesting of restricted shares.

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## ITEM 6. SELECTED FINANCIAL DATA

## Five Year Financial Summary

(Dollars in thousands, except share and per share amounts)	2014	2013	2012	2011	2010
<b>Selected Year-End Balances:</b>					
Total assets	\$ 1,333,323	\$ 1,312,297	\$ 977,018	\$ 928,124	\$ 904,137
Total shareholders' equity	123,373	112,941	102,197	96,090	92,777
Total loans (net)	800,198	785,532	640,283	616,984	606,744
Total deposits	1,026,101	1,008,292	686,184	646,416	625,134
<b>Summary of Operations:</b>					
Interest income	\$ 86,495	\$ 80,212	\$ 76,964	\$ 73,790	\$ 69,848
Interest expense	8,525	8,623	10,111	11,881	13,235
Net interest income	77,970	71,589	66,853	61,909	56,613
Provision for loan losses	16,330	15,085	12,405	14,160	14,959
Net interest income after provision for loan losses	61,640	56,504	54,448	47,749	41,654
Noninterest income	19,571	22,220	20,622	17,171	17,935
Noninterest expenses	64,135	57,612	51,042	46,209	48,530
Income before taxes	17,076	21,112	24,028	18,711	11,059
Income tax expense	4,730	6,710	7,646	5,735	2,949

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Net income	12,346	14,402	16,382	12,976	8,110					
Effective dividends on preferred stock	—	—	311	1,183	1,149					
Net income available to common shareholders	\$ 12,346	\$ 14,402	\$ 16,071	\$ 11,793	\$ 6,961					
Per share:										
Earnings per common share—basic	\$ 3.63	\$ 4.36	\$ 5.00	\$ 3.76	\$ 2.26					
Earnings per common share—assuming dilution	3.59	4.18	4.86	3.72	2.24					
Dividends	1.19	1.16	1.08	1.01	1.00					
Weighted average number of shares—assuming dilution	3,436,278	3,443,982	3,305,902	3,172,277	3,103,469					
Significant Ratios:										
Return on average assets	0.93	%	1.35	%	1.71	%	1.30	%	0.78	%
Return on average common equity	10.34		13.39		17.05		14.86		9.74	
Dividend payout ratio – common shares	32.80		26.61		21.60		26.86		44.25	
Average common equity to average assets	9.02		10.07		10.03		8.75		8.01	

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ITEM 7.MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Cautionary Statement Regarding Forward-Looking Statements

This report contains statements concerning the Corporation’s expectations, plans, objectives, future financial performance and other statements that are not historical facts. These statements may constitute “forward-looking statements” as defined by federal securities laws and may include, but are not limited to, statements regarding future financial performance, liquidity, strategic business initiatives, operating initiatives related to the acquisition of CVBK and continued integration of CVB into C&F Bank, the Corporation’s and each business segment’s loan portfolio, allowance for loan losses, trends regarding the provision for loan losses, trends regarding net loan charge-offs, trends regarding levels of nonperforming assets and troubled debt restructurings and expenses associated with nonperforming assets, provision for indemnification losses, levels of noninterest income and expense, interest rates and yields including possible future rising interest rate environments, the deposit portfolio including trends in deposit maturities and rates, interest rate sensitivity, market risk, regulatory developments, monetary policy implemented by the Federal Reserve Board including quantitative easing programs, capital requirements, growth strategy, hedging strategy and financial and other goals. These statements may address issues that involve estimates and assumptions made by management and risks and uncertainties. Actual results could differ materially from historical results or those anticipated by such statements. Factors that could have a material adverse effect on the operations and future prospects of the Corporation include, but are not limited to, changes in:

- interest rates, such as volatility in yields on U.S. Treasury bonds and increases or volatility in mortgage rates
- general business conditions, as well as conditions within the financial markets
- general economic conditions, including unemployment levels
- the legislative/regulatory climate, including the Dodd-Frank Act and regulations promulgated thereunder, the CFPB and the regulatory and enforcement activities of the CFPB and the Basel III Final Rules
- monetary and fiscal policies of the U.S. Government, including policies of the U.S. Treasury and the Federal Reserve Board, and the effect of these policies on interest rates and business in our markets
- the ability to achieve the operations and results expected after the CVBK acquisition, including anticipated cost savings, continued relationships with major customers and deposit retention, and the ability to effectively integrate CVB into C&F Bank

- the value of securities held in the Corporation's investment portfolios
  
- demand for loan products
  - the quality or composition of the loan portfolios and the value of the collateral securing those loans
  
- the commercial and residential real estate markets
  
- the inventory level and pricing of used automobiles, including sales prices of repossessed vehicles
  
- the level of net charge-offs on loans and the adequacy of our allowance for loan losses
  
- deposit flows
  
- demand in the secondary residential mortgage loan markets

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- the level of indemnification losses related to mortgage loans sold
- the strength of the Corporation's counterparties and the economy in general
- competition from both banks and non-banks
- demand for financial services in the Corporation's market area
- the Corporation's expansion and technology initiatives
- reliance on third parties for key services
- accounting principles, policies and guideline and elections by the Corporation thereunder

Our ability to engage in routine funding transactions could be adversely affected by the actions and commercial soundness of other financial institutions. Financial services institutions are interrelated as a result of trading, clearing, counterparty or other relationships, and we routinely execute transactions with counterparties in the financial industry, including brokers and dealers, commercial banks, and other institutions. As a result, defaults by, or even rumors or questions about defaults by, one or more financial services institutions, or the financial services industry generally, could create another market-wide liquidity crisis similar to that experienced in late 2008 and early 2009 and could lead to losses or defaults by us or by other institutions. There is no assurance that any such losses would not materially adversely affect the Corporation's results of operations.

There can be no assurance that the actions taken by the federal government and regulatory agencies will alleviate the industry or economic factors that may adversely affect the Corporation's business and financial performance. Further, many aspects of the Dodd-Frank Act remain subject to rulemaking and will take effect over several years, making it difficult to anticipate the overall effect on the Corporation's business and financial performance.

These risks and uncertainties, and the risks discussed in more detail in Item 1A, "Risk Factors," should be considered in evaluating the forward-looking statements contained herein. We caution readers not to place undue reliance on those statements, which speak only as of the date of this report.

The following discussion supplements and provides information about the major components of the results of operations, financial condition, liquidity and capital resources of the Corporation. This discussion and analysis should

be read in conjunction with the accompanying consolidated financial statements.

## CRITICAL ACCOUNTING POLICIES

The preparation of financial statements requires us to make estimates and assumptions. Those accounting policies with the greatest uncertainty and that require our most difficult, subjective or complex judgments affecting the application of these policies, and the likelihood that materially different amounts would be reported under different conditions, or using different assumptions, are described below.

**Allowance for Loan Losses:** We establish the allowance for loan losses through charges to earnings in the form of a provision for loan losses. Loan losses are charged against the allowance when we believe that the collection of the principal is unlikely. Subsequent recoveries of losses previously charged against the allowance are credited to the allowance. The allowance represents an amount that, in our judgment, will be adequate to absorb any losses on existing loans that may become uncollectible. Our judgment in determining the level of the allowance is based on evaluations of the collectibility of loans while taking into consideration such factors as trends in delinquencies and charge-offs, changes in the nature and volume of the loan portfolio, current economic conditions that may affect a borrower's ability to repay and the value of collateral, overall portfolio quality and review of specific potential losses. This evaluation is inherently subjective because it requires estimates that are susceptible to significant revision as more information becomes available. For more information see the section titled "Asset Quality" within Item 7.



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**Allowance for Indemnifications:** The allowance for indemnifications is established through charges to earnings in the form of a provision for indemnifications, which is included in other noninterest expenses. A loss is charged against the allowance for indemnifications under certain conditions when a purchaser of a loan (investor) sold by C&F Mortgage incurs a loss due to borrower misrepresentation, fraud, early default, or underwriting error. The allowance represents an amount that, in management's judgment, will be adequate to absorb any losses arising from indemnification requests. Management's judgment in determining the level of the allowance is based on the volume of loans sold, historical experience, current economic conditions and information provided by investors. This evaluation is inherently subjective, as it requires estimates that are susceptible to significant revision as more information becomes available.

**Impairment of Loans:** We consider a loan impaired when it is probable that the Corporation will be unable to collect all interest and principal payments as scheduled in the loan agreement. We do not consider a loan impaired during a period of delay in payment if we expect the ultimate collection of all amounts due. We measure impairment on a loan-by-loan basis for commercial, construction and residential loans in excess of \$500,000 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. Large groups of smaller balance homogeneous loans are collectively evaluated for impairment. We maintain a valuation allowance to the extent that the measure of the impaired loan is less than the recorded investment. Troubled debt restructurings (TDRs) are also considered impaired loans, even if the loan balance is less than \$500,000. A TDR occurs when we agree to significantly modify the original terms of a loan due to the deterioration in the financial condition of the borrower. For more information see the section titled "Asset Quality" within Item 7.

**Loans Acquired in a Business Combination:** The Corporation has accounted for the loans acquired in the acquisition of CVBK and its subsidiary CVB in accordance with FASB Accounting Standards Codification (ASC) Topic 805, Business Combinations. Accordingly, as of the acquisition, CVB's loans were segregated between (i) purchased credit-impaired (PCI) loans and (ii) purchased performing loans and were recorded at estimated fair value without the carryover of the related allowance for loan losses.

PCI loans are those for which there is evidence of credit deterioration since origination and for which it is probable at the date of acquisition that the Corporation will not collect all contractually required principal and interest payments. When determining fair market value, PCI loans were aggregated into pools of loans based on common risk characteristics as of the date of acquisition such as loan type, date of origination, and evidence of credit quality deterioration such as internal risk grades and past due and nonaccrual status. The difference between contractually required payments at acquisition and the cash flows expected to be collected at acquisition is referred to as the "nonaccretable difference," and is not recorded. Any excess of cash flows expected at acquisition over the estimated fair value is referred to as the "accretable" yield and is recognized as interest income over the remaining life of the loan when there is a reasonable expectation about the amount and timing of such cash flows. Subsequent decreases to the expected cash flows will generally result in a provision for loan losses, while subsequent increases in cash flows may result in a reversal of post-acquisition provision for loan losses, or a transfer from nonaccretable difference to accretable yield.

Subsequent to acquisition, we evaluate on a quarterly basis our estimate of cash flows expected to be collected. In the current economic environment, estimates of cash flows for PCI loans require significant judgment. Subsequent decreases to the expected cash flows will generally result in a provision for loan losses resulting in an increase to the allowance for loans losses. Subsequent significant increases in cash flows will generally result in an increase in interest income over the remaining life of the loan, or pool(s) of loans. Disposals of loans, which may include sale of loans to third parties, receipt of payments in full or part from the borrower or foreclosure of the collateral, result in removal of the loan from the PCI loan portfolio at its carrying amount.

The Corporation's PCI loans currently consist of loans acquired in connection with the acquisition of CVB. PCI loans that were classified as nonperforming loans by CVB are no longer classified as nonperforming so long as, at acquisition and quarterly re-estimation periods, we believe we will fully collect the new carrying value of the pools of loans.

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Purchased performing loans are recorded at fair value as of the acquisition using the contractual cash flows method of recognizing discount accretion based on the acquired loans' contractual cash flows. The fair value discount, including a credit discount, is accreted as an adjustment to yield over the estimated lives of the loans. There is no allowance for loan losses established at the acquisition date for purchased performing loans. A provision for loan losses may be required in future periods for any deterioration in these loans subsequent to the acquisition.

**Impairment of Securities:** Impairment of securities occurs when the fair value of a security is less than its amortized cost. For debt securities, impairment is considered other-than-temporary and recognized in its entirety in net income if either (i) we intend to sell the security or (ii) it is more-likely-than-not that we will be required to sell the security before recovery of its amortized cost basis. If, however, we do not intend to sell the security and it is not more-likely-than-not that we will be required to sell the security before recovery, we must determine what portion of the impairment is attributable to a credit loss, which occurs when the amortized cost basis of the security exceeds the present value of the cash flows expected to be collected from the security. If there is no credit loss, there is no other-than-temporary impairment. If there is a credit loss, other-than-temporary impairment exists, and the credit loss must be recognized in net income and the remaining portion of impairment must be recognized in other comprehensive income. For equity securities, impairment is considered to be other-than-temporary based on our ability and intent to hold the investment until a recovery of fair value. Other-than-temporary impairment of an equity security results in a write-down that must be included in net income. We regularly review each investment security for other-than-temporary impairment based on criteria that includes the extent to which cost exceeds market price, the duration of that market decline, the financial health of and specific prospects for the issuer, our best estimate of the present value of cash flows expected to be collected from debt securities, our intention with regard to holding the security to maturity and the likelihood that we would be required to sell the security before recovery.

**Other Real Estate Owned (OREO):** Assets acquired through, or in lieu of, loan foreclosure are held for sale and are initially recorded at the lower of the loan balance or the fair value less costs to sell at the date of foreclosure. Subsequent to foreclosure, management periodically performs valuations of the foreclosed assets based on updated appraisals, general market conditions, recent sales of like properties, length of time the properties have been held, and our ability and intention with regard to continued ownership of the properties. The Corporation may incur additional write-downs of foreclosed assets to fair value less costs to sell if valuations indicate a further other-than-temporary deterioration in market conditions.

**Goodwill:** The Corporation's goodwill was recognized in connection with the Corporation's acquisition of CVBK in October 2013 and C&F Bank's acquisition of C&F Finance Company in September 2002. With the adoption of Accounting Standards Update (ASU) 2011-08, Intangible-Goodwill and Other-Testing Goodwill for Impairment, in 2012, the Corporation may first assess qualitative factors to determine if it is more likely than not that the fair value of goodwill is less than the carrying amount, which determines if the two-step goodwill impairment test is necessary. If the likelihood of impairment is more than 50 percent, the Corporation must perform a test for impairment and we may be required to record impairment charges. In assessing the recoverability of the Corporation's goodwill, major assumptions used in determining impairment are increases in future income, sales multiples in determining terminal value and the discount rate applied to future cash flows. If an impairment test is performed, we will prepare a sensitivity analysis by increasing the discount rate, lowering sales multiples and reducing increases in future income.

Retirement Plan: C&F Bank maintains a non-contributory, defined benefit pension plan for eligible full-time employees as specified by the plan. Plan assets, which consist primarily of mutual funds invested in marketable equity securities and corporate and government fixed income securities, are valued using market quotations. C&F Bank's actuary determines plan obligations and annual pension expense using a number of key assumptions. Key assumptions may include the discount rate, the interest crediting rate, the estimated future return on plan assets and the anticipated rate of future salary increases. Changes in these assumptions in the future, if any, or in the method under which benefits are calculated may impact pension assets, liabilities or expense.

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**Derivative Financial Instruments:** The Corporation recognizes derivative financial instruments at fair value as either an other asset or other liability in the consolidated balance sheet. The Corporation's derivative financial instruments consist of (1) the fair value of interest rate lock commitments (IRLCs) on mortgage loans that will be held for sale and related forward sales commitments and (2) interest rate swaps that qualify as cash flow hedges of the Corporation's trust preferred capital notes. Because the IRLCs and forward sale commitments are not designated as hedging instruments, adjustments to reflect unrealized gains and losses resulting from changes in fair value of the Corporation's IRLCs and forward sales commitments and realized gains and losses upon ultimate sale of the loans are reported as noninterest income. The effective portion of the gain or loss on the Corporation's cash flow hedges is reported as a component of other comprehensive income, net of deferred taxes, and reclassified into earnings in the same period or periods during which the hedged transactions affect earnings.

**Accounting for Income Taxes:** Determining the Corporation's effective tax rate requires judgment. In the ordinary course of business, there are transactions and calculations for which the ultimate tax outcomes are uncertain. In addition, the Corporation's tax returns are subject to audit by various tax authorities. Although we believe that the estimates are reasonable, no assurance can be given that the final tax outcome will not be materially different than that which is reflected in the income tax provision and accrual.

For further information concerning accounting policies, refer to Item 8, "Financial Statements and Supplementary Data," under the heading "Note 1: Summary of Significant Accounting Policies."

## OVERVIEW

Our primary financial goals are to maximize the Corporation's earnings and to deploy capital in profitable growth initiatives that will enhance long-term shareholder value. We track three primary financial performance measures in order to assess the level of success in achieving these goals: (i) return on average assets (ROA), (ii) return on average common equity (ROE), and (iii) growth in earnings. In addition to these financial performance measures, we track the performance of the Corporation's three principal business activities: retail banking, mortgage banking, and consumer finance. We also actively manage our capital through growth, dividends and share repurchases, while considering the need to maintain a strong regulatory capital position.

On October 1, 2013, the Corporation acquired all of the outstanding common stock of CVBK. On March 22, 2014, CVBK was merged with and into the Corporation and CVB was merged with and into C&F Bank. The Corporation's financial position and results of operations as of and for the year ended December 31, 2014 include the acquired assets and assumed liabilities of CVBK that remain on the Corporation's balance sheet and the results of operating such assets and liabilities subsequent to the acquisition of CVBK.

Financial Performance Measures

Net income for the Corporation was \$12.3 million in 2014, or \$3.59 per common share assuming dilution compared with net income of \$14.4 million in 2013 or \$4.18 per common share assuming dilution. The change in financial results for 2014, as compared to 2013, was principally attributable to lower earnings at the Mortgage Banking and Consumer Finance segments, offset in part by an increase in earnings at the Retail Banking segment. At the Mortgage Banking segment, interest rates, low housing inventory, cash buyers, new mortgage lending regulations and other market conditions have led to weaker mortgage loan origination volume and correspondingly lower income from gains on sales of loans and ancillary mortgage lending fees during 2014. Partially offsetting the negative effects of the production decline was a decline in production-based compensation. At the Consumer Finance segment, higher net charge-offs attributable to (1) the continued difficult economic environment for non-prime consumers, (2) reduced sale prices on repossessed vehicles, (3) the effect of easing of underwriting standards by our competitors and (4) our borrowers willingness to default on their loans has resulted in a higher provision for loan losses during 2014, compared to 2013. The Retail Banking segment, which reported an increase in earnings during 2014, compared to 2013, benefited from (1) fair value accounting adjustments associated with the acquisition of CVBK, (2) the effect of the continued low interest rate environment on the costs of deposits, (3) a decline in the provision for loan losses as a result of improvement in asset quality, and (4) a decline in expenses associated with other real estate owned as a result of the sale of a majority of these properties since December 31, 2013.

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See “Principal Business Activities” below for additional discussion.

The Corporation’s ROE and ROA were 10.34 percent and 0.93 percent, respectively, for the year ended December 31, 2014, compared to 13.39 percent and 1.35 percent, respectively, for the year ended December 31, 2013. The decrease in these ratios during 2014 resulted primarily from lower net income during 2014. The decline in ROE was also affected by internal capital growth of 9.2 percent since December 31, 2013 resulting from earnings and an increase in unrealized appreciation of the corporation’s investment securities portfolio, offset by dividends and warrant and share repurchases. The decline in ROA was also affected by average asset growth of 24.0 percent resulting from the corporation’s acquisition of CVBK in 2013.

2015 Outlook

Management believes the Corporation's financial performance in 2015 will be affected by (i) lower accretion income related to the fair value accounting adjustments for the CVBK acquisition, partially offset by an increase in interest income from growth in average loans outstanding, (ii) continued sluggish mortgage loan demand that may continue to depress loan production levels in the Mortgage Banking segment, which could be further affected by increases in interest rates, and (iii) continued elevated charge-off levels and competition in the Consumer Finance segment. The following additional factors could influence the Corporation’s financial performance in 2015:

- Retail Banking: Our ability to achieve loan growth will be a significant influence on the Bank’s performance during 2015. General economic trends in the Bank’s markets have contributed to lackluster demand for new loans and increased competition. It will be challenging to maintain the Retail Banking segment's net interest margin at its current level if funds obtained from loan repayments and from deposit growth cannot be fully used to originate new loans and instead are reinvested in lower-yielding assets, or held as interest-bearing deposits in other banks. As part of our strategy to increase lending and build our brand, C&F Bank has continued to strengthen its commercial lending presence in Hampton Roads and Richmond, Virginia, improved its small business loan platform, and has fully integrated the former CVB branches expanding the branch network to 25. While we incurred initial costs to fully integrate CVB's operations into the Bank, we expect to realize cost savings going forward and will be able to leverage our technology investments over the past several years in systems and products that enhance fraud prevention and deliver state-of-the-art banking products to our customers.
- Mortgage Banking: C&F Mortgage generates significant noninterest income from the sale of residential loan products into the secondary market to investors. Our ability to maintain a level of loan production in 2015 sufficient to sustain profitability will be dependent on market factors beyond our control, such as changes in interest rates, housing starts and loan demand. If mortgage interest rates rise during 2015, C&F Mortgage may experience a continuation of lower loan demand, particularly for mortgage refinancings, which could negatively affect earnings of the Mortgage Banking segment in 2015. In addition, during 2015 C&F Mortgage will continue to (i) incur fixed costs associated with its expansion into new markets (ii) compete to retain and attract qualified loan officers,

especially given the heightened federal regulation of lending practices and loan terms (iii) incur higher costs related to compliance with new residential mortgage regulations and (iv) implementation of new technology.



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- Consumer Finance: C&F Finance provides automobile financing through lending programs that are designed to serve customers in the non-prime market. Increased competition and loan pricing strategies that competitors have used to grow market share have had a significant adverse effect on the growth of the Consumer Finance segment's loan portfolio. In addition, loan performance within this market segment is particularly vulnerable to economic conditions, including a protracted period of unemployment because unemployment benefits expire for those who have not been able to find employment and households may be underemployed. C&F Finance began experiencing higher delinquency levels and charge-offs during the second half of 2013, and if economic conditions for customers in the non-prime finance segment do not improve and if resale values on repossessed vehicles continue to decline, the elevated levels of charge-offs may continue in 2015, which will negatively affect the Consumer Finance segment's earnings in 2015. The combination of these factors may result in slower loan growth and lower earnings in the Consumer Finance segment during 2015. We also expect continued strong competition among automobile finance lenders for qualified personnel in 2015, which may affect personnel costs at C&F Finance during 2015.

## Principal Business Activities

An overview of the financial results for each of the Corporation's principal segments is presented below. A more detailed discussion is included in the section "Results of Operations."

**Retail Banking:** The Retail Banking segment reported net income of \$5.6 million for the year ended December 31, 2014, compared to \$3.3 million for the year ended December 31, 2013. The improvement in financial results for 2014, as compared to 2013, was significantly driven by the fair value accounting adjustments resulting from the acquisition of CVB. These adjustments resulted from marking assets and liabilities acquired from CVB to fair market values as of the acquisition date. Accordingly, yields on loans and investments acquired from CVB increased and the cost of certificates of deposit decreased, the benefits of which were partially offset by the amortization of the core deposit intangible and higher depreciation associated with the write-up of certain buildings recognized in the acquisition of CVB. The net accretion attributable to these adjustments was \$1.9 million, net of taxes (\$3.0 million before taxes), during the year ended December 31, 2014, compared to \$549,000, net of taxes (\$844,000 before taxes) during 2013 after the acquisition of CVB. The improvement in net income of the Retail Banking segment for the year ended December 31, 2014, compared to the year ended December 31, 2013 also resulted from, (1) the effects of the continued low interest rate environment on C&F Bank's cost of deposits throughout 2014, (2) stability in loan credit quality resulting in a \$1.0 million decrease in the loan loss provision for 2014 compared to 2013, and (3) a significant decline in C&F Bank's foreclosed properties resulting in lower holding costs and loss provisions. Partially offsetting these positive factors for Retail Banking were the effects of the following: (1) higher personnel costs associated with increased staff levels and support positions associated with the addition of seven branches through the acquisition of CVB and the addition of commercial loan personnel focused on growing the segment's commercial and small business loan portfolios, (2) one-time costs and ongoing operating expenses associated with the effects of combining CVB's operations into the Bank's, and (3) depreciation of equipment purchased to upgrade CVB's systems and equipment to conform to the Bank's technology infrastructure.

C&F Bank's nonperforming assets were \$5.5 million at December 31, 2014, compared to \$7.2 million at December 31, 2013. Nonperforming assets at December 31, 2014 included \$4.7 million in nonaccrual loans, compared to \$4.4 million at December 31, 2013, and \$786,000 in foreclosed properties, compared to \$2.8 million at December 31, 2013. The increase in nonaccrual loans since December 31, 2013 was generally attributable to smaller balance residential real estate and commercial loans. The decline in OREO during the year ended December 31, 2014 resulted from sales of properties that had a total carrying value of \$2.5 million at December 31, 2013, partially offset by foreclosures in 2014. Troubled debt restructured (TDR) loans were \$5.8 million at December 31, 2014, of which \$2.0 million were included in nonaccrual loans, as compared to \$5.6 million of TDR loans at December 31, 2013, of which \$2.6 million were included in nonaccrual loans.

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Mortgage Banking: C&F Mortgage reported net income of \$411,000 for the year ended December 31, 2014, compared to \$2.0 million for the year ended December 31, 2013. The entire mortgage industry, including the Corporation's Mortgage Banking segment, is experiencing significantly reduced refinancing and historically low purchase activity, which has translated into weaker mortgage loan volume and correspondingly lower income from gains on sales of loans and ancillary mortgage lending fees.

Loan origination volume for the year ended December 31, 2014 declined to \$478.6 million from \$721.3 million for the year ended December 31, 2013. During 2014, the amount of loan originations for refinancings and new and resale home purchases were \$71.8 million and \$406.8 million, respectively, compared to \$223.6 million and \$497.7 million, respectively, during 2013. The decrease in origination volume is largely a result of interest rates, low housing inventory, cash buyers, new mortgage lending regulations and other market conditions. The lower volume of loan originations in 2014 resulted in a decrease in gains on sales of loans, which were \$5.1 million for the year ended December 31, 2014, compared to \$7.5 million for the year ended December 31, 2013.

If conditions influencing the mortgage banking environment, such as interest rates and housing inventories, do not improve, C&F Mortgage may experience a continuation of lower loan demand, particularly for mortgage refinancings, which would negatively affect earnings of the mortgage banking segment in future periods.

Consumer Finance: C&F Finance reported net income of \$6.9 million for the year ended December 31, 2014, compared to \$10.5 million for the year ended December 31, 2013. Average loans for the year ended December 31, 2014 were essentially level with average loans for the year ended December 31, 2013. The lack of portfolio growth year over year, along with a decline of 74 basis points in the average yield on the portfolio for the year ended December 31, 2014 have resulted in a \$2.1 million decline in net interest income during the year. Increased competition and loan pricing strategies that competitors have used to grow market share have had a significant adverse effect on the growth and average yield of the Consumer Finance segment's loan portfolio.

The provision for loan losses increased \$2.3 million as a result of an increase in charge offs and growth in the loan portfolio. The increase in loan charge-offs during 2014 is a result of the current economic environment for non-prime consumers, reduced sales prices of repossessed vehicles and easing of underwriting standards and pricing by competitors. Because of the increase in charge-offs and management's expectation that the factors driving the increased charge-offs will persist, we have increased C&F Finance's allowance for loan losses as a percentage of loans at December 31, 2014 to 8.50 percent, as compared with 8.32 percent at December 31, 2013. Management believes that the current allowance for loan losses is adequate to absorb probable losses in the loan portfolio. However, if the current economic environment continues and credit easing by new entrants and competitors in the automobile financing sector intensifies, the Consumer Finance segment could continue to experience an elevated level of charge-offs during 2015, which may result in higher provisions for loan losses and limit loan portfolio growth.

Other and Eliminations: The net loss for this combined segment was \$587,000 for the year ended December 31, 2014, compared to a net loss of \$1.4 million for the year ended December 31, 2013. The "other segment" includes the Corporation's holding company, which recognized \$1.0 million in transaction costs, net of taxes (\$1.2 million before taxes) during the year ended December 31, 2013 associated with the Corporation's acquisition of CVBK.

#### Capital Management

Total shareholders' equity was \$123.4 million at December 31, 2014, compared to \$112.9 million at December 31, 2013. Capital growth resulted from earnings for the year ended December 31, 2014 and an increase in unrealized holding gains on securities available for sale, which are a component of accumulated other comprehensive income, partially offset by dividends and warrant and share repurchases.

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The Corporation's board of directors continued its policy of paying dividends in 2014 and declared a quarterly cash dividend of 30 cents per common share for the fourth quarter of 2014. The dividend payout ratio was 32.8 percent of basic earnings per share for the year ended December 31, 2014. The board of directors continues to evaluate the dividend payout in light of changes in economic conditions, capital levels and expected future levels of earnings, and the changes to the regulatory capital framework implemented by the Basel III Final Rules that were approved during 2013 by the federal banking agencies and are effective (subject to certain limited phase-in schedules) as of January 1, 2015.

Further affecting capital during 2014 was the Corporation's repurchase from the United States Department of the Treasury (Treasury) of a warrant to purchase 167,504 shares of the Corporation's common stock at an exercise price of \$17.91 per share (Warrant). The Warrant was issued to Treasury in January 2009 in connection with the Corporation's participation in the Troubled Asset Relief Program (TARP) Capital Purchase Program. The Corporation paid an aggregate purchase price of \$2.3 million for the repurchase of the Warrant, which has been cancelled. The repurchase price was based on the fair market value of the Warrant as agreed upon by the Corporation and Treasury. With the repurchase of the Warrant, the Corporation has completely exited the TARP Capital Purchase Program.

During the second quarter of 2014, the Board of Directors of the Corporation authorized a share repurchase program to purchase up to \$5.0 million of the Corporation's common stock. The Corporation purchased 2,800 shares under this repurchase program during 2014 through open market transactions at an average price of \$33.05 per share.

## RESULTS OF OPERATIONS

### NET INTEREST INCOME

The following table shows the average balance sheets for each of the years ended December 31, 2014, 2013 and 2012 and includes the average balances of CVBK since October 1, 2013. The table also shows the amounts of interest earned on earning assets, with related yields, and interest expense on interest-bearing liabilities, with related rates. Net interest income also includes the net interest income of CVBK since October 1, 2013, which includes accretion and amortization associated with the fair value adjustments recognized in connection with the Corporation's purchase of CVBK. Loans include loans held for sale. Loans placed on a nonaccrual status are included in the balances and are included in the computation of yields, but had no material effect. Interest on tax-exempt loans and securities is presented on a taxable-equivalent basis (which converts the income on loans and investments for which no income taxes are paid to the equivalent yield as if income taxes were paid using the federal corporate income tax rate of 34 percent in all three years presented).



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TABLE 1: Average Balances, Income and Expense, Yields and Rates

	2014			2013			2012	
(Dollars in thousands)	Average	Income/	Yield/	Average	Income/	Yield/	Average	Income/
	Balance	Expense	Rate	Balance	Expense	Rate	Balance	Expense
Assets								
Securities:								
Taxable	\$ 96,286	\$ 2,493	2.59 %	\$ 47,886	\$ 1,065	2.22 %	\$ 20,376	\$ 336
Tax-exempt	118,221	6,693	5.66	116,846	6,928	5.93	117,612	7,059
Total securities	214,507	9,186	4.28	164,732	7,993	4.85	137,988	7,395
Loans, net	854,948	79,246	9.27	761,751	74,456	9.77	732,972	71,998
Interest-bearing deposits in other banks and Fed funds sold	157,205	378	0.24	68,093	159	0.23	11,695	22
Total earning assets	1,226,660	88,810	7.24	994,576	82,608	8.31	882,655	79,415
Allowance for loan losses	(35,090)			(34,880)			(35,126)	
Total non-earning assets	132,546			108,088			92,821	
Total assets	\$ 1,324,116			\$ 1,067,784			\$ 940,350	
Liabilities and Shareholders' Equity								
Time and savings deposits:								
Interest-bearing deposits	\$ 186,548	\$ 439	0.24 %	\$ 137,615	\$ 412	0.30 %	\$ 110,237	\$ 410
Money market deposit accounts	181,530	493	0.27	132,449	382	0.29	98,045	369
Savings accounts	97,643	83	0.09	61,237	73	0.12	45,645	45
Certificates of deposit, \$100 thousand or more	139,502	1,299	0.93	133,363	1,464	1.10	134,668	2,047

Other certificates of deposit	241,231	1,766	0.73	179,387	1,920	1.07	163,921	2,454
Total time and savings deposits	846,454	4,080	0.48	644,051	4,251	0.66	552,516	5,325
Borrowings	170,101	4,445	2.61	167,003	4,372	2.62	162,312	4,786
Total interest-bearing liabilities	1,016,555	8,525	0.84	811,054	8,623	1.06	714,828	10,111
Demand deposits	166,928			123,859			104,737	
Other liabilities	21,260			25,348			23,749	
Total liabilities	1,204,743			960,261			843,314	
Shareholders' equity	119,373			107,523			97,036	
Total liabilities and shareholders' equity	\$ 1,324,116			\$ 1,067,784			\$ 940,350	
Net interest income		\$ 80,285			\$ 73,985			\$ 69,304
Interest rate spread			6.40 %			7.25 %		
Interest expense to average earning assets			0.69 %			0.87 %		
Net interest margin			6.55 %			7.44 %		

Interest income and expense are affected by fluctuations in interest rates, by changes in the volume of earning assets and interest-bearing liabilities, and by the interaction of rate and volume factors. The following table shows the direct causes of the year-to-year changes in the components of net interest income on a taxable-equivalent basis, and includes the changes in CVBK's net interest income since October 1, 2013. We calculated the rate and volume variances using a formula prescribed by the SEC. Rate/volume variances, the third element in the calculation, are not shown separately in the table, but are allocated to the rate and volume variances in proportion to the relationship of the absolute dollar amounts of the change in each.



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TABLE 2: Rate-Volume Recap

(Dollars in thousands)	2014 from 2013		Total	2013 from 2012		Total
	Increase (Decrease)			Increase	Increase (Decrease)	
	Due to	Volume	(Decrease)	Due to	Volume	(Decrease)
	Rate			Rate		
Interest income:						
Loans	\$ (3,988)	\$ 8,778	\$ 4,790	\$ (357)	\$ 2,815	\$ 2,458
Securities:						
Taxable	199	1,229	1,428	150	579	729
Tax-exempt	(316)	81	(235)	(85)	(46)	(131)
Interest-bearing deposits in other banks and Fed funds sold	5	214	219	7	130	137
Total interest income	(4,100)	10,302	6,202	(285)	3,478	3,193
Interest expense:						
Time and savings deposits:						
Interest-bearing deposits	(100)	127	27	(89)	91	2
Money market deposit accounts	(23)	134	111	(98)	111	13
Savings accounts	(25)	35	10	11	17	28
Certificates of deposit, \$100 thousand or more	(230)	65	(165)	(563)	(20)	(583)
Other certificates of deposit	(707)	553	(154)	(749)	215	(534)
Total time and savings deposits	(1,085)	914	(171)	(1,488)	414	(1,074)
Borrowings	(8)	81	73	(549)	135	(414)
Total interest expense	(1,093)	995	(98)	(2,037)	549	(1,488)
Change in net interest income	\$ (3,007)	\$ 9,307	\$ 6,300	\$ 1,752	\$ 2,929	\$ 4,681

## 2014 Compared to 2013

Net interest income, on a taxable-equivalent basis, for the year ended December 31, 2014 was \$80.3 million, compared to \$74.0 million for the year ended December 31, 2013. The increase in net interest income for 2014, compared to 2013, was a result of an increase in average earning assets resulting from the acquisition of CVBK, offset in part by a decrease in the net interest margin. Net interest margin decreased 89 basis points to 6.55 percent for 2014 relative to 2013. The decrease in net interest margin during 2014 was attributable to a decrease in the yield on interest-earning assets of 107 basis points, offset in part by decreases in the cost of interest-bearing liabilities and an increase in demand deposits that pay no interest. The decrease in the yield on interest-earning assets was primarily attributable to a large increase in interest-bearing deposits in other banks and federal funds sold, which provides the lowest yield of all earning assets, and decreases in the yields on the investment and loan portfolios. The decrease in the cost of interest-bearing liabilities is a result of the sustained low interest rate environment, the repricing of

higher-rate certificates of deposit as they mature to lower rates, and a shift in the mix of deposits from higher cost interest-bearing deposits to lower cost deposits, including non-interest-bearing demand deposits and low-cost interest-bearing demand deposits, money market deposits and savings accounts.

Average loans, which includes both loans held for investment and loans held for sale, increased \$93.2 million to \$854.9 million for the year ended December 31, 2014, compared to 2013. In total, average loans held for investment increased \$112.4 million for the year ended December 31, 2014 compared to 2013, which included increases attributable to the acquisition of CVBK on October 1, 2013. These increases were offset in part by a \$19.2 million decline in the Mortgage Banking segment's average portfolio of loans held for sale during 2014, compared to 2013. The decline in demand for mortgage loans and refinancing activity during 2014 resulted in a \$242.7 million decrease in loan originations during 2014, representing a 33.6 percent decline compared to 2013.

The overall yield on average loans decreased 50 basis points to 9.27 percent for year ended December 31, 2014, compared to 2013. The majority of the decrease was the result of a 74 basis point decline in the average yield on the Consumer Finance loan portfolio for the year ended December 31, 2014 which was due to increased competition and loan pricing strategies that competitors have used to grow market share. Partially offsetting these factors in 2014 was \$2.7 million of accretion related to the fair value interest adjustments to CVB's loan portfolio, which contributed approximately 32 basis points to the yield on loans and 22 basis points to the yield on interest earning assets and 23 basis points to the net interest margin for 2014.

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Average securities available for sale increased \$49.8 million for the year ended December 31, 2014, compared to 2013, which was primarily attributable to the acquisition of CVB's securities portfolio. The average yield on the securities portfolio decreased due to the (1) lower-yielding securities within CVB's portfolio that were included for the full year, (2) purchase of lower-yielding shorter-term securities and (3) reinvestment of the proceeds from calls and maturities of longer-term, higher yielding securities to shorter-term, lower-yielding taxable securities. The Corporation has utilized the strategy of investing in lower-yielding, shorter-term securities to limit exposure to potential future rising interest rate environments.

