F&M BANK CORP
Form 10-K
March 28, 2017

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D. C. 20549
FORM 10-K

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

For fiscal year ended December 31, 2016
Commission file number: 0-13273

F & M BANK CORP.
(Exact name of registrant as specified in its charter)

| | |
|---|---|
| Virginia | 54-1280811 |
| (State or other jurisdiction of incorporation or organization) | (I.R.S. Employer Identification No.) |

P. O. Box 1111, Timberville, Virginia 22853
(Address of principal executive offices) (Zip Code)

(540) 896-8941
(Registrant's telephone number including area code)

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

Securities registered pursuant to Section 12(g) of the Act:
Common Stock - $5 Par value per share

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

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

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

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definition of “large accelerated filer”, “accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act. (Check one)

| | |
|---|---|
| Large accelerated filer [ ] | Accelerated filer [ ] |
| Non-accelerated filer [ ] (Do not check if a smaller reporting company) | Smaller reporting Company [x] |

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

The registrant’s Common Stock is traded Over-the-Counter under the symbol FMBM. The aggregate market value of the 2,932,649 shares of Common Stock of the registrant issued and outstanding held by non-affiliates on June 30, 2016 was approximately $67,509,580 based on the closing sales price of $23.02 per share on that date. For purposes of this calculation, the term “affiliate” refers to all directors and executive officers of the registrant.

As of the close of business on March 21, 2017, there were 3,271,926 shares of the registrant's Common Stock outstanding.

DOCUMENTS INCORPORATED BY REFERENCE:

Part III: Proxy Statement for the Annual Meeting of Shareholders to be held on May 13, 2017 (the “Proxy Statement”).

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PART I

Item 1. Business

General

F & M Bank Corp. (the "Company" or "we"), incorporated in Virginia in 1983, is a one bank financial holding company pursuant to section 3(a)(1) of the Bank Holding Company Act of 1956, and owns 100% of the outstanding stock of its affiliate, Farmers & Merchants Bank (Bank). TEB Life Insurance Company (TEB) and Farmers & Merchants Financial Services, Inc. (FMFS) are wholly owned subsidiaries of Farmers & Merchants Bank. Farmers & Merchants Bank also holds a majority ownership in VBS Mortgage LLC, (VBS).

Farmers & Merchants Bank was chartered on April 15, 1908, as a state chartered bank under the laws of the Commonwealth of Virginia. TEB was incorporated on January 27, 1988, as a captive life insurance company under the laws of the State of Arizona. FMFS is a Virginia chartered corporation and was incorporated on February 25, 1993. VBS (formerly Valley Broker Services, Inc.) was incorporated on May 11, 1999. The Bank purchased a majority interest in VBS on November 3, 2008.

As a commercial bank, the Bank offers a wide range of banking services including commercial and individual demand and time deposit accounts, commercial and individual loans, internet and mobile banking, drive-in banking services, ATMs at all branch locations and several off-site locations, as well as a courier service for its commercial banking customers. TEB was organized to re-insure credit life and accident and health insurance currently being sold by the Bank in connection with its lending activities. FMFS was organized to write title insurance but now provides brokerage services, commercial and personal lines of insurance to customers of the Bank. VBS originates conventional and government sponsored mortgages through their offices in Harrisonburg, Woodstock and Fishersville.

The Bank makes various types of commercial and consumer loans and has a large portfolio of residential mortgages and a concentration in development lending. The local economy is relatively diverse with strong employment in the agricultural, manufacturing, service and governmental sectors.

The Company's and the Bank's principal executive office is at 205 South Main Street, Timberville, VA 22853, and its phone number is (540) 896-8941.

Filings with the SEC

The Company files annual, quarterly and other reports under the Securities Exchange Act of 1934 with the Securities and Exchange Commission ("SEC"). These reports are posted and are available at no cost on the Company's website, www.FMBankVA.com, as soon as reasonably practicable after the Company files such documents with the SEC. The Company's filings are also available through the SEC's website at www.sec.gov.

Employees

On December 31, 2016, the Bank had 173 full-time and part-time employees; including executive officers, loan and other banking officers, branch personnel, operations personnel and other support personnel. None of the Company's employees is represented by a union or covered under a collective bargaining agreement. Management of the Company considers their employee relations to be excellent. No one employee devotes full-time services to F & M Bank Corp.

Competition

The Bank's offices face strong competition from numerous other financial institutions. These other institutions include large national and regional banks, other community banks, nationally chartered savings banks, credit unions, consumer finance companies, mortgage companies, loan production offices, mutual funds and life insurance companies. Competition for loans and deposits is affected by a variety of factors including interest rates, types of products offered, the number and location of branch offices, marketing strategies and the reputation of the Bank within the communities served.

PART I, continued

Item 1. Business, continued

Regulation and Supervision

General. The operations of F & M Bank Corp. and the Bank are subject to federal and state statutes, which apply to financial holding companies and state member banks of the Federal Reserve System. The common stock of F & M Bank Corp. is registered pursuant to and subject to the periodic reporting requirements of the Securities Exchange Act of 1934 (the “Exchange Act”). These include, but are not limited to, the filing of annual, quarterly, and other current reports with the Securities and Exchange Commission (the “SEC”). As an Exchange Act reporting company, the Company is directly affected by the Sarbanes-Oxley Act of 2002 (“Sarbanes-Oxley”), which is aimed at improving corporate governance and reporting procedures. The Company believes it is in compliance with SEC and other rules and regulations implemented pursuant to Sarbanes-Oxley and intends to comply with any applicable rules and regulations implemented in the future.

F & M Bank Corp., as a financial holding company, is subject to the provisions of the Bank Holding Company Act of 1956, as amended (the "Act") and is supervised by the Board of Governors of the Federal Reserve System (the “Federal Reserve Board”). The Act requires F & M Bank Corp. to secure the prior approval of the Federal Reserve Board before F & M Bank Corp. acquires ownership or control of more than 5% of the voting shares or substantially all of the assets of any institution, including another bank.

As a financial holding company, F & M Bank Corp. is required to file with the Federal Reserve Board an annual report and such additional information as it may require pursuant to the Act. The Federal Reserve Board may also conduct examinations of F & M Bank Corp. and any or all of its subsidiaries. Under Section 106 of the 1970 Amendments to the Act and the regulations of the Federal Reserve Board, a bank holding company and its subsidiaries are prohibited from engaging in certain tie-in arrangements in connection with an extension of credit, provision of credit, sale or lease of property or furnishing of services.

Federal Reserve Board regulations limit activities of financial holding companies to managing or controlling banks or non-banking activities closely related to banking. These activities include the making or servicing of loans, performing certain data processing services, and certain leasing and insurance agency activities. Since 1994, the Company has entered into agreements with the Virginia Community Development Corporation to purchase equity positions in several Low-Income Housing Funds; these funds provide housing for low-income individuals throughout Virginia. Approval of the Federal Reserve Board is necessary to engage in any of the activities described above or to acquire interests engaging in these activities.

The Bank as a state member bank is supervised and regularly examined by the Virginia Bureau of Financial Institutions and the Federal Reserve Board. Such supervision and examination by the Virginia Bureau of Financial Institutions and the Federal Reserve Board is intended primarily for the protection of depositors and not the stockholders of F & M Bank Corp.

Payment of Dividends. The Company is a legal entity, separate and distinct from its subsidiaries. A significant portion of the revenues of the Company result from dividends paid to it by the Bank. There are various legal limitations applicable to the payment of dividends by the Bank to the Company. Under the current regulatory guidelines, prior approval from the Federal Reserve Board is required if cash dividends declared in any given year exceed net income for that year, plus retained net profits of the two preceding years. A bank also may not declare a dividend out of or in excess of its net undivided profits without regulatory approval. The payment of dividends by the Bank or the Company may also be limited by other factors, such as requirements to maintain capital above regulatory guidelines.

Bank regulatory agencies have the authority to prohibit the Bank or the Company from engaging in an unsafe or unsound practice in conducting their businesses. The payment of dividends, depending on the financial condition of the Bank, or the Company, could be deemed to constitute such an unsafe or unsound practice. Based on the Bank's current financial condition, the Company does not expect that any of these laws will have any impact on its ability to obtain dividends from the Bank.

PART I, continued

Item 1. Business, continued

Regulation and Supervision, continued

The Company also is subject to regulatory restrictions on dividends to its shareholders. Regulators have indicated that bank holding companies should generally pay dividends only if the organization's net income available to common shareholders over the past year has been sufficient to fully fund the dividends and the prospective rate of earnings retention appears consistent with the organization's capital needs, asset quality, and overall financial condition. Further, a bank holding company should inform and consult with the Federal Reserve Board prior to declaring a dividend that exceeds earnings for the period (e.g., quarter) for which the dividend is being paid or that could result in a material adverse change to the organization's capital structure.