Average interest-bearing deposits in other banks and federal funds sold increased \$89.1 million for the year ended December 31, 2014, compared to the same period of 2013, which was primarily attributable to the acquisition of CVBK. The remainder of the increase in 2014 resulted from deposit growth and lower loan funding needs of C&F Mortgage due to the decline in demand for mortgage loans during 2014. The average yield on these overnight funds increased one basis point during 2014.

Average interest-bearing time and savings deposits increased \$202.4 million for the year ended December 31, 2014, compared to the same period in 2013, which was primarily attributable to the acquisition of CVB. The average cost of interest-bearing deposits declined 18 basis points during 2014, which resulted from (1) the repricing of time deposits that matured throughout 2013 and into 2014 to lower interest rates, (2) a decline in interest rates paid on NOW and money market deposit accounts in the sustained low interest rate environment, (3) a shift in deposit composition to non-term savings and money market deposits, which pay lower interest rates, and (4) time deposit accretion related to the fair value accounting adjustment to CVB's time deposit, which reduced the cost of interest-bearing deposits by 13 basis points.

Average borrowings increased \$3.1 million for the year ended December 31, 2014, compared to the same period of 2013. This increase was primarily due to the Corporation's assumption of \$5.2 million of trust preferred capital notes in connection with the acquisition of CVBK. The average cost of borrowings declined one basis point during 2014.

The continuing challenge at the Retail Banking segment will be the deployment of excess cash into earning assets as we expect significant competition for loans and the low interest rate environment to continue to suppress yields on investment securities. If market conditions, such as interest rates and housing inventories, do not improve, the Mortgage Banking segment may continue to experience lower loan demand, particularly for refinancings, which could reduce interest income on loans originated for sale, further contributing to a deterioration in net interest margin. The net interest margin at the Consumer Finance segment will be most affected by increasing competition and loan pricing strategies that competitors may use to grow market share in automobile financing. This increased competition may result in lower yields and lower loan growth as the Consumer Finance segment responds to competitive pricing pressures and fewer purchases of automobile retail installment sales contracts.

2013 Compared to 2012

Net interest income, on a taxable-equivalent basis, for the year ended December 31, 2013 was \$74.0 million, compared to \$69.3 million for the year ended December 31, 2012. The increase in net interest income for 2013, compared to 2012, was a result of an increase in average earning assets resulting from the acquisition of CVBK, offset in part by a decrease in the net interest margin. Net interest margin decreased 41 basis points to 7.44 percent for the 2013 relative to 2012. The decrease in net interest margin during 2013 can be attributed to a decrease in the yield on interest-earning assets offset in part by decreases in the cost of interest-bearing liabilities and an increase in demand deposits that pay no interest. The decrease in the yield on interest-earning assets was primarily attributable to a large increase in interest-bearing deposits in other banks and federal funds sold, which segment of earning assets provides the lowest yield of all segments of earning assets, and decreases in the yields on the investment and loan portfolios. The decrease in the cost of interest-bearing liabilities is a result of the sustained low interest rate environment, the repricing of higher-rate certificates of deposit and borrowings as they mature to lower rates, and a shift in the mix of deposits from higher cost interest-bearing deposits to lower cost deposits, including non-interest-bearing demand deposits and low-cost interest-bearing demand deposits, money market deposits and savings accounts.

Average loans, which includes both loans held for investment and loans held for sale, increased \$28.8 million to \$761.8 million for the year ended December 31, 2013, compared to the same period of 2012. In total, average loans held for investment increased \$45.2 million from the year ended December 31, 2012 to the same period in 2013, which included

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increases of \$36.1 million attributable to the acquisition of CVB on October 1, 2013 and \$20.7 million attributable to growth in the Consumer Finance segment's average loan portfolio. These increases were offset in part by a \$12.0 million decline in C&F Bank's portfolio of average loans held for investment, where loan production has been negatively affected by weak demand for new loans in the current economic environment and intense competition for loans in our markets. The Mortgage Banking segment's average portfolio of loans held for sale decreased \$16.4 million during 2013, compared to 2012. The decline in demand for mortgage loans and refinancing activity during 2013 resulted in a \$118.8 million decrease in loan originations during 2013 compared to 2012.

The overall yield on average loans decreased 5 basis points to 9.77 percent for year ended December 31, 2013, when compared to the same period of 2012. While the average loan yield benefited from growth in the higher-yielding Consumer Finance loan portfolio, yields on new loans in this segment have declined in response to aggressive pricing strategies by competitive lenders, and the yield on the Consumer Finance segment's portfolio declined 84 basis points to 17.20 percent. Further contributing to the decline in the loan yield was a 15 basis point decline in the yield on C&F Bank's loan portfolio resulting from the sustained low interest rate environment, coupled with competitive pricing for limited loan demand. Partially offsetting these factors in 2013 were (i) the collection of \$307,000 of nonaccrual interest in connection with the pay-off of \$2.0 million of TDRs related to one commercial relationship, which contributed approximately four basis points to the yield on loans and three basis points to the total yield on interest earning assets and the net interest margin for 2013 and (ii) \$797,000 of accretion related to the fair value interest adjustments to CVB's loan portfolio, which contributed approximately ten basis points to the yield on loans and eight basis points to the yield on interest earning assets and the net interest margin for 2013.

Average securities available for sale increased \$26.7 million for the year ended December 31, 2013, compared to the same period of 2012, of which \$16.3 million was attributable to the acquisition of CVB's securities portfolio since October 1, 2013. Securities also increased at C&F Bank where the average balance of shorter-term securities of U.S. government agencies and corporations increased \$10.1 million. Shifts in the mix of investments from higher-yielding securities to lower-yielding securities were attributable to (1) collateral requirements to support public deposits and (2) reinvesting the proceeds from calls and maturities of longer-term investments to shorter-term taxable securities to limit the Corporation's exposure to potential future rising interest rate environments. The lower yield on the securities portfolio during 2013 resulted from the calls and maturities of higher-yielding securities and purchases of lower-yielding shorter-term securities, as described above, and the inclusion of lower-yielding securities within CVB's portfolio.

Average interest-bearing deposits in other banks and federal funds sold increased \$56.4 million for the year ended December 31, 2013, compared to the same period of 2012, of which \$15.7 million was attributable to the acquisition of CVBK. The remainder of the increase in 2013 resulted from deposit growth and lower loan funding needs of (i) C&F Bank due to weak loan demand and heightened competition for loans and (ii) C&F Mortgage due to the decline in demand for mortgage loans during 2013. The average yield on these overnight funds increased four basis points during 2013.

Average interest-bearing time and savings deposits increased \$91.5 million for the year ended December 31, 2013, compared to the same period in 2012, of which \$68.9 million was attributable to the acquisition of CVB. The remainder of the increase occurred at C&F Bank from higher average interest-bearing demand, money market and savings deposits at C&F Bank, which was offset in part by lower average certificates of deposit. The average cost of interest-bearing deposits declined 30 basis points during 2013, which resulted from (1) the repricing of time deposits that matured throughout 2012 and into 2013 to lower interest rates, (2) a decline in interest rates paid on NOW and money market deposit accounts in the sustained low interest rate environment (3) a shift in deposit composition to non-term savings and money market deposits, which pay lower interest rates, and (4) time deposit accretion related to the fair value accounting adjustment to CVB's time deposit, which reduced the cost of interest-bearing deposits by four basis points.

Average borrowings increased \$4.7 million for the year ended December 31, 2013, compared to the same period of 2012. This increase was primarily due to increases in retail overnight repurchase agreements with commercial depositors during 2013. The average cost of borrowings declined 33 basis points during 2013 because of the maturity of \$10.0 million of FHLB advances during the third quarter of 2012, which were replaced by advances carrying lower interest rates. In addition, \$5.0 million of trust preferred capital notes issued in 2007 converted to a lower variable rate from a higher fixed rate near the end of 2012.

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## NONINTEREST INCOME

TABLE 3: Noninterest Income

(Dollars in thousands)	Year Ended December 31, 2014				Total
	Retail Banking	Mortgage Banking	Consumer Finance	Other and Eliminations	
Gains on sales of loans	\$ —	\$ 5,108	\$ —	\$ —	\$ 5,108
Service charges on deposit accounts	4,468	—	—	—	4,468
Other service charges and fees	3,901	2,314	14	17	6,246
Gains on calls of available for sale securities	29	—	—	—	29
Other income	772	394	1,213	1,341	3,720
Total noninterest income	\$ 9,170	\$ 7,816	\$ 1,227	\$ 1,358	\$ 19,571

(Dollars in thousands)	Year Ended December 31, 2013				Total
	Retail Banking	Mortgage Banking	Consumer Finance	Other and Eliminations	
Gains on sales of loans	\$ —	\$ 7,510	\$ —	\$ —	\$ 7,510
Service charges on deposit accounts	4,197	—	—	—	4,197
Other service charges and fees	2,917	3,131	9	163	6,220
Gains on calls of available for sale securities	6	—	—	270	276
Other income	552	1,177	1,181	1,107	4,017
Total noninterest income	\$ 7,672	\$ 11,818	\$ 1,190	\$ 1,540	\$ 22,220

(Dollars in thousands)	Year Ended December 31, 2012				Total
	Retail Banking	Mortgage Banking	Consumer Finance	Other and Eliminations	
Gains on sales of loans *	\$ —	\$ 7,692	\$ —	\$ —	\$ 7,692
Service charges on deposit accounts	3,326	—	—	—	3,326
Other service charges and fees	2,431	3,669	11	199	6,310

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Gains on calls of available for sale securities	11	—	—	—	11
Other income	356	646	1,138	1,143	3,283
Total noninterest income	\$ 6,124	\$ 12,007	\$ 1,149	\$ 1,342	\$ 20,622

\*Gains on sales of loans at the Mortgage Banking segment have been reclassified to conform to current year presentation.

2014 Compared to 2013

Total noninterest income decreased \$2.6 million, or 11.9 percent, for the year ended December 31, 2014, compared to the same period in 2013. The decrease in total noninterest income for 2014 was attributable to the Mortgage Banking segment where current market conditions caused a decline of 33.6 percent in loan origination volume during 2014 and corresponding decreases of \$2.4 million in gains on sales of loans and \$1.6 million in ancillary loan origination fees constituting a 33.9 percent decline in noninterest income generated by that segment. Noninterest income also declined because of a nonrecurring \$270,000 gain recognized in 2013 from the sale of securities by the Corporation. These decreases were partially offset by higher noninterest income at the Retail Banking segment, which included a full year of CVB noninterest income. In addition, C&F Bank recognized higher activity-based debit card interchange and service charges on its deposit accounts resulting from increased customer activity during 2014.



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## 2013 Compared to 2012

Total noninterest income increased \$1.6 million, or 7.7 percent, for the year ended December 31, 2013, compared to the same period in 2012. The increase in total noninterest income for 2013 included \$668,000 of noninterest income of CVBK since October 1, 2013 consisting of \$285,000 of service charges on deposit accounts, \$237,000 of other service charges and fees and \$146,000 of other income. In addition, noninterest income was affected by the Mortgage Banking segment's election in the second quarter of 2013 to use fair value accounting for its portfolio of loans held for sale and IRLCs, which resulted in a \$333,000 favorable fair value adjustment for the year ended December 31, 2013. Noninterest income for the Mortgage Banking segment was further affected by volatility in mortgage interest rates, which caused a decline of 14.1 percent in loan origination volume during 2013 and a corresponding \$182,000 decrease in gains on sales of loans and \$538,000 decrease in ancillary loan origination fees. C&F Bank recognized higher activity-based debit card interchange and service charges on its deposit accounts resulting from increased customer activity during 2013. The Corporation's holding company, which is included in "Other and Eliminations" above, recognized a \$270,000 gain in the third quarter of 2013 from the sale of its holdings of Fannie Mae and Freddie Mac preferred stock.

## NONINTEREST EXPENSE

TABLE 4: Noninterest Expense

(Dollars in thousands)	Year Ended December 31, 2014				Total
	Retail Banking	Mortgage Banking	Consumer Finance	Other and Eliminations	
Salaries and employee benefits	\$ 22,944	\$ 3,568	\$ 8,962	\$ 836	\$ 36,310
Occupancy expense	6,250	1,832	717	7	8,806
Other expenses:					
OREO expenses	6	—	—	—	6
Provision for indemnification losses	—	240	—	—	240
Other expenses	11,714	2,536	4,022	501	18,773
Total other expenses	11,720	2,776	4,022	501	19,019
Total noninterest expense	\$ 40,914	\$ 8,176	\$ 13,701	\$ 1,344	\$ 64,135

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(Dollars in thousands)	Year Ended December 31, 2013				Total
	Retail Banking	Mortgage Banking	Consumer Finance	Other and Eliminations	
Salaries and employee benefits	\$ 18,361	\$ 4,118	\$ 7,877	\$ 811	\$ 31,167
Occupancy expense	4,665	1,894	823	15	7,397
Other expenses:					
OREO expenses	681	—	—	—	681
Provision for indemnification losses	—	558	—	—	558
Other expenses	9,154	3,429	3,477	1,749	17,809
Total other expenses	9,835	3,987	3,477	1,749	19,048
Total noninterest expense	\$ 32,861	\$ 9,999	\$ 12,177	\$ 2,575	\$ 57,612

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(Dollars in thousands)	Year Ended December 31, 2012				Total
	Retail Banking	Mortgage Banking	Consumer Finance	Other and Eliminations	
Salaries and employee benefits*	\$ 15,562	\$ 3,795	\$ 7,591	\$ 865	\$ 27,813
Occupancy expense	4,041	1,904	827	23	6,795
Other expenses:					
OREO expenses	1,634	—	—	—	1,634
Provision for indemnification losses	—	1,205	—	—	1,205
Other expenses	6,710	3,156	3,273	456	13,595
Total other expenses	8,344	4,361	3,273	456	16,434
Total noninterest expense	\$ 27,947	\$ 10,060	\$ 11,691	\$ 1,344	\$ 51,042

\*Salaries and employee benefits for prior periods at the Mortgage Banking segment have been reclassified to conform to current year presentation.

## 2014 Compared to 2013

Total noninterest expenses increased \$6.5 million, or 11.3 percent, for the year ended December 31, 2014, compared to the same period in 2013. The increase in total noninterest expenses for 2014, which includes a full year of CVBK noninterest expenses, resulted primarily from higher personnel costs during 2014 (1) at C&F Bank due to increased staff levels and support positions associated with the addition of seven branches through the acquisition of CVB and the addition of new personnel dedicated to growing C&F Bank's commercial and small business loan portfolio, (2) due to one-time costs and ongoing operating expenses associated with the effects of combining CVB's operations into C&F Bank's and (3) due to depreciation of equipment purchased to upgrade CVB's systems and equipment to conform to C&F Bank's technology infrastructure. In addition, personnel costs increased at the Consumer Finance segment due to an increase in the number of personnel related to the segment's expansion efforts throughout 2013. These increases were partially offset by a lower OREO expense at the Retail Banking segment, lower variable loan production costs at the Mortgage Banking segment and nonrecurring transaction costs recognized in 2013 associated with the Corporation's acquisition of CVBK.

## 2013 Compared to 2012

Total noninterest expenses increased \$6.6 million, or 12.9 percent, for the year ended December 31, 2013, compared to the same period in 2012. The increase in total noninterest expenses for 2013 included \$2.8 million of noninterest expenses of CVBK since October 1, 2013 consisting of \$1.0 million of salaries and employee benefits, \$282,000 of occupancy expense and \$1.5 million of other expenses. Further increases resulted primarily from higher personnel costs during 2013 at (1) C&F Bank due to increased staffing in the branch network to support customer service initiatives and the addition of new personnel dedicated to growing C&F Bank's commercial and small business loan portfolio, (2) the Mortgage Banking segment due to higher non-production based compensation associated with the expansion into Virginia Beach, Virginia and with regulatory compliance and (3) the Consumer Finance segment due to an increase in the number of personnel to support expansion into new markets. In addition, C&F Bank recognized a \$165,000 loss on the sale of a facility in West Point, Virginia previously used for its deposit operations, and the Corporation's holding company, which is included in "Other and Eliminations" above, recognized \$1.2 million in transaction costs associated with the Corporation's acquisition of CVBK. These increases were partially offset by a lower provision for indemnification losses in connection with loans sold to investors at the Mortgage Banking segment and lower foreclosed properties expenses at C&F Bank.

## INCOME TAXES

Income taxes on 2014 earnings amounted to \$4.7 million, resulting in an effective tax rate of 27.7 percent, compared with \$6.7 million, or 31.8 percent, in 2013 and \$7.6 million, or 31.8 percent, in 2012. Earnings of the Retail Banking segment, which are exempt from state income taxes and include tax-exempt income on securities issued by states and political subdivisions, increased in 2014 and became a larger portion of the Corporation's earnings. Therefore, the Corporation's effective tax rate declined in 2014 as compared to 2013. Further, the Corporation's effective tax rate in 2013 reflected the effect of \$707,000 of non-deductible expenses associated with the acquisition of CVBK on October 1,

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2013. For 2013 compared to 2012, the effective tax rate remained the same even through earnings of the Retail Banking segment increased because of the effect of \$707,000 of non-deductible expenses associated with the acquisition of CVB in 2013.

ASSET QUALITY

Allowance and Provision for Loan Losses

Allowance for Loan Losses Methodology – Retail Banking and Mortgage Banking. We conduct an analysis of the loan portfolio on a regular basis. This analysis includes purchased performing loans acquired in connection with the Corporation's acquisition of CVBK on October 1, 2013. We use this analysis to assess the sufficiency of the allowance for loan losses and to determine the necessary provision for loan losses. The review process generally begins with loan officers or management identifying problem loans to be reviewed on an individual basis for impairment. In addition to these loans, all substandard commercial, construction and residential loans in excess of \$500,000 and all troubled debt restructurings are considered for individual impairment testing. We consider a loan impaired when it is probable that we will be unable to collect all interest and principal payments as scheduled in the loan agreement. A loan is not considered impaired during a period of delay in payment if the ultimate collectibility of all amounts due is expected. If a loan is considered impaired, impairment is measured 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. When a loan is determined to be impaired, we follow a consistent process to measure that impairment in our loan portfolio. We then establish a specific allowance for impaired loans based on the difference between the carrying value of the loan and its estimated fair value. For collateral dependent loans we obtain an updated appraisal if we do not have a current one on file. Appraisals are performed by independent third party appraisers with relevant industry experience. We may make adjustments to the appraised value based on recent sales of like properties or general market conditions when appropriate. We segregate loans meeting the classification criteria for special mention, substandard, doubtful and loss, as well as impaired loans from performing loans within the portfolio. The remaining non-classified loans are grouped by loan type (e.g., commercial, consumer) and by risk rating. We assign each loan type an allowance factor based on the associated risk, current economic conditions, past performance, complexity and size of the individual loans within the particular loan category. We assign classified loans (e.g., special mention, substandard, doubtful, loss) a higher allowance factor than non-classified loans within a particular loan type based on our concerns regarding collectibility or our knowledge of particular elements surrounding the borrower. Our allowance factors increase with the severity of classification. Allowance factors used for unclassified loans are based on our analysis of charge-off history for relevant periods of time which can vary depending on economic conditions, and our judgment based on the overall analysis of the lending environment including the general economic conditions. Our analysis of charge-off history also considers economic cycles and the trends during those cycles. Those cycles that more closely match the current environment are considered more relevant during our review. The allowance for loan losses is the aggregate of specific allowances, the calculated allowance required for classified loans by category and the general allowance for each portfolio type.

In conjunction with the methodology described above, we consider the following risk elements that are inherent in the loan portfolio:

- Real estate residential mortgage loans carry risks associated with the continued credit-worthiness of the borrower and changes in the value of the collateral.
- Real estate construction loans carry risks that the project will not be finished according to schedule, the project will not be finished according to budget and the value of the collateral may, at any point in time, be less than the principal amount of the loan. Construction loans also bear the risk that the general contractor, who may or may not be a loan customer, may be unable to finish the construction project as planned because of financial pressure unrelated to the project.
- Commercial, financial and agricultural loans carry risks associated with the successful operation of a business or a real estate project, in addition to other risks associated with the ownership of real estate, because the repayment of these loans may be dependent upon the profitability and cash flows of the business or project. In addition, there is

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risk associated with the value of collateral other than real estate which may depreciate over time and cannot be appraised with as much precision.

- Equity lines of credit carry risks associated with the continued credit-worthiness of the borrower and changes in the value of the collateral.
- Consumer loans carry risks associated with the continued credit-worthiness of the borrower and the value of the collateral (e.g., rapidly-depreciating assets such as automobiles), or lack thereof. Consumer loans are more likely than real estate loans to be immediately adversely affected by job loss, divorce, illness or personal bankruptcy.

As discussed above we segregate loans meeting the criteria for special mention, substandard, doubtful and loss from non-classified, or pass rated, loans. We review the characteristics of each rating at least annually, generally during the first quarter. The characteristics of these ratings are as follows:

- Pass rated loans are to persons or business entities with an acceptable financial condition, appropriate collateral margins, appropriate cash flow to service the existing loan, and an appropriate leverage ratio. The borrower has paid all obligations as agreed and it is expected that this type of payment history will continue. When necessary, acceptable personal guarantors support the loan.
- Special mention loans have a specific defined weakness in the borrower's operations and the borrower's ability to generate positive cash flow on a sustained basis. The borrower's recent payment history is characterized by late payments. The Corporation's risk exposure is mitigated by collateral supporting the loan. The collateral is considered to be well-margined, well maintained, accessible and readily marketable.
- Substandard loans are considered to have specific and well-defined weaknesses that jeopardize the viability of the Corporation's credit extension. The payment history for the loan has been inconsistent and the expected or projected primary repayment source may be inadequate to service the loan. The estimated net liquidation value of the collateral pledged and/or ability of the personal guarantor(s) to pay the loan may not adequately protect the Corporation. There is a distinct possibility that the Corporation will sustain some loss if the deficiencies associated with the loan are not corrected in the near term. A substandard loan would not automatically meet our definition of impaired unless the loan is significantly past due and the borrower's performance and financial condition provide evidence that it is probable that the Corporation will be unable to collect all amounts due.
- Substandard nonaccrual loans have the same characteristics as substandard loans; however they have a non-accrual classification because it is probable that the Corporation will not be able to collect all amounts due.
- Doubtful rated loans have all the weaknesses inherent in a loan that is classified substandard but with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts,

conditions, and values, highly questionable and improbable. The possibility of loss is extremely high.

- Loss rated loans are not considered collectible under normal circumstances and there is no realistic expectation for any future payment on the loan. Loss rated loans are fully charged off.

Allowance for Loan Losses Methodology - PCI Loans - As previously described, on a quarterly basis we evaluate our estimate of cash flows expected to be collected on PCI loans. These evaluations require the continued assessment of key assumptions and estimates similar to the initial estimate of fair value, such as the effect of collateral value changes, changing loss severities, prepayment speeds and other relevant factors. Subsequent decreases to the expected cash flows will generally result in a provision for loan losses resulting in an increase to the allowance for loans losses. For a more detailed description, see "Critical Accounting Policies" in this Item 7.

Allowance for Loan Losses Methodology – Consumer Finance. The Consumer Finance segment’s loans consist of non-prime automobile loans. These loans carry risks associated with (1) the continued credit-worthiness of borrowers who may be unable to meet the credit standards imposed by most traditional automobile financing sources and (2) the value of



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rapidly-depreciating collateral. These loans do not lend themselves to a classification process because of the short duration of time between delinquency and repossession. Therefore, the loan loss allowance review process generally focuses on the rates of delinquencies, deferrals, defaults, repossessions and losses. Allowance factors also include an analysis of charge-off history for relevant periods of time which can vary depending on economic conditions, and our judgment based on the overall analysis of the lending environment. Loans are segregated between performing and nonperforming loans. Performing loans are those that have made timely payments in accordance with the terms of the loan agreement and are not past due 90 days or more. Nonperforming loans are those that do not accrue interest and are greater than 90 days past due.

In accordance with its policies and guidelines and consistent with industry practices, C&F Finance, at times, offers payment deferrals to borrowers, whereby the borrower is allowed to move up to two payments within a twelve-month rolling period to the end of the loan. A fee will be collected for extensions only in states that permit it. An account for which all delinquent payments are deferred is classified as current at the time the deferment is granted and therefore is not included as a delinquent account. Thereafter, such an account is aged based on the timely payment of future installments in the same manner as any other account. We evaluate the results of this deferment strategy based upon the amount of cash installments that are collected on accounts after they have been deferred versus the extent to which the collateral underlying the deferred accounts has depreciated over the same period of time. Based on this evaluation, we believe that payment deferrals granted according to our policies and guidelines are an effective portfolio management technique and result in higher ultimate cash collections. Payment deferrals may affect the ultimate timing of when an account is charged off. Increased use of deferrals may result in a lengthening of the loss confirmation period, which would increase expectations of credit losses inherent in the portfolio and therefore increase the allowance for loan losses and related provision for loan losses. The average amounts deferred, as a percentage of loans outstanding, was 2.10 percent in 2014, 1.32 percent in 2013 and 0.73 percent in 2012.

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The allowance for loan losses represents an amount that, in our judgment, will be adequate to absorb any losses on existing loans that may become uncollectible. The provision for loan losses increases the allowance, and loans charged off, net of recoveries, reduce the allowance. The following table presents the Corporation's loan loss experience for the periods indicated:

TABLE 5: Allowance for Loan Losses

(Dollars in thousands)	Year Ended December 31,									
	2014	2013	2012	2011	2010					
Allowance, beginning of period	\$ 34,852	\$ 35,907	\$ 33,677	\$ 28,840	\$ 24,027					
Provision for loan losses:										
Retail Banking segment	—	1,030	2,400	6,000	6,500					
Mortgage Banking segment	60	90	165	360	34					
Consumer Finance segment	16,270	13,965	9,840	7,800	8,425					
Total provision for loan losses	16,330	15,085	12,405	14,160	14,959					
Loans charged off:										
Real estate—residential mortgage	161	849	793	1,096	334					
Real estate—construction <sup>1</sup>	—	—	—	—	—					
Commercial, financial and agricultural <sup>2</sup>	271	2,298	2,074	2,566	3,787					
Equity lines	80	126	159	52	44					
Consumer	312	399	337	319	189					
Consumer finance	19,022	16,398	10,134	8,144	7,976					
Total loans charged off	19,846	20,070	13,497	12,177	12,330					
Recoveries of loans previously charged off:										
Real estate—residential mortgage	59	106	35	98	6					
Real estate—construction <sup>1</sup>	—	3	—	—	—					
Commercial, financial and agricultural <sup>2</sup>	210	227	121	173	21					
Equity lines	—	28	79	12	32					
Consumer	250	173	207	122	83					
Consumer finance	3,751	3,393	2,880	2,449	2,042					
Total recoveries	4,270	3,930	3,322	2,854	2,184					
Net loans charged off	15,576	16,140	10,175	9,323	10,146					
Allowance, end of period	\$ 35,606	\$ 34,852	\$ 35,907	\$ 33,677	\$ 28,840					
Ratio of net charge-offs to average total loans outstanding during period for Retail Banking and Mortgage Banking	0.06	%	0.73	%	0.72	%	0.89	%	0.97	%
Ratio of net charge-offs to average total loans outstanding during period for Consumer Finance	5.39	%	4.59	%	2.76	%	2.39	%	2.89	%

1Includes the Corporation's real estate construction lending and consumer real estate lot lending.

2Includes the Corporation's commercial real estate lending, land acquisition and development lending, builder line lending and commercial business lending.

For further information regarding the adequacy of our allowance for loan losses, refer to "Nonperforming Assets" within this Item 7.

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The allocation of the allowance at December 31 for the years indicated and the ratio of related outstanding loan balances to total loans are as follows:

TABLE 6: Allocation of Allowance for Loan Losses

(Dollars in thousands)	December 31,		2012	2011	2010
	2014	2013			
Allocation of allowance for loan losses, end of year:					
Real estate—residential mortgage	\$ 2,313	\$ 2,355	\$ 2,358	\$ 2,379	\$ 1,442
Real estate—construction 1	434	434	424	480	581
Commercial, financial and agricultural 2	7,744	7,805	9,824	10,040	8,688
Equity lines	812	892	885	912	380
Consumer	211	273	283	319	307
Consumer finance	24,092	23,093	22,133	19,547	17,442
Unallocated	—	—	—	—	—
Balance, December 31	\$ 35,606	\$ 34,852	\$ 35,907	\$ 33,677	\$ 28,840
Ratio of loans to total year-end loans:					
Real estate—residential mortgage	21	% 23	% 22	% 22	% 23
Real estate—construction 1	1	1	1	1	2
Commercial, financial and agricultural 2	37	35	30	33	34
Equity lines	6	6	5	5	5
Consumer	1	1	1	1	1
Consumer finance	34	34	41	38	35
	100	% 100	% 100	% 100	% 100

<sup>1</sup> Includes the Corporation's real estate construction lending and consumer real estate lot lending.

<sup>2</sup> Includes the Corporation's commercial real estate lending, land acquisition and development lending, builder line lending and commercial business lending.

Loans by credit quality indicators as of December 31, 2014 were as follows:

TABLE 7A: Credit Quality Indicators \*

(Dollars in thousands)	Pass	Special Mention	Substandard	Substandard Nonaccrual	Total <sup>1</sup>
Real estate – residential mortgage	\$ 171,414	\$ 2,978	\$ 2,953	\$ 2,472	\$ 179,817
Real estate – construction <sup>2</sup>	4,677	—	2,648	—	7,325
Commercial, financial and agricultural <sup>3</sup>	269,631	7,591	27,590	2,033	306,845
Equity lines	48,443	772	750	356	50,321
Consumer	7,984	103	33	43	8,163
	\$ 502,149	\$ 11,444	\$ 33,974	\$ 4,904	\$ 552,471

\*Included in the table above are loans purchased in connection with the acquisition of CVB of \$87.3 million pass rated, \$3.0 million special mention, \$10.7 million substandard and \$603,000 substandard nonaccrual.

(Dollars in thousands)	Performing	Non-Performing	Total
Consumer finance	\$ 282,293	\$ 1,040	\$ 283,333

<sup>1</sup> At December 31, 2014, the Corporation did not have any loans classified as Doubtful or Loss.

<sup>2</sup> Includes the Corporation's real estate construction lending and consumer real estate lot lending.

<sup>3</sup> Includes the Corporation's commercial real estate lending, land acquisition and development lending, builder line lending and commercial business lending.

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Loans by credit quality indicators as of December 31, 2013 were as follows:

TABLE 7B: Credit Quality Indicators

(Dollars in thousands)	Pass	Special Mention	Substandard	Substandard Nonaccrual	Total <sup>1</sup>
Real estate – residential mortgage	\$ 180,670	\$ 2,209	\$ 3,580	\$ 1,996	\$ 188,455
Real estate – construction <sup>2</sup>	2,899	116	2,795	—	5,810
Commercial, financial and agricultural <sup>3</sup>	243,576	8,571	34,573	1,873	288,593
Equity lines	48,603	1,003	898	291	50,795
Consumer	8,616	2	158	231	9,007
	\$ 484,364	\$ 11,901	\$ 42,004	\$ 4,391	\$ 542,660

\*Included in the table above are loans purchased in connection with the acquisition of CVB of \$119.8 million pass rated, \$3.3 million special mention, \$17.8 million substandard and \$652,000 substandard nonaccrual.

(Dollars in thousands)	Performing	Non-Performing	Total
Consumer finance	\$ 276,537	\$ 1,187	\$ 277,724

<sup>1</sup> At December 31, 2013, the Corporation did not have any loans classified as Doubtful or Loss.

<sup>2</sup> Includes the Corporation's real estate construction lending and consumer real estate lot lending.

<sup>3</sup> Includes the Corporation's commercial real estate lending, land acquisition and development lending, builder line lending and commercial business lending.

The Retail Banking segment's allowance for loan losses decreased \$305,000 since December 31, 2013 as a result of net charge-offs during 2014 that were largely provided for through provisions in loan losses recognized in prior periods. While there was a slight increase in substandard nonaccrual loans since December 31, 2013, there was no provision for loan losses at the Retail Banking segment during 2014 because of the overall improvement in the quality of the loan portfolio as indicated by the \$8.0 million decline in substandard loans. The allowance for loan losses to total loans, excluding purchased credit impaired loans, declined to 2.08 percent at December 31, 2014, compared to 2.22 percent at December 31, 2013. We believe that the current level of the allowance for loan losses at C&F Bank is adequate to absorb any losses on existing loans that may become uncollectible. If current economic conditions

continue or worsen, a higher level of nonperforming loans may be experienced in future periods, which may then require a higher provision for loan losses.

The Consumer Finance segment's allowance for loan losses increased by \$999,000 to \$24.1 million at December 31, 2014 from \$23.1 million at December 31, 2013, and its provision for loan losses increased \$2.3 million for the year ended December 31, 2014, as compared to 2013. The increase in provision for loan losses during 2014 and the lack of significant loan portfolio growth since December 31, 2013 resulted in an increase in the ratio of the allowance for loan losses as a percentage of loans at December 31, 2014 to 8.50 percent from 8.32 percent at December 31, 2013. The increase in the provision for loan losses during 2014 was primarily attributable to higher net charge-offs, which resulted from the uncertain economic conditions, lower resale prices of repossessed vehicles and easing of underwriting standards and pricing by our competitors leading to higher default rates. We believe that the current level of the allowance for loan losses at the Consumer Finance segment is adequate to absorb any losses on existing loans that may become uncollectible. However, if factors influencing the Consumer Finance segment result in higher net charge-off ratio in future periods, the Consumer Finance segment may need to increase the level of its allowance for loan losses, which could negatively affect future earnings of the Consumer Finance segment.

#### Nonperforming Assets

A loan's past due status is based on the contractual due date of the most delinquent payment due. Loans are generally placed on nonaccrual status when the collection of principal or interest is 90 days or more past due, or earlier, if collection

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is uncertain based on an evaluation of the net realizable value of the collateral and the financial strength of the borrower. Loans greater than 90 days past due may remain on accrual status if management determines it has adequate collateral to cover the principal and interest. For those loans that are carried on nonaccrual status, payments are first applied to principal outstanding. A loan may be returned to accrual status if the borrower has demonstrated a sustained period of repayment performance in accordance with the contractual terms of the loan and there is reasonable assurance the borrower will continue to make payments as agreed. These policies are applied consistently across our loan portfolio, including purchased loans.

Assets acquired through, or in lieu of, loan foreclosure are held for sale and are initially recorded at the lower of the loan balance or the fair value less costs to sell at the date of foreclosure. Subsequent to foreclosure, management periodically performs valuations of the foreclosed assets based on updated appraisals, general market conditions, recent sales of like properties, length of time the properties have been held, and our ability and intention with regard to continued ownership of the properties. We may incur additional write-downs of foreclosed assets to fair value less costs to sell if valuations indicate a further other-than-temporary deterioration in market conditions. Revenue and expenses from operations and changes in the property valuations are included in net expenses from foreclosed assets and improvements are capitalized.

During periods of economic slowdown or recession, delinquencies, defaults, repossessions and losses generally increase at the Consumer Finance segment. These periods also may be accompanied by decreased consumer demand for used automobiles and declining values of automobiles securing outstanding loans, which weakens collateral coverage and increases the amount of a loss in the event of default. Significant increases in the inventory of used automobiles during periods of economic recession may also depress the prices at which we may sell repossessed automobiles or delay the timing of these sales. Because C&F Finance focuses on non-prime borrowers, the actual rates of delinquencies, defaults, repossessions and losses on these loans are higher than those experienced in the general automobile finance industry and could be more dramatically affected by a general economic downturn. While we manage the higher risk inherent in loans made to non-prime borrowers through the underwriting criteria and collection methods employed by C&F Finance, we cannot guarantee that these criteria or methods will afford adequate protection against these risks. However, we believe that the current allowance for loan losses is appropriate to absorb any losses on existing Consumer Finance segment loans that may become uncollectible.

At the Consumer Finance segment, the automobile repossession process is generally initiated after a loan becomes more than 60 days delinquent. Repossessions are handled by independent repossession firms engaged by C&F Finance. After the prescribed waiting period, the repossessed automobile is sold in a third-party auction. We credit the proceeds from the sale of the automobile, and any other recoveries, against the balance of the loan and related fees. Proceeds from the sale of the repossessed vehicle and other recoveries are usually not sufficient to cover the outstanding balance of the loan, and the resulting deficiency is charged off. The charge-off represents the difference between the actual net sale proceeds minus collections and repossession expenses and the principal balance of the delinquent loan. C&F Finance pursues collection of deficiencies when it deems such action to be appropriate.





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Table 8 summarizes nonperforming assets at December 31 of each of the past five years.

TABLE 8: Nonperforming Assets

## Retail Banking Segment

(Dollars in thousands)	2014	2013	2012	2011	2010
Nonaccrual loans	\$ 4,717	\$ 4,391	\$ 11,461	\$ 10,011	\$ 7,765
OREO*	786	2,768	6,236	6,059	10,295
Total nonperforming assets **	\$ 5,503	\$ 7,159	\$ 17,697	\$ 16,070	\$ 18,060
Accruing loans past due for 90 days or more	\$ 14	\$ 75	\$ —	\$ 68	\$ 1,030
Troubled debt restructurings	\$ 5,827	\$ 5,620	\$ 16,492	\$ 17,094	\$ 9,769
Total loans	\$ 549,183	\$ 539,746	\$ 395,664	\$ 401,745	\$ 412,092
Allowance for loan losses	\$ 10,961	\$ 11,266	\$ 13,381	\$ 13,650	\$ 11,228
Nonperforming assets to total loans and OREO*	1.00 %	1.34 %	4.40 %	3.94 %	4.28 %
Allowance for loan losses to total loans	2.00	2.09	3.38	3.40	2.72
Allowance for loan losses to nonaccrual loans	232.37	256.57	116.75	136.35	144.60

\* OREO is recorded at its fair market value less cost to sell.

\*\*Because the Corporation acquired CVBK on October 1, 2013, and the Corporation did not own CVBK's assets (including CVB's nonperforming assets) prior to October 1, 2013, information regarding CVB's nonperforming assets for periods prior to the acquisition is not included in Table 8. Further, as required by purchase accounting, PCI loans that were considered nonaccrual and TDRs prior to the acquisition lose these designations and are not included in post-acquisition nonperforming assets in Table 8.

## Mortgage Banking Segment

(Dollars in thousands)	2014	2013	2012	2011	2010
Nonaccrual loans	\$ 187	\$ —	\$ —	\$ 621	\$ —
OREO*	—	—	—	—	379
Total nonperforming assets	\$ 187	\$ —	\$ —	\$ 621	\$ 379
Accruing loans past due for 90 days or more	\$ —	\$ —	\$ —	\$ —	\$ —
Troubled debt restructurings	\$ —	\$ —	\$ —	\$ —	\$ —
Total loans	\$ 3,288	\$ 2,914	\$ 2,340	\$ 2,611	\$ 2,739
Allowance for loan losses	\$ 553	\$ 493	\$ 393	\$ 480	\$ 170
Nonperforming assets to total loans and OREO*	5.69 %	— %	— %	23.78 %	12.16 %
Allowance for loan losses to total loans	16.82	16.92	16.79	18.38	6.21
Allowance for loan losses to nonaccrual loans	295.72	—	—	77.29	—

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\*OREO is recorded at its fair market value less cost to sell.

#### Consumer Finance Segment

(Dollars in thousands)	2014	2013	2012	2011	2010
Nonaccrual loans	\$ 1,040	\$ 1,187	\$ 655	\$ 381	\$ 151
Accruing loans past due for 90 days or more	\$ —	\$ —	\$ —	\$ —	\$ —
Total loans	\$ 283,333	\$ 277,724	\$ 278,186	\$ 246,305	\$ 220,753
Allowance for loan losses	\$ 24,092	\$ 23,093	\$ 22,133	\$ 19,547	\$ 17,442
Nonaccrual consumer finance loans to total consumer finance loans	0.37 %	0.43 %	0.24 %	0.15 %	0.07 %
Allowance for loan losses to total consumer finance loans	8.50	8.32	7.96	7.94	7.90

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Table 9 presents the changes in the OREO balance for 2014 and 2013:

TABLE 9: OREO Changes

(Dollars in thousands)	Year Ended December 31,	
	2014	2013
Balance at the beginning of year, gross	\$ 6,904	\$ 10,173
Transfers between loans and other real estate owned	1,960	588
Acquired from CVB	—	395
Charge-offs	(4,135)	(261)
Sales proceeds	(4,382)	(4,209)
Gain on disposition	324	218
Deferred gain on disposition	144	—
Balance at the end of year, gross	815	6,904
Less valuation allowance	(29)	(4,135)
Balance at the end of year, net	\$ 786	\$ 2,769

Nonperforming assets of C&F Bank totaled \$5.5 million at December 31, 2014, compared to \$7.2 million at December 31, 2013, a 23 percent decrease during 2014. C&F Bank's nonperforming assets at December, 2014 included \$4.7 million of nonaccrual loans, compared to \$4.4 million at December 31, 2013, and \$786,000 of OREO compared to \$2.8 million at December 31, 2013. The ratio of the allowance for loan losses to nonaccrual loans decreased to 232.37 percent at December 31, 2014 from 256.57 percent at December 31, 2013. The increase in nonaccrual loans since December 31, 2013 was generally attributable to smaller balance residential real estate and commercial loans.

We believe we have provided adequate loan loss reserves based on our evaluations of collectability of loans, which considers trends in delinquencies and charge-offs, changes in the nature and volume of the loan portfolio, current economic conditions that may affect borrowers' ability to repay and collateral values, overall portfolio quality and review of specific potential losses.

The Corporation's aggregate OREO properties were \$786,000 at December 31, 2014, compared to \$2.8 million at December 31, 2013, and primarily consisted of residential lots. These properties have been written down to their estimated fair values less cost to sell. The decline in OREO during 2014 resulted from sales of properties that had a net carrying value of \$2.5 million at December 31, 2013, partially offset by foreclosures in 2014. In connection with the OREO sales in 2014, the Corporation recognized \$4.1 million of OREO charge-offs which were largely provided

for through OREO loss provisions recognized in prior periods.

Nonaccrual loans at the Consumer Finance segment decreased to \$1.0 million at December 31, 2014 from \$1.2 million at December 31, 2013. As noted above, the allowance for loan losses at the Consumer Finance segment increased from \$23.1 million at December 31, 2013 to \$24.1 million at December 31, 2014, and the ratio of the allowance for loan losses to total consumer finance loans was 8.50 percent as of December 31, 2014, compared to 8.32 percent at December 31, 2013. Nonaccrual consumer finance loans remain low relative to the allowance for loan losses and the total consumer finance loan portfolio because the Consumer Finance segment generally initiates repossession of loan collateral once a loan is 60 days or more past due but before the loan reaches 90 days or more past due and is evaluated for nonaccrual status.

If interest on nonaccrual loans had been recognized, we would have recorded additional gross interest income of \$413,000 for 2014, \$479,000 for 2013 and \$654,000 for 2012. Interest received on nonaccrual loans was \$233,000 in 2014, \$241,000 in 2013 and \$171,000 in 2012.

As discussed above, we measure impaired loans based on the present value of expected future cash flows discounted at the effective interest rate of the loan or, as a practical expedient, at the loan's observable market price or the fair value of the collateral if the loan is collateral dependent. We maintain a valuation allowance to the extent that the measure of the impaired loan is less than the recorded investment. TDRs occur when we agree to significantly modify the original terms

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of a loan by granting a concession due to the deterioration in the financial condition of the borrower. These concessions typically are made for loss mitigation purposes and could include reductions in the interest rate, payment extensions, forgiveness of principal, forbearance or other actions. TDRs are considered impaired loans.

Impaired loans, which included \$5.8 million of TDRs, and the related allowance at December 31, 2014, were as follows:

TABLE 10A: Impaired Loans

(Dollars in thousands)	Recorded Investment in Loans	Unpaid Principal Balance	Related Allowance	Average Balance- Impaired Loans	Interest Income Recognized
Real estate – residential mortgage	\$ 3,000	\$ 3,094	\$ 417	\$ 2,931	\$ 139
Commercial, financial and agricultural:					
Commercial real estate lending	2,786	2,908	440	2,735	150
Builder line lending	—	—	—	—	—
Commercial business lending	103	103	15	115	7
Equity lines	30	32	1	25	2
Consumer	95	95	6	95	4
Total	\$ 6,014	\$ 6,232	\$ 879	\$ 5,901	\$ 302

Impaired loans, which included \$5.6 million of TDR loans, and the related allowance at December 31, 2013, were as follows:

TABLE 10B: Impaired Loans

	Recorded Investment in	Unpaid Principal	Related	Average Balance Total	Interest Income
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(Dollars in thousands)	Loans	Balance	Allowance	Loans	Recognized
Real estate – residential mortgage	\$ 2,601	\$ 2,694	\$ 390	\$ 2,090	\$ 99
Commercial, financial and agricultural:					
Commercial real estate lending	2,729	2,780	504	2,748	99
Builder line lending	13	16	4	14	1
Commercial business lending	695	756	131	562	11
Equity lines	131	132	—	33	—
Consumer	93	93	14	95	9
Total	\$ 6,262	\$ 6,471	\$ 1,043	\$ 5,542	\$ 219

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TDRs at December 31, 2014 and 2013 were as follows:

TABLE 11: Troubled Debt Restructurings

(Dollars in thousands)	December 31,	
	2014	2013
Accruing TDRs	\$ 3,801	\$ 3,026
Nonaccrual TDRs <sup>1</sup>	2,026	2,594
Total TDRs <sup>2</sup>	\$ 5,827	\$ 5,620

<sup>1</sup> Included in nonaccrual loans in Table 8: Nonperforming Assets.

<sup>2</sup> Included in impaired loans in Tables 10A and 10B: Impaired Loans.

While TDRs are considered impaired loans, not all TDRs are on nonaccrual status. If a loan was on nonaccrual status at the time of the TDR modification, the loan will remain on nonaccrual status following the modification and may be returned to accrual status based on the Corporation's policy for returning loans to accrual status. If a loan was accruing prior to being modified as a TDR and if the Corporation concludes that the borrower is able to make such modified payments, and there are no other factors or circumstances that would cause it to conclude otherwise, the TDR will remain on an accruing status.

#### Allowance and Provision for Indemnification Losses

C&F Mortgage sells substantially all of the residential mortgage loans it originates to third-party counterparties. As is customary in the industry, the agreements with these counterparties require C&F Mortgage to extend representations and warranties with respect to program compliance, borrower misrepresentation, fraud, and early payment performance. Under the agreements, the counterparties are entitled to make loss claims and repurchase requests of C&F Mortgage for loans that contain covered deficiencies. C&F Mortgage has obtained early payment default recourse waivers for a significant portion of its business. Recourse periods for early payment default for the remaining counterparties vary from 90 days up to one year. Recourse periods for borrower misrepresentation, fraud, or underwriting error do not have a stated time limit. C&F Mortgage maintains an indemnification reserve for potential claims made under these recourse provisions. C&F Mortgage has adopted a reserve methodology whereby provisions are made to an expense account to fund a reserve maintained as a liability account on the balance sheet for potential losses. The loan performance data of sold loans is not made available to C&F Mortgage making the evaluation of potential losses inherently subjective as it requires estimates that are susceptible to significant revision as more



information becomes available. A schedule of expected losses on loans with claims or indemnifications is maintained to ensure the reserve is adequate to cover estimated losses. Often times, claims are not factually validated and they are rescinded. Once claims are validated and the actual or potential loss is agreed upon with the counterparties, the reserve is charged and a cash payment is made to settle the claim. The balance of the indemnification reserve has adequately provided for all claims in each of the three years ended December 31, 2014. The following table presents the changes in the allowance for indemnification losses for the periods presented:

TABLE 12: Allowance for Indemnification Losses

(Dollars in thousands)	Year Ended December 31,		
	2014	2013	2012
Allowance, beginning of period	\$ 2,415	\$ 2,092	\$ 1,702
Provision for indemnification losses	240	558	1,205
Payments	(566)	(235)	(815)
Allowance, end of period	\$ 2,089	\$ 2,415	\$ 2,092

The higher levels of the provision for indemnification losses and payments during 2012 relative to 2014 and 2013 were attributable to more claims arising throughout the mortgage banking industry from more stringent agency (i.e., Fannie Mae, Freddie Mac) loan reviews.

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FINANCIAL CONDITION

SUMMARY

A financial institution's primary sources of revenue are generated by its earning assets and sales of financial assets, while its major expenses are produced by the funding of those assets with interest-bearing liabilities, provisions for loan losses and compensation to employees. Effective management of these sources and uses of funds is essential in attaining a financial institution's maximum profitability while maintaining an acceptable level of risk.

At December 31, 2014, the Corporation had total assets of \$1.33 billion compared to \$1.31 billion at December 31, 2013. The significant components of the Corporation's balance sheet are discussed below.

LOAN PORTFOLIO

General

Through the Retail Banking segment, we engage in a wide range of lending activities, which include the origination, primarily in the Retail Banking segment's market area, of (1) one-to-four family and multi-family residential mortgage loans, (2) commercial real estate loans, (3) construction loans, (4) land acquisition and development loans, (5) consumer loans and (6) commercial business loans. We engage in non-prime automobile lending through the Consumer Finance segment and in residential mortgage lending through the Mortgage Banking segment with the majority of the loans sold to third-party investors. At December 31, 2014, the Corporation's loans held for investment in all categories totaled \$800.2 million and loans held for sale had a fair value of \$28.3 million.

Tables 13 and 14 present information pertaining to the composition of loans and maturity/repricing of loans.

TABLE 13: Summary of Loans Held for Investment

(Dollars in thousands)	December 31,				
	2014	2013	2012	2011	2010
Real estate—residential mortgage	\$ 179,817	\$ 188,455	\$ 149,257	\$ 147,135	\$ 146,073
Real estate—construction 1	7,325	5,810	5,062	5,737	12,095
Commercial, financial, and agricultural 2	306,845	288,593	205,052	212,235	219,226
Equity lines	50,321	50,795	33,324	33,192	32,187
Consumer	8,163	9,007	5,309	6,057	5,250
Consumer finance	283,333	277,724	278,186	246,305	220,753
Total loans	835,804	820,384	676,190	650,661	635,584
Less allowance for loan losses	(35,606)	(34,852)	(35,907)	(33,677)	(28,840)
Total loans, net	\$ 800,198	\$ 785,532	\$ 640,283	\$ 616,984	\$ 606,744

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<sup>1</sup> Includes the Corporation's real estate construction lending and consumer real estate lot lending.

<sup>2</sup> Includes the Corporation's commercial real estate lending, land acquisition and development lending, builder line lending and commercial business lending.

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TABLE 14: Maturity/Repricing Schedule of Loans

(Dollars in thousands)	December 31, 2014	
	Commercial, Financial, and Agricultural	Real Estate Construction
Variable Rate:		
Within 1 year	\$ 67,736	\$ 4,953
1 to 5 years	26,045	—
After 5 years	37,873	—
Fixed Rate:		
Within 1 year	\$ 14,873	\$ 2,372
1 to 5 years	85,646	—
After 5 years	74,672	—

The increase in total loans primarily occurred in the Bank's real estate loans for commercial, land acquisition and development and builder line purposes, which was offset in part by a decline in residential mortgage and commercial business loans.

Total loans at December 31, 2014 and 2013 include loans purchased in connection with the Corporation's acquisition of CVB on October 1, 2013. These loans were recorded at estimated fair value on the date of acquisition without the carryover of the related allowance for loan losses. The acquired loans fall into two categories, purchased performing loans and purchased credit-impaired (PCI) loans. On the date of acquisition, the Corporation acquired PCI loans with a fair value of \$35.3 million and acquired purchased performing loans with a fair value of \$111.8 million. The following tables present the outstanding principal balance and the carrying amount of purchased loans that are included in the Corporation's balance sheet at December 31, 2014 and 2013:

TABLE 15: PCI and Purchased Performing Loans

December 31, 2014	
Purchased	
Credit	Purchased

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(Dollars in thousands)	Impaired	Performing	Total
Outstanding principal balance	\$ 36,541	\$ 85,015	\$ 121,556
Carrying amount			
Real estate – residential mortgage	\$ 1,723	\$ 18,688	\$ 20,411
Real estate – construction	—	—	—
Commercial, financial and agricultural	19,367	45,015	64,382
Equity lines	318	15,464	15,782
Consumer	16	979	995
Total acquired loans	\$ 21,424	\$ 80,146	\$ 101,570

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(Dollars in thousands)	December 31, 2013		
	Credit Impaired	Purchased Performing	Total
Outstanding principal balance	\$ 49,041	\$ 110,977	\$ 160,018
Carrying amount			
Real estate – residential mortgage	\$ 2,694	\$ 29,285	\$ 31,979
Real estate – construction	771	917	1,688
Commercial, financial and agricultural	28,602	55,204	83,806
Equity lines	332	16,909	17,241
Consumer	121	2,156	2,277
Total acquired loans	\$ 32,520	\$ 104,471	\$ 136,991

See "Critical Accounting Policies" in this Item 7 for a description of the Corporation's accounting for purchased performing and PCI loans.

## Credit Policy

The Corporation's credit policy establishes minimum requirements and provides for appropriate limitations on overall concentration of credit within the Corporation. The policy provides guidance in general credit policies, underwriting policies and risk management, credit approval, and administrative and problem asset management policies. The overall goal of the Corporation's credit policy is to ensure that loan growth is accompanied by acceptable asset quality with uniform and consistently applied approval, administration, and documentation practices and standards.

## Residential Mortgage Lending – Held for Sale

The Mortgage Banking segment's guidelines for underwriting conventional conforming loans comply with the underwriting criteria established by Fannie Mae, Freddie Mac and/or the applicable third party investor. The guidelines for non-conforming conventional loans are based on the requirements of private investors and information provided by third-party investors. The guidelines used by C&F Mortgage to originate FHA-insured, USDA-guaranteed and VA-guaranteed loans comply with the criteria established by HUD, the USDA, the VA and/or the applicable third party investor. The conventional loans that C&F Mortgage originates or purchases that have loan-to-value ratios greater than 80 percent at origination are generally insured by private mortgage insurance.

## Residential Mortgage Lending – Held for Investment

The Retail Banking segment originates residential mortgage loans secured by first and second liens on properties located in its primary market area in southeastern and central Virginia. The Bank offers various types of residential first mortgage loans in addition to traditional long-term, fixed-rate loans. The majority of such loans include 10, 15 and 30 year amortizing mortgage loans with fixed rates of interest and fixed-rate mortgage loans with terms of 20, 25 and 30 years but subject to call after five years at the Bank's option. Second mortgage loans are offered with fixed and adjustable rates. Second mortgage loans are granted for a fixed period of time, usually between five and 20 years. Call option provisions are included in the loan documents for some longer-term, fixed-rate second mortgage loans, and these provisions allow the Bank to make interest rate adjustments for such loans.

Loans associated with residential mortgage lending are included in the real estate—residential mortgage category in Table 13: Summary of Loans Held for Investment.

#### Construction Lending

The Retail Banking segment has a real estate construction lending program. We make loans primarily for the construction of one-to-four family residences and, to a lesser extent, multi-family dwellings. The Bank also makes

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construction loans for office and warehouse facilities and other nonresidential projects, generally limited to borrowers that present other business opportunities for the Retail Banking segment.

The amounts, interest rates and terms for construction loans vary, depending upon market conditions, the size and complexity of the project, and the financial strength of the borrower and any guarantors of the loan. The term for a typical construction loan ranges from nine months to 15 months for the construction of an individual residence and from 15 months to a maximum of three years for larger residential or commercial projects. We do not typically amortize construction loans, and the borrower pays interest monthly on the outstanding principal balance of the loan. The interest rates on construction loans are fixed and variable. We do not generally finance the construction of commercial real estate projects built on a speculative basis. For residential builder loans, we limit the number of models and/or speculative units allowed depending on market conditions, the builder's financial strength and track record and other factors. Generally, the maximum loan-to-value ratio for one-to-four family residential construction loans is 80 percent of the property's fair market value, or 85 percent of the property's fair market value if the property will be the borrower's primary residence. The fair market value of a project is determined on the basis of an appraisal of the project conducted by an appraiser acceptable to the Bank. For larger projects where unit absorption or leasing is a concern, we may also obtain a feasibility study or other acceptable information from the borrower or other sources about the likely disposition of the property following the completion of construction.

Construction loans for nonresidential projects and multi-unit residential projects are generally larger and involve a greater degree of risk to the Bank than residential mortgage loans. We attempt to minimize such risks (1) by making construction loans in accordance with our underwriting standards and to established customers in our primary market area and (2) by monitoring the quality, progress and cost of construction. Generally, our maximum loan-to-value ratio for non-residential projects and multi-unit residential projects is 80 percent; however, this maximum can be waived for particularly strong borrowers on an exception basis.

Loans associated with construction lending are included in the real estate—construction category in Table 13: Summary of Loans Held for Investment.

## Consumer Lot Lending

Consumer lot loans are loans made to individuals for the purpose of acquiring an unimproved building site for the construction of a residence that generally will be occupied by the borrower. Consumer lot loans are made only to individual borrowers, and each borrower generally must certify his or her intention to build and occupy a single-family residence on the lot. These loans typically have a maximum term of either three or five years with a balloon payment of the entire balance of the loan being due in full at the end of the initial term. The interest rate for these loans is fixed or variable at a rate that is slightly higher than prevailing rates for one-to-four family residential mortgage loans. We do not believe consumer lot loans bear as much risk as land acquisition and development loans



because such loans are not made for the construction of residences for immediate resale, are not made to developers and builders, and are not concentrated in any one subdivision or community.

Loans associated with consumer lot lending are included in the real estate—construction category in Table 13: Summary of Loans Held for Investment.

#### Commercial Real Estate Lending

The Retail Banking segment's commercial real estate loans are primarily secured by the value of real property. The proceeds of commercial real estate loans are generally used by the borrower to finance or refinance the cost of acquiring and/or improving a commercial property. The properties that typically secure these loans are office and warehouse facilities, hotels, retail facilities, restaurants and other commercial properties. Present policy is generally to restrict the making of commercial real estate loans to borrowers who will occupy or use the financed property in connection with their normal business operations. However, we also will consider making commercial real estate loans under the following two conditions: (1) the borrower is in strong financial condition and presents a substantial business opportunity for the Corporation and (2) the borrower has substantially pre-leased the improvements to high-caliber tenants.

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Our commercial real estate loans are usually amortized over a period of time ranging from 15 years to 25 years and usually have a term to maturity ranging from five years to 15 years. These loans normally have provisions for interest rate adjustments after the loan is three to five years old. The maximum loan-to-value ratio for a commercial real estate loan is 80 percent; however, this maximum can be waived for particularly strong borrowers on an exception basis. Most commercial real estate loans are further secured by one or more unconditional personal guarantees.

In recent years, we have structured a portion of our commercial real estate loans as mini-permanent loans. The amortization period, term and interest rates for these loans vary based on borrower preferences and our assessment of the loan and the degree of risk involved. If the borrower prefers a fixed rate of interest, we usually offer a loan with a fixed rate of interest for a term of three to ten years with an amortization period of up to 25 years. The remaining balance of the loan is due and payable in a single balloon payment at the end of the initial term. We believe these loan terms provide some protection from changes in the borrower's business and income as well as changes in general economic conditions. In the case of fixed-rate commercial real estate loans, shorter maturities also provide an opportunity to adjust the interest rate on this type of interest-earning asset in accordance with our asset and liability management strategies.

Loans secured by commercial real estate are generally larger and involve a greater degree of risk than residential mortgage loans. Because payments on loans secured by commercial real estate are usually dependent on successful operation or management of the properties securing such loans, repayment of such loans is subject to changes in both general and local economic conditions and the borrower's business and income. As a result, events beyond our control, such as a downturn in the local economy, could adversely affect the performance of the commercial real estate loan portfolio. We seek to minimize these risks by lending to established customers and generally restricting our commercial real estate loans to our primary market area. Emphasis is placed on the income producing characteristics and quality of the collateral.

Loans associated with commercial real estate lending are included in the commercial, financial and agricultural category in Table 13: Summary of Loans Held for Investment.

### Land Acquisition and Development Lending

Land acquisition and development loans are made to builders and developers for the purpose of acquiring unimproved land to be developed for residential building sites, residential housing subdivisions, multi-family dwellings and a variety of commercial uses. Our policy is to make land acquisition loans to borrowers for the purpose of acquiring developed lots for single-family, townhouse or condominium construction. We will make both land acquisition and development loans to residential builders, experienced developers and others in strong financial condition to provide additional construction and mortgage lending opportunities for the Bank.

We underwrite and process land acquisition and development loans in much the same manner as commercial construction loans and commercial real estate loans. For land acquisition and development loans, we use lower loan-to-value ratios, which are a maximum of 65 percent for raw land, 75 percent for land development and improved lots and 80 percent of the discounted appraised value of the property as determined in accordance with the appraisal policies for developed lots for single-family or townhouse construction. We can waive the maximum loan-to-value ratio for particularly strong borrowers on an exception basis. The term of land acquisition and development loans ranges from a maximum of two years for loans relating to the acquisition of unimproved land to, generally, a maximum of three years for other types of projects. All land acquisition and development loans generally are further secured by one or more unconditional personal guarantees. Because these loans are usually in a larger amount and involve more risk than consumer lot loans, we carefully evaluate the borrower's assumptions and projections about market conditions and absorption rates in the community in which the property is located and the borrower's ability to carry the loan if the borrower's assumptions prove inaccurate.

Loans associated with land acquisition and development lending are included in the commercial, financial and agricultural category in Table 13: Summary of Loans Held for Investment.

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### Builder Line Lending

The Retail Banking segment offers builder lines of credit to residential home builders to support their land and lot inventory needs. A construction loan facility for a builder will typically have an expiration of 12 months or less. Each loan that is made under the master loan facility will have a stated maturity that allows time for the residential unit to be constructed and sold to a homebuyer under prevailing market conditions. Specific terms vary based on the purpose of the loan (e.g., lot inventory, spec or non pre-sold units, pre-sold units) and previous sales activity to new homebuyers in the particular development. Repayment relies upon the successful performance of the underlying residential real estate project. This type of lending carries a higher level of risk related to residential real estate market conditions, a functioning first and secondary market in which to sell residential properties, and the borrower's ability to manage inventory and run projects. We manage this risk by lending to experienced builders and by using specific underwriting policies and procedures for these types of loans.

Loans associated with builder line lending are included in the commercial, financial and agricultural category in Table 13: Summary of Loans Held for Investment.

### Commercial Business Lending

Commercial business loan products include revolving lines of credit to provide working capital, term loans to finance the purchase of vehicles and equipment, letters of credit to guarantee payment and performance, and other commercial loans. In general, these credit facilities carry the unconditional guaranty of the owners and/or stockholders.

Revolving and operating lines of credit are typically secured by all current assets of the borrower, provide for the acceleration of repayment upon any event of default, are monitored monthly or quarterly to ensure compliance with loan covenants, and are re-underwritten or renewed annually. Interest rates generally will float at a spread tied to the Bank's prime lending rate. Term loans are generally advanced for the purchase of, and are secured by, vehicles and equipment and are normally fully amortized over a term of two to five years, on either a fixed or floating rate basis.

Loans associated with commercial business lending are included in the commercial, financial and agricultural category in Table 13: Summary of Loans Held for Investment.

### Equity Line Lending

The Retail Banking segment offers its customers home equity lines of credit that enable customers to borrow funds secured by the equity in their homes. Currently, home equity lines of credit are offered with adjustable rates of interest that are generally priced at a spread to the prime lending rate. Home equity lines of credit are made on an open-end, revolving basis. Home equity loans generally do not present as much risk to the Bank as other types of consumer loans. These loans must satisfy our underwriting criteria, including loan-to-value and credit score guidelines.

Loans associated with equity line lending are included in the equity lines category in Table 13: Summary of Loans Held for Investment.

### Consumer Lending

The Retail Banking segment offers a variety of consumer loans, including automobile, personal secured and unsecured, and loans secured by savings accounts or certificates of deposit. The shorter terms and generally higher interest rates on consumer loans help the Bank maintain a profitable spread between its average loan yield and its cost of funds. Consumer loans secured by collateral other than a personal residence generally involve more credit risk than residential mortgage loans because of the type and nature of the collateral or, in certain cases, the absence of collateral. However, we believe the higher yields generally earned on such loans compensate for the increased credit risk associated with such loans.

Loans associated with consumer lending are included in the consumer category in Table 13: Summary of Loans Held for Investment.

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### Consumer Finance

C&F Finance has an extensive automobile dealer network through which it purchases installment contracts throughout its markets. Credit approval is centralized in two locations, which along with the application processing system, ensures that contract purchase decisions comply with C&F Finance's underwriting policies and procedures.

Finance contract application packages completed by prospective borrowers are submitted by the automobile dealers electronically through a third-party online automotive sales and finance platform to C&F Finance's automated origination and application system, which processes the credit bureau report, generates all relevant loan calculations and recommends the contract structure. C&F Finance personnel with credit authority review the system-generated recommendations and determine whether to approve or deny the purchase of the contract. The purchase decision is based primarily on the applicant's credit history with emphasis on prior auto loan history, current employment status, income, collateral type and mileage, and the loan-to-value ratio.

C&F Finance's underwriting and collateral guidelines form the basis for the purchase decision. Exceptions to credit policies and authorities must be approved by a designated credit officer. C&F Finance's typical customers have experienced prior credit difficulties. Because C&F Finance serves customers who are unable to meet the credit standards imposed by most traditional automobile financing sources, we expect C&F Finance to sustain a higher level of credit losses than traditional automobile financing sources. However, C&F Finance generally purchases contracts with interest at higher rates than those charged by traditional financing sources. These higher rates should more than offset the increase in the provision for loan losses for this segment of the Corporation's loan portfolio.

Loans associated with automobile sales finance are included in the consumer finance category in Table 13: Summary of Loans Held for Investment.

## SECURITIES

The investment portfolio plays a primary role in the management of the Corporation's interest rate sensitivity. In addition, the portfolio serves as a source of liquidity and is used as needed to meet collateral requirements. The investment portfolio consists of securities available for sale, which may be sold in response to changes in market interest rates, changes in prepayment risk, increases in loan demand, general liquidity needs and other similar factors. These securities are carried at estimated fair value.

Table 16 sets forth the composition of the Corporation's securities available for sale in dollar amounts at fair value and as a percentage of the Corporation's total securities available for sale at the dates indicated.

TABLE 16: Securities Available for Sale

(Dollars in thousands)	December 31, 2014			December 31, 2013		
	Amount	Percent		Amount	Percent	
U.S. Treasury securities	\$ —	*	%	\$ 10,000	5	%
U.S. government agencies and corporations	22,934	10		29,950	14	
Mortgage-backed securities	67,619	31		50,863	23	
Obligations of states and political subdivisions	131,344	59		127,139	58	
Corporate and other debt securities	—	*		158	*	
Total available for sale securities at fair value	\$ 221,897	100	%	\$ 218,110	100	%

\*Less than one percent

The Corporation seeks to diversify its portfolio to minimize risk, including by purchasing mortgage-backed securities for cash flow and reinvestment opportunities and securities issued by states and political subdivisions due to the tax benefits and the higher yield obtained from these securities. All of the Corporation's mortgage-backed securities are direct issues of United States government agencies or government-sponsored enterprises. The municipal bond sector, which is included in the Corporation's obligations of states and political subdivisions category of securities, is the largest component within the

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securities portfolio. At December 31, 2014, approximately 97 percent of the Corporation's obligations of states and political subdivisions, as measured by market value, were rated "A" or better by Standard & Poor's or Moody's Investors Service. The securities portfolio composition has changed considerably during 2014 with the purchase of mortgage-backed securities that, while lower yielding, are of shorter duration which minimizes exposure to interest rate risk.

Table 17 presents additional information pertaining to the composition of the securities portfolio by the earlier of contractual maturity or expected maturity, excluding preferred stock. Expected maturities will differ from contractual maturities because borrowers may have the right to prepay obligations with or without call or prepayment penalties.

TABLE 17: Maturity of Securities

(Dollars in thousands)	Year Ended December 31, 2014		2013		2012	
	Amortized Cost	Weighted Average Yield	Amortized Cost	Weighted Average Yield	Amortized Cost	Weighted Average Yield
U.S. Treasury securities:						
Maturing within 1 year	\$ —	—	% \$ 10,000	0.01	% \$ —	—
Maturing after 1 year, but within 5 years	—	—	—	—	—	—
Maturing after 5 years, but within 10 years	—	—	—	—	—	—
Maturing after 10 years	—	—	—	—	—	—
Total U.S. Treasury securities	—	—	10,000	0.01	—	—
U.S. government agencies and corporations:						
Maturing within 1 year	15,252	2.35	16,482	2.21	18,514	1.42
Maturing after 1 year, but within 5 years	998	0.74	1,502	0.68	—	—
Maturing after 5 years, but within 10 years	6,160	2.21	5,534	2.20	2,991	2.20
Maturing after 10 years	999	2.51	8,985	3.27	3,123	2.39
Total U.S. government agencies and corporations	23,409	2.25	32,503	2.43	24,628	1.64



Mortgage-backed securities:								
Maturing within 1 year	3	6.24	2	4.50	28	4.68		
Maturing after 1 year, but within 5 years	41,535	2.34	1,403	3.00	2,099	2.35		
Maturing after 5 years, but within 10 years	21,954	2.76	2,392	2.68	—	—		
Maturing after 10 years	3,224	2.86	47,521	2.76	—	—		
Total mortgage-backed securities	66,716	2.50	51,318	2.76	2,127	2.38		
States and municipals:1								
Maturing within 1 year	15,946	5.36	11,188	5.94	13,030	4.63		
Maturing after 1 year, but within 5 years	68,551	4.95	51,002	5.66	34,474	5.86		
Maturing after 5 years, but within 10 years	20,405	5.36	38,547	5.26	46,168	5.97		
Maturing after 10 years	19,410	6.45	22,992	6.42	23,207	6.60		
Total states and municipals	124,312	5.30	123,729	5.70	116,879	5.91		
Corporate and other debt securities:								
Maturing within 1 year	—	—	—	—	—	—		
Maturing after 1 year, but within 5 years	—	—	—	—	—	—		
Maturing after 5 years, but within 10 years	—	—	—	—	—	—		
Maturing after 10 years	—	—	158	9.44	—	—		
Total corporate and other debt securities	—	—	158	9.44	—	—		
Total securities:2								
Maturing within 1 year	31,201	3.89	37,672	2.73	31,572	2.75		
Maturing after 1 year, but within 5 years	111,084	4.06	53,907	5.45	36,573	5.66		
Maturing after 5 years, but within 10 years	48,519	3.78	46,473	4.76	49,159	5.74		
Maturing after 10 years	23,633	5.79	79,656	3.89	26,330	6.10		
Total securities	\$ 214,437	4.16	% \$ 217,708	4.26	% \$ 143,634	5.13		%

<sup>1</sup> Yields on tax-exempt securities have been computed on a taxable-equivalent basis.

<sup>2</sup> Total securities exclude preferred stock at amortized cost of \$27,000 at December 31, 2012 (estimated fair value of \$104,000 at December 31, 2012). The Corporation did not hold any preferred stock at December 31, 2014 and 2013.

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## DEPOSITS

The Corporation's predominant source of funds is depository accounts, which are comprised of demand deposits, savings and money market accounts, and time deposits. The Corporation's deposits are principally provided by individuals and businesses located within the communities served.

Deposits totaled \$1.03 billion at December 31, 2014, compared to \$1.01 billion at December 31, 2013. The \$17.8 million increase in deposits from December 31, 2013 to December 31, 2014 occurred primarily in non-term accounts, as depositors shifted from time deposits in order to position themselves for flexibility regarding the availability of their funds in the event of a favorable shift in interest rates.

The Corporation had \$3.1 million in brokered money market deposits outstanding at December 31, 2014, compared to \$2.4 million in brokered money market deposits at December 31, 2013. The source of these brokered deposits is uninvested cash balances held in third-party brokerage sweep accounts. The Corporation uses brokered deposits as a means of diversifying liquidity sources, as opposed to a long-term deposit gathering strategy.

Table 18 presents the average deposit balances and average rates paid for the years 2014, 2013 and 2012.

TABLE 18: Average Deposits and Rates Paid

(Dollars in thousands)	Year Ended December 31, 2014		2013		2012			
	Average Balance	Average Rate	Average Balance	Average Rate	Average Balance	Average Rate		
Noninterest-bearing demand deposits	\$ 166,928		\$ 123,859		\$ 104,737			
Interest-bearing transaction accounts	186,548	0.24 %	137,615	0.30 %	110,237	0.37 %		
Money market deposit accounts	181,530	0.27	132,449	0.29	98,045	0.38		
Savings accounts	97,643	0.09	61,237	0.12	45,645	0.10		
	139,502	0.93	133,363	1.10	134,668	1.52		

Certificates of deposit, \$100 thousand or more									
Other certificates of deposit	241,231	0.73		179,387	1.07		163,921	1.50	
Total interest-bearing deposits	846,454	0.48	%	644,051	0.66	%	552,516	0.96	%
Total deposits	\$ 1,013,382			\$ 767,910			\$ 657,253		

Table 19 details maturities of certificates of deposit with balances of \$100,000 or more at December 31, 2014.

TABLE 19: Maturities of Certificates of Deposit with Balances of \$100,000 or More

(Dollars in thousands)	December 31, 2014
3 months or less	\$ 16,807
3-6 months	19,130
6-12 months	43,137
Over 12 months	80,998
Total	\$ 160,072

## BORROWINGS

In addition to deposits, the Corporation utilizes short-term and long-term borrowings. Short-term borrowings from the Federal Reserve Bank and the FHLB are used to fund the Corporation's day-to-day operations. Short-term borrowings also include securities sold under agreements to repurchase, which are secured transactions with customers and generally mature the day following the day sold, and overnight unsecured fed funds lines with correspondent banks. Long-term borrowings consist of advances from the FHLB, advances under a non-recourse revolving bank line of credit, and securities sold under agreement to repurchase with a third-party correspondent bank. All FHLB advances are secured by a blanket floating lien on all of C&F Bank's qualifying closed-end and revolving open-end loans secured by 1-4 family residential

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properties. All Federal Reserve Bank advances are secured by loan-specific liens on certain qualifying loans of C&F Bank that are not otherwise pledged. The bank line of credit is non-recourse and is secured by loans at C&F Finance. The repurchase agreement is secured by a portion of the C&F Bank's securities portfolio.

In December, 2007, Trust II, a wholly-owned subsidiary of the Corporation, was formed for the purpose of issuing trust preferred capital securities for general corporate purposes including the refinancing of existing debt. On December 14, 2007, Trust II issued \$10.0 million of trust preferred capital securities in a private placement to an institutional investor and \$310,000 in common equity to the Corporation. The principal asset of Trust II is \$10.3 million of the Corporation's trust preferred capital notes. In July 2005, Trust I, a wholly-owned subsidiary of the Corporation, was formed for the purpose of issuing trust preferred capital securities to partially fund the Corporation's purchase of 427,186 shares of its common stock. On July 21, 2005, Trust I issued \$10.0 million of trust preferred capital securities in a private placement to an institutional investor and \$310,000 in common equity to the Corporation. The principal asset of Trust I is \$10.3 million of the Corporation's trust preferred capital notes. In December 2003, CVBK Trust I was formed for the purpose of issuing \$5.0 million of trust preferred capital securities in private placements to institutional investors. The principal asset of CVBK Trust I is \$5.2 million of trust preferred capital notes originally issued by CVBK and then assumed by the Corporation.

For further information concerning the Corporation's borrowings, refer to Item 8, "Financial Statements and Supplementary Data," under the heading "Note 9: Borrowings."