Capital Requirements. In 2013, the Federal Reserve, the FDIC and the OCC approved a new rule that substantially amends the regulatory risk-based capital rules applicable to us. The final rule implements the "Basel III" regulatory capital reforms and changes required by the Dodd-Frank Act (see definition below). The final rule includes new minimum risk-based capital and leverage ratios which was effective for us on January 1, 2015, and refines the definition of what constitutes "capital" for purposes of calculating these ratios. The new minimum capital requirements are: (i) a new common equity Tier 1 ("CET1") capital ratio of 4.5%; (ii) a Tier 1 to risk-based assets capital ratio of 6%, which is increased from 4%; (iii) a total capital ratio of 8%, which is unchanged from the previous rules; and (iv) a Tier 1 leverage ratio of 4%. The final rule also establishes a "capital conservation buffer" of 2.5% above the new regulatory minimum capital ratios, and when fully effective in 2019, will result in the following minimum ratios: (a) a common equity Tier 1 capital ratio of 7.0%; (b) a Tier 1 to risk-based assets capital ratio of 8.5%; and (c) a total capital ratio of 10.5%. The capital conservation buffer is being phased in from 0.00% for 2015 to 2.50% by 2019. An institution will be subject to limitations on paying dividends, engaging in share repurchases, and paying discretionary bonuses if its capital level falls below the buffer amount. These limitations will establish a maximum percentage of eligible retained income that can be utilized for such activities.

The CETI and Tier 1 leverage ratio of the Bank as of December 31, 2016, were 13.86% and 11.83%, respectively, which are significantly above the minimum requirements. The guidelines also provide that banking organizations experiencing internal growth or making acquisitions will be expected to maintain strong capital positions substantially above the minimum supervisory levels, without significant reliance on intangible assets.

The Gramm-Leach-Bliley Act. Effective on March 11, 2001, the Gramm-Leach-Bliley Act (the "GLB Act") allows a bank holding company or other company to certify status as a financial holding company, which will allow such company to engage in activities that are financial in nature, that are incidental to such activities, or are complementary to such activities. The GLB Act enumerates certain activities that are deemed financial in nature, such as underwriting insurance or acting as an insurance principal, agent or broker; dealing in or making markets in securities; and engaging in merchant banking under certain restrictions. It also authorizes the Federal Reserve to determine by regulation what other activities are financial in nature, or incidental or complementary thereto.

USA Patriot Act of 2001. In October 2001, the USA Patriot Act of 2001 was enacted in response to the terrorist attacks in New York, Pennsylvania and Northern Virginia which occurred on September 11, 2001. The Patriot Act is intended to strengthen U.S. law enforcements' and the intelligence communities' abilities to work cohesively to combat terrorism on a variety of fronts. The continuing and potential impact of the Patriot Act and related regulations and policies on financial institutions of all kinds is significant and wide ranging. The Patriot Act contains sweeping anti-money laundering and financial transparency laws, and imposes various regulations, including standards for verifying client identification at account opening, and rules to promote cooperation among financial institutions,

regulators and law enforcement entities in identifying parties that may be involved in terrorism or money laundering.

Community Reinvestment Act. The requirements of the Community Reinvestment Act are also applicable to the Bank. The act 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 needs currently are evaluated as part of the examination process pursuant to twelve assessment factors. These factors are also considered in evaluating mergers, acquisitions and applications to open a branch or facility.

PART I, continued

Item 1. Business, continued

Regulation and Supervision, continued

Dodd-Frank Wall Street Reform and Consumer Protection Act. The Dodd-Frank Act was signed into law on July 21, 2010. Its wide-ranging provisions affect all federal financial regulatory agencies and nearly every aspect of the American financial services industry. Among the provisions of the Dodd-Frank Act that directly impact the Company is the creation of an independent Consumer Financial Protection Bureau (CFPB), which has the ability to implement, examine and enforce complains with federal consumer protection laws, which govern all financial institutions. For smaller financial institutions, such as the Company and the Bank, their primary regulators will continue to conduct its examination activities.

The Dodd-Frank Act contains provisions designed to reform mortgage lending, which includes the requirement of additional disclosures for consumer mortgages. In addition, the Federal Reserve has issued new rules that have the effect of limiting the fees charged to merchants for debit card transactions. The result of these rules will be to limit the amount of interchange fee income available explicitly to larger banks and indirectly to us. The Dodd-Frank Act also contains provisions that affect corporate governance and executive compensation.

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

Mortgage Lending. In 2013, the CFPB adopted a rule, effective in January 2014, to implement certain sections of the Dodd-Frank Act requiring creditors to make a reasonable, good faith determination of a consumer's ability to repay any closed-end consumer credit transaction secured by a 1-4 family dwelling. The rule also establishes certain protections from liability under this requirement to ensure a borrower's ability to repay for loans that meet the definition of "qualified mortgage." Loans that satisfy this "qualified mortgage" safe harbor will be presumed to have complied with the new ability-to-repay standard.

Forward-Looking Statements

Certain information contained in this report may include "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Exchange Act. These forward-looking statements are generally identified by phrases such as "we expect," "we believe" or words of similar import. Such forward-looking statements involve known and unknown risks including, but not limited to:

Changes in the quality or composition of our loan or investment portfolios, including adverse developments in borrower industries, declines in real estate values in our markets, or in the repayment ability of individual borrowers or issuers;

The strength of the economy in our target market area, as well as general economic, market, or business conditions;

An insufficient allowance for loan losses as a result of inaccurate assumptions;

Our ability to maintain our "well-capitalized" regulatory status;

Changes in the interest rates affecting our deposits and our loans;

Changes in our competitive position, competitive actions by other financial institutions and the competitive nature of the financial services industry and our ability to compete effectively against other financial institutions in our banking markets;

Our ability to manage growth;

Our potential growth, including our entrance or expansion into new markets, the opportunities that may be presented to and pursued by us and the need for sufficient capital to support that growth;

Our exposure to operational risk;

Our ability to raise capital as needed by our business;

Changes in laws, regulations and the policies of federal or state regulators and agencies; and

Other circumstances, many of which are beyond our control.

PART I, continued

Item 1. Business, continued

Forward looking statements, continued

Although we believe that our expectations with respect to the forward-looking statements are based upon reliable assumptions within the bounds of our knowledge of our business and operations, there can be no assurance that our actual results, performance or achievements will not differ materially from any future results, performance or achievements expressed or implied by such forward-looking statements.

Item 1A. Risk Factors

General economic conditions in our market area could adversely affect us.

We are affected by the general economic conditions in the local markets in which we operate. Since the recession began in 2008, our market has experienced a significant downturn in which we have seen falling home prices, rising foreclosures and an increased level of commercial and consumer delinquencies. Although economic conditions have improved, many businesses and individuals are still experiencing difficulty as a result of the economic downturn and protracted recovery. If economic conditions in our market deteriorate from current conditions, we could experience further adverse consequences, including a decline in demand for our products and services and an increase in problem assets, forecloses and loan losses. Future economic conditions in our market will depend on factors outside of our control such as political and market conditions, broad trends in industry and finance, legislative and regulatory changes, changes in government, military and fiscal policies and inflation, any of which could negatively affect our performance and financial condition.

Our allowance for loan losses may prove to be insufficient to absorb losses in the loan portfolio.

Like all financial institutions, we maintain an allowance for loan losses to provide for loans that our borrowers may not repay in their entirety. We believe that we maintain an allowance for loan losses at a level adequate to absorb probable losses inherent in the loan portfolio. Through a periodic review and consideration of the loan portfolio, management determines the amount of the allowance for loan losses by considering general market conditions, credit quality of the loan portfolio, the collateral supporting the loans and performance of customers relative to their financial obligations with us. At December 31, 2016, our non-performing loans were $4.9 million, compared to $6.5 million at December 31, 2015. The Company did not record a provision for loan losses for the year ended December 31, 2016, and our loan loss allowance was $7.5 million, or 1.27% of total loans held for investment at December 31, 2016.

The amount of future losses is susceptible to changes in economic, operating and other conditions, including changes in interest rates, which may be beyond our control, and these losses may exceed current estimates. Although we believe the allowance for loan losses is a reasonable estimate of known and inherent losses in the loan portfolio, it cannot fully predict such losses or that the loss allowance will be adequate in the future. While the risk of nonpayment is inherent in banking, we could experience greater nonpayment levels than we anticipate. In addition, we have loan participation arrangements with several other banks within the region and may not be able to exercise control of negotiations with borrowers in the event these loans do not perform. Additional problems with asset quality could cause our interest income and net interest margin to decrease and our provisions for loan losses to increase, which could adversely affect our results of operations and financial condition.

Federal and state regulators periodically review our allowance for loan losses and may require us to increase our provision for loan losses or recognize further loan charge-offs, based on judgments different than those of

management. Any increase in the amount of the provision or loans charged-off as required by these regulatory agencies could have a negative effect on our operating results.

PART I, continued

Item 1A. Risk Factors, continued

Our loan concentrations could, as a result of adverse market conditions, increase credit losses which could adversely impact earnings.

We offer a variety of secured loans, including commercial lines of credit, commercial term loans, real estate, construction, home equity, consumer and other loans. Many of our loans are secured by real estate (both residential and commercial) in our market area, which could result in adverse consequences to us in the event of a prolonged economic downturn in our market. As of December 31, 2016, approximately 90% of our loans had real estate as a primary or secondary component of collateral. A significant decline in real estate values in our market would mean that the collateral for many of our loans would provide less security. As a result, we would be more likely to suffer losses on defaulted loans because our ability to fully recover on defaulted loans by selling the real estate collateral would be diminished. In addition, our consumer loans (such as automobile loans) are collateralized, if at all, with assets that may not provide an adequate source of repayment of the loan due to depreciation, damage or loss.

In addition, we have a large portfolio of residential mortgages and a concentration in development lending, both of which could be adversely affected by a decline in the real estate markets. Construction and development lending entails significant additional risks, because these loans, which often involve larger loan balances concentrated with single borrowers or groups of related borrowers, are dependent on the successful completion of real estate projects. Loan funds for construction and development loans often are advanced upon the security of the land or home under construction, which value is estimated prior to the completion of construction. The deterioration of one or a few of these loans could cause a significant increase in the percentage of non-performing loans. An increase in non-performing loans could result in a loss of earnings from these loans, an increase in the provision for loan losses and an increase in charge-offs, all of which could have a material adverse effect on our financial condition.

Our small-to-medium sized business target market may have fewer financial resources to weather continued downturn in the economy.

We target our commercial development and marketing strategy primarily to serve the banking and financial services needs of small and medium sized businesses. These businesses generally have less capital or borrowing capacity than larger entities. If general economic conditions negatively impact this major economic sector in the markets in which we operate, our results of operations and financial condition may be adversely affected.

Our inability to maintain adequate sources of funding and liquidity may negatively impact our current financial condition or our ability to grow.

Our access to funding and liquidity sources in amounts adequate to finance our activities on terms which are acceptable to us could be impaired by factors that affect us specifically or the financial services industry or economy in general. In managing our balance sheet, a primary source of funding asset growth and liquidity historically has been deposits, including both local customer deposits and brokered deposits. If the level of deposits were to materially decrease, we would have to raise additional funds by increasing the interest that we pay on certificates of deposit or other depository accounts, seek other debt or equity financing, or draw upon our available lines of credit. Our access to these funding and liquidity sources could be detrimentally impacted by a number of factors, including operating losses, rising levels of non-performing assets, a decrease in the level of our business activity as a result of a downturn in the markets in which our loans or deposits are concentrated or regulatory restrictions. In addition, our ability to continue to attract deposits and other funding or liquidity sources is subject to variability based upon additional factors including volume and volatility in the securities markets and the relative interest rates that we are prepared to pay for these liabilities. We do not maintain significant additional sources of liquidity through

potential sales in our investment portfolio or liquid assets at the holding company level. Our potential inability to maintain adequate sources of funding or liquidity may, among other things, inhibit our ability to fund asset growth or negatively impact our financial condition, including our ability to pay dividends or satisfy our obligations.

PART I, continued

Item 1A. Risk Factors, continued

If we do not maintain our capital requirements and our status as a “well-capitalized” bank, there could an adverse effect on our liquidity and our ability to fund our loan portfolio.

We are subject to regulatory capital adequacy guidelines. If we fail to meet the capital adequacy guidelines for a “well-capitalized” bank, it could increase the regulatory scrutiny for the Bank and the Company. In addition, if we failed to be “well capitalized” for regulatory capital purposes, we would not be able to renew or accept brokered deposits without prior regulatory approval and we would not be able to offer interest rates on our deposit accounts that are significantly higher than the average rates in our market area. As a result, it would be more difficult for us to attract new deposits as our existing brokered deposits mature and do not roll over and to retain or increase existing, non-brokered deposits. If we are prohibited from renewing or accepting brokered deposits and are unable to attract new deposits, our liquidity and our ability to fund our loan portfolio may be adversely affected. In addition, we would be required to pay higher insurance premiums to the FDIC, which would reduce our earnings.

We are subject to more stringent capital requirements as a result of the Basel III regulatory capital reforms and the Dodd-Frank Act which could adversely affect our results of operations and future growth.

In 2013, the Federal Reserve, the FDIC and the OCC approved a new rule that substantially amends the regulatory risk-based capital rules applicable to us. The final rule implements the “Basel III” regulatory capital reforms and changes required by the Dodd-Frank Act. The final rule includes new minimum risk-based capital and leverage ratios which was effective for us on January 1, 2015, and refines the definition of what constitutes “capital” for purposes of calculating these ratios. The new minimum capital requirements are: (i) a new common equity Tier 1 (“CET1”) capital ratio of 4.5%; (ii) a Tier 1 to risk-based assets capital ratio of 6%, which is increased from 4%; (iii) a total capital ratio of 8%, which is unchanged from the previous rules; and (iv) a Tier 1 leverage ratio of 4%. The final rule also establishes a “capital conservation buffer” of 2.5% above the new regulatory minimum capital ratios, and when fully effective in 2019, will result in the following minimum ratios: (a) a common equity Tier 1 capital ratio of 7.0%; (b) a Tier 1 to risk-based assets capital ratio of 8.5%; and (c) a total capital ratio of 10.5%. The capital conservation buffer is being phased in from 0.00% for 2015 to 2.50% by 2019. An institution will be subject to limitations on paying dividends, engaging in share repurchases, and paying discretionary bonuses if its capital level falls below the buffer amount. These limitations will establish a maximum percentage of eligible retained income that can be utilized for such activities. In addition, the final rule provides for a number of new deductions from and adjustments to capital and prescribes a revised approach for risk weightings that could result in higher risk weights for a variety of asset categories.

The application of these more stringent capital requirements for us could, among other things, result in lower returns on equity, require the raising of additional capital, adversely affect our future growth opportunities, and result in regulatory actions such as a prohibition on the payment of dividends or on the repurchase shares if we are unable to comply with such requirements.

New regulations could adversely impact our earnings due to, among other things, increased compliance costs or costs due to noncompliance.

The Consumer Financial Protection Bureau has issued a rule, effective as of January 14, 2014, designed to clarify for lenders how they can avoid monetary damages under the Dodd-Frank Act, which would hold lenders accountable for ensuring a borrower’s ability to repay a mortgage. Loans that satisfy this “qualified mortgage” safe-harbor will be presumed to have complied with the new ability-to-repay standard. Under the Consumer Financial Protection Bureau’s rule, a “qualified mortgage” loan must not contain certain specified features, including but not limited to:

excessive upfront points and fees (those exceeding 3% of the total loan amount, less “bona fide discount points” for prime loans);

interest-only payments;

negative-amortization; and

terms longer than 30 years.

PART I, continued

Item 1A. Risk Factors, continued

Also, to qualify as a “qualified mortgage,” a borrower’s total monthly debt-to-income ratio may not exceed 43%. Lenders must also verify and document the income and financial resources relied upon to qualify the borrower for the loan and underwrite the loan based on a fully amortizing payment schedule and maximum interest rate during the first five years, taking into account all applicable taxes, insurance and assessments. The Consumer Financial Protection Bureau’s rule on qualified mortgages could limit our ability or desire to make certain types of loans or loans to certain borrowers, or could make it more expensive and/or time consuming to make these loans, which could adversely impact our growth or profitability.

Additionally, on December 10, 2013, five financial regulatory agencies, including our primary federal regulator, the Federal Reserve, adopted final rules implementing a provision of the Dodd-Frank Act, commonly referred to as the Volcker Rule. The Final Rules prohibit banking entities from, among other things, engaging in short-term proprietary trading of securities, derivatives, commodity futures and options on these instruments for their own account; or owning, sponsoring, or having certain relationships with hedge funds or private equity funds, referred to as “covered funds.” On January 14, 2014, the five financial regulatory agencies, approved an adjustment to the final rule by allowing banks to keep certain collateralized debt obligations (“CDOs”) acquired the bank before the Volcker Rule was finalized, if the CDO was established before May 2010 and is backed primarily by trust preferred securities issued by banks with less than $15 billion in assets established. The rules were effective April 1, 2014, but the conformance period has been extended from its statutory end date of July 21, 2014 until July 21, 2015. This will not have an impact on the Company.

Our future success is dependent on our ability to effectively compete in the face of substantial competition from other financial institutions in our primary markets.

We encounter significant competition for deposits, loans and other financial services from banks and other financial institutions, including savings and loan associations, savings banks, finance companies, and credit unions in our market area. A number of these banks and other financial institutions are significantly larger than us and have substantially greater access to capital and other resources, larger lending limits, more extensive branch systems, and may offer a wider array of banking services. To a limited extent, we compete with other providers of financial services, such as money market mutual funds, brokerage firms, consumer finance companies, insurance companies and governmental organizations any of which may offer more favorable financing rates and terms than us. Many of these non-bank competitors are not subject to the same extensive regulations that govern us. As a result, these non-bank competitors may have advantages in providing certain services. This competition may reduce or limit our margins and our market share and may adversely affect our results of operations and financial condition.

Our exposure to operational risk may adversely affect us.

Similar to other financial institutions, we are exposed to many types of operational risk, including reputational risk, legal and compliance risk, the risk of fraud or theft by employees or outsiders, unauthorized transactions by employees or operational errors, including clerical or record-keeping errors or those resulting from faulty or disabled computer or telecommunications systems.

PART I, continued

Item 1A. Risk Factors, continued

Changes in market interest rates could affect our cash flows and our ability to successfully manage our interest rate risk.

Our profitability and financial condition depend to a great extent on our ability to manage the net interest margin, which is the difference between the interest income earned on loans and investments and the interest expense paid for deposits and borrowings. The amounts of interest income and interest expense are principally driven by two factors; the market levels of interest rates, and the volumes of earning assets or interest bearing liabilities. The management of the net interest margin is accomplished by our Asset Liability Management Committee. Short term interest rates are highly sensitive to factors beyond our control and are effectively set and managed by the Federal Reserve, while longer term rates are generally determined by the market based on investors' inflationary expectations. Thus, changes in monetary and or fiscal policy will affect both short term and long term interest rates which in turn will influence the origination of loans, the prepayment speed of loans, the purchase of investments, the generation of deposits and the rates received on loans and investment securities and paid on deposits or other sources of funding. The impact of these changes may be magnified if we do not effectively manage the relative sensitivity of our earning assets and interest bearing liabilities to changes in market interest rates. We generally attempt to maintain a neutral position in terms of the volume of earning assets and interest bearing liabilities that mature or can re-price within a one year period in order that we may maintain the maximum net interest margin; however, interest rate fluctuations, loan prepayments, loan production and deposit flows are constantly changing and greatly influence this ability to maintain a neutral position.