#### OFF-BALANCE-SHEET ARRANGEMENTS

To meet the financing needs of customers, the Corporation is a party, in the normal course of business, to financial instruments with off-balance-sheet risk. These financial instruments include commitments to extend credit, commitments to sell loans and standby letters of credit. These instruments involve elements of credit and interest rate risk in addition to the amount on the balance sheet. The Corporation'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 written is represented by the contractual amount of these instruments. We use the same credit policies in making these commitments and conditional obligations as we do for on-balance-sheet instruments. We obtain collateral based on our credit assessment of the customer in each circumstance.

Loan commitments are agreements to extend credit to a customer provided that there are no violations of the terms of the contract prior to funding. Commitments have fixed expiration dates or other termination clauses and may require payment of a fee by the customer. Since many of the commitments may expire without being completely drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The total amount of unused loan commitments was \$136.0 million at December 31, 2014, and \$129.2 million at December 31, 2013.

Standby letters of credit are written conditional commitments issued by the Bank to guarantee the performance of a customer to a third party. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loans to customers. The total contract amount of standby letters of credit was \$13.4 million at December 31, 2014, and \$13.7 million at December 31, 2013.

At December 31, 2014, C&F Mortgage had rate lock commitments to originate mortgage loans aggregating \$38.4 million and loans held for sale of \$28.3 million. At December 31, 2014, each loan held for sale by C&F Mortgage was subject to a forward sales agreement. C&F Mortgage enters into IRLCs with customers and will sell the underlying loans to investors on either a best efforts or a mandatory delivery basis. C&F Mortgage mitigates interest rate risk on IRLCs and loans held for sale by (a) entering into forward loan sales contracts with investors for loans to be delivered on a best efforts basis or (b) entering into forward sales contracts of mortgage-backed to-be-announced securities (TBAs) for loans to be delivered on a mandatory basis. Both the IRLCs with customers and the forward sales contracts are considered derivative financial instruments. At December 31, 2014, C&F Mortgage had forward sales contracts with a notional value of \$66.7 million. The fair value of these derivative instruments at December 31, 2014 was \$448,000, which was included in other assets.

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C&F Mortgage sells substantially all of the residential mortgage loans it originates to third-party counterparties. As is customary in the industry, the agreements with these counterparties require C&F Mortgage to extend representations and warranties with respect to lending program compliance, borrower misrepresentation, fraud, and early payment performance. Under the agreements, the counterparties are entitled to make loss claims and repurchase requests of C&F Mortgage for loans that contain covered deficiencies. C&F Mortgage has obtained early payment default recourse waivers for a significant portion of its business. Recourse periods for early payment default for the remaining counterparties vary from 90 days up to one year. Recourse periods for borrower misrepresentation or fraud, or underwriting error do not have a stated time limit. C&F Mortgage maintains an indemnification reserve that, in management's judgment, will be adequate to absorb any losses arising from valid indemnification requests. Payments made under these recourse provisions were \$566,000 in 2014, \$235,000 in 2013 and \$815,000 in 2012.

Risks also arise from the possible inability of counterparties to meet the terms of their contracts. C&F Mortgage has procedures in place to evaluate the credit risk of investors and does not expect any counterparty to fail to meet its obligations.

The Corporation uses derivatives to manage exposure to interest rate risk through the use of interest rate swaps. Interest rate swaps involve the exchange of fixed and variable rate interest payments between two parties, based on a common notional principal amount and maturity date with no exchange of underlying principal amounts. The Corporation's interest rate swaps qualify as cash flow hedges. The Corporation's cash flow hedges effectively modify the Corporation's exposure to interest rate risk by converting variable rates of interest on \$10.0 million and \$15.0 million of the Corporation's trust preferred capital notes to fixed rates of interest until September 2015 and December 2019, respectively. The cash flow hedges' total notional amount is \$25.0 million. At December 31, 2014, the \$15.0 million cash flow hedges had a fair value of \$40,000, which is recorded in other assets, and the \$10.0 million cash flow hedges had a fair value of (\$143,000), which is recorded in other liabilities. The cash flow hedges were fully effective at December 31, 2014. Therefore, the net loss on the cash flow hedges was recognized as a component of other comprehensive income (loss), net of deferred income taxes.

## LIQUIDITY

The objective of the Corporation's liquidity management is to ensure the continuous availability of funds to satisfy the credit needs of our customers and the demands of our depositors, creditors and investors. Stable core deposits and a strong capital position are the components of a solid foundation for the Corporation's liquidity position. Additional sources of liquidity available to the Corporation include cash flows from operations, loan payments and payoffs, deposit growth, sales of securities, the issuance of brokered certificates of deposit and the capacity to borrow additional funds.

Liquid assets, which include cash and due from banks, interest-bearing deposits at other banks, federal funds sold and nonpledged securities available for sale, totaled \$279.1 million at December 31, 2014. The increase in liquid assets during 2014 resulted primarily from the increase in interest-bearing deposits at other banks, as the Corporation increased deposits at other banks as it could not deploy funds into newly-originated loans or into securities at attractive risk-adjusted returns. The Corporation's funding sources, including capacity, amount outstanding and amount available at December 31, 2014 are presented in Table 20.

TABLE 20: Funding Sources

(Dollars in thousands)	December 31, 2014		Available
	Capacity	Outstanding	
Unsecured federal funds agreements	\$ 65,000	\$ —	\$ 65,000
Repurchase agreements	5,000	5,000	—
Repurchase lines of credit	50,000	—	50,000
Borrowings from FHLB	142,881	47,000	95,881
Borrowings from Federal Reserve Bank	26,013	—	26,013
Revolving line of credit	120,000	75,488	44,512
Total	\$ 408,894	\$ 127,488	\$ 281,406

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We have no reason to believe these arrangements will not be renewed at maturity. Additional loans and securities are available that can be pledged as collateral for future borrowings from the Federal Reserve Bank or the FHLB above the current lendable collateral value. Our ability to maintain sufficient liquidity may be affected by numerous factors, including economic conditions nationally and in our markets. Depending on our liquidity levels, our capital position, conditions in the capital markets and other factors, we may from time to time consider the issuance of debt, equity or other securities or other possible capital market transactions, the proceeds of which could provide additional liquidity for our operations.

Time deposits of \$100,000 or more, maturing in less than a year, totaled \$79.1 million at December 31, 2014; time deposits of \$100,000 or more, maturing in more than one year, totaled \$81.0 million.

The Corporation's contractual obligations and scheduled payment amounts due at various intervals over the next five years and beyond as of December 31, 2014 are presented in Table 21.

Table 21: Contractual Obligations

(Dollars in thousands)	Payments Due by Period				
	Total	Less than 1 Year	1 3 Years	3 5 Years	More than 5 Years
Bank lines of credit	\$ 75,488	\$ —	\$ 75,488	\$ —	\$ —
FHLB advances 1	47,000	7,500	25,000	14,500	—
Trust preferred capital notes	25,103	—	—	—	25,103
Securities sold under agreements to repurchase	19,436	14,436	—	5,000	—
Operating leases	4,885	1,266	1,992	1,191	436
Total <sup>2</sup>	\$ 171,912	\$ 23,202	\$ 102,480	\$ 20,691	\$ 25,539

<sup>1</sup>. FHLB advances include convertible advances of \$17.5 million maturing in 2017 and \$5.0 million maturing in 2018. These advances have fixed rates of interest unless the FHLB exercises its option to convert the interest on these advances from fixed-rate to variable-rate (i.e., the conversion date). We can elect to repay the advances in whole or in part on their respective conversion dates and on any interest payment dates thereafter without the payment of a fee if the FHLB elects to convert the advances. However, we would incur a fee if we repay the advances prior to their respective conversion dates, if the FHLB does not convert the advance on the conversion date, or, after notification of conversion, on any date other than the conversion date or any interest payment date thereafter. FHLB



advances also include fixed rate hybrid advances of \$7.5 million, \$7.5 million \$2.5 million, and \$7.0 million maturing in 2015, 2016, 2018, and 2019, respectively. These advances provide fixed-rate funding until the stated maturity date. We may add interest rate caps or floors at a future date, at which time the cost of the caps or floors will be added to the advance rate. For further information concerning the Corporation's FHLB borrowings, refer to Item 8, "Financial Statements and Supplementary Data," under the heading "Note 9: Borrowings."

- <sup>2</sup>. At December 31, 2014 there were no outstanding federal funds purchased or borrowings from the Federal Reserve Bank.

As a result of the Corporation's management of liquid assets and the ability to generate liquidity through liability funding, we believe that we maintain overall liquidity sufficient to satisfy the Corporation's operational requirements and contractual obligations.

## CAPITAL RESOURCES

The assessment of capital adequacy depends on such factors as asset quality, liquidity, earnings performance, and changing competitive conditions and economic forces. We regularly review the adequacy of the Corporation's capital. We maintain a structure that will assure an adequate level of capital to support anticipated asset growth and to absorb potential losses. While we will continue to look for opportunities to invest capital in profitable growth, share purchases are another tool that facilitates improving shareholder return, as measured by ROE and earnings per share.

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The capital positions of the Corporation and C&F Bank continue to exceed regulatory minimum requirements. The primary indicators relied on by bank regulators in measuring the capital position at December 31, 2014 and December 31, 2013, are the Tier 1 capital, total risk-based capital, and leverage ratios, as further described in Item 8. "Financial Statements and Supplementary Data" under the heading "Note 15: Regulatory Requirements and Restrictions." The Corporation's Tier 1 capital to risk-weighted assets ratio was 13.3 percent at December 31, 2014, compared with 13.4 percent at December 31, 2013. The total capital to risk-weighted assets ratio was 14.5 percent at December 31, 2014, compared with 14.7 percent at December 31, 2013. The Tier 1 leverage ratio was 9.2 percent at December 31, 2014, compared with 8.9 percent at December 31, 2013. These ratios are in excess of the mandated minimum requirements. These ratios include the trust preferred securities issued by the Corporation in December 2003, December 2007 and July 2005, as well as issued by CVBK in 2003 and assumed by the Corporation in March 2014.

Shareholders' equity was \$123.4 million at year-end 2014 compared with \$112.9 million at year-end 2013. During 2014, the Corporation declared common stock dividends of \$1.19 per share, compared to \$1.16 per share declared in 2013 and \$1.08 per share declared in 2012. The dividend payout ratio was 32.8 percent of basic earnings per share for the year ended December 31, 2014, compared to 26.6 percent in 2013 and 21.6 percent in 2012. On April 11, 2012, the Corporation redeemed the remaining \$10.0 million of the total \$20.0 million of Series A Preferred Stock. The funds for this redemption were provided by existing financial resources of the Corporation and no new capital was issued. In addition, on May 14, 2014, the Corporation repurchased the ten-year warrant to purchase up to 167,504 shares of the Corporation's common stock, par value \$1.00 per share at an initial exercise price of \$17.91 per share for \$2.3 million. The funds for this redemption were provided by existing financial resources of the Corporation and no new capital was issued.

In June 2013, the federal bank regulatory agencies adopted the Basel III Final Rules (i) to implement the Basel III capital framework and (ii) for calculating risk-weighted assets. These rules are effective beginning January 1, 2015, subject to limited phase-in periods. Refer to Item 1. "Business" under the heading "Regulation and Supervision" for an overview of the Basel III Final Rules.

#### RECENT ACCOUNTING PRONOUNCEMENTS

Recent accounting pronouncements affecting the Corporation are described in Item 8, "Financial Statements and Supplementary Data," under the heading "Note 1: Summary of Significant Accounting Policies-Recent Significant Accounting Pronouncements."

#### EFFECTS OF INFLATION AND CHANGING PRICES

The Corporation's financial statements included herein have been prepared in accordance with accounting principles generally accepted in the United States ("GAAP"). GAAP presently requires the Corporation to measure financial position and operating results primarily in terms of historic dollars. Changes in the relative value of money due to inflation or recession are generally not considered. The primary effect of inflation on the operations of the Corporation is reflected in increased operating costs. In management's opinion, changes in interest rates affect the financial condition of a financial institution to a far greater degree than changes in the inflation rate. While interest rates are greatly influenced by changes in the inflation rate, they do not necessarily change at the same rate or in the same magnitude as the inflation rate. Interest rates are highly sensitive to many factors that are beyond the control of the Corporation, including changes in the expected rate of inflation, the influence of general and local economic conditions and the monetary and fiscal policies of the United States government, its agencies and various other governmental regulatory authorities.

#### ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The Corporation's primary component of market risk is interest rate volatility. Fluctuations in interest rates will impact the amount of interest income and expense the Corporation receives or pays on a significant portion of its assets and liabilities and the market value of its interest-earning assets and interest-bearing liabilities, excluding those which have a very short term until maturity. The Corporation does not subject itself to foreign currency exchange rate risk or commodity price risk due to the current nature of its operations. The Corporation had four outstanding interest rate swaps used as hedging transactions at December 31, 2014. The interest rate swaps were entered into to fix the rate of interest

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paid on \$25.0 million of the Corporation's variable rate trust preferred capital notes. Two interest rate swaps with a total notional value of \$10.0 million mature in 2015 and two interest rate swaps with a total notional value of \$15.0 million mature in 2019.

The primary objective of the Corporation's asset/liability management process is to maximize current and future net interest income within acceptable levels of interest rate risk while satisfying liquidity and capital requirements. Management recognizes that a certain amount of interest rate risk is inherent and appropriate. Thus the goal of interest rate risk management is to maintain a balance between risk and reward such that net interest income is maximized while risk is maintained at an acceptable level.

The Corporation assumes interest rate risk as a result of its normal operations. The fair values of most of the Corporation's financial instruments will change when interest rates change and that change may be either favorable or unfavorable to the Corporation. Management attempts to match maturities and repricing dates of assets and liabilities to the extent believed necessary to balance minimizing interest rate risk and increasing net interest income in current market conditions. However, borrowers with fixed rate obligations are less likely to prepay in a rising rate environment and more likely to prepay in a falling rate environment. Conversely, depositors who are receiving fixed rates are more likely to withdraw funds before maturity in a rising rate environment and less likely to do so in a falling rate environment. Management monitors rates, maturities and repricing dates of assets and liabilities and attempts to manage interest rate risk by adjusting terms of new loans, deposits and borrowings and by investing in securities with terms that manage the Corporation's overall interest rate risk.

We use simulation analysis to assess earnings at risk and economic value of equity (EVE) analysis to assess economic value at risk. These methods allow management to regularly monitor both the direction and magnitude of the Corporation's interest rate risk exposure. These modeling techniques involve assumptions and estimates that inherently cannot be measured with complete precision. Key assumptions in the analyses include maturity and repricing characteristics of both assets and liabilities, prepayments on amortizing assets, other embedded options, non-maturity deposit sensitivity and loan and deposit pricing. These assumptions are inherently uncertain due to the timing, magnitude and frequency of rate changes and changes in market conditions and management strategies, among other factors. However, the analyses are useful in quantifying risk and provide a relative gauge of the Corporation's interest rate risk position over time.

Simulation analysis evaluates the potential effect of upward and downward changes in market interest rates on future net interest income. The analysis involves changing the interest rates used in determining net interest income over the next twelve months. The resulting percentage change in net interest income in various rate scenarios is an indication of the Corporation's shorter-term interest rate risk. The analysis utilizes a "static" balance sheet approach, which assumes changes in interest rates without any management response to change the composition of the balance sheet. The measurement date balance sheet composition is maintained over the simulation time period with maturing and repayment dollars being rolled back into like instruments for new terms at current market rates. Additional assumptions are applied to modify volumes and pricing under the various rate scenarios. These assumptions include

loan prepayments, time deposit early withdrawals, the sensitivity of deposit repricing to changes in market rates, withdrawal behavior of non-maturing deposits, and other factors that management deems significant.

The simulation analysis results are presented in the table below. These results, based on a measurement date balance sheet as of December 31, 2014, indicate that the Corporation would expect net interest income to decrease over the next twelve months 2.82 percent assuming an immediate downward shift in market interest rates of 200 basis points (BP) and to increase 1.79 percent if rates shifted upward in the same manner.

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## 1-Year Net Interest Income Simulation (dollars in thousands)

Assumed Market Interest Rate Shift	Hypothetical Change in Net Interest Income for the Year Ended December 31, 2014		
	Dollars	Percentage	
-200 BP shock	\$ (2,152)	(2.82)	%
+200 BP shock	\$ 1,366	1.79	%

The EVE analysis provides information on the risk inherent in the balance sheet that might not be taken into account in the simulation analysis due to the shorter time horizon used in that analysis. The EVE of the balance sheet is defined as the discounted present value of expected asset cash flows minus the discounted present value of the expected liability cash flows. The analysis involves changing the interest rates used in determining the expected cash flows and in discounting the cash flows. The resulting percentage change in net present value in various rate scenarios is an indication of the longer term repricing risk and options embedded in the balance sheet.

The EVE analysis results are presented in the table below. These results as of December 31, 2014 indicate that the EVE would decrease 9.59 percent assuming an immediate downward shift in market interest rates of 200 BP and would increase 1.52 percent if rates shifted upward in the same manner.

## Static EVE Change (dollars in thousands)

Assumed Market Interest Rate Shift	Hypothetical Change in EVE		
	Dollars	Percentage	
-200 BP shock	\$ (19,844)	(9.59)	%
+200 BP shock	\$ 3,150	1.52	%

In the net interest income simulation above, net interest income increases over the next twelve months in the event of an immediate upward shift in interest rates, but declines in the event of an immediate downward shift in interest rates. In a rising rate environment, the Corporation's assets would reprice quicker than what the Corporation pays on its

borrowings and deposits primarily due to the shorter maturity or repricing dates of its interest-bearing deposits in other banks and loan portfolios. However, in a falling rate environment the simulation assumes that adjustable-rate assets will continue to reprice downward, subject to floors on certain loans, and fixed-rate assets with prepayment or callable options will reprice at lower rates while certain deposits cannot reprice any lower.

The EVE analysis above indicates an increase in the EVE in an immediate upward shift in interest rates, and a decrease in the EVE in an immediate downward shift in interest rates. The Corporation's assets would reprice quicker over time than what the Corporation pays on its borrowings and deposits due to the shorter maturity or repricing dates of its interest-bearing deposits in other banks and investment and loan portfolios as compared to time deposits and borrowings and the longer average life of non-maturing deposits, such as interest checking and money market accounts. During 2014, balances in interest-bearing deposits in other banks increased, the maturity or repricing dates in the Corporation's investment portfolio were shortened, and the maturity or repricing dates in the Corporation's borrowings were lengthened.

We believe that our current interest rate exposure is manageable and does not indicate any significant exposure to interest rate changes.

C&F Mortgage enters into IRLCs with customers and will sell the underlying loans to investors on either a best efforts or a mandatory basis. C&F Mortgage mitigates interest rate risk on IRLCs and loans held for sale by (a) entering into forward loan sales contracts with investors for loans to be delivered on a best efforts basis or (b) entering into forward sales contracts of TBAs for loans to be delivered on a mandatory basis. Both the IRLCs with customers and the forward sales contracts are considered derivative financial instruments. At December 31, 2014, the Corporation had forward sales contracts with a notional value of \$66.7 million. The fair value of these derivative instruments at December 31, 2014 was \$448,000, which was included in other assets.

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## ITEM 8.FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

## CONSOLIDATED BALANCE SHEETS

(Dollars in thousands, except for share and per share amounts)	December 31,	
	2014	2013
<b>Assets</b>		
Cash and due from banks	\$ 10,749	\$ 14,666
Interest-bearing deposits in other banks	156,867	41,750
Federal funds sold	—	91,723
Total cash and cash equivalents	167,616	148,139
Securities—available for sale at fair value, amortized cost of \$214,437 and \$217,708, respectively	221,897	218,110
Loans held for sale, at fair value	28,279	35,879
Loans, net of allowance for loan losses of \$35,606 and \$34,852, respectively	800,198	785,532
Restricted stocks, at cost	3,442	4,336
Corporate premises and equipment, net	37,295	38,232
Other real estate owned, net of valuation allowance of \$29 and \$4,135, respectively	786	2,769
Accrued interest receivable	6,421	6,360
Goodwill	14,425	14,425
Core deposit intangible, net	2,583	3,774
Bank-owned life insurance	14,484	13,988
Other assets	35,897	40,753
Total assets	\$ 1,333,323	\$ 1,312,297
<b>Liabilities</b>		
<b>Deposits</b>		
Noninterest-bearing demand deposits	\$ 161,839	\$ 147,520
Savings and interest-bearing demand deposits	497,755	460,889
Time deposits	366,507	399,883
Total deposits	1,026,101	1,008,292
Short-term borrowings	14,436	11,780
Long-term borrowings	127,488	132,987
Trust preferred capital notes	25,103	25,068
Accrued interest payable	740	843
Other liabilities	16,082	20,386
Total liabilities	1,209,950	1,199,356
Commitments and contingent liabilities	—	—



Shareholders' Equity

Common stock (\$1.00 par value, 8,000,000 shares authorized, 3,418,750 and 3,388,793 shares issued and outstanding, respectively, includes, 135,600 and 120,183 of nonvested shares, respectively)	3,283	3,269
Additional paid-in capital	9,456	10,686
Retained earnings	107,548	99,252
Accumulated other comprehensive income (loss), net	3,086	(266)
Total shareholders' equity	123,373	112,941
Total liabilities and shareholders' equity	\$ 1,333,323	\$ 1,312,297

See notes to consolidated financial statements.

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## CONSOLIDATED STATEMENTS OF INCOME

(Dollars in thousands, except per share amounts)	Year Ended December 31,		
	2014	2013	2012
Interest income			
Interest and fees on loans	\$ 79,207	\$ 74,415	\$ 71,947
Interest on interest-bearing deposits and federal funds sold	378	159	22
Interest and dividends on securities			
U.S. government agencies and corporations	1,918	914	273
Tax-exempt obligations of states and political subdivisions	4,417	4,573	4,659
Taxable obligations of states and political subdivisions	184	47	—
Corporate bonds and other	391	104	63
Total interest income	86,495	80,212	76,964
Interest expense			
Savings and interest-bearing deposits	1,015	867	824
Time deposits	3,065	3,384	4,501
Borrowings	3,485	3,561	3,799
Trust preferred capital notes	960	811	987
Total interest expense	8,525	8,623	10,111
Net interest income	77,970	71,589	66,853
Provision for loan losses	16,330	15,085	12,405
Net interest income after provision for loan losses	61,640	56,504	54,448
Noninterest income			
Gains on sales of loans	5,108	7,510	7,692
Service charges on deposit accounts	4,468	4,197	3,326
Other service charges and fees	6,246	6,220	6,310
Investment services income	1,229	1,060	1,017
Gains on calls and sales of available for sale securities	29	276	11
Other income	2,491	2,957	2,266
Total noninterest income	19,571	22,220	20,622
Noninterest expenses			
Salaries and employee benefits	36,310	31,167	27,813
Occupancy expenses	8,806	7,397	6,795
Other expenses	19,019	19,048	16,434
Total noninterest expenses	64,135	57,612	51,042
Income before income taxes	17,076	21,112	24,028
Income tax expense	4,730	6,710	7,646
Net income	12,346	14,402	16,382
Effective dividends on preferred stock	—	—	311
Net income available to common shareholders	\$ 12,346	\$ 14,402	\$ 16,071
Earnings per common share—basic	\$ 3.63	\$ 4.36	\$ 5.00
Earnings per common share—assuming dilution	\$ 3.59	\$ 4.18	\$ 4.86

See notes to consolidated financial statements.

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## CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(Dollars in thousands)	Year Ended December 31,		
	2014	2013	2012
Net income	\$ 12,346	\$ 14,402	\$ 16,382
Other comprehensive income (loss), net:			
Changes in defined benefit plan assets and benefit obligations			
Changes in net (loss) gain arising during the period <sup>1</sup>	(2,048)	985	31
Tax effect	717	(344)	(11)
Amortization of prior service cost arising during the period <sup>1</sup>	(68)	(68)	(68)
Tax effect	24	24	24
Net of tax amount	(1,375)	597	(24)
Unrealized gain on cash flow hedging instruments			
Unrealized holding gain arising during the period	227	182	1
Tax effect	(89)	(71)	—
Net of tax amount	138	111	1
Unrealized holding gains (losses) on securities			
Unrealized holding gains (losses) arising during the period	7,088	(8,478)	2,096
Tax effect	(2,480)	2,967	(734)
Reclassification adjustment for gains included in net income <sup>2</sup>	(29)	(276)	(11)
Tax effect	10	97	4
Net of tax amount	4,589	(5,690)	1,355
Other comprehensive income (loss), net:	3,352	(4,982)	1,332
Comprehensive income, net	\$ 15,698	\$ 9,420	\$ 17,714

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<sup>1</sup> These items are included in the computation of net periodic benefit cost, which is a component of salaries and employee benefits expense on the consolidated statements of income. See Note 12, Employee Benefit Plans, for additional information.

<sup>2</sup> Gains are included in "Net gains on calls and sales of available for sale securities" on the consolidated statements of income.

See notes to consolidated financial statements.

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## CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

	Preferred	Common	Additional Paid - In	Retained	Accumulated Other Comprehensive	Total Shareholders'
(Dollars in thousands, except per share amounts)	Stock	Stock	Capital	Earnings	Income (Loss)	Equity
Balance December 31, 2011	\$ 10	\$ 3,091	\$ 13,438	\$ 76,167	\$ 3,384	\$ 96,090
Comprehensive income:						
Net income	—	—	—	16,382	—	16,382
Other comprehensive income, net	—	—	—	—	1,332	1,332
Stock options exercised	—	49	1,260	—	—	1,309
Share-based compensation	—	—	537	—	—	537
Restricted stock vested	—	16	13	—	—	29
Accretion of preferred stock discount	—	—	172	(172)	—	—
Preferred stock redemption	(10)	—	(9,990)	—	—	(10,000)
Common stock issued	—	6	194	—	—	200
Cash dividends declared – common stock (\$1.08 per share)	—	—	—	(3,479)	—	(3,479)
Cash dividends paid – preferred stock (5% per annum)	—	—	—	(203)	—	(203)
Balance December 31, 2012	—	3,162	5,624	88,695	4,716	102,197
Comprehensive income:						
Net income	—	—	—	14,402	—	14,402
Other comprehensive income (loss), net	—	—	—	—	(4,982)	(4,982)
Stock options exercised	—	94	4,207	—	—	4,301
Share-based compensation	—	—	687	—	—	687
Restricted stock vested	—	11	101	—	—	112
Common stock issued	—	3	122	—	—	125
Common stock purchased	—	(1)	(55)	—	—	(56)
Cash dividends declared – common stock (\$1.16 per share)	—	—	—	(3,845)	—	(3,845)
Balance December 31, 2013	—	3,269	10,686	99,252	(266)	112,941
Comprehensive income:						
Net income	—	—	—	12,346	—	12,346
Other comprehensive income, net	—	—	—	—	3,352	3,352

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Common stock warrant repurchased	—	—	(2,303)	—	—	(2,303)
Stock options exercised	—	—	11	—	—	11
Share-based compensation	—	—	1,024	—	—	1,024
Restricted stock vested	—	15	65	—	—	80
Common stock issued	—	3	130	—	—	133
Common stock purchased	—	(4)	(157)	—	—	(161)
Cash dividends declared – common stock (\$1.19 per share)	—	—	—	(4,050)	—	(4,050)
Balance December 31, 2014	\$ —	\$ 3,283	\$ 9,456	\$ 107,548	\$ 3,086	\$ 123,373

See notes to consolidated financial statements.

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## CONSOLIDATED STATEMENTS OF CASH FLOWS

(Dollars in thousands)	Year Ended December 31,		
	2014	2013	2012
Operating activities:			
Net income	\$ 12,346	\$ 14,402	\$ 16,382
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation	2,739	2,349	2,270
Deferred income taxes	2,247	2,286	(848)
Provision for loan losses	16,330	15,085	12,405
Provision for indemnifications	240	558	1,205
Provision for other real estate owned losses	29	459	1,250
Share-based compensation	1,104	743	566
Net accretion of certain acquisition-related fair value adjustments	(2,969)	(844)	—
Accretion of discounts and amortization of premiums on securities, net	1,406	812	731
Realized gains on sales and calls of securities	(29)	(276)	(11)
Net realized gains on sales of other real estate owned	(324)	(218)	(39)
Net realized (gain) loss on sale of premises and equipment	(96)	165	—
Increase in bank-owned life insurance cash surrender value	(497)	(188)	(108)
Origination of loans held for sale	(478,641)	(721,340)	(840,140)
Proceeds from sales of loans held for sale	491,349	765,698	845,167
Gains on sales of loans held for sale	(5,108)	(7,510)	(7,692)
Change in other assets and liabilities:			
Accrued interest receivable	(61)	333	(431)
Other assets	(1,285)	484	(1,172)
Accrued interest payable	(103)	(905)	(274)
Other liabilities	(4,500)	(8,455)	18
Net cash provided by operating activities	34,177	63,638	29,279
Investing activities:			
Proceeds from maturities, calls and sales of securities available for sale	38,660	79,441	34,100
Purchases of securities available for sale	(36,246)	(33,823)	(40,906)
Net redemptions of FHLB stock	894	2,090	23
Net increase in customer loans	(30,288)	(13,030)	(39,570)
Other real estate owned improvements	—	—	(205)
Proceeds from sales of other real estate owned	4,382	4,209	2,683
Purchases of corporate premises and equipment, net	(1,815)	(3,654)	(891)
Acquisition of Central Virginia Bankshares, Inc., net of cash paid	—	55,579	—
Net cash (used in) provided by investing activities	(24,413)	90,812	(44,766)
Financing activities:			

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Net increase in demand, interest-bearing demand and savings deposits	51,185	20,955	61,102
Net decrease in time deposits	(32,258)	(14,002)	(21,334)
Net (decrease) increase in borrowings	(2,844)	(39,465)	1,595
Redemption of preferred stock	—	—	(10,000)
Repurchase of common stock warrant	(2,303)	—	—
Issuance of common stock	133	125	200
Repurchase of common stock	(161)	—	—
Proceeds from exercise of stock options	11	4,301	1,309
Cash dividends	(4,050)	(3,845)	(3,682)
Net cash provided by (used in) financing activities	9,713	(31,931)	29,190
Net increase in cash and cash equivalents	19,477	122,519	14,113
Cash and cash equivalents at beginning of year	148,139	25,620	11,507
Cash and cash equivalents at end of year	\$ 167,616	\$ 148,139	\$ 25,620
Supplemental disclosure			
Interest paid	\$ 9,710	\$ 9,528	\$ 10,385
Income taxes paid	3,577	5,986	8,949
Supplemental disclosure of noncash investing and financing activities			
Unrealized gains (losses) on securities available for sale	\$ 7,059	\$ (8,754)	\$ 2,085
Transfers between loans and other real estate owned	(1,960)	(588)	(3,866)
Pension adjustment	(2,116)	917	(37)
Unrealized gains on cash flow hedging instruments	227	182	1
Assets acquired, excluding cash and cash equivalents of \$59,775	—	311,173	—
Liabilities assumed	—	366,752	—

See notes to consolidated financial statements.



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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1: Summary of Significant Accounting Policies

**Principles of Consolidation:** The accompanying consolidated financial statements include the accounts of C&F Financial Corporation (the Corporation) and its wholly owned subsidiary, Citizens and Farmers Bank (the Bank or C&F Bank). All significant intercompany accounts and transactions have been eliminated in consolidation. In addition, C&F Financial Corporation owns C&F Financial Statutory Trust I and C&F Financial Statutory Trust II, and Central Virginia Bankshares Statutory Trust I, all of which are unconsolidated subsidiaries. The subordinated debt owed to these trusts is reported as a liability of the Corporation. The accounting and reporting policies of C&F Financial Corporation and Subsidiaries conform to accounting principles generally accepted in the United States of America (U.S. GAAP) and to predominant practices within the banking industry.

**Nature of Operations:** C&F Financial Corporation is a bank holding company incorporated under the laws of the Commonwealth of Virginia. The Corporation owns all of the stock of its subsidiary, C&F Bank, which is an independent commercial bank chartered under the laws of the Commonwealth of Virginia. On October 1, 2013, the Corporation acquired Central Virginia Bankshares, Inc. (CVBK) and its wholly-owned subsidiary, Central Virginia Bank (CVB), which was an independent commercial bank chartered under the laws of the Commonwealth of Virginia. On March 22, 2014, CVBK was merged with and into C&F Financial Corporation and CVB was merged with and into C&F Bank.

C&F Bank has five wholly-owned active subsidiaries: C&F Mortgage Corporation and Subsidiary (C&F Mortgage), C&F Finance Company (C&F Finance), C&F Investment Services, Inc., C&F Insurance Services, Inc., and CVB Title Services, Inc. all incorporated under the laws of the Commonwealth of Virginia. C&F Mortgage, organized in September 1995, was formed to originate and sell residential mortgages and through its subsidiary, Certified Appraisals LLC, provides ancillary mortgage loan production services for residential appraisals. C&F Finance, acquired on September 1, 2002, is a finance company providing automobile loans through indirect lending programs. C&F Investment Services, Inc., organized in April 1995, is a full-service brokerage firm offering a comprehensive range of investment services. C&F Insurance Services, Inc., organized in July 1999, owns an equity interest in an insurance agency that sells insurance products to customers of C&F Bank, C&F Mortgage and other financial institutions that have an equity interest in the agency. CVB Title Services, Inc., was organized for the primary purpose of owning membership interests in two insurance-related limited liability companies. Business segment data is presented in Note 18.

**Basis of Presentation:** The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and 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. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses, the allowance for indemnifications, impairment of loans, impairment of securities, the valuation of other real estate owned, the projected benefit obligation under the defined benefit pension plan, the valuation of deferred taxes, fair value measurements and goodwill impairment. In the opinion of management, all adjustments, consisting only of normal recurring adjustments, which are necessary for a fair presentation of the results of operations in these financial statements, have been made. Certain reclassifications have been made to prior period amounts to conform to the current year presentation.

**Significant Group Concentrations of Credit Risk:** The Corporation invests in a variety of securities, principally obligations of U.S. government agencies and obligations of states and political subdivisions. At December 31, 2014, securities issued by the Commonwealth of Virginia and its political subdivisions comprised 10.5 percent of its state and political subdivision portfolio and securities issued by the Virginia State Housing Authority comprised 2.8 percent of its state and political subdivision portfolio. There are no other concentrations in any one state greater than 10.0 percent and no other individual issuers greater than 1.5 percent. The Corporation does not have any other significant securities concentrations in any one industry or geographic region, or to any one issuer. Note 3 discusses the Corporation's securities portfolio and investment activities.

Substantially all of the Corporation's lending activities are with customers located in Virginia, Georgia and Tennessee. At December 31, 2014, 36.7 percent of the Corporation's loan portfolio consisted of commercial, financial and agricultural

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loans, which include loans secured by real estate for builder lines, acquisition and development and commercial development, as well as commercial loans secured by personal property. In addition, 33.9 percent of the Corporation's loan portfolio consisted of non-prime consumer finance loans to individuals, secured by automobiles. The Corporation does not have any significant loan concentrations to any one customer. Note 4 discusses the Corporation's lending activities.

**Business Combination:** On October 1, 2013, C&F Financial Corporation acquired CVBK. This acquisition was accounted for using the acquisition method of accounting, meaning the assets and liabilities of CVBK were recorded at their respective fair values as of October 1, 2013. These fair values were preliminary and subject to refinement for up to one year after the closing date of the transaction (the Measurement Period) as information relative to closing date fair values became available. The Corporation's financial position and results of operations as of and for the year ended December 31, 2013 include CVBK's financial position as of December 31, 2013 and CVBK's results of operations from October 1, 2013. Note 2 presents the Measurement Period adjustments to the preliminary fair values.

**Cash and Cash Equivalents:** For purposes of the consolidated statements of cash flows, cash and cash equivalents include cash, balances due from banks, interest-bearing deposits in banks and federal funds sold, all of which mature within 90 days. The Bank is required to maintain average balances on hand or with the Federal Reserve Bank (FRB). At December 31, 2014, the minimum requirement was \$713,000 for C&F Bank. At December 31, 2013, the minimum requirement was \$373,000 for C&F Bank and \$90,000 for CVB. The Corporation is required to maintain collateral against all loss positions in its interest rate swaps which are described in Note 19. At December 31, 2014, the Corporation was required to maintain collateral of \$620,000 in connection with its interest rate swaps.

**Securities:** Investments in debt and equity securities with readily determinable fair values are classified as either held to maturity, available for sale, or trading, based on management's intent. Currently all of the Corporation's investment securities are classified as available for sale. Available for sale securities are carried at estimated fair value with the corresponding unrealized gains and losses excluded from earnings and reported in other comprehensive income. Gains or losses are recognized in earnings on the trade date using the amortized cost of the specific security sold. Purchase premiums and discounts are recognized in interest income using the interest method over the terms of the securities.

Impairment of securities occurs when the fair value of a security is less than its amortized cost. For debt securities, impairment is considered other-than-temporary and recognized in its entirety in net income if either (i) we intend to sell the security or (ii) it is more-likely-than-not that we will be required to sell the security before recovery of its amortized cost basis. If, however, the Corporation does not intend to sell the security and it is not more-likely-than-not that the Corporation will be required to sell the security before recovery, the Corporation must determine what portion of the impairment is attributable to a credit loss, which occurs when the amortized cost basis of the security exceeds the present value of the cash flows expected to be collected from the security. If there is no credit loss, there is no other-than-temporary impairment. If there is a credit loss, other-than-temporary impairment exists, and the credit loss must be recognized in net income and the remaining portion of impairment must be recognized in other comprehensive income. For equity securities, impairment is considered to be other-than-temporary based on the

Corporation's ability and intent to hold the investment until a recovery of fair value. Other-than-temporary impairment of an equity security results in a write-down that must be included in net income. The Corporation regularly reviews each investment security for other-than-temporary impairment based on criteria that include the extent to which cost exceeds market price, the duration of that market decline, the financial health of and specific prospects for the issuer, the Corporation's best estimate of the present value of cash flows expected to be collected from debt securities, the Corporation's intention with regard to holding the security to maturity and the likelihood that the Corporation would be required to sell the security before recovery.