Generally, our earnings will be more sensitive to fluctuations in interest rates the greater the difference between the volume of earning assets and interest bearing liabilities that mature or are subject to re-pricing in any period. The extent and duration of this sensitivity will depend on the cumulative difference over time, the velocity and direction of interest rate changes, and whether we are more asset sensitive or liability sensitive. Additionally, the Asset Liability Management Committee may desire to move our position to more asset sensitive or more liability sensitive depending upon their expectation of the direction and velocity of future changes in interest rates in an effort to maximize the net interest margin. Should we not be successful in maintaining the desired position, or should interest rates not move as anticipated, our net interest margin may be negatively impacted.

In December of 2016 the Federal Open Market Committee (FOMC) voted to raise the fed funds rate from .25%-.50% to .50%-.75% in a unanimous decision, with indication rates would increase again in 2017. As indicated above the Company analyzes their risk and is prepared for future changes in interest rates.

Our inability to successfully manage growth or implement our growth strategy may adversely affect our results of operations and financial condition.

We may not be able to successfully implement our growth strategy if we are unable to identify attractive markets, locations or opportunities to expand in the future. Our ability to manage growth successfully also depends on whether we can maintain capital levels adequate to support our growth, maintain cost controls, asset quality and successfully integrate any businesses acquired into the organization.

As we continue to implement our growth strategy, we may incur increased personnel, occupancy and other operating expenses. We must absorb those higher expenses while we begin to generate new deposits, and there is a further time lag involved in redeploying new deposits into attractively priced loans and other higher yielding earning assets. Thus, our plans to branch could depress earnings in the short run, even if we efficiently execute a branching strategy leading to long-term financial benefits.

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PART I, continued

Item 1A. Risk Factors, continued

Our operations rely on certain external vendors.

We are reliant upon certain external vendors to provide products and services necessary to maintain our day-to-day operations. Accordingly, our operations are exposed to risk that these vendors will not perform in accordance with the contracted arrangements under service agreements. Although we maintain a system of comprehensive policies and a control framework designed to monitor vendor risks, the failure of an external vendor to perform in accordance with the contracted arrangements under service agreements could be disruptive to our operations, which could have a material adverse impact on our business and, in turn, our financial condition and results of operations.

Our operations may be adversely affected by cyber security risks.

In the ordinary course of business, we collect and store sensitive data, including proprietary business information and personally identifiable information of its customers and employees in systems and on networks. The secure processing, maintenance and use of this information is critical to operations and our business strategy. We have invested in accepted technologies and review processes and practices that are designed to protect our networks, computers and data from damage or unauthorized access. Despite these security measures, our computer systems and infrastructure may be vulnerable to attacks by hackers or breached due to employee error, malfeasance or other disruptions. A breach of any kind could compromise systems and the information stored there could be accessed, damaged or disclosed. A breach in security could result in legal claims, regulatory penalties, disruption in operations, and damage to our reputation, which could adversely affect our business.

Legislative or regulatory changes or actions, or significant litigation, could adversely impact us or the businesses in which we are engaged.

We are subject to extensive state and federal regulation, supervision and legislation that govern almost all aspects of our operations. Laws and regulations may change from time to time and are primarily intended for the protection of consumers, depositors and the deposit insurance funds. The impact of any changes to laws and regulations or other actions by regulatory agencies may negatively impact us or our ability to increase the value of our business. Additionally, actions by regulatory agencies or significant litigation against us could cause us to devote significant time and resources to defending ourselves and may lead to penalties that materially affect us. Future changes in the laws or regulations or their interpretations or enforcement could be materially adverse us and our shareholders.

Changes in accounting standards could impact reported earnings.

The accounting standard setters, including the FASB, SEC and other regulatory bodies, periodically change the financial accounting and reporting standards that govern the preparation of our consolidated financial statements. These changes can be hard to predict and can materially impact how we record and report our financial condition and results of operations. In some cases, we could be required to apply a new or revised standard retroactively, resulting in the restatement of prior period financial statements.

Item 1B. Unresolved Staff Comments

The Company does not have any unresolved staff comments to report for the year ended December 31, 2016.

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PART I, continued

Item 2. Properties

The locations of F & M Bank Corp. and its subsidiaries are shown below.

Timberville Branch and Administrative Offices
205 South Main Street
Timberville, VA 22853

Elkton Branch
127 West Rockingham Street
Elkton, VA 22827

Broadway Branch
126 Timberway
Broadway, VA 22815

Port Road Branch
1085 Port Republic Road
Harrisonburg, VA 22801

Bridgewater Branch
100 Plaza Drive
Bridgewater, VA 22812

Edinburg Branch
120 South Main Street
Edinburg, VA 22824

Woodstock Branch
161 South Main Street
Woodstock, VA 22664

Crossroads Branch
80 Cross Keys Road
Harrisonburg, VA 22801

Luray Branch
700 East Main Street
Luray, VA 22835

Dealer Finance Division
4759 Spotswood Trail
Penn Laird, VA 22846

Fishersville Loan Production Office
1842 Jefferson Hwy
Fishersville, VA 22939

North Augusta Branch
2813 North Augusta Street
Staunton, VA 22401

Craigsville Branch
125 W. Craig Street
Craigsville, VA 24430

Grottoes Branch
200 Augusta Avenue
Grottoes, VA 24441

With the exception of the Edinburg Branch, Port Road Branch, Luray Branch, Dealer Finance Division, the Fishersville Loan Production Office and the North Augusta Branch, the remaining facilities are owned by Farmers & Merchants Bank. ATMs are available at all branch locations.

Through an agreement with FCTI, Inc., the Bank also operates cash only ATMs at five Food Lion grocery stores, one in Mt. Jackson, VA and four in Harrisonburg, VA. The Bank has an agreement with CardTronics ATM to operate twelve cash only ATMs in various Rite Aid Pharmacies, CVS Pharmacies and Target Stores in Rockingham and Augusta Counties of VA. The Bank also has an agreement with ATM USA to operate ATMs in Foodlion stores in our market area.

VBS' offices are located at:

Harrisonburg Office
2040 Deyerle Avenue
Suite 107
Harrisonburg, VA 22801

Fishersville Loan Production Office
1842 Jefferson Hwy
Fishersville, VA 22939

Woodstock Offic
161 South Main Street
Woodstock, VA 22664

Item 3. Legal Proceedings

In the normal course of business, the Company may become involved in litigation arising from banking, financial, or other activities of the Company. Management after consultation with legal counsel, does not anticipate that the ultimate liability, if any, arising out of these matters will have a material effect on the Company's financial condition, operating results or liquidity.

Item 4. Mine Safety Disclosures

None.

PART II

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

Stock Listing

The Company's Common Stock is quoted under the symbol "FMBM" on the OTCQX Market. The bid and ask price is quoted at www.OTCMARKETS.com/Stock/FMBM/quote. With its inclusion on the OTCQX Markets, there are now several active market makers for FMBM stock.

Transfer Agent and Registrar

Broadridge Financial Solutions
2 Journal Plaza Square, 7th Floor
Jersey City, NJ 07306

Stock Performance

The following graph compares the cumulative total return to the shareholders of the Company for the last five fiscal years with the total return of the Russell 2000 Index and the SNL Bank Index, as reported by SNL Financial, LC, assuming an investment of $100 in the Company's common stock on December 31, 2011, and the reinvestment of dividends.

| | Period Ending | | | | | |
|---|---|---|---|---|---|---|
| Index | 12/31/11 | 12/31/12 | 12/31/13 | 12/31/14 | 12/31/15 | 12/31/16 |
| F & M Bank Corp. | 100.00 | 115.93 | 146.35 | 160.04 | 192.81 | 228.52 |
| Russell 2000 | 100.00 | 116.35 | 161.52 | 169.43 | 161.95 | 196.45 |
| SNL Bank | 100.00 | 134.95 | 185.28 | 207.12 | 210.65 | 266.16 |

PART II, continued

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

Recent Stock Prices and Dividends

Dividends to common shareholders totaled $2,628,000 and $2,405,000 in 2016 and 2015, respectively. Preferred stock dividends were $487,000 and $510,000 in 2016 and 2015, respectively. Regular quarterly dividends have been declared for at least 24 years. The payment of dividends depends on the earnings of the Company and its subsidiaries, the financial condition of the Company and other factors including capital adequacy, regulatory requirements, general economic conditions and shareholder returns. The ratio of dividends per common share to net income per common share was 28.88% in 2016, compared to 30.42% in 2015.

Refer to Payment of Dividends in Item 1. Business, Regulation and Supervision section above for restrictions on dividends.

Stock Repurchases

As previously reported, on September 18, 2008, the Company's Board of Directors approved an increase in the number of shares of common stock that the Company can repurchase under the share repurchase program from 150,000 to 200,000 shares. Shares repurchased through the end of 2016 totaled 199,992 shares; of this amount, 22,583 were repurchased in 2016. On October 20, 2016, the Company's Board of Directors approved a new plan to repurchase up to 150,000 shares of common stock.