**Loans Held for Sale:** During the second quarter of 2013, the Corporation elected to begin using fair value accounting for its entire portfolio of loans held for sale (LHFS) in accordance with ASC 820 - Fair Value Measurement and Disclosures. Fair value of the Corporation's LHFS is based on observable market prices for similar instruments traded in the secondary mortgage loan markets in which the Corporation conducts business. Substantially all loans originated by C&F Mortgage are held for sale to outside investors.

**Loans Acquired in a Business Combination:** Loans acquired in a business combination, such as C&F Financial Corporation's acquisition of CVB, are recorded at estimated fair value on the date of acquisition without the carryover of

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the related allowance for loan losses. Purchased credit-impaired (PCI) loans are those for which there is evidence of credit deterioration since origination and for which it is probable at the date of acquisition that the Corporation will not collect all contractually required principal and interest payments. When determining fair market value, PCI loans were aggregated into pools of loans based on common risk characteristics as of the date of acquisition such as loan type, date of origination, and evidence of credit quality deterioration such as internal risk grades and past due and nonaccrual status. The difference between contractually required payments at acquisition and the cash flows expected to be collected at acquisition is referred to as the "nonaccretable difference," and is not recorded. Any excess of cash flows expected at acquisition over the estimated fair value is referred to as the accretable yield and is recognized as interest income over the remaining life of the loan when there is a reasonable expectation about the amount and timing of such cash flows. Subsequent decreases to the expected cash flows will generally result in a provision for loan losses, while subsequent increases in cash flows may result in a reversal of post-acquisition provision for loan losses, or a transfer from nonaccretable difference to accretable yield.

Loans not designated PCI loans as of the acquisition date are designated Purchased Performing Loans. The Corporation accounts for purchased performing loans using the contractual cash flows method of recognizing discount accretion based on the acquired loans' contractual cash flows. Purchased performing loans are recorded at fair value, including a credit discount. The fair value discount is accreted as an adjustment to yield over the estimated lives of the loans. There is no allowance for loan losses established at the acquisition date for purchased performing loans. A provision for loan losses is recorded for any deterioration in these loans subsequent to the acquisition.

Originated Loans: The Corporation makes mortgage, commercial and consumer loans to customers. Our recorded investment in loans that management has the intent and ability to hold for the foreseeable future or until maturity or pay-off generally are reported at their unpaid principal balances adjusted for charges-offs, unearned discounts, any deferred fees or costs on originated loans, and the allowance for loan losses. Interest on loans is credited to operations based on the principal amount outstanding. Loan fees and origination costs are deferred and the net amount is amortized as an adjustment of the related loan's yield using the level-yield method. The Corporation is amortizing these amounts over the contractual life of the related loans.

A loan's past due status is based on the contractual due date of the most delinquent payment due. Loans are generally placed on nonaccrual status when the collection of principal or interest is 90 days or more past due, or earlier, if collection is uncertain based on an evaluation of the net realizable value of the collateral and the financial strength of the borrower. Loans greater than 90 days past due may remain on accrual status if management determines it has adequate collateral to cover the principal and interest. For those loans that are carried on nonaccrual status, payments are first applied to principal outstanding. A loan may be returned to accrual status if the borrower has demonstrated a sustained period of repayment performance in accordance with the contractual terms of the loan and there is reasonable assurance the borrower will continue to make payments as agreed. These policies are applied consistently across our loan portfolio.

The Corporation considers a loan impaired when it is probable that the Corporation will be unable to collect all interest and principal payments as scheduled in the loan agreement. A loan is not considered impaired during a period of delay in payment if the ultimate collectibility of all amounts due is expected. Impairment is measured on a loan by loan basis for commercial, construction and residential loans in excess of \$500,000 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. Large groups of smaller balance homogeneous loans are collectively evaluated for impairment. Accordingly, the Corporation does not separately identify individual consumer, residential and certain small commercial loans that are less than \$500,000 for impairment disclosures, except for troubled debt restructurings (TDRs) as noted below. Consistent with the Corporation's method for nonaccrual loans, payments on impaired loans are first applied to principal outstanding, except potentially for TDRs as noted below.

TDRs occur when the Corporation agrees to significantly modify the original terms of a loan due to the deterioration in the financial condition of the borrower. TDRs are considered impaired loans. Upon designation as a TDR, the Corporation evaluates the borrower's payment history, past due status and ability to make payments based on the revised terms of the loan. If a loan was accruing prior to being modified as a TDR and if the Corporation concludes that the borrower is able to make such payments, and there are no other factors or circumstances that would cause it to conclude otherwise, the loan will remain on an accruing status. If a loan was on nonaccrual status at the time of the TDR, the loan will remain on

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nonaccrual status following the modification and may be returned to accrual status based on the policy for returning loans to accrual status as noted above. As of December 31, 2014 and 2013, the Corporation had \$5.83 million and \$5.62 million, respectively, of loans classified as TDRs.

Allowance for Loan Losses: The allowance for loan losses is established through charges to earnings in the form of a provision for loan losses. Loan losses are charged against the allowance for loan losses for the difference between the carrying value of the loan and the estimated net realizable value or fair value of the collateral, if collateral dependent, when:

- Management believes that the collectibility of the principal is unlikely regardless of delinquency status.
- The loan is a consumer loan and is 120 days past due.
- The loan is a non-consumer loan and is 180 days past due, unless the loan is well secured and recovery is probable.
- The borrower is in bankruptcy, unless the debt has been reaffirmed, is well secured and recovery is probable.

Subsequent recoveries, if any, are credited to the allowance.

The allowance represents an amount that, in management's judgment, will be adequate to absorb any losses on existing loans that may become uncollectible. Management's judgment in determining the level of the allowance is based on evaluations of the collectibility of loans while taking into consideration such factors as trends in delinquencies and charge-offs, changes in the nature and volume of the loan portfolio, current economic conditions that may affect a borrower's ability to repay and the value of collateral, overall portfolio quality and review of specific potential losses. This evaluation is inherently subjective, as it requires estimates that are susceptible to significant revision as more information becomes available. The evaluation also considers the following risk characteristics of each loan portfolio:

- Real estate residential mortgage loans carry risks associated with the continued credit-worthiness of the borrower and changes in the value of the collateral.
- Real estate construction loans carry risks that the project will not be finished according to schedule, the project will not be finished according to budget and the value of the collateral may, at any point in time, be less than the principal amount of the loan. Construction loans also bear the risk that the general contractor, who may or may not be a loan customer, may be unable to finish the construction project as planned because of financial pressure unrelated to the project.
- Commercial, financial and agricultural loans carry risks associated with the successful operation of a business or a real estate project, in addition to other risks associated with the ownership of real estate, because the repayment of these loans may be dependent upon the profitability and cash flows of the business or project. In addition, there is risk associated with the value of collateral other than real estate which may depreciate over time and cannot be appraised with as much precision.
- Consumer loans carry risks associated with the continued credit-worthiness of the borrower and the value of the collateral (e.g., rapidly-depreciating assets such as automobiles), or lack thereof. Consumer loans are more likely

- than real estate loans to be immediately adversely affected by job loss, divorce, illness or personal bankruptcy.
- Equity lines of credit carry risks associated with the continued credit-worthiness of the borrower and changes in the value of the collateral.
  - Consumer finance loans carry risks associated with the continued credit-worthiness of borrowers who may be unable to meet the credit standards imposed by most traditional automobile financing sources and the value of rapidly-depreciating collateral.



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The allowance consists of specific and general components. The specific component relates to loans that are classified as impaired, and is established when the discounted cash flows (or collateral value or observable market price) of the impaired loan is lower than the carrying value of that loan. For collateral dependent loans, an updated appraisal will be ordered if a current one is not on file. Appraisals are performed by independent third-party appraisers with relevant industry experience. Adjustments to the appraised value may be made based on recent sales of like properties or general market conditions when appropriate. The general component covers non-classified loans and those loans classified as doubtful, substandard or special mention that are not impaired. The general component is based on historical loss experience adjusted for qualitative factors, such as current economic conditions, including current home sales and foreclosures, unemployment rates and retail sales. Relative to non-classified loans, non-impaired classified loans are assigned a higher allowance factor which increases with the severity of classification. The characteristics of the loan ratings are as follows:

- Pass rated loans are to persons or business entities with an acceptable financial condition, appropriate collateral margins, appropriate cash flow to service the existing loan, and an appropriate leverage ratio. The borrower has paid all obligations as agreed and it is expected that this type of payment history will continue. When necessary, acceptable personal guarantors support the loan.
- Special mention loans have a specifically identified weakness in the borrower's operations and in the borrower's ability to generate positive cash flow on a sustained basis. The borrower's recent payment history is characterized by late payments. The Corporation's risk exposure is mitigated by collateral supporting the loan. The collateral is considered to be well-margined, well maintained, accessible and readily marketable.
- Substandard loans are considered to have specific and well-defined weaknesses that jeopardize the viability of the Corporation's credit extension. The payment history for the loan has been inconsistent and the expected or projected primary repayment source may be inadequate to service the loan. The estimated net liquidation value of the collateral pledged and/or ability of the personal guarantor(s) to pay the loan may not adequately protect the Corporation. There is a distinct possibility that the Corporation will sustain some loss if the deficiencies associated with the loan are not corrected in the near term. A substandard loan would not automatically meet our definition of impaired unless the loan is significantly past due and the borrower's performance and financial condition provide evidence that it is probable that the Corporation will be unable to collect all amounts due.
- Substandard nonaccrual loans have the same characteristics as substandard loans; however, they have a non-accrual classification because it is probable that the Corporation will not be able to collect all amounts due.
- Doubtful rated loans have all the weaknesses inherent in a loan that is classified substandard but with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions, and values, highly questionable and improbable. The possibility of loss is extremely high.
- Loss rated loans are not considered collectible under normal circumstances and there is no realistic expectation for any future payment on the loan. Loss rated loans are fully charged off.

The consumer finance loans are segregated between performing and nonperforming loans. Performing loans are those that have made timely payments in accordance with the terms of the loan agreement and are not past due 90 days or more. Nonperforming loans are those that do not accrue interest and are greater than 90 days past due.

**Allowance for Indemnifications:** The allowance for indemnifications is established through charges to earnings in the form of a provision for indemnifications, which is included in other noninterest expenses. A loss is charged against the

allowance for indemnifications when a purchaser of a loan (investor) sold by C&F Mortgage incurs a validated indemnified loss due to borrower misrepresentation, fraud, early payment default or underwriting error.

The allowance represents an amount that, in management's judgment, will be adequate to absorb any losses arising from valid indemnification requests. Management's judgment in determining the level of the allowance is based on the volume of loans sold, current economic conditions and information provided by investors. This evaluation is inherently subjective, as it requires estimates that are susceptible to significant revision as more information becomes available.

Restricted Stocks: Restricted stocks include Federal Home Loan Bank (FHLB) stock and Community Bankers Bank (CBB) stock owned by C&F Bank at December 31, 2014. At December 31, 2013 restricted stocks included FHLB stock

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owned by C&F Bank and FHLB stock, FRB stock and CBB stock owned by CVB. All of CVB's FRB stock was redeemed and C&F Bank assumed ownership of the CBB stock when CVB merged with and into C&F Bank on March 22, 2014. FHLB stock and CBB stock are carried at cost. No ready market exists for this stock and it has no quoted market value. For presentation purposes, such stock is assumed to have a market value that is equal to cost. Management reviews FHLB stock and CBB stock for impairment based on the ultimate recoverability of the cost basis.

**Other Real Estate Owned (OREO):** Assets acquired through, or in lieu of, loan foreclosure are held for sale and are initially recorded at fair value less costs to sell at the date of foreclosure. Subsequent to foreclosure, management periodically performs valuations of the foreclosed assets based on updated appraisals, general market conditions, recent sales of like properties, length of time the properties have been held, and our ability and intention with regard to continued ownership of the properties. The Corporation may incur additional write-downs of foreclosed assets to fair value less costs to sell if valuations indicate a further deterioration in market conditions. Revenue and expenses from operations and changes in the property valuations are included in net expenses from foreclosed assets and improvements are capitalized.

**Corporate Premises and Equipment:** Land is carried at cost. Buildings and equipment are carried at cost less accumulated depreciation computed using a straight-line method over the estimated useful lives of the assets. Estimated useful lives range from ten to forty years for buildings and from three to ten years for equipment, furniture and fixtures. Maintenance and repairs are charged to expense as incurred and major improvements are capitalized. Upon sale or retirement of depreciable properties, the cost and related accumulated depreciation are netted against proceeds and any resulting gain or loss is included in income. Depreciation expense for the years ended December 31, 2014, 2013 and 2012 was \$2.74 million, \$2.35 million and \$2.27 million, respectively.

**Goodwill:** The Corporation's goodwill was recognized in connection with the Corporation's acquisition of CVBK in October 2013 and its acquisition of C&F Finance in September 2002. With the adoption of Accounting Standards Update (ASU) 2011-08, Intangible-Goodwill and Other-Testing Goodwill for Impairment, in 2012, the Corporation may first assess qualitative factors to determine if it is more likely than not that the fair value of goodwill is less than the carrying amount, which determines if the two-step goodwill impairment test is necessary. If the likelihood of impairment is more than 50 percent, the Corporation must perform a test for impairment and may be required to record impairment charges. While not required to do so, as of December 31, 2014 the Corporation completed an annual test for impairment of goodwill related to the acquisition of C&F Finance and determined there was no impairment to be recognized in 2014.

**Core Deposit Intangible:** The Corporation's core deposit intangible (CDI) was recognized in connection with the Corporation's acquisition of CVB in October 2013, and represents the value of long-term deposit relationships acquired in this transaction. The Corporation is amortizing the CDI over an estimated weighted average life of six years using the sum-of-the-years digits method.

Transfer of Financial Assets: Transfers of loans are accounted for as sales when control over the loans has been surrendered. Control over transferred loans is deemed to be surrendered when (1) the loans have been isolated from the Corporation, (2) the transferee obtains the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred loans and (3) the Corporation does not maintain effective control over the transferred loans through an agreement to repurchase them before their maturity.

Income Taxes: The Corporation determines deferred income tax assets and liabilities using the liability (or balance sheet) method. Under this method, the net deferred tax asset or liability is determined annually for differences between the financial statement and tax bases of assets and liabilities that will result in taxable or deductible amounts in the future based on enacted tax laws and rates applicable to the periods in which the differences are expected to affect taxable income. Income tax expense is the tax payable or refundable for the period plus or minus the change during the period in deferred tax assets and liabilities.

When tax returns are filed, it is highly certain that some positions taken will be sustained upon examination by the taxing authorities, while others are subject to uncertainty about the merits of the position taken or the amount of the position that will be ultimately sustained. The benefit of a tax position is recognized in the financial statements in the period during which, based on all available evidence, management believes it is more likely than not that the position will be sustained

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upon examination, including the resolution of appeals or litigation processes, if any. Tax positions taken are not offset or aggregated with other positions. Tax positions that meet the more-likely-than-not recognition threshold are measured as the largest amount of tax benefit that is more than 50 percent likely of being realized upon settlement with the applicable taxing authority. The portion of the benefits associated with tax positions taken that exceeds the amount measured as described above is reflected as a liability for unrecognized tax benefits in the accompanying balance sheet along with any associated interest and penalties that would be payable to the taxing authorities upon examination. The Corporation did not have any liabilities resulting from unrecognized tax benefits as of December 31, 2014 and December 31, 2013. Interest and penalties associated with unrecognized tax benefits are classified as additional income taxes in the statements of income.

**Retirement Plan:** The Corporation recognizes the overfunded or underfunded status of its defined benefit postretirement plan as an asset or liability in the balance sheet and recognizes a change in the plan's funded status in the year in which the change occurs through other comprehensive income. The funded status of a benefit plan is measured as the difference between plan assets at fair value and the benefit obligation. For the Corporation's pension plan, the benefit obligation is the projected benefit obligation as of December 31. In addition, enhanced disclosures about certain effects on net periodic benefit cost for the next fiscal year that arise from delayed recognition of the gains or losses, prior service costs or credits and transition asset or obligation are presented in the notes to financial statements. Valuations at December 31, 2014 and 2013 determined that the Corporation's pension plan was overfunded. As a result, the Corporation recognized a pension asset of \$502,000 and \$965,000 at December 31, 2014 and 2013, respectively, and recognized a net loss of \$1.4 million in 2014, a net gain of \$597,000 in 2013 and a net loss of \$24,000 in 2012 as components of other comprehensive income (loss). The Corporation's pension plan is described more fully in Note 12.

**Share-Based Compensation:** Compensation expense for grants of restricted shares is accounted for using the fair market value of the Corporation's common stock on the date the restricted shares are awarded. Compensation expense for restricted shares is charged to income ratably over the vesting period. Compensation expense for the years ended December 31, 2014, 2013 and 2012 included \$967,000 (\$600,000 after tax), \$659,000 (\$409,000 after tax) and \$488,000 (\$303,000 after tax), respectively, for restricted stock granted during 2009 through 2014. As of December 31, 2014, there was \$2.79 million of unrecognized compensation expense related to unvested restricted stock that will be recognized over the remaining vesting periods. The Corporation estimates forfeitures when recognizing compensation expense and this estimate of forfeitures is adjusted over the requisite service period or vesting schedule based on the extent to which actual forfeitures differ from such estimates. Changes in estimated forfeitures in future periods, if any, will be recognized through a cumulative catch-up adjustment in the period of change, which will affect the amount of estimated unamortized compensation expense to be recognized in future periods. The Corporation's share-based compensation plans are described more fully in Note 14.

**Earnings Per Common Share:** The Financial Accounting Standards Board (FASB) guidance requires that all outstanding unvested share-based payment awards that contain rights to nonforfeitable dividends participate in undistributed earnings with common shareholders. This conclusion affects entities that accrue cash dividends on share-based payment awards during the awards' service period when the dividends do not need to be returned if the employees forfeit the awards. Because the awards are considered participating securities, the issuing entity is required

to apply the two-class method of computing basic and diluted earnings per share (EPS). The Corporation has applied the two-class method of computing basic and diluted EPS for each of the years ended December 31, 2014, 2013 and 2012 because the Corporation's unvested restricted shares outstanding contain rights to nonforfeitable dividends. Accordingly, the weighted average number of common shares used in the calculation of basic and diluted EPS includes both vested and unvested common shares outstanding. EPS calculations are presented in Note 10.

**Comprehensive Income:** Accounting principles generally require that recognized revenue, expenses, gains and losses be included in net income. Although certain changes in assets and liabilities, such as unrealized gains and losses on available for sale securities, changes in defined benefit plan assets and liabilities, and unrealized gains and losses on cash flow hedging instruments 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. These components are presented in the Corporation's Consolidated Statements of Comprehensive Income and are described more fully in Note 10.

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**Off-Balance-Sheet Credit Related Financial Instruments:** In the ordinary course of business, the Corporation has entered into commitments to extend credit and standby letters of credit. Such financial instruments are recorded when they are funded.

**Rate Lock Commitments:** C&F Mortgage enters into interest rate lock commitments (IRLCs) to originate residential mortgage loans for sale whereby the interest rate on the loan is determined prior to funding. The period of time between issuance of a loan commitment and closing and sale of the loan generally ranges from 15 to 90 days. C&F Mortgage protects itself from changes in interest rates by (a) entering into forward loan sales contracts with investors for loans to be delivered on a best efforts basis or (b) entering into forward sales contracts of mortgage-backed to-be-announced securities (TBAs) for loans to be delivered on a mandatory basis. Both the IRLCs with customers and the forward sales contracts are considered derivative financial instruments, which are discussed below.

**Derivative Financial Instruments:** The Corporation recognizes derivative financial instruments at fair value as either an other asset or other liability in the consolidated balance sheet. The Corporation's derivative financial instruments as of December 31, 2014 consisted of (1) the fair value of interest rate lock commitments (IRLCs) on mortgage loans that will be sold in the secondary market and the related forward commitments to sell mortgage loans and mortgage-backed securities (MBS) and (2) interest rate swaps that qualified as cash flow hedges on the Corporation's trust preferred capital notes. Because the IRLCs and forward sales commitments are not designated as hedging instruments, adjustments to reflect unrealized gains and losses resulting from changes in fair value of the Corporation's IRLCs and forward sales commitments and realized gains and losses upon ultimate sale of the loans are classified as noninterest income. The Corporation's IRLCs and forward loan sales commitments are described more fully in Note 16 and Note 17. The effective portion of the gain or loss on the Corporation's cash flow hedges is reported as a component of other comprehensive income, net of deferred income taxes, and reclassified into earnings in the same period or period(s) during which the hedged transactions affect earnings. The cash flow hedges are described more fully in Note 19.

**Recent Significant Accounting Pronouncements:**

In January 2014, the FASB issued ASU 2014-01, Investments-Equity Method and Joint Ventures - Accounting for Investments in Qualified Affordable Housing Projects (a consensus of the FASB Emerging Issues Task Force). The amendments in this ASU permit reporting entities to make an accounting policy election to account for their investments in qualified affordable housing projects using the proportional amortization method if certain conditions are met. Under the proportional amortization method, an entity amortizes the initial cost of the investment in proportion to the tax credits and other tax benefits received and recognizes the net investment performance in the income statement as a component of income tax expense (benefit). The amendments in this ASU should be applied retrospectively to all periods presented. A reporting entity that uses the effective yield method to account for its investments in qualified affordable housing projects before the date of adoption may continue to apply the effective yield method for those preexisting investments. The amendments in this ASU are effective for public business entities for annual periods and interim reporting periods within those annual periods, beginning after December 15, 2014.

Early adoption is permitted. The Corporation does not expect the adoption of ASU 2014-01 to have a material effect on its financial statements.

In January 2014, the FASB issued ASU 2014-04, Receivables - Troubled Debt Restructurings by Creditors - Reclassification of Residential Real Estate Collateralized Consumer Mortgage Loans upon Foreclosure (a consensus of the FASB Emerging Issues Task Force). The amendments in this ASU clarify that if or when an in substance repossession or foreclosure occurs, and a creditor is considered to have received physical possession of residential real estate property collateralizing a consumer mortgage loan, upon either (1) the creditor obtaining legal title to the residential real estate property upon completion of a foreclosure or (2) the borrower conveying all interest in the residential real estate property to the creditor to satisfy that loan through completion of a deed in lieu of foreclosure or through a similar legal agreement. Additionally, the amendments require interim and annual disclosure of both (1) the amount of foreclosed residential real estate property held by the creditor and (2) the recorded investment in consumer mortgage loans collateralized by residential real estate property that are in the process of foreclosure according to local requirements of the applicable jurisdiction. The amendments in this ASU are effective for public business entities for annual periods, and interim periods within those annual periods, beginning after December 15, 2014. The Corporation does not expect the adoption of ASU 2014-04 to have a material effect on its financial statements.



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In April 2014, the FASB issued ASU 2014-08, Presentation of Financial Statements (Topic 205) and Property, Plant, and Equipment (Topic 360): Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity. The amendments in this ASU change the criteria for reporting discontinued operations while enhancing disclosures in this area. Under the new guidance, only disposals representing a strategic shift in operations should be presented as discontinued operations. Those strategic shifts should have a major effect on the organization's operations and financial results and include disposals of a major geographic area, a major line of business, or a major equity method investment. The new guidance requires expanded disclosures about discontinued operations that will provide financial statement users with more information about the assets, liabilities, income, and expenses of discontinued operations. Additionally, the new guidance requires disclosure of the pre-tax income attributable to a disposal of a significant part of an organization that does not qualify for discontinued operations reporting. The amendments in the ASU are effective for public business entities for annual periods, and interim periods within those annual periods, beginning after December 15, 2014. Early adoption is permitted. The Corporation does not expect the adoption of ASU 2014-08 to have a material effect on its financial statements.

In June 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers: Topic 606. This ASU applies to any entity using U.S. GAAP that either enters into contracts with customers to transfer goods or services or enters into contracts for the transfer of nonfinancial assets unless those contracts are within the scope of other standards. The guidance supersedes the revenue recognition requirements in Revenue Recognition-Topic 605, most industry-specific guidance, and some cost guidance included in Revenue Recognition-Construction-Type and Production-Type Contracts-Subtopic 605-35. The core principle of the guidance is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. To be in alignment with the core principle, an entity must apply a five step process including: identification of the contract(s) with a customer, identification of performance obligations in the contract(s), determination of the transaction price, allocation of the transaction price to the performance obligations, and recognition of revenue when (or as) the entity satisfies a performance obligation. Additionally, the existing requirements for the recognition of a gain or loss on the transfer of nonfinancial assets that are not in a contract with a customer have also been amended to be consistent with the guidance on recognition and measurement. The amendments in this ASU are effective for annual reporting periods beginning after December 15, 2016, including interim periods within that reporting period. Early adoption is not permitted. The Corporation is currently assessing the effect that ASU 2014-09 will have on its financial statements.

In June 2014, the FASB issued ASU No. 2014-11, Transfers and Servicing (Topic 860): Repurchase-to-Maturity Transactions, Repurchase Financings, and Disclosures. This ASU aligns the accounting for repurchase-to-maturity transactions and repurchase agreements executed as a repurchase financing with the accounting for other typical repurchase agreements. The new guidance eliminates sale accounting for repurchase-to-maturity transactions and supersedes the guidance under which a transfer of a financial asset and a contemporaneous repurchase financing could be accounted for on a combined basis as a forward agreement. The amendments in the ASU also require a new disclosure for transactions economically similar to repurchase agreements in which the transferor retains substantially all of the exposure to the economic return on the transferred financial assets throughout the term of the transaction. Additional disclosures will be required for the nature of collateral pledged in repurchase agreements and similar transactions accounted for as secured borrowings. The amendments in this ASU are effective for the first interim or annual period beginning after December 15, 2014; however, the disclosure for transactions accounted for as secured borrowings is required to be presented for annual periods beginning after December 15, 2014, and interim periods

beginning after March 15, 2015. Early adoption is not permitted. The Corporation is currently assessing the effect that ASU 2014-11 will have on its financial statements.

In June 2014, the FASB issued ASU No. 2014-12, Compensation - Stock Compensation (Topic 718): Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved after the Requisite Service Period. The new guidance applies to reporting entities that grant employees share-based payments in which the terms of the award allow a performance target to be achieved after the requisite service period. The amendments in the ASU require that a performance target that affects vesting and that could be achieved after the requisite service period be treated as a performance condition. Existing guidance in Compensation - Stock Compensation (Topic 718), should be applied to account for these types of awards. The amendments in this ASU are effective for annual periods and interim periods within those annual periods beginning after December 15, 2015. Early adoption is permitted and reporting

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entities may choose to apply the amendments in the ASU either on a prospective or retrospective basis. The Corporation is currently assessing the effect that ASU 2014-12 will have on its financial statements.

In August 2014, the FASB issued ASU No. 2014-14, Receivables - Troubled Debt Restructurings by Creditors (Subtopic 310-40): Classification of Certain Government-Guaranteed Mortgage Loans upon Foreclosure. The amendments in this ASU apply to creditors that hold government-guaranteed mortgage loans and is intended to eliminate the diversity in practice related to the classification of these guaranteed loans upon foreclosure. The new guidance stipulates that a mortgage loan be derecognized and a separate other receivable be recognized upon foreclosure if (1) the loan has a government guarantee that is not separable from the loan prior to foreclosure, (2) at the time of foreclosure, the creditor has the intent to convey the real estate property to the guarantor and make a claim on the guarantee, and the creditor has the ability to recover under that claim, and (3) at the time of foreclosure, any amount of the claim that is determined on the basis of the fair value of the real estate is fixed. Upon foreclosure, the other receivable should be measured on the amount of the loan balance (principal and interest) expected to be recovered from the guarantor. The amendments in this ASU are effective for annual periods and interim periods within those annual periods beginning after December 15, 2014. Entities may adopt the amendments on a prospective basis or modified retrospective basis as of the beginning of the annual period of adoption; however, the entity must apply the same method of transition as elected under ASU 2014-04. Early adoption is permitted provided the entity has already adopted ASU 2014-04. The Corporation is currently assessing the effect that ASU 2014-14 will have on its financial statements.

In August 2014, the FASB issued ASU No. 2014-15, Presentation of Financial Statements - Going Concern (Subtopic 205-40): Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern. This update is intended to provide guidance about management's responsibility to evaluate whether there is substantial doubt about an entity's ability to continue as a going concern and to provide related footnote disclosures. Management is required under the new guidance to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about the entity's ability to continue as a going concern within one year after the date the financial statements are issued when preparing financial statements for each interim and annual reporting period. If conditions or events are identified, the ASU specifies the process that must be followed by management and also clarifies the timing and content of going concern footnote disclosures in order to reduce diversity in practice. The amendments in this ASU are effective for annual periods and interim periods within those annual periods beginning after December 15, 2016. Early adoption is permitted. The Corporation does not expect the adoption of ASU 2014-15 to have a material effect on its financial statements.

In November 2014, the FASB issued ASU No. 2014-16, Derivatives and Hedging (Topic 815): Determining Whether the Host Contract in a Hybrid Financial Instrument Issued in the Form of a Share Is More Akin to Debt or to Equity. The amendments in ASU do not change the current criteria in U.S. GAAP for determining when separation of certain embedded derivative features in a hybrid financial instrument is required. The amendments clarify how current U.S. GAAP should be interpreted in evaluating the economic characteristics and risks of a host contract in a hybrid financial instrument that is issued in the form of a share. Specifically, the amendments clarify that an entity should consider all relevant terms and features, including the embedded derivative feature being evaluated for bifurcation, in evaluating the nature of the host contract. Furthermore, the amendments clarify that no single term or feature would

necessarily determine the economic characteristics and risks of the host contract. Rather, the nature of the host contract depends upon the economic characteristics and risks of the entire hybrid financial instrument. The amendments in this ASU also clarify that, in evaluating the nature of a host contract, an entity should assess the substance of the relevant terms and features (i.e., the relative strength of the debt-like or equity-like terms and features given the facts and circumstances) when considering how to weight those terms and features. The amendments in this ASU are effective for public business entities for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2015. Early adoption, including adoption in an interim period, is permitted. The Corporation does not expect the adoption of ASU 2014-16 to have a material effect on its financial statements.

In November 2014, the FASB issued ASU No. 2014-17, Business Combinations (Topic 805): Pushdown Accounting. The amendments in ASU provide an acquired entity with an option to apply pushdown accounting in its separate financial statements upon occurrence of an event in which an acquirer obtains control of the acquired entity. An acquired entity may elect the option to apply pushdown accounting in the reporting period in which the change-in-control event occurs. An acquired entity should determine whether to elect to apply pushdown accounting for each individual change-in-control event in which an acquirer obtains control of the acquired entity. If pushdown accounting is not applied in the reporting

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period in which the change-in-control event occurs, an acquired entity will have the option to elect to apply pushdown accounting in a subsequent reporting period to the acquired entity's most recent change-in-control event. An election to apply pushdown accounting in a reporting period after the reporting period in which the change-in-control event occurred should be considered a change in accounting principle in accordance with Topic 250, Accounting Changes and Error Corrections. If pushdown accounting is applied to an individual change-in-control event, that election is irrevocable. The amendments in this ASU are effective on November 18, 2014. After the effective date, an acquired entity can make an election to apply the guidance to future change-in-control events or to its most recent change-in-control event. However, if the financial statements for the period in which the most recent change-in-control event occurred already have been issued or made available to be issued, the application of this guidance would be a change in accounting principle. The Corporation does not expect the adoption of ASU 2014-17 to have a material effect on its financial statements.

In January 2015, the FASB issued ASU No. 2015-01, Income Statement—Extraordinary and Unusual Items (Subtopic 225-20): Simplifying Income Statement Presentation by Eliminating the Concept of Extraordinary Items. The amendments in this ASU eliminate from U.S. GAAP the concept of extraordinary items. Subtopic 225-20, Income Statement - Extraordinary and Unusual Items, required that an entity separately classify, present, and disclose extraordinary events and transactions. Presently, an event or transaction is presumed to be an ordinary and usual activity of the reporting entity unless evidence clearly supports its classification as an extraordinary item. If an event or transaction meets the criteria for extraordinary classification, an entity is required to segregate the extraordinary item from the results of ordinary operations and show the item separately in the income statement, net of tax, after income from continuing operations. The entity also is required to disclose applicable income taxes and either present or disclose earnings-per-share data applicable to the extraordinary item. The amendments in this ASU are effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2015. Early adoption is permitted provided that the guidance is applied from the beginning of the fiscal year of adoption. The Corporation does not expect the adoption of ASU 2015-01 to have a material effect on its financial statements.

NOTE 2: Business Combinations

On October 1, 2013, the Corporation completed its acquisition of CVBK, the one-bank holding company for CVB. Pursuant to the Agreement and Plan of Merger dated June 10, 2013, CVBK's shareholders received \$0.32 for each share of CVBK common stock they owned, or approximately \$846,000 in the aggregate. In addition, the Corporation purchased from the U.S. Treasury for \$3.35 million all of CVBK's preferred stock and warrants issued to the U.S. Treasury under the Capital Purchase Program, including accrued and unpaid dividends on the preferred stock. CVB had seven retail bank branches located in the Virginia counties of Powhatan, Cumberland, Chesterfield and Henrico.

The Corporation accounted for the acquisition using the acquisition method of accounting in accordance with ASC 805, Business Combinations. Under the acquisition method of accounting, the assets and liabilities of CVBK were

recorded at their respective acquisition date fair values. Determining the fair value of assets and liabilities, particularly related to the loan portfolio, is a complicated process involving significant judgment regarding methods and assumptions used to calculate the estimated fair values. The fair values determined on the acquisition date were preliminary and subject to refinement during the Measurement Period as additional information relative to the acquisition date fair values became available. Goodwill of \$5.91 million was initially recorded at the time of the CVBK acquisition. As a result of retrospective fair value mark refinements during the Measurement Period in accordance with ASC 805 and related guidance, the

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Corporation reduced goodwill related to the CVBK acquisition from \$5.91 million, as estimated in the Corporation's 2013 audited financial statements, to \$3.70 million.

(Dollars in thousands)	Amounts Previously Recognized as of October 1, 2013 (1)	Measurement Period Adjustments	Adjusted Amounts Recognized as of October 1, 2013
Cash consideration paid for:			
CVBK common stock	\$ 846		\$ 846
CVBK preferred stock and warrants	3,350		3,350
Total cash consideration paid	4,196		4,196
Identifiable assets acquired:			
Cash and cash equivalents	\$ 59,775	\$ —	59,775
Securities available for sale	120,097	—	120,097
Loans	147,066	—	147,066
Corporate premises and equipment (2)	10,948	(910)	10,038
Other real estate owned	395	—	395
Core deposit intangibles	4,107	—	4,107
Deferred tax asset (3)	6,029	3,235	9,264
Other assets (4)	16,624	(120)	16,504
Total identifiable assets acquired	365,041	2,205	367,246
Identifiable liabilities assumed:			
Deposits	315,421	—	315,421
Borrowings	42,124	—	42,124
Trust preferred capital notes	4,439	—	4,439
Other liabilities	4,768	—	4,768
Total identifiable liabilities assumed	366,752	—	366,752
Net identifiable assets (liabilities) assumed	\$ (1,711)	\$ 2,205	\$ 494
Goodwill resulting from acquisition	\$ 5,907		\$ 3,702

<sup>1</sup> As previously reported in the Corporation's 2013 Form 10-K.

<sup>2</sup> The fair value of CVBK's premises, including land, buildings and improvements, was determined based upon appraisal by licensed appraisers. Based on information as of the acquisition date that became available during the Measurement Period, the fair value of CVBK's premises was reduced by \$910,000.

<sup>3</sup> The \$3.24 million adjustment to the acquired deferred tax asset primarily resulted from management's determination during 2014 that the amount of future deductible losses on the purchased credit impaired loan portfolio was greater than the amount originally estimated and recorded.

<sup>4</sup> During 2014, management determined that the amount of accrued interest receivable recorded at the time of the acquisition was overstated by \$120,000.





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## NOTE 3: Securities

The Corporation's debt and equity securities, all of which are classified as available for sale, at December 31, 2014 and 2013 are summarized as follows:

	December 31, 2014			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
(Dollars in thousands)				
U.S. government agencies and corporations	\$ 23,409	\$ 1	\$ (476)	\$ 22,934
Mortgage-backed securities	66,716	935	(32)	67,619
Obligations of states and political subdivisions	124,312	7,158	(126)	131,344
	\$ 214,437	\$ 8,094	\$ (634)	\$ 221,897

	December 31, 2013			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
(Dollars in thousands)				
U.S. Treasury securities	\$ 10,000	\$ —	\$ —	\$ 10,000
U.S. government agencies and corporations	32,503	4	(2,557)	29,950
Mortgage-backed securities	51,318	100	(555)	50,863
Obligations of states and political subdivisions	123,729	4,223	(813)	127,139
Corporate and other debt securities	158	—	—	158
	\$ 217,708	\$ 4,327	\$ (3,925)	\$ 218,110

The amortized cost and estimated fair value of securities at December 31, 2014 and 2013, by the earlier of contractual maturity or expected maturity, are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to prepay obligations with or without call or prepayment penalties.

December 31, 2014

December 31, 2013

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(Dollars in thousands)	Amortized Cost	Estimated Fair Value	Amortized Cost	Estimated Fair Value
Due in one year or less	\$ 31,201	\$ 31,243	\$ 37,672	\$ 36,580
Due after one year through five years	111,084	115,304	53,907	55,608
Due after five years through ten years	48,519	49,968	46,473	46,338
Due after ten years	23,633	25,382	79,656	79,584
	\$ 214,437	\$ 221,897	\$ 217,708	\$ 218,110

Proceeds from the maturities, calls and sales of securities available for sale in 2014 were \$38.66 million, resulting in gross realized gains of \$50,000 and gross realized losses of \$21,000; in 2013 were \$79.44 million, resulting in gross realized gains of \$276,000; in 2012 were \$34.10 million, resulting in gross realized gains of \$11,000.

The Corporation pledges securities to primarily secure public deposits and repurchase agreements. Securities with an aggregate amortized cost of \$106.31 million and an aggregate fair value of \$110.37 million were pledged at

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December 31, 2014. Securities with an aggregate amortized cost of \$149.22 million and an aggregate fair value of \$149.83 million were pledged at December 31, 2013.

Securities in an unrealized loss position at December 31, 2014, by duration of the period of the unrealized loss, are shown below.

(Dollars in thousands)	Less Than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
U.S. government agencies and corporations	\$ 1,966	\$ 2	\$ 21,234	\$ 474	\$ 23,200	\$ 476
Mortgage-backed securities	—	—	4,518	32	4,518	32
Obligations of states and political subdivisions	6,279	51	6,049	75	12,328	126
Total temporarily impaired securities	\$ 8,245	\$ 53	\$ 31,801	\$ 581	\$ 40,046	\$ 634

There are 64 debt securities totaling \$40.05 million considered temporarily impaired at December 31, 2014. The primary cause of the temporary impairments in the Corporation's investments in debt securities was fluctuations in interest rates. Interest rates declined throughout 2014, primarily in the middle and long-end of the United States Treasury yield curve, thereby reducing unrealized losses on the Corporation's debt securities. Weaker global economic conditions increased demand for United States debt securities, as the domestic economy improved even as the Federal Reserve wound down its "quantitative easing" program of buying long-term bonds aimed at stimulating the economy. The municipal bond sector, which includes the Corporation's obligations of states and political subdivisions, benefited from strong investor demand as general credit quality improved throughout 2014 while the supply of new municipal bonds fell as compared to last year. At December 31, 2014, approximately 97 percent of the Corporation's obligations of states and political subdivisions, as measured by market value, were rated "A" or better by Standard & Poor's or Moody's Investors Service. Of those in a net unrealized loss position, approximately 91 percent were rated "A" or better, as measured by market value, at December 31, 2014. For the approximately nine percent not rated "A" or better, as measured by market value at December 31, 2014, the Corporation considers these to meet regulatory credit quality standards, such that the securities have low risk of default by the obligor, and the full and timely repayment of principal and interest is expected over the expected life of the investment. Because the Corporation intends to hold these investments in debt securities to maturity and it is more likely than not that the Corporation will not be required to sell these investments before a recovery of unrealized losses, the Corporation does not consider these investments to be other-than-temporarily impaired at December 31, 2014 and no other-than-temporary impairment has been recognized.

Securities in an unrealized loss position at December 31, 2013, by duration of the period of the unrealized loss, are shown below.

(Dollars in thousands)	Less Than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
U.S. government agencies and corporations	\$ 29,430	\$ 1,385	\$ 8,948	\$ 1,172	\$ 38,378	\$ 2,557
Mortgage-backed securities	40,090	555	—	—	40,090	555
Obligations of states and political subdivisions	21,260	656	3,078	157	24,338	813
Total temporarily impaired securities	\$ 90,780	\$ 2,596	\$ 12,026	\$ 1,329	\$ 102,806	\$ 3,925

The Corporation's investment in restricted stocks totaled \$3.44 million at December 31, 2014, and was comprised of \$3.30 million of FHLB stock and \$145,000 of CBB Stock. Restricted stock is generally viewed as a long-term investment and as restricted investment securities, which are carried at cost, because there is no market for the stock, other than the FHLBs or member institutions. Therefore, when evaluating restricted stock for impairment, their respective values are based on the ultimate recoverability of the par value rather than by recognizing temporary declines in value. The Corporation does not consider its investment in restricted stocks to be other-than-temporarily impaired at December 31, 2014 and no impairment has been recognized. Total restricted stocks is shown as a separate line item on the balance sheet and is not a

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part of the available for sale securities portfolio. At December 31, 2013, the Corporation's restricted stocks included \$347,000 of stock in the FRB, of which CVB was a member, and \$145,000 of CBB stock owned by CVB.

## NOTE 4: Loans

Major classifications of loans are summarized as follows:

(Dollars in thousands)	December 31,	
	2014	2013
Real estate – residential mortgage	\$ 179,817	\$ 188,455
Real estate – construction	7,325	5,810
Commercial, financial and agricultural <sup>1</sup>	306,845	288,593
Equity lines	50,321	50,795
Consumer	8,163	9,007
Consumer finance	283,333	277,724
	835,804	820,384
Less allowance for loan losses	(35,606)	(34,852)
Loans, net	\$ 800,198	\$ 785,532

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<sup>1</sup> Includes the Corporation's commercial real estate lending, land acquisition and development lending, builder line lending and commercial business lending.

Consumer loans included \$355,000 and \$354,000 of demand deposit overdrafts at December 31, 2014 and 2013, respectively.

The outstanding principal balance and the carrying amount of loans acquired pursuant to the Corporation's acquisition of CVB (or acquired loans) that were recorded at fair value at the acquisition date and are included in the consolidated balance sheet at December 31, 2014 and 2013 were as follows:

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(Dollars in thousands)	December 31, 2014		Acquired Loans - Total
	Acquired Loans - Purchased Credit Impaired	Acquired Loans - Purchased Performing	
Outstanding principal balance	\$ 36,541	\$ 85,015	\$ 121,556
Carrying amount			
Real estate – residential mortgage	\$ 1,723	\$ 18,688	\$ 20,411
Real estate – construction	—	—	—
Commercial, financial and agricultural	19,367	45,015	64,382
Equity lines	318	15,464	15,782
Consumer	16	979	995
Total acquired loans	\$ 21,424	\$ 80,146	\$ 101,570

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(Dollars in thousands)	December 31, 2013		Acquired Loans - Total
	Acquired Loans - Purchased Credit Impaired	Acquired Loans - Purchased Performing	
Outstanding principal balance	\$ 49,041	\$ 110,977	\$ 160,018
Carrying amount			
Real estate – residential mortgage	\$ 2,694	\$ 29,285	\$ 31,979
Real estate – construction	771	917	1,688
Commercial, financial and agricultural	28,602	55,204	83,806
Equity lines	332	16,909	17,241
Consumer	121	2,156	2,277
Total acquired loans	\$ 32,520	\$ 104,471	\$ 136,991

Loans on nonaccrual status at December 31, 2014 and 2013 were as follows:

(Dollars in thousands)	December 31,	
	2014	2013
Real estate – residential mortgage	\$ 2,472	\$ 1,996
Real estate – construction:		
Construction lending <sup>1</sup>	—	—
Consumer lot lending <sup>1</sup>	—	—
Commercial, financial and agricultural:		
Commercial real estate lending	2,033	1,486
Land acquisition & development lending <sup>1</sup>	—	—
Builder line lending	—	13
Commercial business lending	—	374
Equity lines	356	291
Consumer	43	231
Consumer finance	1,040	1,187
Total loans on nonaccrual status	\$ 5,944	\$ 5,578

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<sup>1</sup> At December 31, 2014 and 2013 there were no real estate construction lending loans, real estate consumer lot lending loans or land acquisition and development lending loans on nonaccrual status.

If interest income had been recognized on nonaccrual loans at their stated rates during years 2014, 2013 and 2012, interest income would have increased by approximately \$413,000, \$479,000 and \$654,000, respectively.





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The past due status of loans as of December 31, 2014 was as follows:

(Dollars in thousands)	30 59 Days Past Due <sup>2,3</sup>	60 89 Days Past Due <sup>2,3</sup>	90+ Days Past Due <sup>2,3</sup>	Total Past Due	Current <sup>1,2,3</sup>	Total Loans	90+ Days Past Due and Accruing
Real estate – residential mortgage	\$ 1,717	\$ 256	\$ 892	\$ 2,865	\$ 176,952	\$ 179,817	\$ —
Real estate – construction:							
Construction lending	—	—	—	—	3,839	3,839	—
Consumer lot lending	—	—	—	—	3,486	3,486	—
Commercial, financial and agricultural:							
Commercial real estate lending	264	53	115	432	184,348	184,780	—
Land acquisition & development lending	—	—	218	218	47,255	47,473	—
Builder line lending	—	—	—	—	20,255	20,255	—
Commercial business lending	21	53	—	74	54,263	54,337	—
Equity lines	319	205	122	646	49,675	50,321	14
Consumer	15	37	6	58	8,105	8,163	—
Consumer finance	12,421	2,599	1,040	16,060	267,273	283,333	—
Total	\$ 14,757	\$ 3,203	\$ 2,393	\$ 20,353	\$ 815,451	\$ 835,804	\$ 14

<sup>1</sup> For the purposes of the table above, “Current” includes loans that are 1-29 days past due

<sup>2</sup> The table above includes nonaccrual loans that are current of \$3.06 million, 30-59 days past due of \$697,000, 60 89 days past due of \$417,000 and 90+ days past due of \$1.77 million.

<sup>3</sup> The table above includes loans purchased in the acquisition of CVB that are current of \$99.54 million, 30-59 days past due of \$1.05 million, 60-89 days past due of \$141,000 and 90+ days past due of \$846,000.

The past due status of loans as of December 31, 2013 was as follows:

90+ Days

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(Dollars in thousands)	30 - 59 Days Past Due <sup>2,3</sup>	60 - 89 Days Past Due <sup>2,3</sup>	90+ Days Past Due <sup>2,3</sup>	Total Past Due	Current <sup>1,2,3</sup>	Total Loans	Past Due and Accruing
Real estate – residential mortgage	\$ 1,547	\$ 952	\$ 1,547	\$ 4,046	\$ 184,409	\$ 188,455	\$ —
Real estate – construction:							
Construction lending	—	—	—	—	3,728	3,728	—
Consumer lot lending	—	—	—	—	2,082	2,082	—
Commercial, financial and agricultural:							
Commercial real estate lending	5,567	228	72	5,867	162,255	168,122	72
Land acquisition & development lending	—	—	272	272	25,368	25,640	—
Builder line lending	—	—	—	—	13,426	13,426	—
Commercial business lending	306	368	2,033	2,707	78,698	81,405	—
Equity lines	264	45	173	482	50,313	50,795	—
Consumer	54	46	195	295	8,712	9,007	3
Consumer finance	14,174	2,998	1,187	18,359	259,365	277,724	—
Total	\$ 21,912	\$ 4,637	\$ 5,479	\$ 32,028	\$ 788,356	\$ 820,384	\$ 75

<sup>1</sup> For the purposes of the table above, “Current” includes loans that are 1-29 days past due

<sup>2</sup> The table above includes nonaccrual loans that are current of \$2.15 million, 30-59 days past due of \$7,000, 60-89 days past due of \$306,000 and 90+ days past due of \$3.11 million.

<sup>3</sup> The table above includes loans purchased in the acquisition of CVB that are current of \$136.30 million, 30-59 days past due of \$1.35 million, 60-89 days past due of \$841,000 and 90+ days past due of \$2.98 million of which \$3,000 are 90+ days past due and accruing.

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Loan modifications that were classified as TDRs during the years ended December 31, 2014 and 2013 were as follows:

	Year Ended December 31, 2014		2013	
	Number of Loans	Post- Modification Recorded Investment	Number of Loans	Post- Modification Recorded Investment
(Dollars in thousands)				
Real estate – residential mortgage – interest reduction	2	\$ 124	—	\$ —
Real estate – residential mortgage – interest rate concession	3	674	2	268
Commercial, financial and agricultural:				
Commercial real estate lending – interest reduction	1	103	—	—
Commercial real estate lending – interest rate concession	1	96	4	1,829
Builder line lending – interest rate concession	—	—	1	17
Commercial business lending – interest rate concession	—	—	1	117
Commercial business lending – term concession	—	—	1	77
Equity lines – term concession	—	—	1	30
Consumer – interest rate concession	1	3	—	—
Total	8	\$ 1,000	10	\$ 2,338

For the purposes of the above table, the pre-modification recorded investment for TDRs were the same as the post-modification recorded investment for TDRs for December 31, 2014 and 2013.

TDR payment defaults during the years ended December 31, 2014 and 2013 were as follows:

	Year Ended December 31, 2014		2013	
	Number of Loans	Recorded Investment	Number of Loans	Recorded Investment
(Dollars in thousands)				
Commercial real estate lending	—	\$ —	1	\$ 3

For purposes of this disclosure, a TDR payment default occurs when, within 12 months of the original TDR modification, either a full or partial charge-off occurs or a TDR becomes 90 days or more past due.

Impaired loans, which included TDRs of \$5.83 million, and the related allowance at December 31, 2014 were as follows:

(Dollars in thousands)	Recorded Investment in Loans	Unpaid Principal Balance	Related Allowance	Average Balance- Impaired Loans	Interest Income Recognized
Real estate – residential mortgage	\$ 3,000	\$ 3,094	\$ 417	\$ 2,931	\$ 139
Commercial, financial and agricultural:					
Commercial real estate lending	2,786	2,908	440	2,735	150
Builder line lending	—	—	—	—	—
Commercial business lending	103	103	15	115	7
Equity lines	30	32	1	25	2
Consumer	95	95	6	95	4
Total	\$ 6,014	\$ 6,232	\$ 879	\$ 5,901	\$ 302

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Impaired loans, which included TDR loans of \$5.62 million, and the related allowance at December 31, 2013 were as follows:

(Dollars in thousands)	Recorded Investment in Loans	Unpaid Principal Balance	Related Allowance	Average Balance- Impaired Loans	Interest Income Recognized
Real estate – residential mortgage	\$ 2,601	\$ 2,694	\$ 390	\$ 2,090	\$ 99
Commercial, financial and agricultural:					
Commercial real estate lending	2,729	2,780	504	2,748	99
Builder line lending	13	16	4	14	1
Commercial business lending	695	756	131	562	11
Equity lines	131	132	—	33	—
Consumer	93	93	14	95	9
Total	\$ 6,262	\$ 6,471	\$ 1,043	\$ 5,542	\$ 219

PCI loans had an unpaid principal balance of \$36.54 million and a carrying value of \$21.42 million at December 31, 2014. Determining the fair value of purchased credit impaired loans required the Corporation to estimate cash flows expected to result from those loans and to discount those cash flows at appropriate rates of interest. For such loans, the excess of the cash flows expected at acquisition over the estimated fair value is recognized as interest income over the remaining lives of the loans and is called the accretable yield. The difference between contractually required payments at acquisition and the cash flows expected to be collected at acquisition reflects the impact of estimated credit losses and is called the nonaccretable difference. In accordance with GAAP, there was no carry-over of previously established allowance for loan losses from acquired loans.

The PCI loan portfolio related to the CVB acquisition was accounted for at fair value on the date of acquisition as follows:

(Dollars in thousands)	October 1, 2013
Contractual principal and interest due	\$ 70,390
Nonaccretable difference	(26,621)
Expected cash flows	43,769
Accretable yield	(8,454)
Purchase credit impaired loans - estimated fair value	\$ 35,315

The following table presents a summary of the change in the accretable yield of the PCI loan portfolio for the years ended December 31, 2014 and 2013:

(Dollars in thousands)	Year Ended December 31,	
	2014	2013
Accretable yield, balance at beginning of period	\$ 7,776	\$ 8,454
Accretion	(3,234)	(678)
Reclassification of nonaccretable difference due to improvement in expected cash flows	10,593	—
Other changes, net	(1,647)	—
Accretable yield, balance at end of period	\$ 13,488	\$ 7,776

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## NOTE 5: Allowance for Loan Losses

Changes in the allowance for loan losses were as follows:

(Dollars in thousands)	Year Ended December 31,		
	2014	2013	2012
Balance at the beginning of year	\$ 34,852	\$ 35,907	\$ 33,677
Provision charged to operations	16,330	15,085	12,405
Loans charged off	(19,846)	(20,070)	(13,497)
Recoveries of loans previously charged off	4,270	3,930	3,322
Balance at the end of year	\$ 35,606	\$ 34,852	\$ 35,907

The following table presents, as of December 31, 2014, the total allowance for loan losses, the allowance by impairment methodology (individually evaluated for impairment, collectively evaluated for impairment or PCI loans), the total loans and loans by impairment methodology (individually evaluated for impairment, collectively evaluated for impairment or PCI loans).

(Dollars in thousands)	Real Estate	Commercial,			Consumer	Consumer	Total
	Residential	Real Estate	Financial &	Equity			
	Mortgage	Construction	Agricultural	Lines	Finance		
Allowance for loan losses:							
Balance at the beginning of year	\$ 2,355	\$ 434	\$ 7,805	\$ 892	\$ 273	\$ 23,093	\$ 34,852
Provision charged to operations	60	—	—	—	—	16,270	16,330
Loans charged off	(161)	—	(271)	(80)	(312)	(19,022)	(19,846)
Recoveries of loans previously charged off	59	—	210	—	250	3,751	4,270
Ending balance	\$ 2,313	\$ 434	\$ 7,744	\$ 812	\$ 211	\$ 24,092	\$ 35,606
Ending balance:							
individually evaluated for impairment	\$ 417	\$ —	\$ 455	\$ 1	\$ 6	\$ —	\$ 879
	\$ 1,896	\$ 434	\$ 7,289	\$ 811	\$ 205	\$ 24,092	\$ 34,727

Ending balance: collectively evaluated for impairment							
Ending balance: acquired loans - purchase credit impaired	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —
Loans:							
Ending balance	\$ 179,817	\$ 7,325	\$ 306,845	\$ 50,321	\$ 8,163	\$ 283,333	\$ 835,804
Ending balance: individually evaluated for impairment	\$ 3,000	\$ —	\$ 2,889	\$ 30	\$ 95	\$ —	\$ 6,014
Ending balance: collectively evaluated for impairment	\$ 175,094	\$ 7,325	\$ 284,589	\$ 49,973	\$ 8,052	\$ 283,333	\$ 808,366
Ending balance: acquired loans - purchase credit impaired	\$ 1,723	\$ —	\$ 19,367	\$ 318	\$ 16	\$ —	\$ 21,424



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The following table presents, as of December 31, 2013, the total allowance for loan losses, the allowance by impairment methodology (individually evaluated for impairment or collectively evaluated for impairment), the total loans and loans by impairment methodology (individually evaluated for impairment or collectively evaluated for impairment).

(Dollars in thousands)	Real Estate Residential Mortgage	Real Estate Construction	Commercial, Financial & Agricultural	Equity Lines	Consumer	Consumer Finance	Total
Allowance for loan losses:							
Balance at the beginning of year	\$ 2,358	\$ 424	\$ 9,824	\$ 885	\$ 283	\$ 22,133	\$ 35,907
Provision charged to operations	740	7	52	105	216	13,965	15,085
Loans charged off	(849)	—	(2,298)	(126)	(399)	(16,398)	(20,070)
Recoveries of loans previously charged off	106	3	227	28	173	3,393	3,930
Ending balance:	\$ 2,355	\$ 434	\$ 7,805	\$ 892	\$ 273	\$ 23,093	\$ 34,852
Ending balance: individually evaluated for impairment	\$ 390	\$ —	\$ 639	\$ —	\$ 14	\$ —	\$ 1,043
Ending balance: collectively evaluated for impairment	\$ 1,965	\$ 434	\$ 7,166	\$ 892	\$ 259	\$ 23,093	\$ 33,809
Ending balance: acquired loans - purchase credit impaired	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —
Loans:							
Ending balance	\$ 188,455	\$ 5,810	\$ 288,593	\$ 50,795	\$ 9,007	\$ 277,724	\$ 820,384
Ending balance: individually evaluated for impairment	\$ 2,601	\$ —	\$ 3,437	\$ 131	\$ 93	\$ —	\$ 6,262
Ending balance: collectively evaluated for impairment	\$ 183,160	\$ 5,039	\$ 256,554	\$ 50,332	\$ 8,793	\$ 277,724	\$ 781,602
Ending balance: acquired loans - purchase credit impaired	\$ 2,694	\$ 771	\$ 28,602	\$ 332	\$ 121	\$ —	\$ 32,520

Loans by credit quality indicators as of December 31, 2014 were as follows:

(Dollars in thousands)	Pass	Special Mention	Substandard	Substandard Nonaccrual	Total <sup>1</sup>
Real estate – residential mortgage	\$ 171,414	\$ 2,978	\$ 2,953	\$ 2,472	\$ 179,817
Real estate – construction:					
Construction lending	1,191	—	2,648	—	3,839
Consumer lot lending	3,486	—	—	—	3,486
Commercial, financial and agricultural:					
Commercial real estate lending	165,804	4,136	12,807	2,033	184,780
Land acquisition & development lending	43,693	1,136	2,644	—	47,473
Builder line lending	18,321	1,389	545	—	20,255
Commercial business lending	41,813	930	11,594	—	54,337
Equity lines	48,443	772	750	356	50,321
Consumer	7,984	103	33	43	8,163
	\$ 502,149	\$ 11,444	\$ 33,974	\$ 4,904	\$ 552,471

Included in the table above are loans purchased in connection with the acquisition of CVB of \$87.26 million pass rated, \$2.99 million special mention, \$10.71 million substandard and \$603,000 substandard nonaccrual.

(Dollars in thousands)	Performing	Non Performing	Total
Consumer finance	\$ 282,293	\$ 1,040	\$ 283,333

<sup>1</sup> At December 31, 2014, the Corporation does not have any loans classified as Doubtful or Loss.

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Loans by credit quality indicators as of December 31, 2013 were as follows:

(Dollars in thousands)	Pass	Special Mention	Substandard	Substandard Nonaccrual	Total <sup>1</sup>
Real estate – residential mortgage	\$ 180,670	\$ 2,209	\$ 3,580	\$ 1,996	\$ 188,455
Real estate – construction:					
Construction lending	1,068	11	2,649	—	3,728
Consumer lot lending	1,831	105	146	—	2,082
Commercial, financial and agricultural:					
Commercial real estate lending	152,017	2,934	11,685	1,486	168,122
Land acquisition & development lending	18,236	1,601	5,803	—	25,640
Builder line lending	11,608	1,278	527	13	13,426
Commercial business lending	61,715	2,758	16,558	374	81,405
Equity lines	48,603	1,003	898	291	50,795
Consumer	8,616	2	158	231	9,007
	\$ 484,364	\$ 11,901	\$ 42,004	\$ 4,391	\$ 542,660

Included in the table above are loans purchased in connection with the acquisition of CVB of \$119.75 million pass rated, \$3.30 million special mention, \$17.77 million substandard and \$652,000 substandard nonaccrual.

(Dollars in thousands)	Performing	Non-Performing	Total
Consumer finance	\$ 276,537	\$ 1,187	\$ 277,724

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<sup>1</sup> At December 31, 2013, the Corporation did not have any loans classified as Doubtful or Loss.

## NOTE 6: Other Real Estate Owned

At December 31, 2014 and 2013, OREO was \$786,000 and \$2.77 million, respectively. OREO is primarily comprised of residential properties and non-residential properties associated with commercial relationships, and are located primarily in the state of Virginia. Changes in the balance for OREO are as follows:

(Dollars in thousands)	Year Ended December 31,	
	2014	2013
Balance at the beginning of year, gross	\$ 6,904	\$ 10,173
Transfers between loans and other real estate owned	1,960	588
Acquisition of CVB	—	395
Charge-offs	(4,135)	(261)
Sales proceeds	(4,382)	(4,209)
Gain on disposition	324	218
Deferred gain on disposition	144	—
Balance at the end of year, gross	815	6,904
Less valuation allowance	(29)	(4,135)
Balance at the end of year, net	\$ 786	\$ 2,769

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Changes in the allowance for OREO losses are as follows:

(Dollars in thousands)	Year Ended December 31,		
	2014	2013	2012
Balance at the beginning of year	\$ 4,135	\$ 3,937	\$ 3,927
Provision for losses	29	459	1,250
Charge-offs, net	(4,135)	(261)	(1,240)
Balance at the end of year	\$ 29	\$ 4,135	\$ 3,937

Net expenses applicable to OREO, other than the provision for losses, were \$6,000, \$253,000 and \$384,000 for the years ended December 31, 2014, 2013 and 2012, respectively.

## NOTE 7: Corporate Premises and Equipment

Major classifications of corporate premises and equipment are summarized as follows:

(Dollars in thousands)	December 31,	
	2014	2013
Land	\$ 8,431	\$ 8,431
Buildings	33,917	32,493
Equipment, furniture and fixtures	36,956	40,100
	79,304	81,024
Less accumulated depreciation	(42,009)	(42,792)
	\$ 37,295	\$ 38,232

NOTE 8: Time Deposits

Time deposits are summarized as follows:

(Dollars in thousands)	December 31,	
	2014	2013
Certificates of deposit, over \$250	\$ 60,565	\$ 63,159
Other time deposits	305,942	336,724
	\$ 366,507	\$ 399,883

Remaining maturities on time deposits at December 31, 2014 are as follows:

(Dollars in thousands)	
2015	\$ 199,395
2016	73,019
2017	44,127
2018	28,013
2019	13,849
Thereafter	8,104
	\$ 366,507



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## NOTE 9: Borrowings

The table below presents selected information on short-term borrowings:

(Dollars in thousands)	December 31,	
	2014	2013
Balance outstanding at year end <sup>1</sup>	\$ 14,436	\$ 11,780
Maximum balance at any month end during the year	\$ 15,488	\$ 15,812
Average balance for the year	\$ 12,745	\$ 12,276
Weighted average rate for the year	0.39 %	0.40 %
Weighted average rate on borrowings at year end	0.38 %	0.40 %
Estimated fair value at year end	\$ 14,436	\$ 11,780

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<sup>1</sup> Consists entirely of secured transactions with customers, which generally mature the day following the day sold.

Long-term borrowings at December 31, 2014 consist of a repurchase agreement with a third-party correspondent bank, which is secured by investment securities; advances under a non-recourse revolving bank line of credit secured by loans at C&F Finance; and advances from the FHLB, which are secured by a blanket floating lien on all qualifying closed-end and revolving, open-end loans secured by 1-4 family residential properties. The interest rate on the repurchase agreement, which matures in 2018, is 3.55% (7.00% minus three-month LIBOR with a maximum rate of 3.55%) and the outstanding balance as of December 31, 2014 was \$5.00 million. The interest rate on the revolving bank line of credit, which matures in 2017, floats at the one-month LIBOR rate plus a range of 200 to 225 basis points, depending upon the average balance outstanding on the line, and the outstanding balance as of December 31, 2014 was \$75.49 million. C&F Finance's revolving bank line of credit agreement contains covenants regarding C&F Finance's capital adequacy, collateral performance, adequacy of the allowance for loan losses and interest expense coverage. C&F Finance satisfied all such covenants during 2014. Long-term advances from the FHLB at December 31, 2014 consist of \$22.50 million of convertible advances and \$24.50 million of fixed rate hybrid advances. The convertible advances have fixed rates of interest unless the FHLB exercises its option to convert the interest on these advances from fixed rate to variable rate. The fixed rate hybrid advances provide fixed-rate funding until the stated maturity date. C&F Bank may add interest rate caps or floors at a future date, at which time the cost of the caps or floors will be added to the advance rate. The table below presents selected information on the FHLB advances:

(Dollars in thousands)



Balance Outstanding at December 31, 2014	Interest Rate	Maturity Date	Next Conversion Option Date
Fixed Rate Hybrid Advances			
\$ 7,500	3.39	% 08/10/15	
\$ 7,500	0.80	08/30/16	
\$ 2,500	1.28	08/30/18	
\$ 7,000	1.95	12/04/19	
Convertible Advances			
\$ 7,500	3.70	10/19/17	01/20/15
\$ 5,000	4.06	10/25/17	01/26/15
\$ 5,000	2.93	11/27/17	02/27/15
\$ 5,000	3.59	06/06/18	

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The contractual maturities of long-term borrowings at December 31, 2014 are as follows:

(Dollars in thousands)	Fixed Rate	Floating Rate	Total
2015	\$ 7,500	\$ —	\$ 7,500
2016	7,500	—	7,500
2017	17,500	75,488	92,988
2018	7,500	5,000	12,500
2019	7,000	—	7,000
Thereafter	—	—	—
	\$ 47,000	\$ 80,488	\$ 127,488

The Corporation's unused lines of credit for future borrowings total approximately \$281.40 million at December 31, 2014, which consists of \$95.88 million available from the FHLB, \$44.51 million on C&F Finance's revolving bank line of credit, \$26.01 million available from the FRB, \$65.00 million under unsecured federal funds agreements with third party financial institutions, \$50.00 million in repurchase lines of credit with third party financial institutions. Additional loans and securities are available that can be pledged as collateral for future borrowings from the FRB or the FHLB above the current lendable collateral value.

In December 2007, C&F Financial Statutory Trust II (Trust II), a wholly-owned non-operating subsidiary of the Corporation, was formed for the purpose of issuing trust preferred capital securities for general corporate purposes including the refinancing of existing debt. On December 14, 2007, Trust II issued \$10.00 million of trust preferred capital securities in a private placement to an institutional investor and \$310,000 in common equity to the Corporation in exchange for cash. The securities mature in December 2037, are redeemable at the Corporation's option beginning after five years, and require quarterly distributions by Trust II to the holder of the securities at a rate equal to the three-month LIBOR rate plus 3.15%. During 2014, in order to mitigate the effect of rising interest rates in the future, the Corporation entered into an interest rate swap agreement whereby the effective fixed interest rate on all \$10.00 million of the securities became 4.82%. The interest rate swap matures in December 2019. The principal asset of Trust II is \$10.31 million of the Corporation's trust preferred capital notes with like maturities and like interest rates to the trust preferred capital securities. The interest payments by the Corporation on the debt securities will be used by Trust II to pay the quarterly distributions payable by Trust II to the holders of the trust preferred capital securities.

In July 2005, C&F Financial Statutory Trust I (Trust I), a wholly-owned non-operating subsidiary of the Corporation, was formed for the purpose of issuing trust preferred capital securities to partially fund the Corporation's purchase of 427,186 shares of its common stock. On July 21, 2005, Trust I issued \$10.00 million of trust preferred capital securities in a private placement to an institutional investor and \$310,000 in common equity to the Corporation in exchange for cash. The securities mature in September 2035, are redeemable at the Corporation's option beginning after five years, and require quarterly distributions by Trust I to the holder of the securities at a rate equal to the

three-month LIBOR rate plus 1.57%. During 2010, in order to mitigate the effect of rising interest rates in the future, the Corporation entered into two interest rate swap agreements whereby the effective fixed interest rate on \$5.00 million of the securities became 3.48% and the effective fixed interest rate on the remaining \$5.00 million of the securities became 4.31%. The interest rate swaps mature in September 2015. The principal asset of Trust I is \$10.31 million of the Corporation's trust preferred capital notes with like maturities and like interest rates to the trust preferred capital securities. The interest payments by the Corporation on the debt securities will be used by Trust I to pay the quarterly distributions payable by Trust I to the holders of the trust preferred capital securities.

In December 2003, Central Virginia Bankshares Statutory Trust I (CVBK Trust I) was formed as a wholly-owned non-operating subsidiary of CVBK for the purpose of issuing trust preferred capital securities for general corporate purposes. On December 17, 2003, CVBK Trust I issued \$5.00 million of trust preferred capital securities in a private placement to an institutional investor and \$155,000 in common equity to CVBK in exchange for cash. CVBK Trust I became a wholly-owned non-operating subsidiary of the Corporation pursuant to the merger of CVBK with and into the Corporation in March 2014, and the Corporation assumed CVBK's obligations on the underlying trust preferred capital notes. The securities mature in December 2033, are redeemable at the Corporation's option beginning after five years, and require quarterly distributions by CVBK Trust I to the holder of the securities at a rate equal to the three-month LIBOR plus

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2.85%. During 2014, in order to mitigate the effect of rising interest rates in the future, the Corporation entered into an interest rate swap agreement whereby the effective fixed interest rate on all \$5.00 million of the securities became 4.54%. The interest rate swap matures in December 2019. The principal asset of CVBK Trust I is \$5.16 million of trust preferred capital notes originally issued by CVBK and assumed by the Corporation with like maturities and like interest rates to the trust preferred capital securities. The interest payments by the Corporation on the debt securities will be used by CVBK Trust I to pay the quarterly distributions payable by CVBK Trust I to the holders of the trust preferred capital securities. The trust preferred capital securities issued by CVBK Trust I were adjusted to fair market value on the date of acquisition of CVBK. The resulting fair value adjustment was a discount of \$716,000, which is being accreted over 20 years on a straight-line basis, and the balance of which was \$672,000 as of December 31, 2014.

Subject to certain exceptions and limitations, the Corporation may elect from time to time to defer interest payments on the junior subordinated debt securities, which would result in a deferral of distribution payments on the related capital securities.

## NOTE 10: Shareholders' Equity, Other Comprehensive Income and Earnings Per Common Share

## Accumulated Other Comprehensive Income (Loss)

The following table presents the cumulative balances of the components of accumulated other comprehensive income (loss), net of deferred taxes of \$1.66 million, \$163,000 and \$2.51 million as of December 31, 2014, 2013 and 2012, respectively.

(Dollars in thousands)	December 31,		
	2014	2013	2012
Net unrealized gains on securities	\$ 4,850	\$ 261	\$ 5,951
Net unrecognized loss on cash flow hedges	(64)	(202)	(313)
Net unrecognized losses on defined benefit plan	(1,700)	(325)	(922)
Total accumulated other comprehensive income (loss)	\$ 3,086	\$ (266)	\$ 4,716

## Shareholders' Equity

Preferred Shares. On January 9, 2009, as part of the Capital Purchase Program (Capital Purchase Program) established by the U.S. Department of the Treasury (Treasury) under the Emergency Economic Stabilization Act of 2008 (EESA),

the Corporation issued and sold to Treasury for an aggregate purchase price of \$20.00 million in cash (1) 20,000 shares of the Corporation's fixed rate cumulative perpetual preferred stock, Series A, par value \$1.00 per share, having a liquidation preference of \$1,000 per share (Series A Preferred Stock) and (2) a ten-year warrant to purchase up to 167,504 shares of the Corporation's common stock, par value \$1.00 per share (Common Stock), at an initial exercise price of \$17.91 per share (Warrant). Of the aggregate amount of \$20.00 million proceeds received from the issuance of the Series A Preferred Stock, approximately \$792,000 was attributable to the Warrant, based on the relative fair value of the Warrant on the date of issuance.

On July 27, 2011, the Corporation redeemed \$10.00 million of the total \$20.00 million liquidation preference of its Series A Preferred Stock. The Corporation paid \$10.10 million to redeem this portion of the Series A Preferred Stock, consisting of \$10.00 million in liquidation preference and \$100,000 of accrued and unpaid dividends associated with the preferred stock being redeemed. On April 11, 2012, the Corporation redeemed the remaining \$10.00 million of the total \$20.00 million liquidation preference of its Series A Preferred Stock. The Corporation paid \$10.08 million to redeem this portion of the Series A Preferred Stock, consisting of \$10.00 million in liquidation preference and \$78,000 of accrued and unpaid dividends associated with the preferred stock redemption. The funds for both of these redemptions were provided by existing financial resources of the Corporation; therefore, there was no dilution to the Corporation's common shareholders. Further, the Corporation will pay no future dividends on the Series A Preferred Stock.

On May 14, 2014, the Corporation repurchased the warrant for \$2.30 million. The repurchase price was based on the fair market value of the warrant as agreed upon by the Corporation and Treasury. The funds for this redemption were provided

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by existing financial resources of the Corporation; therefore, there was no dilution to the Corporation's common shareholders.

Common Shares. The Corporation repurchased 4,608 and 1,215 shares of its common stock during the years ended December 31, 2014 and 2013, respectively. During the year ended December 31, 2014, 2,800 shares were purchased under a share repurchase program authorized by the Corporation's Board of Directors for the purchase of up to \$5.0 million of the Corporation's common stock through May 2015. During the years ended December 31, 2014 and 2013, 1,808 and 1,215 shares were withheld from employees to satisfy tax withholding obligations arising upon the vesting of restricted shares. The Corporation did not repurchase any shares of its common stock during the year ended December 31, 2012.

## Earnings Per Common Share

The components of the Corporation's earnings per common share calculations are as follows:

(Dollars in thousands)	December 31,		
	2014	2013	2012
Net income	\$ 12,346	\$ 14,402	\$ 16,382
Accumulated dividends on Series A Preferred Stock	—	—	(139)
Amortization of Series A Preferred Stock discount	—	—	(172)
Net income available to common shareholders	\$ 12,346	\$ 14,402	\$ 16,071
Weighted average number of common shares used in earnings per common share—basic	3,404,112	3,305,132	3,215,049
Effect of dilutive securities:			
Stock option awards and warrant	32,166	138,850	90,853
Weighted average number of common shares used in earnings per common share—assuming dilution	3,436,278	3,443,982	3,305,902

Potential common shares that may be issued by the Corporation for its stock option awards and Warrant are determined using the treasury stock method. Approximately 150,000, 18,000 and 215,000 shares issuable upon exercise of options for the years ended December 31, 2014, 2013 and 2012, respectively, were not included in computing diluted earnings per common share because they were anti-dilutive.