The number of common shareholders of record was approximately 2,012 as of March 14, 2017. This amount includes all shareholders, whether titled individually or held by a brokerage firm or custodian in street name.

Quarterly Stock Information

These quotes include the terms of trades transacted through a broker. The terms of exchanges occurring between individual parties may not be known to the Company.

| | 2016 | | | 2015 | | |
|---|---|---|---|---|---|---|
| | Stock Price Range | | Per Share | Stock Price Range | | Per Share |
| Quarter | Low | High | Dividends Declared | Low | High | Dividends Declared |
| 1st | 21.75 | 23.55 | $.19 | 19.30 | 20.95 | $.18 |
| 2nd | 23.02 | 25.00 | .19 | 20.00 | 24.50 | .18 |
| 3rd | 23.50 | 26.25 | .20 | 20.98 | 22.45 | .18 |
| 4th | 24.82 | 27.00 | .22 | 21.10 | 24.47 | .19 |

| | | |
|---|---|---|
| Total | $.80 | $.73 |

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PART II, continued

Item 6. Selected Financial Data

Five Year Summary of Selected Financial Data

| (Dollars in thousands, except per share data) | 2016 | 2015 | 2014 | 2013 | 2012 |
|---|---|---|---|---|---|
| Income Statement Data: | | | | | |
| Interest and Dividend Income | $32,095 | $29,353 | $26,772 | $25,966 | $27,225 |
| Interest Expense | 3,599 | 2,876 | 3,648 | 4,773 | 6,294 |
| Net Interest Income | 28,496 | 26,477 | 23,124 | 21,193 | 20,931 |
| Provision for Loan Losses | - | 300 | 2,250 | 3,775 | 4,200 |
| Net Interest Income After Provision for Loan Losses | 28,496 | 26,177 | 20,874 | 17,418 | 16,731 |
| Noninterest Income | 4,395 | 3,895 | 3,530 | 4,032 | 3,773 |
| Low income housing partnership losses | (731) | (619) | (608) | (856) | (621) |
| Noninterest Expenses | 19,299 | 17,986 | 15,656 | 14,720 | 13,362 |
| Income before income taxes | 12,861 | 11,467 | 8,140 | 5,874 | 6,521 |
| Income Tax Expense | 3,099 | 2,886 | 2,293 | 1,051 | 1,474 |
| Net income attributable to noncontrolling interest | (194) | (164) | (45) | (107) | (146) |
| Net Income attributable to F & M Bank Corp. | $9,568 | $8,417 | $5,802 | $4,716 | $4,901 |
| Per Common Share Data: | | | | | |
| Net Income – basic | $2.77 | $2.40 | $1.82 | $1.88 | $1.96 |
| Net Income - diluted | $2.57 | $2.25 | $1.80 | $- | $- |
| Dividends Declared | .80 | .73 | .68 | .68 | .64 |
| Book Value per Common Share | 24.18 | 22.38 | 20.77 | 21.56 | 19.76 |
| Balance Sheet Data: | | | | | |
| Assets | $744,889 | $665,357 | $605,308 | $552,788 | $596,904 |
| Loans Held for Investment | 591,636 | 544,053 | 518,202 | 478,453 | 465,819 |
| Loans Held for Sale | 62,735 | 57,806 | 13,382 | 3,804 | 77,207 |
| Securities | 39,411 | 25,329 | 22,305 | 38,486 | 18,807 |
| Deposits | 537,085 | 494,670 | 491,505 | 464,149 | 453,796 |
| Short-Term Debt | 40,000 | 24,954 | 14,358 | 3,423 | 34,597 |
| Long-Term Debt | 64,237 | 48,161 | 9,875 | 21,691 | 47,905 |
| Stockholders' Equity | 86,682 | 82,950 | 77,798 | 54,141 | 49,384 |
| Average Common Shares Outstanding – basic | 3,282 | 3,291 | 3,119 | 2,504 | 2,496 |
| Average Common Shares Outstanding – diluted | 3,717 | 3,735 | 3,230 | - | - |
| Financial Ratios: | | | | | |
| Return on Average Assets1 | 1.34% | 1.31% | 1.00% | .82% | .86% |
| Return on Average Equity1 | 11.18% | 10.46% | 8.65% | 9.11% | 10.26% |
| Net Interest Margin | 4.34% | 4.43% | 4.30% | 4.02% | 3.95% |
| Efficiency Ratio 2 | 58.79% | 58.28% | 58.51% | 58.15% | 54.03% |
| Dividend Payout Ratio - Common | 28.88% | 30.42% | 37.36% | 36.17% | 32.65% |
| Capital and Credit Quality Ratios: | | | | | |
| Average Equity to Average Assets1 | 11.97% | 12.49% | 11.59% | 9.00% | 8.35% |

| | | | | | |
|---|---|---|---|---|---|
| Allowance for Loan Losses to Loans3 | 1.27% | 1.61% | 1.68% | 1.71% | 1.75% |
| Nonperforming Loans to Total Assets4 | .65% | .98% | 1.15% | 2.28% | 2.24% |
| Nonperforming Assets to Total Assets5 | .94% | 1.34% | 1.73% | 2.75% | 2.73% |
| Net Charge-offs to Total Loans3 | .21% | .04% | .33% | .78% | .64% |

1
Ratios are primarily based on daily average balances.
2
The Efficiency Ratio equals noninterest expenses divided by the sum of tax equivalent net interest income and noninterest income. Noninterest income excludes gains (losses) on securities transactions, LIH Partnership losses and minority interest.
3
Calculated based on Loans Held for Investment, excludes Loans Held for Sale.
4
Calculated based on 90 day past due and non-accrual to Total Assets.
5
Calculated based on 90 day past due, non-accrual and OREO to Total Assets

PART II, continued

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

The following discussion provides information about the major components of the results of operations and financial condition, liquidity and capital resources of F & M Bank Corp. and its subsidiaries. This discussion and analysis should be read in conjunction with the Consolidated Financial Statements and the Notes to the Consolidated Financial Statements presented in Item 8, Financial Statements and Supplementary Information, of this Form 10-K.

Capital Activities

The Company raised $12 million through the sale of common stock in a private placement offering in March of 2014. In addition, the Company raised $9.4 million through the sale of Series A preferred stock in a public offering in December 2014. Both amounts are net of fees related to the offering.

Lending Activities

Credit Policies

The principal risk associated with each of the categories of loans in our portfolio is the creditworthiness of our borrowers. Within each category, such risk is increased or decreased, depending on prevailing economic conditions. In an effort to manage the risk, our loan policy gives loan amount approval limits to individual loan officers based on their position and level of experience and to our loan committees based on the size of the lending relationship. The risk associated with real estate and construction loans, commercial loans and consumer loans varies, based on market employment levels, consumer confidence, fluctuations in the value of real estate and other conditions that affect the ability of borrowers to repay indebtedness. The risk associated with real estate construction loans varies, based on the supply and demand for the type of real estate under construction.

We have written policies and procedures to help manage credit risk. We have a loan review policy that includes regular portfolio reviews to establish loss exposure and to ascertain compliance with our loan policy.

We use a management loan committee and a directors' loan committee to approve loans. The management loan committee is comprised of members of senior management, and the directors' loan committee is composed of any six directors. Both committees approve new, renewed and or modified loans that exceed officer loan authorities. The directors' loan committee also reviews any changes to our lending policies, which are then approved by our board of directors.

Construction and Development Lending

We make construction loans, primarily residential, and land acquisition and development loans. The construction loans are secured by residential houses under construction and the underlying land for which the loan was obtained. The average life of a construction loan is approximately 12 months, and it is typically re-priced as the prime rate of interest changes. The majority of the interest rates charged on these loans float with the market. Construction lending entails significant additional risks, compared with residential mortgage lending. Construction loans often involve larger loan balances concentrated with single borrowers or groups of related borrowers. Another risk involved in construction lending is attributable to the fact that loan funds are advanced upon the security of the land or home under construction, which value is estimated prior to the completion of construction. Thus, it is more difficult to evaluate accurately the total loan funds required to complete a project and related loan-to-value ratios. To mitigate the risks associated with construction lending, we generally limit loan amounts to 75% to 90% of appraised value, in addition to analyzing the creditworthiness of our borrowers. We also obtain a first lien on the property as security for

our construction loans and typically require personal guarantees from the borrower's principal owners.

PART II, continued

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

Commercial Real Estate Lending

Commercial real estate loans are secured by various types of commercial real estate in our market area, including multi-family residential buildings, commercial buildings and offices, shopping centers and churches. Commercial real estate lending entails significant additional risks, compared with residential mortgage lending. Commercial real estate loans typically involve larger loan balances concentrated with single borrowers or groups of related borrowers. Additionally, the payment experience on loans secured by income producing properties is typically dependent on the successful operation of a business or a real estate project and thus may be subject, to a greater extent, to adverse conditions in the real estate market or in the economy in general. Our commercial real estate loan underwriting criteria require an examination of debt service coverage ratios and the borrower's creditworthiness, prior credit history and reputation. We also evaluate the location of the security property and typically require personal guarantees or endorsements of the borrower's principal owners.

Business Lending

Business loans generally have a higher degree of risk than residential mortgage loans but have higher yields. To manage these risks, we generally obtain appropriate collateral and personal guarantees from the borrower's principal owners and monitor the financial condition of our business borrowers. Residential mortgage loans generally are made on the basis of the borrower's ability to make repayment from employment and other income and are secured by real estate whose value tends to be readily ascertainable. In contrast, business loans typically are made on the basis of the borrower's ability to make repayment from cash flow from its business and are secured by business assets, such as real estate, accounts receivable, equipment and inventory. As a result, the availability of funds for the repayment of business loans is substantially dependent on the success of the business itself. Furthermore, the collateral for business loans may depreciate over time and generally cannot be appraised with as much precision as residential real estate.