## NOTE 11: Income Taxes

Principal components of income tax expense as reflected in the consolidated statements of income are as follows:

(Dollars in thousands)	Year Ended December 31,		
	2014	2013	2012
Current taxes	\$ 2,483	\$ 4,424	\$ 8,494
Deferred taxes	2,247	2,286	(848)
	\$ 4,730	\$ 6,710	\$ 7,646

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The income tax provision is less than would be obtained by application of the statutory federal corporate tax rate to pre-tax accounting income as a result of the following items:

(Dollars in thousands)	Year Ended December 31,		Percent of		Percent of		Percent of	
	2014	Pre-tax Income	2013	Pre-tax Income	2012	Pre-tax Income		
Income tax computed at federal statutory rates	\$ 5,977	35.0	% \$ 7,389	35.0	% \$ 8,410	35.0	%	
Tax effect of exclusion of interest income on obligations of states and political subdivisions	(1,546)	(9.0)	(1,600)	(7.6)	(1,631)	(6.8)		
Reduction of interest expense incurred to carry tax-exempt assets	42	0.3	59	0.3	78	0.3		
State income taxes, net of federal tax benefit	532	3.1	938	4.4	1,133	4.7		
Nondeductible expenses primarily related to the acquisition of CVBK	—	—	251	1.2	—	—		
Tax credits	(180)	(1.1)	(225)	(1.1)	(225)	(0.9)		
Other	(95)	(0.6)	(102)	(0.4)	(119)	(0.5)		
	\$ 4,730	27.7	% \$ 6,710	31.8	% \$ 7,646	31.8	%	

The Corporation's net deferred income taxes totaled \$20.7 million and \$25.2 million at December 31, 2014 and 2013, respectively. The tax effects of each type of significant item that gave rise to deferred taxes are:

(Dollars in thousands)	December 31,	
	2014	2013
Deferred tax asset		
Allowance for loan losses and OREO losses	\$ 13,590	\$ 14,787
Fair market value adjustments related to acquisition	6,603	9,192
Reserve for indemnification losses	794	917
Deferred compensation	1,821	2,617
Share-based compensation	791	517



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Interest on nonaccrual loans	1,222	645
Depreciation	149	—
Cash flow hedges	40	129
Other	2,677	1,556
Deferred tax asset	27,687	30,360
Deferred tax liability		
Goodwill and other intangible assets	(3,291)	(3,079)
Core deposit intangible	(904)	(1,321)
Defined benefit plan	(176)	(513)
Depreciation	—	(132)
Net unrealized gain on securities available for sale	(2,611)	(141)
Deferred tax liability	(6,982)	(5,186)
Net deferred tax asset	\$ 20,705	\$ 25,174

The Corporation files income tax returns in the U.S. federal jurisdiction and several states. With few exceptions, the Corporation is no longer subject to U.S. federal, state and local income tax examinations by tax authorities for years prior to 2011.

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NOTE 12: Employee Benefit Plans

C&F Bank maintains a Defined Contribution Profit-Sharing Plan (the Profit-Sharing Plan) sponsored by the Virginia Bankers Association (VBA). The Profit-Sharing Plan includes a 401(k) savings provision that authorizes a maximum voluntary salary deferral of up to 90% of compensation (with a partial company match), subject to statutory limitations. The Profit-Sharing Plan provides for an annual discretionary contribution to the account of each eligible employee based in part on C&F Bank's profitability for a given year and on each participant's yearly earnings. All full-time employees who have attained the age of eighteen and have at least three months of service are eligible to participate. Contributions and earnings may be invested in various investment vehicles offered through the VBA. All employee contributions are fully vested upon contribution. An employee is 20% vested in C&F Bank's contributions after two years of service, 40% after three years, 60% after four years, 80% after five years and fully vested after six years, or earlier in the event of retirement, death or attainment of age 65 while an employee. The amounts charged to expense under this plan were \$557,000, \$417,000 and \$387,000 in 2014, 2013 and 2012, respectively.

C&F Mortgage maintains a Defined Contribution 401(k) Savings Plan that authorizes a voluntary salary deferral of from 1% to 100% of compensation (with a discretionary company match), subject to statutory limitations. Substantially all employees who have attained the age of eighteen are eligible to participate on the first day of the next month following employment date. The plan provides for an annual discretionary contribution to the account of each eligible employee based in part on C&F Mortgage's profitability for a given year, and on each participant's contributions to the plan. Contributions may be invested in various investment funds offered under the plan. All employee contributions are fully vested upon contribution. An employee is vested 25% in the employer's contributions after two years of service, 50% after three years, 75% after four years, and fully vested after five years. The amounts charged to expense under this plan were \$16,000, \$104,000 and \$29,000 in 2014, 2013 and 2012, respectively.

C&F Finance maintains a Defined Contribution Profit-Sharing Plan sponsored by the VBA with plan features similar to the Profit-Sharing Plan of C&F Bank. The amounts charged to expense under this plan were \$199,000, \$155,000 and \$147,000 in 2014, 2013 and 2012, respectively.

Central Virginia Bank maintained a qualified defined contribution plan for all eligible full-time and part-time employees prior to March 22, 2014. The plan was sponsored by the VBA. CVB did not make any profit sharing contributions to the plan during 2014, 2013 and 2012. On March 22, 2014 the CVB plan was terminated and the CVB plan assets totaling \$6.6 million were transferred into the Profit-Sharing Plan and the CVB plan participants became participants of the Profit-Sharing Plan subject to its provisions.

Individual performance bonuses are awarded annually to certain members of management under the Corporation's Management Incentive Plan. The Corporation's Compensation Committee recommends to the Corporation's Board of Directors the bonuses to be paid to the Chief Executive Officer and the President and Chief Financial Officer of the

Corporation, and recommends to the C&F Bank's Board of Directors bonuses to be paid to certain other senior C&F Bank and C&F Finance officers. In addition, the Chief Executive Officer recommends bonuses to be paid to other officers of the C&F Bank and C&F Finance. In determining the awards, performance, including the Corporation's growth rate, returns on average assets and equity, and absolute levels of income are considered. In addition, C&F Bank's Board of Directors considers the individual performance of the members of management who may receive awards. The expense for these bonus awards is accrued in the year of performance. Expenses under these plans were \$1.20 million, \$1.32 million and \$1.02 million in 2014, 2013 and 2012, respectively. In accordance with employment agreements for certain senior officers of C&F Mortgage, performance bonuses of \$173,000, \$932,000 and \$1.05 million were expensed in 2014, 2013 and 2012, respectively. Performance used in determining the awards is directly related to the profitability of C&F Mortgage.

C&F Bank has a non-contributory, defined benefit pension plan (Cash Balance Plan) for all full-time employees over 21 years of age. Under the Cash Balance Plan, the benefit account for each participant will grow each year with annual pay credits based on age and years of service and monthly interest credits based on the prior year's December average yield on 30-year Treasuries plus 150 basis points. C&F Bank funds pension costs in accordance with the funding provisions of the Employee Retirement Income Security Act.

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The Corporation has a nonqualified defined contribution plan for certain executives. The plan allows for elective salary and bonus deferrals. The plan also allows for employer contributions to make up for limitations on covered compensation imposed by the Internal Revenue Code with respect to the Bank's Profit Sharing Plan and Cash Balance Plan and to enhance retirement benefits by providing supplemental contributions from time to time. Expenses under this plan were \$215,000, \$185,000 and \$175,000 in 2014, 2013 and 2012, respectively. Investments for this plan are held in a Rabbi trust. These investments are included in other assets and the related liability is included in other liabilities.

The following table summarizes the projected benefit obligations, plan assets, funded status and rate assumptions associated with the C&F Bank's Cash Balance Plan based upon actuarial valuations.

(Dollars in thousands)	December 31,		
	2014	2013	2012
Change in benefit obligation			
Projected benefit obligation, beginning	\$ 10,659	\$ 10,058	\$ 8,768
Service cost	763	776	636
Interest cost	451	425	395
Actuarial loss	1,882	91	505
Benefits paid	(173)	(691)	(246)
Projected benefit obligation, ending	\$ 13,582	\$ 10,659	\$ 10,058
Change in plan assets			
Fair value of plan assets, beginning	\$ 11,624	\$ 9,612	\$ 8,295
Actual return on plan assets	633	1,703	1,063
Employer contributions	2,000	1,000	500
Benefits paid	(173)	(691)	(246)
Fair value of plan assets, ending	\$ 14,084	\$ 11,624	\$ 9,612
Funded status	\$ 502	\$ 965	\$ (446)
Amounts recognized as an other asset (liability)	\$ 502	\$ 965	\$ (446)
Amounts recognized in accumulated other comprehensive loss			
Net loss	\$ 3,558	\$ 1,510	\$ 2,495
Prior service cost	(942)	(1,010)	(1,077)
Deferred taxes	(916)	(175)	(496)
Total recognized in accumulated other comprehensive loss	\$ 1,700	\$ 325	\$ 922
Weighted-average assumptions for benefit obligation at valuation date			
Discount rate	3.6	% 4.4	% 4.0
Expected return on plan assets	7.5	8.0	8.0
Rate of compensation increase	3.0	3.0	3.0



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The accumulated benefit obligation was \$13.58 million and \$10.66 million as of the actuarial valuation dates December 31, 2014 and 2013, respectively.

(Dollars in thousands)	Year Ended December 31,		
	2014	2013	2012
Components of net periodic benefit cost			
Service cost	\$ 763	\$ 776	\$ 636
Interest cost	451	425	395
Expected return on plan assets	(832)	(748)	(633)
Amortization of prior service cost	(68)	(68)	(68)
Amortization of net obligation at transition	—	—	—
Recognized net actuarial loss	33	121	106
Net periodic benefit cost	347	506	436
Other changes in plan assets and benefit obligations recognized in other comprehensive loss			
Net loss (gain)	2,048	(985)	(31)
Amortization of net obligation at transition	—	—	—
Amortization of prior service costs	68	68	68
Deferred taxes	(741)	320	(13)
Total recognized in accumulated other comprehensive loss (income)	1,375	(597)	24
Total recognized in net periodic benefit cost and other comprehensive loss (income)	\$ 1,722	\$ (91)	\$ 460

Weighted-average assumptions for net periodic benefit cost as of	January 1,					
	2014		2013		2012	
Discount rate	4.4	%	4.0	%	4.5	%
Expected return on plan assets	7.5		8.0		8.0	
Rate of compensation increase	3.0		3.0		3.0	

The benefits expected to be paid by the plan in the next ten years are as follows:

(Dollars in thousands)	
2015	\$ 1,249
2016	633
2017	734
2018	2,155
2019	771
2020 – 2024	4,822
	\$ 10,364

C&F Bank selects the expected long-term rate of return on assets in consultation with its investment advisors and actuary. This rate is intended to reflect the average rate of earnings expected to be earned on the funds invested or to be invested to provide plan benefits. Historical performance is reviewed, especially with respect to real rates of return (net of inflation), for the major asset classes held or anticipated to be held by the trust and for the trust itself. Undue weight is not given to recent experience, which may not continue over the measurement period. Higher significance is placed on current forecasts of future long-term economic conditions.

Because assets are held in a qualified trust, anticipated returns are not reduced for taxes. Further, solely for this purpose, the plan is assumed to continue in force and not terminate during the period during which assets are invested. However, consideration is given to the potential impact of current and future investment policy, cash flow into and out of the trust, and expenses (both investment and non-investment) typically paid from plan assets (to the extent such expenses are not explicitly within periodic costs).

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C&F Bank's defined benefit pension plan's weighted average asset allocations by asset category are as follows:

	December 31,			
	2014		2013	
Mutual funds-fixed income	39	%	38	%
Mutual funds-equity	61		62	
Cash and equivalents	*		*	
	100	%	100	%

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\* Less than one percent.

The following table summarizes the fair value of the defined benefit plan assets as of December 31, 2014 and 2013. For more information about fair value measurements, see "Note 17: Fair Value of Assets and Liabilities."

(Dollars in thousands)	December 31, 2014			Assets at Fair Value
	Fair Value Measurements Using			
	Level 1	Level 2	Level 3	
Mutual funds-fixed income 1	\$ 5,540	\$ —	\$ —	\$ 5,540
Mutual funds-equity 2	8,533	—	—	8,533
Cash and equivalents 3	11	—	—	11
Total pension assets	\$ 14,084	\$ —	\$ —	\$ 14,084

(Dollars in thousands)	December 31, 2013			Assets at Fair Value
	Fair Value Measurements Using			
	Level 1	Level 2	Level 3	
Mutual funds-fixed income 1	\$ 4,431	\$ —	\$ —	\$ 4,431
Mutual funds-equity 2	7,181	—	—	7,181
Cash and equivalents 3	12	—	—	12
Total pension assets	\$ 11,624	\$ —	\$ —	\$ 11,624



- <sup>1</sup> This category includes investments in mutual funds focused on fixed income securities with both short-term and long-term investments. The funds are valued using the net asset value method in which an average of the market prices for the underlying investments is used to value the funds.
- <sup>2</sup> This category includes investments in mutual funds focused on equity securities with a diversified portfolio and includes investments in large cap and small cap funds, growth funds, international focused funds and value funds. The funds are valued using the net asset value method in which an average of the market prices for the underlying investments is used to value the funds.
- <sup>3</sup> This category comprises cash and short-term cash equivalent funds. The funds are valued at cost which approximates fair value.

The trust fund is sufficiently diversified to maintain a reasonable level of risk without imprudently sacrificing return, with a targeted asset allocation of 40% fixed income and 60% equities. The investment advisor selects investment fund managers with demonstrated experience and expertise, and funds with demonstrated historical performance, for the implementation of the plan's investment strategy. The investment manager will consider both actively and passively managed investment strategies and will allocate funds across the asset classes to develop an efficient investment structure.

It is the responsibility of the trustee to administer the investments of the trust within reasonable costs, being careful to avoid sacrificing quality. These costs include, but are not limited to, management and custodial fees, consulting fees, transaction costs and other administrative costs chargeable to the trust.

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NOTE 13: Related Party Transactions

Loans outstanding to directors and executive officers totaled \$2.45 million and \$2.72 million at December 31, 2014 and 2013, respectively. There were no new advances to directors and officers and repayments totaled \$262,000 in the year ended December 31, 2014. Total deposits for directors and executive officers were \$3.4 million and \$3.6 million at December 31, 2014 and 2013, respectively. In the opinion of management, these transactions were made in the ordinary course of business on substantially the same terms and conditions, including interest rates, collateral and repayment terms, as those prevailing at the same time for comparable transactions with unrelated persons, and, in the opinion of management and the Corporation's Board of Directors, do not involve more than normal risk or present other unfavorable features.

NOTE 14: Share-Based Plans

On April 16, 2013, the Corporation's shareholders approved the C&F Financial Corporation 2013 Stock and Incentive Compensation Plan (the 2013 Plan) for the grant of equity awards to certain key employees of the Corporation, as well as non-employee directors (including non-employee regional or advisory directors). The 2013 Plan authorizes an aggregate of 500,000 shares of the Corporation's common stock to be issued as equity awards in the form of stock options, tandem stock appreciation rights, restricted stock, restricted stock units and/or other stock-based awards. Since the 2013 Plan's approval, equity awards have only been issued in the form of restricted stock, which are accounted for using the fair market value of the Corporation's common stock on the date the restricted shares are awarded.

Prior to the approval of the 2013 Plan, the Corporation granted equity awards under the Amended and Restated C&F Financial Corporation 2004 Incentive Stock Plan (the Amended 2004 Plan). The Amended 2004 Plan authorized an aggregate of 500,000 shares of Corporation common stock to be issued as equity awards in the form of stock options, stock appreciation rights, restricted stock and/or restricted stock units to key employees and non-employee directors. Since 2006, all equity awards that were issued under the Amended 2004 Plan were in the form of restricted stock, which were accounted for using the fair market value of the Corporation's common stock on the date the restricted shares are awarded.

Prior to the amendment of the Amended 2004 Plan in 2008, the Corporation awarded options to purchase common stock and/or grants of restricted shares of common stock to certain key employees of the Corporation under the plan that was approved by the Corporation's shareholders on April 20, 2004. Options were issued to employees at a price equal to the fair market value of common stock at the date granted. Restricted shares were accounted for using the fair market value of the Corporation's common stock on the date the restricted shares were awarded. All options outstanding under this plan are exercisable as of December 31, 2014. All options expire ten years from the grant date.

In 1998, the Board of Directors authorized 25,000 shares of common stock for issuance under the C&F Financial Corporation 1998 Non-Employee Director Stock Compensation Plan (the Director Plan). In 1999, the Director Plan was amended to authorize a total of 150,000 shares for issuance. Under the Director Plan, options were issued to non-employee directors at a price equal to the fair market value of common stock at the date granted. All options outstanding under the Director Plan are exercisable as of December 31, 2014. All options expire ten years from the grant date. In 2008, the Corporation ceased granting awards to non-employee directors under the Director Plan, which expired in 2008, and non-employee directors were added to the group of eligible award recipients under the Amended 2004 Plan.

Stock option transactions under the various plans for the periods indicated were as follows:

	2014			2013			2012		
	Shares	Exercise Price*	Intrinsic Value	Shares	Exercise Price*	Shares	Exercise Price*	Intrinsic Value	
(Dollars in thousands, except for per share amounts)									
Outstanding at beginning of year	164,150	\$ 38.21		276,432	\$ 39.14	325,067	\$ 38.21		
Granted	—	—		—	—	—	—		
Exercised	(271)	39.29		(94,382)	40.41	(48,635)	40.87		
Cancelled	(63,117)	38.95		(17,900)	40.87	—			
Outstanding and exercisable at end of year	100,762	\$ 37.75	\$ 200	164,150	\$ 38.21	276,432	\$ 38.21	\$ 200	

\*Weighted average

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The total intrinsic value of in-the-money options exercised in 2014 was less than \$1,000. Cash received from option exercises during 2014 was \$11,000, and less than a \$1,000 tax benefit was recognized in additional paid-in capital in connection with nonqualified option exercises. The Corporation has a policy of issuing new shares to satisfy the exercise of stock options.

The following table summarizes information about stock options outstanding and exercisable at December 31, 2014:

Range of Exercise Prices	Options Outstanding and Exercisable		Exercise Price*
	Number Outstanding at December 31, 2014	Remaining Contractual Life (Years)*	
\$35.20 to \$39.60	100,762	1.2	\$ 37.75

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\*Weighted average

As permitted under the 2013 Plan and Amended 2004 Plan, the Corporation awards shares of restricted stock to certain key employees and non-employee directors. Restricted shares awarded to employees generally vest on the fifth anniversary of the grant date and restricted shares awarded to non-employee directors generally vest on the third anniversary of the grant date. A summary of the activity for restricted stock awards for the periods indicated is presented below:

	2014		2013		2012	
	Shares	Weighted-Average Grant Date Fair Value	Shares	Weighted-Average Grant Date Fair Value	Shares	Weighted-Average Grant Date Fair Value
Nonvested at beginning of year	120,183	\$ 31.18	97,700	\$ 24.69	87,125	\$ 22.59
Granted	32,625	39.84	35,594	45.24	29,025	33.16
Vested	(15,208)	20.13	(10,700)	18.16	(16,100)	28.85
Cancelled	(2,000)	42.14	(2,411)	36.42	(2,350)	22.60

Nonvested at end of year	135,600	\$ 34.34	120,183	\$ 31.18	97,700	\$ 24.69
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Compensation is accounted for using the fair market value of the Corporation's common stock on the date the restricted shares are awarded. The weighted-average grant date fair value of restricted stock granted for the years 2014, 2013 and 2012 was \$39.84, \$45.24 and \$33.16, respectively. Compensation expense is charged to income ratably over the vesting periods, and was \$967,000 in 2014, \$659,000 in 2013 and \$488,000 in 2012. As of December 31, 2014, there was \$2.79 million of total unrecognized compensation cost related to restricted stock granted under the 2013 Plan and the Amended 2004 Plan. This amount is expected to be recognized through 2019.

#### NOTE 15: Regulatory Requirements and Restrictions

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

Quantitative measures established by regulations effective as of December 31, 2014 and December 31, 2013 to ensure capital adequacy have required the Corporation, C&F Bank and CVB to maintain minimum amounts and ratios (set forth in the table below) of total and Tier 1 capital to risk-weighted assets and of Tier 1 capital to average assets (all as defined

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in the regulations). Per the regulatory capital standards effective as of December 31, 2014 and December 31, 2013, for the Corporation, C&F Bank and CVB Tier 1 capital consists of shareholders' equity excluding any net unrealized gain (loss) on securities available for sale, amounts resulting from changes in the funded status of the pension plan and goodwill net of any related deferred tax liability, and total capital consists of Tier 1 capital and a portion of the allowance for loan losses. As of these dates and for the Corporation only, Tier 1 and total capital also include trust preferred securities and exclude the unrealized loss on cash flow hedging instruments. Risk-weighted assets for the Corporation and C&F Bank were \$896.6 million and \$894.08 million, respectively at December 31, 2014. Risk-weighted assets for the Corporation, C&F Bank and CVB were \$850.67 million, \$692.50 million and \$157.85 million, respectively, at December 31, 2013. Management believes that, as of December 31, 2014, the Corporation and C&F Bank met all capital adequacy requirements to which they are subject.

As of December 31, 2014, the most recent notification from the Federal Deposit Insurance Corporation (FDIC) for C&F Bank categorized the Bank as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized, under regulations applicable at December 31, 2014 the Bank was required to maintain minimum total risk-based, Tier 1 risk-based and Tier 1 leverage ratios as set forth in the table below.

The Corporation's and the Bank's actual capital amounts and ratios are presented in the following table as of December 31, 2014 and 2013:

(Dollars in thousands)	Actual		Minimum Capital Requirements				Minimum To Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio		
As of December 31, 2014:								
Total Capital (to Risk-Weighted Assets)								
Corporation	\$ 130,401	14.5 %	\$ 71,731	8.0 %	N/A	N/A		
C&F Bank	129,228	14.5	71,527	8.0	\$ 89,408	10.0 %		
Tier 1 Capital (to Risk-Weighted Assets)								
Corporation	118,892	13.3	35,866	4.0	N/A	N/A		
C&F Bank	117,753	13.2	35,763	4.0	53,645	6.0		
Tier 1 Capital (to Average Tangible Assets)								
Corporation	118,892	9.2	51,974	4.0	N/A	N/A		
C&F Bank	117,753	9.1	51,959	4.0	77,939	6.0		

As of December 31, 2013:

Total Capital (to Risk-Weighted Assets)								
Corporation	\$ 125,159	14.7	%	\$ 68,054	8.0	%	N/A	N/A
C&F Bank	100,538	14.5		55,400	8.0		\$ 69,250	10.0 %
CVB	19,602	12.4		12,628	8.0		\$ 15,785	10.0 %
Tier 1 Capital (to Risk-Weighted Assets)								
Corporation	114,227	13.4		34,027	4.0		N/A	N/A
C&F Bank	91,559	13.2		27,700	4.0		41,550	6.0
CVB	19,567	12.4		6,314	4.0		9,471	6.0
Tier 1 Capital (to Average Tangible Assets)								
Corporation	114,227	8.9		51,623	4.0		N/A	N/A
C&F Bank	91,559	9.4		38,964	4.0		58,447	6.0
CVB	19,567	5.9		13,290	4.0		19,935	6.0

In December 2013, The Federal Reserve Board issued a final rule that makes technical changes to its market risk capital rule to align it with the Basel III regulatory capital framework and meet certain requirements of the Dodd-Frank Act. The Basel III final rules require the Company to comply with the following new minimum capital ratios, effective January 1,

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2015: (1) a new common equity Tier 1 capital ratio of 4.5% of risk-weighted assets; (2) a Tier 1 capital ratio of 6% of risk-weighted assets (increased from the current requirement of 4%); (3) a total capital ratio of 8% of risk-weighted assets (unchanged from the current requirement); and, (4) a leverage ratio of 4% of total assets. The Basel III Final Rules establish a capital conservation buffer of 2.5%, which is added to the 4.5% common equity Tier 1 capital ratio as the buffer is phased in, effectively resulting in a minimum ratio of common equity Tier 1 capital to risk-weighted assets of at least 7%. The Basel III Final Rules also establish risk weightings that applied to many classes of assets held by community banks, importantly including applying higher risk weightings to certain commercial real estate loans. The Basel III Final Rules were effective January 1, 2015, and the Basel III Final Rules capital conservation buffer will be phased in from 2015 to 2019.

Based on management's interpretation and understanding of the new rules, the Company has evaluated the effect of the Basel III final rules and expects the Company will continue to exceed the well capitalized minimum capital requirements based on the December 31, 2014 balance sheet composition. For additional information about the Basel III Final Rules, see "Item 1. Business" under the heading "Regulation and Supervision" in this Annual Report on Form 10-K.

On January 9, 2009, as part of the Capital Purchase Program, the Corporation issued and sold to the U.S. Treasury 20,000 shares of the Corporation's Series A Preferred Stock having a liquidation preference of \$1,000 per share and a Warrant for the purchase of up to 167,504 shares of the Corporation's Common Stock, for a total price of \$20.0 million. The Corporation has redeemed 100 percent of the Series A Preferred Stock, \$10.00 million in April 2012 and \$10.00 million in July 2011 and the warrant was repurchased in May 2014 for \$2.30 million.

On December 14, 2007, the Corporation issued \$10.00 million of trust preferred securities through a statutory business trust for general corporate purposes including the refinancing of existing debt. On July 21, 2005, the Corporation issued \$10.00 million of trust preferred securities through a statutory business trust to partially fund the purchase of 427,186 shares of the Corporation's common stock at \$41 per share on July 27, 2005. On December 17, 2003, CVBK issued \$5.00 million of trust preferred securities through a statutory business trust for general corporate purposes. Based on the Corporation's Tier 1 capital levels, the entire \$25.00 million of trust preferred securities was eligible for inclusion in the Corporation's Tier 1 capital as of December 31, 2014 and 2013.

Federal and state banking regulations place certain restrictions on dividends paid and loans or advances made by C&F Bank (and prior to being merged into C&F Bank, CVB) to the Corporation. The total amount of dividends that may be paid at any date by C&F Bank is generally limited to the retained earnings of C&F Bank, and loans or advances are limited to 10 percent of C&F Bank's capital stock and surplus on a secured basis.

NOTE 16: Commitments and Financial Instruments with Off-Balance-Sheet Risk



The Corporation 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, commitments to sell loans, and standby letters of credit. These instruments involve elements of credit and interest rate risk in excess of the amount on the balance sheet. The contract amounts of these instruments reflect the extent of involvement the Corporation has in particular classes of financial instruments. The Corporation'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 written is represented by the contractual amount of these instruments. The Corporation uses the same credit policies in making commitments and conditional obligations as it does for on-balance-sheet instruments. Collateral is obtained based on management's credit assessment of the customer.

Loan commitments are agreements to extend credit to a customer provided that there are no violations of the terms of the contract prior to funding. Commitments have fixed expiration dates or other termination clauses and may require payment of a fee by the customer. Since many of the commitments may expire without being completely drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Bank evaluates each customer's creditworthiness on a case-by-case basis. The amount of loan commitments was \$136.00 million at December 31, 2014 and \$129.24 million (including loan commitments at CVB) at December 31, 2013.

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Standby letters of credit are written conditional commitments issued by the Bank to guarantee the performance of a customer to a third party. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loans to customers. The total contract amount of standby letters of credit, whose contract amounts represent credit risk, was \$13.40 million at December 31, 2014 and \$13.72 million (including loan commitments at CVB) at December 31, 2013.

C&F Mortgage had rate lock commitments (or IRLCs) to originate mortgage loans amounting to approximately \$38.40 million and loans held for sale of \$28.28 million. At December 31, 2014, each loan held for sale by C&F Mortgage was subject to a forward sales agreement. C&F Mortgage enters into IRLCs with customers and will sell the underlying loans to investors on either a best efforts or a mandatory delivery basis. C&F Mortgage mitigates interest rate risk on IRLCs and loans held for sale by (a) entering into forward loan sales contracts with investors for loans to be delivered on a best efforts basis or (b) entering into forward sales contracts of MBS for loans to be delivered on a mandatory basis. Both the IRLCs with customers and the forward sales contracts are considered derivative financial instruments. At December 31, 2014, the Corporation had forward sales contracts with a notional value of \$66.68 million. The fair value of these derivative instruments at December 31, 2014 was \$448,000, which was included in other assets.

C&F Mortgage sells substantially all of the residential mortgage loans it originates to third-party counterparties. As is customary in the industry, the agreements with these counterparties require C&F Mortgage to extend representations and warranties with respect to program compliance, borrower misrepresentation, fraud, and early payment performance. Under the agreements, the counterparties are entitled to make loss claims and repurchase requests of C&F Mortgage for loans that contain covered deficiencies. C&F Mortgage has obtained early payment default recourse waivers for a significant portion of its business. Recourse periods for early payment default for the remaining counterparties vary from 90 days up to one year. Recourse periods for borrower misrepresentation or fraud, or underwriting error do not have a stated time limit. C&F Mortgage maintains an indemnification reserve for potential claims made under these recourse provisions. C&F Mortgage has adopted a reserve methodology whereby provisions are made to an expense account to fund a reserve maintained as a liability account on the balance sheet for potential losses. The loan performance data of sold loans is not made available to C&F Mortgage by the counterparties making the evaluation of potential losses inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available. A schedule of expected losses on loans with claims or indemnifications is maintained to ensure the reserve is adequate to cover estimated losses. Often times, claims are not factually validated and they are rescinded. Once claims are validated and the actual or potential loss is agreed upon with the counterparties, the reserve is charged and a cash payment is made to settle the claim. The balance of the indemnification reserve has adequately provided for all claims in each of the three years ended December 31, 2014. The following table presents the changes in the allowance for indemnification losses for the periods presented:

(Dollars in thousands)	Year Ended December 31,		
	2014	2013	2012

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Allowance, beginning of period	\$ 2,415	\$ 2,092	\$ 1,702
Provision for indemnification losses	240	558	1,205
Payments	(566)	(235)	(815)
Allowance, end of period	\$ 2,089	\$ 2,415	\$ 2,092

Risks also arise from the possible inability of counterparties to meet the terms of their contracts. C&F Mortgage has procedures in place to evaluate the credit risk of investors and does not expect any counterparty to fail to meet its obligations.

The Corporation is committed under noncancelable operating leases for certain office locations. Rent expense associated with the Corporation's operating leases was \$1.25 million, \$1.39 million and \$1.47 million for the years ended December 31, 2014, 2013 and 2012, respectively.

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Future minimum lease payments due under the Corporation's operating leases as of December 31, 2014 are as follows:

(Dollars in thousands)	
2015	\$ 1,266
2016	1,073
2017	919
2018	682
2019	509
Thereafter	436
	\$ 4,885

## NOTE 17: Fair Value of Assets and Liabilities

Fair value is defined as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. U.S. GAAP requires that valuation techniques maximize the use of observable inputs and minimize the use of unobservable inputs. U.S. GAAP also establishes a fair value hierarchy which prioritizes the valuation inputs into three broad levels. Based on the underlying inputs, each fair value measurement in its entirety is reported in one of the three levels. These levels are:

- Level 1—Valuation is based upon quoted prices for identical instruments traded in active markets. Level 1 assets and liabilities include debt and equity securities traded in an active exchange market, as well as U.S. Treasury securities.
- Level 2—Valuation is based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model based valuation techniques for which all significant assumptions are observable in the market or can be corroborated by observable market data for substantially the full term of the assets or liabilities.
- Level 3—Valuation is determined using model-based techniques that use at least one significant assumption not observable in the market. These unobservable assumptions reflect the Corporation's estimates of assumptions that market participants would use in pricing the respective asset or liability. Valuation techniques may include the use of pricing models, discounted cash flow models and similar techniques.

U.S. GAAP allows an entity the irrevocable option to elect fair value (the fair value option) for the initial and subsequent measurement for certain financial assets and liabilities on a contract-by-contract basis. The Corporation has not made any fair value options elections as of December 31, 2014, except that during the second quarter of 2013, the Corporation elected to begin using fair value accounting for its entire portfolio of LHFS.

#### Assets and Liabilities Measured at Fair Value on a Recurring Basis

The following describes the valuation techniques and inputs used by the Corporation in determining the fair value of certain assets recorded at fair value on a recurring basis in the financial statements.

Securities available for sale. The Corporation primarily values its investment portfolio using Level 2 fair value measurements, but may also use Level 1 or Level 3 measurements if required by the composition of the portfolio. At December 31, 2014 and 2013, the Corporation's entire investment securities portfolio was comprised of securities available for sale, which were valued using Level 2 fair value measurements. The Corporation has contracted with third party portfolio accounting service vendors for valuation of its securities portfolio. The vendors' sources for security valuation are Standard & Poor's Securities Evaluations Inc. (SPSE), Thomson Reuters Pricing Service (TRPS), and Interactive Data Pricing and Reference Data LLC (IDC). Each source provides opinions, known as evaluated prices, as to the value of individual securities based on model-based pricing techniques that are partially based on available market data, including prices for similar instruments in active markets and prices for identical assets in markets that are not active. SPSE and IDC provide evaluated prices for the Corporation's obligations of states and political subdivisions category of securities. Both sources use proprietary pricing models and pricing systems, mathematical tools and judgment to determine an evaluated

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price for a security based upon a hierarchy of market information regarding that security or securities with similar characteristics. TRPS and IDC provide evaluated prices for the Corporation's U.S. government agencies and corporations and mortgage-backed categories of securities. Fixed-rate callable securities of the U.S. government agencies and corporations category are individually evaluated on an option adjusted spread basis for callable issues or on a nominal spread basis incorporating the term structure of agency market spreads and the appropriate risk free benchmark curve for non-callable issues. Fixed-rate securities issued by the Small Business Association in the U.S. government agencies and corporations category are individually evaluated based upon a hierarchy of security specific information and market data regarding that security or securities with similar characteristics. Pass-through mortgage-backed securities in the mortgage-backed category are grouped into aggregate categories defined by issuer program, weighted average coupon, and weighted average maturity. Each aggregate is benchmarked to a relative mortgage-backed to-be-announced (TBA) or other benchmark price. TBA prices are obtained from market makers and live trading systems. Collateralized mortgage obligations in the mortgage-backed category are individually evaluated based upon a hierarchy of security specific information and market data regarding that security or securities with similar characteristics. Each evaluation is determined using an option adjusted spread and prepayment model based on volatility-driven, multi-dimensional spread tables.

Loans held for sale. Fair value of the Corporation's LHFS is based on observable market prices for similar instruments traded in the secondary mortgage loan markets in which the Corporation conducts business. The Corporation's portfolio of LHFS is classified as Level 2.

Derivative asset (liability) - IRLCs. The Corporation recognizes IRLCs at fair value. Fair value of IRLCs is based on either (i) the price of the underlying loans obtained from an investor for loans that will be delivered on a best efforts basis or (ii) the observable price for individual loans traded in the secondary market for loans that will be delivered on a mandatory basis. All of the Corporation's IRLCs are classified as Level 2.

Derivative asset (liability) - forward sales commitments. Forward commitments to sell mortgage loans and TBAs are used to mitigate interest rate risk for residential mortgage LHFS and IRLCs. Forward commitments to sell mortgage loans and TBAs are considered derivatives and are recorded at fair value, based on (i) committed sales prices from investors for commitments to sell mortgage loans or (ii) observable market data inputs for commitments to sell TBAs. The Corporation's forward sales commitments are classified as Level 2.

Derivative asset (liability) - cash flow hedges. The Corporation's derivative financial instruments have been designated as and qualify as cash flow hedges. The fair value of the Corporation's cash flow hedges is determined using the discounted cash flow method.

The following table presents the balances of financial assets measured at fair value on a recurring basis.

(Dollars in thousands)	December 31, 2014			Assets at Fair Value
	Fair Value Measurements Using Level 1	Level 2	Using Level 3	
<b>Assets:</b>				
Securities available for sale				
U.S. government agencies and corporations	\$ —	\$ 22,934	\$ —	\$ 22,934
Mortgage-backed securities	—	67,619	—	67,619
Obligations of states and political subdivisions	—	131,344	—	131,344
Total securities available for sale	—	221,897	—	221,897
Loans held for sale	—	28,279	—	28,279
Derivative asset - IRLC	—	448	—	448
Derivative asset - cash flow hedges	—	40	—	40
Total assets	\$ —	\$ 250,664	\$ —	\$ 250,664
<b>Liabilities:</b>				
Derivative liability - cash flow hedges	\$ —	\$ 143	\$ —	\$ 143

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(Dollars in thousands)	December 31, 2013			Assets at Fair Value
	Fair Value Measurements Using Level 1	Level 2	Using Level 3	
Assets:				
Securities available for sale				
U.S. Treasury securities	\$ —	\$ 10,000	\$ —	\$ 10,000
U.S. government agencies and corporations	—	29,950	—	29,950
Mortgage-backed securities	—	50,863	—	50,863
Obligations of states and political subdivisions	—	127,139	—	127,139
Corporate and other debt securities	—	158	—	158
Total securities available for sale	—	218,110	—	218,110
Loans held for sale	—	35,879	—	35,879
Derivative asset - IRLC	—	511	—	511
Derivative asset - forward sales commitments	—	22	—	22
Total assets	\$ —	\$ 254,522	\$ —	\$ 254,522
Liabilities:				
Derivative liability - cash flow hedges	\$ —	\$ 331	\$ —	\$ 331

## Assets and Liabilities Measured at Fair Value on a Nonrecurring Basis

The Corporation may be required, from time to time, to measure and recognize certain assets at fair value on a nonrecurring basis in accordance with GAAP. The following describes the valuation techniques and inputs used by the Corporation in determining the fair value of certain assets recorded at fair value on a nonrecurring basis in the financial statements.

Impaired loans. The Corporation does not record loans at fair value on a recurring basis. However, there are instances when a loan is considered impaired and an allowance for loan losses is established. A loan is considered impaired when it is probable that the Corporation will be unable to collect all interest and principal payments as scheduled in the loan agreement. All TDRs are considered impaired loans. The Corporation measures impairment on a loan-by-loan basis for commercial, construction and residential loans in excess of \$500,000 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. Additionally, management reviews current market conditions, borrower history, past experience with similar loans and economic conditions. Based on management's review, additional write-downs to fair value may be incurred. The Corporation maintains a valuation allowance to the extent that the measure of the impaired loan is less than the recorded investment. When the fair value of an impaired loan is based solely on observable cash flows, market price or a current appraisal, the Corporation records the impaired loan as nonrecurring Level 2. However, if based on management's review, additional write-downs to fair value are required, the Corporation records the impaired loan as nonrecurring Level 3.



The measurement of impaired loans of less than \$500,000 is based on each loan's future cash flows discounted at the loan's effective interest rate rather than the market rate of interest, which is not a fair value measurement and is therefore excluded from fair value disclosure requirements.

Other real estate owned (OREO). Assets acquired through, or in lieu of, loan foreclosure are held for sale and are initially recorded at fair value less costs to sell at the date of foreclosure. Initial fair value is based upon appraisals the Corporation obtains from independent licensed appraisers. Subsequent to foreclosure, management periodically performs valuations of the foreclosed assets based on updated appraisals, general market conditions, recent sales of like properties, length of time the properties have been held, and our ability and intention with regard to continued ownership of the properties. The

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Corporation may incur additional write-downs of foreclosed assets to fair value less costs to sell if valuations indicate a further other-than-temporary deterioration in market conditions. As such, we record OREO as nonrecurring Level 3.

The following table presents the balances of financial assets measured at fair value on a non-recurring basis.

(Dollars in thousands)	December 31, 2014			
	Fair Value Measurements Using Assets at Fair			
	Level 1	Level 2	Level 3	Value
Impaired loans, net	\$ —	\$ —	\$ 1,224	\$ 1,224
Other real estate owned net	—	—	786	786
Total	\$ —	\$ —	\$ 2,010	\$ 2,010

(Dollars in thousands)	December 31, 2013			
	Fair Value Measurements Using Assets at Fair			
	Level 1	Level 2	Level 3	Value
Impaired loans, net	\$ —	\$ —	\$ 3,646	\$ 3,646
Other real estate owned, net	—	—	2,769	2,769
Total	\$ —	\$ —	\$ 6,415	\$ 6,415

The following table presents quantitative information about Level 3 fair value measurements for financial assets measured at fair value on a non-recurring basis as of December 31, 2014:

(Dollars in thousands)	Fair Value Measurements at December 31, 2014			
	Fair Value	Valuation Technique(s)	Unobservable Inputs	Range of Inputs
Impaired loans, net	\$ 1,224	Appraisals	Discount to reflect current market conditions and estimated selling costs	10% - 50%
Other real estate owned, net	786	Appraisals	Discount to reflect current market conditions and estimated selling costs	0% - 56%

Total \$ 2,010

#### Fair Value of Financial Instruments

FASB ASC 825, Financial Instruments, requires disclosure about fair value of financial instruments, including those financial assets and financial liabilities that are not required to be measured and reported at fair value on a recurring or nonrecurring basis. ASC 825 excludes certain financial instruments and all nonfinancial instruments from its disclosure requirements. Accordingly, the aggregate fair value amounts presented may not necessarily represent the underlying fair value of the Corporation.

The following describes the valuation techniques used by the Corporation to measure its financial instruments at fair value as of December 31, 2014 and 2013.

Cash and short-term investments. The nature of these instruments and their relatively short maturities provide for the reporting of fair value equal to the historical cost.

Loans, net. The fair value of performing loans is estimated using a discounted expected future cash flows analysis based on current rates being offered on similar products in the market. An overall valuation adjustment is made for specific credit risks as well as general portfolio risks. Based on the valuation methodologies used in assessing the fair value of loans and the associated valuation allowance, these loans are considered Level 3. See Note 1 for more information on the valuation methodologies used in creating the valuation allowance for performing loans.

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Loan totals, as listed in the table below, include impaired loans. For valuation techniques used in relation to impaired loans, see the Assets and Liabilities Measured at Fair Value on a Nonrecurring Basis section in this Note 17.

Loans held for sale, net. As described in Assets and Liabilities Measured at Fair Value on a Recurring Basis section in this Note 17, the Corporation elected to carry its portfolio of loans held for sale (or LHFS) at fair value, measured on a recurring basis, during the second quarter of 2013.

Accrued interest receivable. The carrying amount of accrued interest receivable approximates fair value.

Bank-owned life insurance (BOLI). The fair value of BOLI is estimated using information provided by insurance carriers. These policies are carried at their cash surrender value, which approximates the fair value.

Deposits. The fair value of all demand deposit accounts is the amount payable at the report date. For all other deposits, the fair value is determined using the discounted cash flow method. The discount rate was equal to the rate currently offered on similar products in active markets (Level 2).

Borrowings. The fair value of borrowings is determined using the discounted cash flow method. The discount rate was equal to the rate currently offered on similar products in active markets (Level 2).

Accrued interest payable. The carrying amount of accrued interest payable approximates fair value.

Letters of credit. The estimated fair value of letters of credit is based on estimated fees the Corporation would pay to have another entity assume its obligation under the outstanding arrangements. These fees are not considered material.

Unused portions of lines of credit. The estimated fair value of unused portions of lines of credit is based on estimated fees the Corporation would pay to have another entity assume its obligation under the outstanding arrangements. These fees are not considered material.

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The following tables reflect the carrying amounts and estimated fair values of the Corporation's financial instruments whether or not recognized on the balance sheet at fair value.

(Dollars in thousands)	Carrying Value	Fair Value Measurements at December 31, 2014 Using			Total Fair Value
		Level 1	Level 2	Level 3	
<b>Financial assets:</b>					
Cash and short-term investments	\$ 167,616	\$ 167,616	\$ —	\$ —	\$ 167,616
Securities available for sale	221,897	—	221,897	—	221,897
Loans, net	800,198	—	—	813,010	813,010
Loans held for sale	28,279	—	28,279	—	28,279
Derivative asset - IRLC	448	—	448	—	448
Derivative asset - cash flow hedges	40	—	40	—	40
Accrued interest receivable	6,421	6,421	—	—	6,421
<b>Financial liabilities:</b>					
Demand deposits	\$ 659,594	\$ 659,594	\$ —	\$ —	\$ 659,594
Time deposits	366,507	—	369,538	—	369,538
Borrowings	167,027	—	160,052	—	160,052
Derivative liability - cash flow hedges	143	—	143	—	143
Accrued interest payable	740	740	—	—	740

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(Dollars in thousands)	Carrying Value	Fair Value Measurements at December 31, 2013			Total Fair Value
		Level 1	Level 2	Level 3	
Financial assets:					
Cash and short-term investments	\$ 148,139	\$ 148,139	\$ —	\$ —	\$ 148,139
Securities available for sale	218,110	—	218,110	—	218,110
Loans, net	785,532	—	—	800,488	800,488
Loans held for sale	35,879	—	35,879	—	35,879
Derivative asset - IRLC	511	—	511	—	511
Derivative asset - forward sales commitments	22	—	22	—	22
Accrued interest receivable	6,360	6,360	—	—	6,360
Financial liabilities:					
Demand deposits	\$ 608,409	\$ 608,409	\$ —	\$ —	\$ 608,409
Time deposits	399,883	—	403,291	—	403,291
Borrowings	169,835	—	162,194	—	162,194
Derivative liability - cash flow hedges	331	—	331	—	331
Accrued interest payable	843	843	—	—	843

The Corporation assumes interest rate risk (the risk that general interest rate levels will change) as a result of its normal operations. As a result, the fair values of the Corporation's financial instruments will change when interest rate levels change and that change may be either favorable or unfavorable to the Corporation. Management attempts to match maturities of assets and liabilities to the extent believed necessary to balance minimizing interest rate risk and increasing net interest income in current market conditions. However, borrowers with fixed rate obligations are less likely to prepay in a rising rate environment and more likely to prepay in a falling rate environment. Conversely, depositors who are receiving fixed rates are more likely to withdraw funds before maturity in a rising rate environment and less likely to do so in a falling rate environment. Management monitors interest rates, maturities and repricing dates of assets and liabilities and attempts to manage interest rate risk by adjusting terms of new loans, deposits and borrowings and by investing in securities with terms that mitigate the Corporation's overall interest rate risk.

## NOTE 18: Business Segments

The Corporation operates in a decentralized fashion in three principal business segments: Retail Banking, Mortgage Banking and Consumer Finance. Revenues from Retail Banking operations consist primarily of interest earned on loans and investment securities and service charges on deposit accounts. Mortgage Banking operating revenues consist principally of gains on sales of loans in the secondary market, loan origination fee income and interest earned on mortgage loans held for sale. Revenues from Consumer Finance consist primarily of interest earned on purchased automobile retail installment sales contracts.

The Corporation's other segment includes an investment company that derives revenues from brokerage services, an insurance company that derives revenues from insurance services, and a title company that derives revenues from title insurance services. The results of the other segment are not significant to the Corporation as a whole and have been included

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in “Other.” Revenue and expenses of the Corporation are also included in “Other,” and consist primarily of interest expense associated with the Corporation’s trust preferred capital notes and other general corporate expenses.

(Dollars in thousands)	Year Ended December 31, 2014					Consolidated
	Retail Banking	Mortgage Banking	Consumer Finance	Other	Eliminations	
<b>Revenues:</b>						
Interest income	\$ 43,616	\$ 1,304	\$ 46,569	\$ —	\$ (4,994)	\$ 86,495
Gains on sales of loans	—	5,108	—	—	—	5,108
Other noninterest income	9,170	2,708	1,227	1,358	—	14,463
Total operating income	52,786	9,120	47,796	1,358	(4,994)	106,066
<b>Expenses:</b>						
Provision for loan losses	—	60	16,270	—	—	16,330
Interest expense	5,915	199	6,445	960	(4,994)	8,525
Salaries and employee benefits	22,944	3,568	8,962	836	—	36,310
Other noninterest expenses	17,970	4,608	4,739	508	—	27,825
Total operating expenses	46,829	8,435	36,416	2,304	(4,994)	88,990
Income (loss) before income taxes	5,957	685	11,380	(946)	—	17,076
Income tax (benefit) expense	377	274	4,438	(359)	—	4,730
Net income (loss)	\$ 5,580	\$ 411	\$ 6,942	\$ (587)	\$ —	\$ 12,346
Total assets	\$ 1,178,270	\$ 42,143	\$ 283,984	\$ 4,208	\$ (175,282)	\$ 1,333,323
Goodwill	\$ 3,702	\$ —	\$ 10,723	\$ —	\$ —	\$ 14,425
Capital expenditures	\$ 1,657	\$ 92	\$ 177	\$ 1	\$ —	\$ 1,927

(Dollars in thousands)	Year Ended December 31, 2013					Consolidated
	Retail Banking	Mortgage Banking	Consumer Finance	Other	Eliminations	
<b>Revenues:</b>						
Interest income	\$ 34,777	\$ 1,865	\$ 48,735	\$ 2	\$ (5,167)	\$ 80,212
Gains on sales of loans	—	7,510	—	—	—	7,510
Other noninterest income	7,672	4,308	1,190	1,540	—	14,710
Total operating income	42,449	13,683	49,925	1,542	(5,167)	102,432



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Expenses:						
Provision for loan losses	1,030	90	13,965	—	—	15,085
Interest expense	6,135	343	6,501	811	(5,167)	8,623
Salaries and employee benefits	18,361	4,118	7,877	811	—	31,167
Other noninterest expenses	14,500	5,881	4,300	1,764	—	26,445
Total operating expenses	40,026	10,432	32,643	3,386	(5,167)	81,320
Income (loss) before income taxes	2,423	3,251	17,282	(1,844)	—	21,112
Income tax (benefit) expense	(884)	1,300	6,740	(446)	—	6,710
Net income (loss)	\$ 3,307	\$ 1,951	\$ 10,542	\$ (1,398)	\$ —	\$ 14,402
Total assets	\$ 1,157,228	\$ 50,803	\$ 278,855	\$ 4,017	\$ (178,606)	\$ 1,312,297
Goodwill	\$ 3,702	\$ —	\$ 10,723	\$ —	\$ —	\$ 14,425
Capital expenditures	\$ 3,294	\$ 535	\$ 53	\$ 2	\$ —	\$ 3,884

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(Dollars in thousands)	Year Ended December 31, 2012					
	Retail Banking	Mortgage Banking	Consumer Finance	Other	Eliminations	Consolidated
<b>Revenues:</b>						
Interest income	\$ 32,301	\$ 2,358	\$ 47,403	\$ —	\$ (5,098)	\$ 76,964
Gains on sales of loans	—	7,692	—	—	—	7,692
Other noninterest income	6,124	4,315	1,149	1,322	20	12,930
Total operating income	38,425	14,365	48,552	1,322	(5,078)	97,586
<b>Expenses:</b>						
Provision for loan losses	2,400	165	9,840	—	—	12,405
Interest expense	7,404	483	6,334	988	(5,098)	10,111
Salaries and employee benefits	15,562	3,795	7,591	865	—	27,813
Other noninterest expenses	12,385	6,265	4,100	479	—	23,229
Total operating expenses	37,751	10,708	27,865	2,332	(5,098)	73,558
Income (loss) before income taxes	674	3,657	20,687	(1,010)	20	24,028
Income tax (benefit) expense	(1,479)	1,466	8,042	(383)	—	7,646
Net income (loss)	\$ 2,153	\$ 2,191	\$ 12,645	\$ (627)	\$ 20	\$ 16,382
Total assets	\$ 813,817	\$ 86,978	\$ 280,205	\$ 3,570	\$ (207,552)	\$ 977,018
Goodwill	\$ —	\$ —	\$ 10,723	\$ —	\$ —	\$ 10,723
Capital expenditures	\$ 739	\$ 272	\$ 179	\$ —	\$ —	\$ 1,190

The Retail Banking segment extends a warehouse line of credit to the Mortgage Banking segment, providing a portion of the funds needed to originate mortgage loans. The Retail Banking segment charges the Mortgage Banking segment interest at the daily FHLB advance rate plus 50 basis points. The Retail Banking segment also provides the Consumer Finance segment with a portion of the funds needed to originate loans by means of variable rate notes that carry interest at one-month LIBOR plus 200 basis points and fixed rate notes that carry interest rates ranging from 3.8 percent to 8.0 percent. The Retail Banking segment acquires certain residential real estate loans from the Mortgage Banking segment at prices similar to those paid by third-party investors. These transactions are eliminated to reach consolidated totals. Certain corporate overhead costs incurred by the Retail Banking segment are not allocated to the Mortgage Banking, Consumer Finance and Other segments.

## NOTE 19: Interest Rate Swaps

The Corporation uses interest rate swaps to manage exposure of its trust preferred capital notes to interest rate risk. Interest rate swaps involve the exchange of fixed and variable rate interest payments between two parties, based on a common notional principal amount and maturity date with no exchange of underlying principal amounts. The Corporation's interest rate swaps qualify as cash flow hedges. The Corporation's cash flow hedges effectively modify

the Corporation's exposure to interest rate risk by converting variable rates of interest on \$10.00 million and \$15.00 million of the Corporation's trust preferred capital notes to fixed rates of interest until September 2015 and December 2019, respectively.

The cash flow hedges total notional amount is \$25.00 million. At December 31, 2014, the \$15.0 million of cash flow hedges entered into during 2014 had a fair value of \$40,000, which is recorded in other assets, and the other \$10.0 million of cash flow hedges had a fair value of (\$143,000), which is recorded in other liabilities. The cash flow hedges were fully effective at December 31, 2014 and therefore the net loss on the cash flow hedges was recognized as a component of other comprehensive income (loss), net of deferred income taxes.

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## NOTE 20: Parent Company Condensed Financial Information

Financial information for the parent company is as follows:

(Dollars in thousands)	December 31,	
	2014	2013
Balance Sheets		
Assets		
Cash	\$ 662	\$ 958
Securities available for sale	—	—
Other assets	2,506	7,549
Investments in subsidiaries	145,790	130,009
Total assets	\$ 148,958	\$ 138,516
Liabilities and shareholders' equity		
Trust preferred capital notes	\$ 25,103	\$ 20,620
Other liabilities	482	4,955
Shareholders' equity	123,373	112,941
Total liabilities and shareholders' equity	\$ 148,958	\$ 138,516

(Dollars in thousands)	Year Ended December 31,		
	2014	2013	2012
Statements of Income			
Interest expense on borrowings	\$ (916)	\$ (757)	\$ (987)
Dividends received from C&F Bank	5,596	31,150	13,232
Equity in undistributed net income (loss) of subsidiaries	8,182	(14,768)	4,246
Gain on sale of securities	—	270	—
Other income	20	53	737
Other expenses	(536)	(1,546)	(846)
Net income	\$ 12,346	\$ 14,402	\$ 16,382

(Dollars in thousands)	Year Ended December 31,		
	2014	2013	2012

## Statements of Cash Flows

## Operating activities:

Net income	\$ 12,346	\$ 14,402	\$ 16,382
Adjustments to reconcile net income to net cash provided by operating activities:			
Equity in undistributed (earnings) loss of subsidiaries	(8,182)	14,768	(4,246)
Share-based compensation	1,104	743	566
Amortization of acquisition-related fair value adjustment	27	—	—
Gain on sale of securities	—	(270)	—
Decrease (increase) in other assets	4,882	(4,710)	(217)
(Decrease) increase in other liabilities	(4,263)	4,550	(46)
Net cash provided by operating activities	5,914	29,483	12,439
Investing activities:			
Proceeds from sale of securities	—	296	—
Acquisition of Central Virginia Bankshares, Inc.	—	(4,196)	—
Investment in Central Virginia Bank	—	(26,058)	—
Merger of Central Virginia Bankshares, Inc. into C&F Financial Corporation	160	—	—
Net cash provided by (used in) investing activities	160	(29,958)	—
Financing activities:			
Net proceeds from issuance of preferred stock	—	—	—
Net proceeds from issuance of common stock	133	125	200
Redemption of preferred stock	—	—	(10,000)
Repurchase of common stock warrant	(2,303)	—	—
Common stock repurchases	(161)	—	—
Cash dividends	(4,050)	(3,845)	(3,682)
Proceeds from exercise of stock options	11	4,301	1,309
Net cash (used in) provided by financing activities	(6,370)	581	(12,173)
Net (decrease) increase in cash and cash equivalents	(296)	106	266
Cash at beginning of year	958	852	586
Cash at end of year	\$ 662	\$ 958	\$ 852

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## NOTE 21: Other Noninterest Expenses

The following table presents the significant components in the statements of income line “Noninterest Expenses-Other Expenses.”

(Dollars in thousands)	Year Ended December 31,		
	2014	2013	2012
Data processing fees	\$ 3,616	\$ 2,700	\$ 2,273
Loan and OREO expenses	364	1,001	1,982
Amortization of core deposit intangible	1,190	333	—
Professional fees	2,101	2,326	1,688
Telecommunication expenses	1,507	1,231	1,181
Travel and educational expenses	1,109	1,032	957
Marketing and advertising expenses	1,333	964	813
Provision for indemnification losses	240	558	1,205
Acquisition transactions cost	315	1,351	—
All other noninterest expenses	7,244	7,552	6,335
Total Other Noninterest Expenses	\$ 19,019	\$ 19,048	\$ 16,434

## NOTE 22: Quarterly Condensed Statements of Income—Unaudited

Dollars in thousands (except per share amounts)	2014 Quarter Ended			
	March 31	June 30	September 30	December 31
Total interest income	\$ 21,294	\$ 21,712	\$ 21,838	\$ 21,651
Net interest income after provision for loan losses	15,564	16,306	15,582	14,188
Other income	4,812	5,349	4,706	4,704
Other expenses	16,354	16,339	15,668	15,774
Income before income taxes	4,022	5,316	4,620	3,118
Net income	2,893	3,742	3,294	2,417
Net income available to common shareholders	2,893	3,742	3,294	2,417
Earnings per common share—assuming dilution	0.83	1.09	0.97	0.71
Dividends declared per common share	0.29	0.30	0.30	0.30

2013 Quarter Ended

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Dollars in thousands (except per share amounts)	March 31	June 30	September 30	December 31
Total interest income	\$ 19,123	\$ 19,230	\$ 19,654	\$ 22,205
Net interest income after provision for loan losses	13,795	14,028	13,745	14,936
Other income	5,098	6,963	5,639	4,520
Other expenses	13,029	14,548	14,524	15,511
Income before income taxes	5,864	6,443	4,860	3,945
Net income	4,006	4,178	3,366	2,852
Net income available to common shareholders	4,006	4,178	3,366	2,852
Earnings per common share—assuming dilution	1.19	1.22	0.97	0.81
Dividends declared per common share	0.29	0.29	0.29	0.29

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Shareholders

C&F Financial Corporation

West Point, Virginia

We have audited the accompanying consolidated balance sheets of C&F Financial Corporation and Subsidiary as of December 31, 2014 and 2013, and the related consolidated statements of income, comprehensive income, changes in shareholders' equity, and cash flows for each of the three years in the period ended December 31, 2014. These financial statements are the responsibility of the Corporation'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 financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes 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 C&F Financial Corporation and Subsidiary as of December 31, 2014 and 2013, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2014, in conformity with U.S. generally accepted accounting principles.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), C&F Financial Corporation and Subsidiary's internal control over financial reporting as of December 31, 2014, based on criteria established in Internal Control — Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission in 2013, and our report dated March 11, 2015 expressed an unqualified opinion on the effectiveness of C&F Financial Corporation and Subsidiary's internal control over financial reporting.

/s/ Yount, Hyde & Barbour, P.C.



Winchester, Virginia

March 11, 2015

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ITEM 9.CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None

ITEM 9A.CONTROLS AND PROCEDURES

Disclosure Controls and Procedures. The Corporation's management, including the Corporation's Chief Executive Officer and the Chief Financial Officer, has evaluated the effectiveness of the Corporation's disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934, as amended (the Exchange Act)) as of the end of the period covered by this report. Based on that evaluation, the Chief Executive Officer and the Chief Financial Officer have concluded that the Corporation's disclosure controls and procedures were effective as of December 31, 2014 to ensure that information required to be disclosed by the Corporation in reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms and that such information is accumulated and communicated to the Corporation's management, including the Corporation's Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that the Corporation's disclosure controls and procedures will detect or uncover every situation involving the failure of persons within the Corporation or its subsidiaries to disclose material information required to be set forth in the Corporation's periodic reports.

Management's Report on Internal Control over Financial Reporting. Management of the Corporation is also responsible for establishing and maintaining adequate internal control over financial reporting (as defined in Rule 13a-15(f) under the Exchange Act). Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Therefore, even those systems determined to be effective can provide only reasonable assurance with respect to financial statement preparation and presentation.

Management assessed the effectiveness of the Corporation's internal control over financial reporting as of December 31, 2014. In making this assessment, management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in Internal Control – Integrated Framework (2013). Based on our assessment, we believe that, as of December 31, 2014, the Corporation's internal control over financial reporting was effective based on those criteria.

The effectiveness of the Corporation's internal control over financial reporting as of December 31, 2014 has been audited by Yount, Hyde & Barbour, P.C., the independent registered public accounting firm who also audited the

Corporation's consolidated financial statements included in this Annual Report on Form 10-K. Yount, Hyde & Barbour, P.C.'s attestation report on the Corporation's internal control over financial reporting appears on the following page.

Changes in Internal Controls. There were no changes in the Corporation's internal control over financial reporting during the Corporation's quarter ended December 31, 2014 that have materially affected, or are reasonably likely to materially affect, the Corporation's internal control over financial reporting.

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Shareholders

C&F Financial Corporation

West Point, Virginia

We have audited C&F Financial Corporation and Subsidiary's (the Corporation) internal control over financial reporting as of December 31, 2014, based on criteria established in Internal Control — Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission in 2013. The Corporation's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting included in Management's Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the Corporation's internal control over financial reporting based on our audit.

We conducted our audit 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 effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audit also included performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (a) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (b) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (c) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the Corporation maintained, in all material respects, effective internal control over financial reporting as of December 31, 2014, based on criteria established in Internal Control — Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission in 2013.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets as of December 31, 2014 and 2013, and the related consolidated statements of income, comprehensive income, changes in shareholders' equity, and cash flows for each of the three years in the period ended December 31, 2014 of C&F Financial Corporation and Subsidiary, and our report dated March 11, 2015 expressed an unqualified opinion.

/s/ Yount, Hyde & Barbour, P.C.

Winchester, Virginia

March 11, 2015

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ITEM 9B.OTHER INFORMATION

On December 16, 2014, the Corporation's Compensation Committee approved an additional compensation benefit for Chairman and Chief Executive Officer Larry G. Dillon to provide post-retirement medical and dental insurance premiums for Mr. Dillon and his spouse for life. The new benefit is effective as of January 1, 2015, although Mr. Dillon is not eligible to begin receiving this benefit until he retires at or after age 65.

PART III

ITEM 10.DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

The information with respect to the directors of the Corporation is contained in the 2015 Proxy Statement under the caption, "Election of Directors," and is incorporated herein by reference. The information regarding the Section 16(a) reporting requirements of the directors and executive officers is contained in the 2015 Proxy Statement under the caption, "Section 16(a) Beneficial Ownership Reporting Compliance," and is incorporated herein by reference. The information concerning executive officers of the Corporation is included after Item 4 of this Form 10-K under the caption, "Executive Officers of the Registrant." The information regarding the Corporation's Audit Committee is contained in the 2015 Proxy Statement under the caption "Report of the Audit Committee" and is incorporated herein by reference.

The Corporation has adopted a Code of Business Conduct and Ethics (Code) that applies to its directors, executives and employees including the principal executive officer, principal financial officer, principal accounting officer and controller, or persons performing similar functions. This Code is posted on our Internet website at <http://www.cffc.com> under "Investor Relations." We will provide a copy of the Code to any person without charge upon written request to C&F Financial Corporation, c/o Secretary, P.O. Box 391, West Point, Virginia 23181. We intend to provide any required disclosure of any amendment to or waiver of the Code that applies to our principal executive officer, principal financial officer, principal accounting officer or controller, or persons performing similar functions, on <http://www.cffc.com> under "Investor Relations" promptly following the amendment or waiver. We may elect to disclose any such amendment or waiver in a report on Form 8-K filed with the SEC either in addition to or in lieu of the website disclosure. The information contained on or connected to our Internet website is not incorporated by reference in this report and should not be considered part of this or any other report that we file or furnish to the SEC.

The Corporation provides an informal process for security holders to send communications to its board of directors. Security holders who wish to contact the board of directors or any of its members may do so by addressing their written correspondence to C&F Financial Corporation, Board of Directors, c/o Corporate Secretary, P.O. Box 391, West Point, Virginia 23181. Correspondence directed to an individual board member will be referred, unopened, to that member. Correspondence not directed to a particular board member will be referred, unopened, to the Chairman of the Board.

#### ITEM 11.EXECUTIVE COMPENSATION

The information contained in the 2015 Proxy Statement under the captions, “Compensation Committee Interlocks and Insider Participation,” “Compensation Policies and Practices as They Relate to Risk Management,” “Executive Compensation” and “Compensation Committee Report,” and the compensation tables that follow the Compensation Committee Report in the 2015 Proxy Statement are incorporated herein by reference. The information regarding director compensation contained in the 2015 Proxy Statement under the caption, “Director Compensation,” is incorporated herein by reference.

#### ITEM 12.SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

The information contained in the 2015 Proxy Statement under the caption, “Security Ownership of Certain Beneficial Owners and Management,” is incorporated herein by reference.

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The information contained in the 2015 Proxy Statement under the caption, “Equity Compensation Plan Information,” is incorporated herein by reference.

ITEM 13.CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE

The information contained in the 2015 Proxy Statement under the caption, “Interest of Management in Certain Transactions,” is incorporated herein by reference. The information contained in the 2015 Proxy Statement under the caption, “Director Independence,” is incorporated herein by reference.

ITEM 14.PRINCIPAL ACCOUNTANT FEES AND SERVICES

The information contained in the 2015 Proxy Statement under the captions, “Principal Accountant Fees” and “Audit Committee Pre-Approval Policy,” is incorporated herein by reference.



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PART IV

ITEM 15.EXHIBITS, FINANCIAL STATEMENT SCHEDULES

(a) Exhibits:

- 2.1 Agreement and Plan of Merger dated as of June 10, 2013 by and among C&F Financial Corporation, Special Purpose Sub, Inc. and Central Virginia Bankshares, Inc. (incorporated by reference to Exhibit 2.1 to Form 8-K filed June 14, 2013)
- 3.1 Articles of Incorporation of C&F Financial Corporation (incorporated by reference to Exhibit 3.1 to Form 10-KSB filed March 29, 1996)
- 3.1.1 Amendment to Articles of Incorporation of C&F Financial Corporation (incorporated by reference to Exhibit 3.1.1 to Form 8-K filed January 14, 2009)
- 3.2 Amended and Restated Bylaws of C&F Financial Corporation, as adopted December 16, 2014 (incorporated by reference to Exhibit 3.1 to Form 8-K filed December 22, 2014)

Certain instruments relating to trust preferred securities not being registered have been omitted in accordance with Item 601(b)(4)(iii) of Regulation S-K. The registrant will furnish a copy of any such instrument to the Securities and Exchange Commission upon its request.

- \*10.1 Amended and Restated Change in Control Agreement dated December 30, 2008 between C&F Financial Corporation and Larry G. Dillon (incorporated by reference to Exhibit 10.1 to Form 10-K filed March 9, 2009)
- \*10.3 Amended and Restated Change in Control Agreement dated December 30, 2008 between C&F Financial Corporation and Thomas F. Cherry (incorporated by reference to Exhibit 10.3 to Form 10-K filed March 9, 2009)
- \*10.3.1 Amendment to Amended and Restated Change in Control Agreement dated March 1, 2012 between C&F Financial Corporation and Thomas F. Cherry (incorporated by reference to Exhibit 10.3.1 to Form 10-K filed March 5, 2012)

- \*10.4 Restated VBA Executives' Non-Qualified Deferred Compensation Plan for C&F Financial Corporation (incorporated by reference to Exhibit 10.4 to Form 10-K filed March 7, 2008)
- \*10.4.1 Adoption Agreement for the Restated VBA Executives' Non-Qualified Deferred Compensation Plan for C&F Financial Corporation dated as of December 31, 2008 (incorporated by reference to Exhibit 10.4.1 to Form 10-K filed March 9, 2009)
- \*10.4.2 Attachment to the Adoption Agreement for the Restated VBA Executives' Non-Qualified Deferred Compensation Plan for C&F Financial Corporation dated as of January 1, 2008 (incorporated by reference to Exhibit 10.4.2 to Form 10-K filed March 7, 2008)
- \*10.4.3 Amendment to Adoption Agreement for the Restated VBA Executives' Non-Qualified Deferred Compensation Plan for C&F Financial Corporation effectively dated as of December 31, 2008 (incorporated by reference to Exhibit 10.4.3 to Form 10-K filed March 9, 2009)
- \*10.4.4 Amendment to Adoption Agreement for the Restated VBA Executives' Non-Qualified Deferred Compensation Plan for C&F Financial Corporation effectively dated as of January 1, 2009 (incorporated by reference to Exhibit 10.4.4 to Form 10-K filed March 3, 2010)

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- \*10.5 Restated VBA Directors' Deferred Compensation Plan for C&F Financial Corporation (incorporated by reference to Exhibit 10.5 to Form 10-K filed March 7, 2008)
- \*10.5.1 Adoption Agreement for the Restated VBA Director's Deferred Compensation Plan for C&F Financial Corporation dated as of December 31, 2008 (incorporated by reference to Exhibit 10.5.1 to Form 10-K filed March 9, 2009)
- \*10.5.2 Amendment to Adoption Agreement for the Restated VBA Directors' Deferred Compensation Plan for C&F Financial Corporation effectively dated as of December 31, 2008 (incorporated by reference to Exhibit 10.5.2 to Form 10-K filed March 9, 2009)
- \*10.7 Amended and Restated C&F Financial Corporation 1998 Non-Employee Director Stock Compensation Plan (incorporated by reference to Exhibit 10.7 to Form 10-K filed March 7, 2008)
- \*10.9 C&F Financial Corporation Management Incentive Plan dated February 25, 2005, as amended January 18, 2011 (incorporated by reference to Exhibit 10.9 to Form 10-K filed March 3, 2011)
- \*10.10 Amended and Restated C&F Financial Corporation 2004 Incentive Stock Plan (incorporated by reference to Exhibit 10.10 to Form 10-K filed March 7, 2008)
- \*10.10.1 Form of C&F Financial Corporation Restricted Stock Agreement (incorporated by reference to Exhibit 10.10.1 to Form 10-Q filed August 8, 2008)
- \*10.10.2 Form of C&F Financial Corporation Restricted Stock Agreement (incorporated by reference to Exhibit 10.10.2 to Form 8-K filed December 8, 2009)
- \*10.10.3 Form of C&F Financial Corporation TARP-Compliant Restricted Stock Agreement (incorporated by reference to Exhibit 10.10.3 to Form 8-K filed December 8, 2009)
- \*10.10.4 Form of C&F Financial Corporation Restricted Stock Agreement (approved May 2012) (incorporated by reference to Exhibit 10.10.4 to Form 10-K filed March 5, 2013)
- \*10.11 Form of C&F Financial Corporation Incentive Stock Option Agreement (incorporated by reference to Exhibit 10.2 to Form 8-K filed December 29, 2004)
- \*10.11.1 Form of Notice of Amendment to C&F Financial Corporation Incentive Stock Option Agreement (incorporated by reference to Exhibit 10.11.1 to Form 10-Q filed on November 8, 2011)
- \*10.12 Employment Agreement (Amended and Restated) between C&F Mortgage Corporation and Bryan McKernon, dated January 1, 2013 (incorporated by reference to Exhibit 10.12 to Form 10-K filed March 5, 2013)
- \*10.14 Amended and Restated Change in Control Agreement dated December 30, 2008 between C&F Financial Corporation and Bryan McKernon (incorporated by reference to Exhibit 10.14 to Form 10-K filed March 9, 2009)

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- \*10.14.1 Amendment to Amended and Restated Change in Control Agreement dated March 1, 2012 between C&F Financial Corporation and Bryan McKernon (incorporated by reference to Exhibit 10.14.1 to Form 10-K filed March 5, 2012)
- \*10.15 Schedule of C&F Financial Corporation Non-Employee Directors' Annual Compensation
- \*10.16 Base Salaries for Executive Officers of C&F Financial Corporation

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- \*10.17 Form of C&F Financial Corporation Restricted Stock Agreement (incorporated by reference to Exhibit 10.16 to Form 8-K filed December 18, 2006)
- 10.19 Amended and Restated Loan and Security Agreement by and between Wells Fargo Preferred Capital, Inc., various financial institutions and C&F Finance Company dated as of August 25, 2008 (incorporated by reference to Exhibit 10.19 to Form 8-K filed August 28, 2008)
- 10.19.1 First Amendment to Amended and Restated Loan and Security Agreement by and among Wells Fargo Preferred Capital, Inc., various financial institutions and C&F Finance Company dated as of July 1, 2010 (incorporated by reference to Exhibit 10.19.1 to Form 10-Q filed August 6, 2010)
- 10.19.2 Second Amendment to Amended and Restated Loan and Security Agreement by and among Wells Fargo Bank, N.A., various financial institutions and C&F Finance Company dated as of September 17, 2012 (incorporated by reference to Exhibit 10.19.2 to Form 10-Q filed November 8, 2012)
- 10.19.3 Third Amendment to Amended and Restated Loan and Security Agreement by and among Wells Fargo Bank, N.A., various financial institutions and C&F Finance Company dated as of November 12, 2013 (incorporated by reference to Exhibit 10.19.3 to Form 10-K filed March 7, 2014)
- \*10.29 C&F Financial Corporation 2013 Stock and Incentive Compensation Plan (incorporated by reference to Appendix A to the Corporation's Proxy Statement filed March 15, 2013)
- \*10.30 Form of C&F Financial Corporation Restricted Stock Agreement under 2013 Stock and Incentive Compensation Plan (approved May 21, 2013) (incorporated by reference to Exhibit 10.30 to Form 8-K filed May 24, 2013)
- 10.31 Securities Purchase Agreement dated as of July 17, 2013 by and among the United States Department of the Treasury, Central Virginia Bankshares, Inc. and C&F Financial Corporation (incorporated by reference to Exhibit 10.31 to Form 8-K filed July 22, 2013)
- 10.32 Amendment No. 1 to Securities Purchase Agreement dated as of September 13, 2013 by and among the United States Department of the Treasury, Central Virginia Bankshares, Inc. and C&F Financial Corporation (incorporated by reference to Exhibit 10.32 to Form 8K filed October 2, 2013)
- \*10.33 Change in Control Agreement dated October 9, 2012 between C&F Financial Corporation and John Anthony Seaman (incorporated by reference to Exhibit 10.33 to Form 10-K filed March 7, 2014)
- 21 Subsidiaries of the Registrant
- 23 Consent of Yount, Hyde & Barbour, P.C.
- 31.1 Certification of CEO pursuant to Rule 13a-14(a)
- 31.2 Certification of CFO pursuant to Rule 13a-14(a)
- 32 Certification of CEO/CFO pursuant to 18 U.S.C. Section 1350

101.INS XBRL Instance Document

101.SCH XBRL Taxonomy Extension Schema Document

101.CAL XBRL Taxonomy Extension Calculation Linkbase Document

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101.DEF XBRL Taxonomy Extension Definition Linkbase Document

101.LAB XBRL Taxonomy Extension Label Linkbase Document

101.PRE XBRL Taxonomy Presentation Linkbase Document

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\*Indicates management contract

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SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

C&F FINANCIAL CORPORATION  
(Registrant)

Date: March 11, 2015 By: /S/ LARRY G. DILLON  
Larry G. Dillon  
Chairman and Chief Executive Officer  
(Principal Executive Officer)

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

/S/ LARRY G. DILLON  
Larry G. Dillon, Chairman and  
Chief Executive Officer  
(Principal Executive Officer) Date: March 11, 2015

/S/ THOMAS F. CHERRY  
Thomas F. Cherry, President,  
Chief Financial Officer, Secretary and Director  
(Principal Financial and Accounting Officer) Date: March 11, 2015

/S/ J. P. CAUSEY JR.  
J. P. Causey Jr., Director Date: March 11, 2015

/S/ BARRY R. CHERNACK  
Barry R. Chernack, Director Date: March 11, 2015

/S/ AUDREY D. HOLMES  
Audrey D. Holmes, Director Date: March 11, 2015

/S/ JAMES H. HUDSON III  
James H. Hudson III, Director Date: March 11, 2015



/S/ JOSHUA H. LAWSON  
Joshua H. Lawson, Director

Date: March 11, 2015

/S/ C. ELIS OLSSON  
C. Elis Olsson, Director

Date: March 11, 2015

/S/ PAUL C. ROBINSON  
Paul C. Robinson, Director

Date: March 11, 2015