Consumer Lending

We offer various consumer loans, including personal loans and lines of credit, automobile loans, deposit account loans, installment and demand loans, and home equity lines of credit and loans. Such loans are generally made to clients with whom we have a pre-existing relationship. We currently originate all of our consumer loans in our geographic market area.

The underwriting standards employed by us for consumer loans include a determination of the applicant's payment history on other debts and an assessment of their ability to meet existing obligations and payments on the proposed loan. The stability of the applicant's monthly income may be determined by verification of gross monthly income from primary employment and additionally from any verifiable secondary income. Although creditworthiness of the applicant is of primary consideration, the underwriting process also includes an analysis of the value of the security in relation to the proposed loan amount. For home equity lines of credit and loans, our primary consumer loan category, we require title insurance, hazard insurance and, if required, flood insurance.

Residential Mortgage Lending

The Bank makes residential mortgage loans for the purchase or refinance of existing loans with loan to value limits ranging between 80 and 90% depending on the age of the property, borrower's income and credit worthiness. Loans that are retained in our portfolio generally carry adjustable rates that can change every three to five years, based on amortization periods of twenty to thirty years.

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PART II, continued

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

Loans Held for Sale

The Bank makes fixed rate mortgage loans with terms of typically fifteen or thirty years through its subsidiary VBS Mortgage. These loans are typically on the Bank's books for two to three weeks prior to being sold to investors in the secondary market. Similarly, the Bank also has a relationship with Northpointe Bank in Grand Rapids, MI whereby it purchases fixed rate conforming 1-4 family mortgage loans for short periods of time pending those loans being sold to investors in the secondary market. These loans have an average duration of ten days to two weeks, but occasionally remain on the Bank's books for up to 60 days. The Bank began its relationship with Northpointe Bank in 2014 and had a program with a prior bank since 2003. This relationship allows the Bank to achieve a higher rate of return than is available on other short term investment opportunities.

Dealer Finance Division

On September 25, 2012, the Bank began a loan production office in Penn Laird, VA which specializes in providing automobile financing through a network of automobile dealers. The Dealer Finance Division was staffed with three officers that have extensive experience in Dealer Finance. This office is serving the automobile finance needs for customers of dealers throughout the existing geographic footprint of the Bank. Approximately fifty dealers have signed contracts to originate loans on behalf of the Bank.

Critical Accounting Policies

General

The Company's financial statements are prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP"). The financial information contained within the statements is, to a significant extent, financial information that is based on measures of the financial effects of transactions and events that have already occurred. The Company's financial position and results of operations are affected by management's application of accounting policies, including estimates, assumptions and judgments made to arrive at the carrying value of assets and liabilities and amounts reported for revenues, expenses and related disclosures. Different assumptions in the application of these policies could result in material changes in the Company's consolidated financial position and/or results of operations.

In addition, GAAP itself may change from one previously acceptable method to another method. Although the economics of these transactions would be the same, the timing of events that would impact these transactions could change. Following is a summary of the Company's significant accounting policies that are highly dependent on estimates, assumptions and judgments.

Allowance for Loan Losses

The allowance for loan losses is an estimate of the losses that may be sustained in the loan portfolio. The allowance is based on two basic principles of accounting: (i) ASC 450 (formerly SFAS No. 5) "Contingencies", which requires that losses be accrued when they are probable of occurring and estimable and (ii) ASC 310 (formerly SFAS No. 114), "Receivables", which requires that losses be accrued based on the differences between the value of collateral, present value of future cash flows or values that are observable in the secondary market and the loan balance. The Company's allowance for loan losses is the accumulation of various components that are calculated based on independent methodologies. All components of the allowance represent an estimation performed pursuant to either ASC 450 or

ASC 310. Management's estimate of each ASC 450 component is based on certain observable data that management believes are most reflective of the underlying credit losses being estimated. This evaluation includes credit quality trends; collateral values; loan volumes; geographic, borrower and industry concentrations; seasoning of the loan portfolio; the findings of internal credit quality assessments and results from external bank regulatory examinations. These factors, as well as historical losses and current economic and business conditions, are used in developing estimated loss factors used in the calculations.

PART II, continued

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

Allowance for Loan Losses, continued

Allowances for loans are determined by applying estimated loss factors to the portfolio based on management's evaluation and "risk grading" of the loan portfolio. Specific allowances are typically provided on all impaired loans in excess of a defined loan size threshold that are classified in the Substandard or Doubtful risk grades. The specific reserves are determined on a loan-by-loan basis based on management's evaluation of the Company's exposure for each credit, given the current payment status of the loan and the value of any underlying collateral.

While management uses the best information available to establish the allowance for loan and lease losses, future adjustments to the allowance may be necessary if economic conditions differ substantially from the assumptions used in making the valuations or, if required by regulators, based upon information available to them at the time of their examinations. Such adjustments to original estimates, as necessary, are made in the period in which these factors and other relevant considerations indicate that loss levels may vary from previous estimates.

Goodwill and Intangibles

In June 2001, the Financial Accounting Standards Board issued ASC 805 (formerly SFAS No. 141), Business Combinations and ASC 350 (formerly SFAS No. 142), Intangibles. ASC 805 requires that the purchase method of accounting be used for all business combinations initiated after June 30, 2001. Additionally, it further clarifies the criteria for the initial recognition and measurement of intangible assets separate from goodwill. ASC 350 was effective for fiscal years beginning after December 15, 2001 and prescribes the accounting for goodwill and intangible assets subsequent to initial recognition. The provisions of ASC 350 discontinue the amortization of goodwill and intangible assets with indefinite lives. Instead, these assets are subject to an annual impairment review and more frequently if certain impairment indicators are in evidence. ASC 350 also requires that reporting units be identified for the purpose of assessing potential future impairments of goodwill.

The Company adopted ASC 350 on January 1, 2002. Goodwill totaled $2,639,000 at January 1, 2002. As of December 31, 2008, the Company recognized $30,000 in additional goodwill related to the purchase of 70% ownership in VBS Mortgage. The goodwill is not amortized but is tested for impairment at least annually. Based on this testing, there were no impairment charges for 2016, 2015 or 2014.

Income Tax

The determination of income taxes represents results in income and expense being recognized in different periods for financial reporting purposes versus for the purpose of computing income taxes currently payable. Deferred taxes are provided on such temporary differences and are measured using the enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be realized or settled. Further, the Company seeks strategies that minimize the tax effect of implementing its business strategies. Management makes judgments regarding the ultimate consequence of long-term tax planning strategies, including the likelihood of future recognition of deferred tax benefits. As a result, it is considered a significant estimate.

PART II, continued

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

Fair Value

The estimate of fair value involves the use of (1) quoted prices for identical instruments traded in active markets, (2) 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 using significant assumptions that are observable in the market or (3) model-based techniques that use significant assumptions not observable in the market. When observable market prices and parameters are not fully available, management's judgment is necessary to estimate fair value possibly including estimates that incorporate estimates of current market participant expectations of future cash flows, risk premiums, among other things. Additionally, significant judgment may be required to determine whether certain assets measured at fair value are classified within the fair value hierarchy as Level 2 or Level 3. The estimation process and the potential materiality of the amounts involved result in this item being identified as critical.

Pension Plan Accounting

The accounting guidance for the measurement and recognition of obligations and expense related to pension plans generally applies the concept that the cost of benefits provided during retirement should be recognized over the employees' active working life. Inherent in this concept is the requirement to use various actuarial assumptions to predict and measure costs and obligations many years prior to the settlement date. Major actuarial assumptions that require significant management judgment and have a material impact on the measurement of benefits expense and accumulated obligation include discount rates, expected return on assets, mortality rates, and projected salary increases, among others. Changes in assumptions or judgments related to any of these variables could result in significant volatility in the Company's financial condition and results of operations. As a result, accounting for the Company's pension expense and obligation is considered a significant estimate. The estimation process and the potential materiality of the amounts involved result in this item being identified as critical.

Securities

The Company follows the accounting guidance related to recognition and presentation of other-than-temporary impairment. The guidance specifies that if (a) an entity does not have the intent to sell a debt security prior to recovery and (b) it is more likely than not that the entity will not have to sell the debt security prior to recovery, the security would not be considered other-than-temporarily impaired, unless there is a credit loss. When criteria (a) and (b) are met, the entity will recognize the credit component of other-than-temporary impairment of a debt security in earnings and the remaining portion in other comprehensive income. For held-to-maturity debt securities, the amount of other-than-temporary impairment recorded in other comprehensive income for the noncredit portion of a previous other-than- temporary impairment is amortized prospectively over the remaining life of the security on the basis of the timing of future estimated cash flows of the security.

Other Real Estate Owned (OREO)

OREO is held for sale and represents real estate acquired through or in lieu of foreclosure. OREO is initially recorded at fair value less costs to sell when acquired, establishing a new cost basis. Physical possession of residential real estate property collateralizing a consumer mortgage loan occurs when legal title is obtained upon completion of foreclosure or when the borrower conveys all interest in the property to satisfy the loan through completion of a deed in lieu of foreclosure or through a similar legal agreement. The Company's policy is to carry OREO on its balance sheet at the lower of cost or fair value less estimated costs to sell. If fair value declines subsequent to foreclosure, a valuation allowance is recorded through expense. Operating costs after acquisition are expensed.

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PART II, continued

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

Overview

The Company's net income for 2016 totaled $9,568,000 or $2.77 per common share, an increase of 13.67% from $8,417,000 or $2.40 a share in 2015. Return on average equity increased in 2016 to 11.18% versus 10.46% in 2015, and the return on average assets increased from 1.31%in 2015 to 1.34% in 2016.

See page 15 for a five-year summary of selected financial data.

Changes in Net Income per Common Share (Basic)

| | 2016 to 2015 | 2015 to 2014 |
|---|---|---|
| Prior Year Net Income Per Common Share (Basic) | $2.40 | $1.82 |
| Change from differences in: | | |
| Net interest income | .62 | 1.02 |
| Provision for loan losses | .09 | .59 |
| Noninterest income, excluding securities gains | (.08) | .08 |
| Noninterest expenses | (.40) | (.71) |
| Income taxes | .12 | (.18) |
| Effect of preferred stock dividend | .01 | (.12) |
| Effect of increase in average shares outstanding | .01 | (.10) |
| Total Change | .37 | .58 |
| Net Income Per Common Share (Basic) | $2.77 | $2.40 |

Net Interest Income

The largest source of operating revenue for the Company is net interest income, which is calculated as the difference between the interest earned on earning assets and the interest expense paid on interest bearing liabilities. The net interest margin is the net interest income expressed as a percentage of interest earning assets. Changes in the volume and mix of interest earning assets and interest bearing liabilities, along with their yields and rates, have a significant impact on the level of net interest income. Net interest income for 2016 was $28,496,000 representing an increase of $2,019,000 or 7.63% over the prior year. A 14.50% increase in 2015 versus 2014 resulted in total net interest income of $26,477,000.

In this discussion and in the tabular analysis of net interest income performance, entitled "Consolidated Average Balances, Yields and Rates," (found on page 23), the interest earned on tax exempt loans and investment securities has been adjusted to reflect the amount that would have been earned had these investments been subject to normal income taxation. This is referred to as tax equivalent net interest income. For a reconciliation of tax equivalent net interest income to GAAP measures, see the table on page 25.

Tax equivalent income on earning assets increased $2,744,000. Loans held for investment, expressed as a percentage of total earning assets, decreased in 2016 to 86.02% as compared to 88.60% in 2015. During 2016, yields on earning assets decreased 2 basis points (BP), primarily due to a 17BP decrease in the yield on installment loans. Dealer finance yields have decreased due growth in loans to higher credit borrowers. The average cost of interest bearing liabilities increased 9BP in 2016, following a decrease of 23BP in 2015. The increase in 2016 is primarily a result of increased cost of time deposits and savings deposits.

The analysis on the next page reveals a decrease in the net interest margin to 4.34% in 2016 primarily due to changes in balance sheet leverage due to growth in the loans held for sale producing higher yields, which were primarily funded by growth in deposits at higher cost of funds and growth in borrowings increasing interest expense.

PART II, Continued

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

Consolidated Average Balances, Yields and Rates1

| | 2016 | | | 2015 | | | 2014 | | |
|---|---|---|---|---|---|---|---|---|---|
| | Balance | Interest | Rate | Balance | Interest | Rate | Balance | Interest | Rate |
| ASSETS | | | | | | | | | |
| Loans2 | | | | | | | | | |
| Commercial | $176,389 | $8,362 | 4.74% | $170,272 | $8,103 | 4.76% | $164,666 | $7,810 | 4.74% |
| Real estate | 312,435 | 15,781 | 5.05% | 295,892 | 14,976 | 5.06% | 281,052 | 14,542 | 5.17% |
| Installment | 78,524 | 5,805 | 7.39% | 65,870 | 4,981 | 7.56% | 50,695 | 3,960 | 7.81% |
| Loans held for investment4 | 567,348 | 29,948 | 5.28% | 532,034 | 28,060 | 5.27% | 496,413 | 26,312 | 5.30% |
| Loans held for sale | 68,438 | 1,888 | 2.76% | 40,450 | 1,100 | 2.72% | 9,072 | 312 | 3.44% |
| Investment securities3 | | | | | | | | | |
| Fully taxable | 15,714 | 354 | 2.25% | 17,372 | 302 | 1.74% | 13,392 | 205 | 1.53% |
| Partially taxable | 125 | - | - | 125 | - | - | 116 | - | - |
| Total investment securities | 15,839 | 354 | 2.25% | 17,497 | 302 | 1.74% | 13,508 | 205 | 1.53% |
| Interest bearing deposits in banks | 727 | 2 | .41% | 1,223 | - | - | 896 | - | - |
| Federal funds sold | 7,195 | 35 | .49% | 9,310 | 21 | .23% | 20,602 | 44 | .21% |
| Total Earning Assets | 659,547 | 32,227 | 4.89% | 600,514 | 29,483 | 4.91% | 540,491 | 26,873 | 4.97% |
| Allowance for loan losses | (8,162) | | | (8,933) | | | (8,476) | | |
| Nonearning assets | 63,205 | | | 52,378 | | | 47,036 | | |
| Total Assets | $714,590 | | | $643,959 | | | $579,051 | | |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | | | | | | | | |
| Deposits | | | | | | | | | |
| Demand –interest bearing | $113,525 | $499 | .44% | $112,334 | $539 | .48% | $117,396 | $664 | .57% |
| Savings | 100,298 | 441 | .44% | 76,491 | 212 | .28% | 60,460 | 122 | .20% |
| Time deposits | 160,221 | 1,440 | .90% | 171,829 | 1,402 | .82% | 195,933 | 1,704 | .87% |
| | 374,044 | 2,380 | .64% | 360,654 | 2,153 | .60% | 373,789 | 2,490 | .67% |

| | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| Total interest bearing deposits | | | | | | | | | |
| Short-term debt | 37,716 | 55 | .15% | 32,017 | 69 | .22% | 3,872 | 9 | .23% |
| Long-term debt | 56,253 | 1,164 | 2.07% | 31,856 | 654 | 2.05% | 21,501 | 1,149 | 5.34% |
| Total interest bearing liabilities | 468,013 | 3,599 | .77% | 424,527 | 2,876 | .68% | 399,162 | 3,648 | .91% |
| Noninterest bearing deposits | 141,180 | | | 125,665 | | | 107,647 | | |
| Other liabilities | 19,824 | | | 13,318 | | | 5,134 | | |
| Total liabilities | 629,017 | | | 563,510 | | | 511,943 | | |
| Stockholders' equity | 85,572 | | | 80,449 | | | 67,108 | | |
| Total liabilities and stockholders' equity | $714,590 | | | $643,959 | | | $579,051 | | |
| Net interest earnings | | $28,628 | | | $26,607 | | | $23,225 | |
| Net yield on interest earning assets (NIM) | | | 4.34% | | | 4.43% | | | 4.30% |

1
Income and yields are presented on a tax-equivalent basis using the applicable federal income tax rate.
2
Interest income on loans includes loan fees.
3
Average balance information is reflective of historical cost and has not been adjusted for changes in market value.
4
Includes nonaccrual loans.

PART II, Continued

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

The following table illustrates the effect of changes in volumes and rates.

| | 2016 Compared to 2015 | | | 2015 Compared to 2014 | | |
|---|---|---|---|---|---|---|
| | Increase (Decrease) | | | Increase (Decrease) | | |
| | Due to Change | | Increase | Due to Change | | Increase |
| | in Average: | | Or | in Average: | | or |
| | Volume | Rate | (Decrease) | Volume | Rate | (Decrease) |
| Interest income | | | | | | |
| Loans held for investment | $1,861 | $27 | $1,888 | $1,888 | $(140) | $1,748 |
| Loans held for sale | 760 | 28 | 788 | 1,079 | (292) | 787 |
| Investment securities | | | | | | |
| Fully taxable | (29) | 80 | 51 | 61 | 37 | 98 |
| Partially taxable | - | - | - | - | - | - |
| Interest bearing deposits in banks | - | 3 | 3 | - | - | - |
| Federal funds sold | (5) | 19 | 14 | (24) | 1 | (23) |
| Total Interest Income | 2,587 | 157 | 2,744 | 3,004 | (394) | 2,610 |
| Interest expense | | | | | | |
| Deposits | | | | | | |
| Demand - interest bearing | 6 | (46) | (40) | (29) | (96) | (125) |
| Savings | 67 | 162 | 229 | 32 | 58 | 90 |
| Time deposits | (95) | 133 | 38 | (210) | (92) | (302) |
| Short-term debt | 13 | (27) | (14) | 65 | (5) | 60 |
| Long-term debt | 500 | 10 | 510 | 553 | (1,048) | (495) |
| Total Interest Expense | 491 | 232 | 723 | 411 | (1,183) | (772) |
| Net Interest Income | $2,097 | $(76) | $2,021 | $2,593 | $789 | $3,382 |

Note: Volume changes have been determined by multiplying the prior years' average rate by the change in average balances outstanding. The rate change is determined by multiplying the change in average balances outstanding by the change in rate from the prior year to the current year.

Interest Income

Tax equivalent interest income increased $2,744,000 or 9.31% in 2016, after increasing 9.71% or $2,610,000 in 2015. Overall, the yield on earning assets decreased .02%, from 4.91% to 4.89%. Average loans held for investment grew during 2016, with average loans outstanding increasing $35,314,000 to $567,348,000. Average real estate loans increased 5.59%, commercial loans increased 3.59% and installment loans increased 19.21% on average. The increase in average consumer loans is a result of the growth in our Dealer Finance division which opened at the end of 2012. The increase in tax equivalent interest income is primarily due to the growth in the Dealer Finance division as well as the volume in the short-term loans held for sale participation program with Northpointe Bank.

PART II, Continued

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

The following table provides detail on the components of tax equivalent net interest income:

| GAAP Financial Measurements:<br>(Dollars in thousands). | 2016 | 2015 | 2014 |
|---|---|---|---|
| Interest Income – Loans | $31,704 | $29,029 | $26,523 |
| Interest Income - Securities and Other Interest-Earnings Assets | 391 | 324 | 249 |
| Interest Expense – Deposits | 2,380 | 2,153 | 2,490 |
| Interest Expense - Other Borrowings | 1,219 | 723 | 1,158 |
| Total Net Interest Income | 28,496 | 26,477 | 23,124 |
| | | | |
| Non-GAAP Financial Measurements: | | | |
| Add: Tax Benefit on Tax-Exempt Interest Income – Loans | 132 | 130 | 101 |
| Add: Tax Benefit on Tax-Exempt Interest Income - Securities and Other Interest-Earnings Assets | - | - | - |
| Total Tax Benefit on Tax-Exempt Interest Income | 132 | 130 | 101 |
| Tax-Equivalent Net Interest Income | $28,628 | $26,607 | $23,225 |

Interest Expense

Interest expense increased $723,000 or 25.14% during 2016, which followed a 21.16% decrease or $772,000 in 2015. The average cost of funds of .77% increased .09% compared to 2015. Average interest bearing liabilities increased $43,486,000 in 2016 following an increase of $25,365,000 in 2015. The increase in interest bearing liabilities was the result of an increase in FHLB borrowings to support loan growth as well as an overall goal to increase deposits. Time deposits balances decreased $3.8 million with an increase in expense of $38,000 or 2.71% in 2016. Changes in the cost of funds attributable to rate and volume variances can be found in the table at the top of page 24.

Noninterest Income

Noninterest income continues to be an increasingly important factor in maintaining and growing profitability. Management is conscious of the need to constantly review fee income and develop additional sources of complementary revenue.

Noninterest income increased 11.84% or $388,000, in 2016 following an increase of 12.11% in 2015. The majority of the increase is from another record earning year at VBS mortgage ($453,000), due to increased volume in our low interest rate environment and slight economic improvement. The losses on low income house projects increased 18.09% in 2016.

There were no security transactions in 2016, 2015 or 2014 which resulted in a gain or loss.

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PART II, Continued

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

Noninterest Expense

Noninterest expenses increased from $17,986,000 in 2015 to $19,299,000 in 2016, a 7.30% increase. Salary and benefits increased 10.61% to $11,122,000 in 2016, following a 14.14% increase in 2015. This increase was the result of normal salary increases, additions to staff for new branches and administrative positions as well as increasing benefit costs (including health care cost, pension expense and profit sharing expenses). Other operating expenses increased $808,000 in 2016, following a $909,000 increase in 2015. The primary increases were in advertising and employee appreciation ($70,000), other loan related costs ($127,000), legal and professional expense ($108,000) and checking account program expenses ($257,000). Noninterest expenses continue to be substantially lower than peer group averages. Total noninterest expense as a percentage of average assets totaled 2.70%, 2.79%, and 2.70%, in 2016, 2015 and 2014, respectively. Peer group averages (as reported in the most recent Uniform Bank Performance Report) have ranged between 2.84%, 2.86% and 2.89% over the same time period.

Provision for Loan Losses

Management evaluates the loan portfolio in light of national and local economic trends, changes in the nature and volume of the portfolio and industry standards. Specific factors considered by management in determining the adequacy of the level of the allowance for loan losses include internally generated loan review reports, past due reports and historical loan loss experience. This review also considers concentrations of loans in terms of geography, business type and level of risk. Management evaluates nonperforming loans relative to their collateral value, when deemed collateral dependent, and makes the appropriate adjustments to the allowance for loan losses when needed. Based on the factors outlined above, the current year provision for loan losses decreased from $300,000 in 2015 to $0 in 2016. The decrease in the provision for loan losses and the current levels of the allowance for loan losses reflect reductions in specific reserves required related to nonperforming loans, reductions in adversely rated loans, increased net charge-off activity, loan growth, improvements in delinquency trends and other credit risk factors that the Company considers in assessing the adequacy of the allowance for loan losses.

Actual net loan charge-offs were $1,238,000 in 2016 and $244,000 in 2015. Loan losses as a percentage of loans held for investment totaled ..21% and .04% in 2016 and 2015, respectively. As stated in the most recently available Uniform Bank Performance Report (UPBR), peer group loss averages were .11% in 2016 and .12% in 2015.

Balance Sheet

Total assets increased 11.95% during the year to $744,889,000, an increase of $79,532,000 from $665,357,000 in 2015. Average earning assets increased 9.83% or $59,033,000 to $659,547,000 at December 31, 2016. The increase in earning assets is due largely to the growth in the short-term loan participation program with Northpointe Bank and in loans held for investment. Average interest bearing deposits increased $13,390,000 for 2016 or 3.71%, with increases in both interest-bearing demand accounts and savings accounts, there was an $11,608,000 decrease in the time deposit category. The Company continues to utilize its assets well, with 92.30% of average assets consisting of earning assets.

Investment Securities

Average balances in investment securities decreased 9.48% in 2016 to $15,839,000. At year end, 2.40% of average earning assets of the Company were held as investment securities, all of which are unpledged. Management strives to match the types and maturities of securities owned to balance projected liquidity needs, interest rate sensitivity and to maximize earnings through a portfolio bearing low credit risk. Portfolio yields averaged 2.25% for 2016, up from

1.74% in 2015.

There were no security gains or losses and no Other Than Temporary Impairment (OTTI) write-downs in 2016, 2015 or 2014.

PART II, Continued

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

Investment Securities, continued

The composition of securities at December 31 was:

| (Dollars in thousands) | 2016 | 2015 | 2014 |
|---|---|---|---|
| Available for Sale1 | | | |
| U.S. Treasuries | $24,014 | $12,095 | $12,058 |
| Mortgage-backed obligations of federal agencies2 | 634 | 817 | 1,022 |
| Equity securities | 135 | 135 | 135 |
| Total | 24,783 | 13,047 | 13,215 |
| Held to Maturity | | | |
| U.S. Treasury and Agency | 125 | 125 | 125 |
| Total | 125 | 125 | 125 |
| Other Equity Investments | 14,503 | 12,157 | 8,965 |
| Total Securities | $39,411 | $25,329 | $22,305 |

1
At estimated fair value. See Note 4 to the Consolidated Financial Statements for amortized cost.
2
Issued by a U.S. Government Agency or secured by U.S. Government Agency collateral.

Maturities and weighted average yields of securities at December 31, 2016 are presented in the table below. Amounts are shown by contractual maturity; expected maturities will differ as issuers may have the right to call or prepay obligations. Maturities of Other Investments are not readily determinable due to the nature of the investment; see Note 4 to the Consolidated Financial Statements for a description of these investments.

| | Less | | One to | | Five to | | Over | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | Than one Year | | Five Years | | Ten Years | | Ten Years | | | |
| (Dollars in thousands) | Amount | Yield | Amount | Yield | Amount | Yield | Amount | Yield | Total | Yield |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Debt Securities Available for Sale | | | | | | | | |
| U.S. Treasuries | $24,014 | .36% | $- | $- | | $- | $24,014 | .36% |
| Mortgage-backed obligations of federal agencies | | | | 634 | 2.38% | - | 634 | 2.38% |
| Equity securities | - | | - | - | | 135 | 135 | |
| Total | $24,014 | .36% | $- | $634 | 2.38% | $135 | $24,783 | .41% |
| Debt Securities Held to Maturity | | | | | | | | |
| U.S. Treasury & Agency | $125 | .35% | | | | | $125 | .35% |
| Total | $125 | .35% | | | | | $125 | .35% |

PART II, Continued

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

Analysis of Loan Portfolio

The Company's market area has a relatively stable economy which tends to be less cyclical than the national economy. Major industries in the market area include agricultural production and processing, higher education, retail sales, services and light manufacturing.

The Company's portfolio of loans held for investment totaled $591,636,000 at December 31, 2016 compared with $544,053,000 at the beginning of the year. The Company's policy has been to make conservative loans that are held for future interest income. Collateral required by the Company is determined on an individual basis depending on the purpose of the loan and the financial condition of the borrower. Commercial loans, including agricultural and multifamily loans, increased 14.10% during 2016 to $201,873,000. Real estate mortgages increased $6,310,000 or 2.72%. Growth has included a variety of loan and collateral types including owner occupied residential real estate and residential rental properties.

Construction loans increased $6,413,000 or 9.19%. The increase in construction lending is a result of improvement in the economy in the Bank's primary market area. The Bank also has loan participation arrangements with several other banks within the region to aid in diversification of the loan portfolio geographically, by collateral type and by borrower.

Consumer installment loans increased $9,809,000 or 15.76%. This category includes personal loans, auto loans and other loans to individuals. This category began increasing during the fourth quarter of 2012 due to the opening of the Dealer Finance Division in Penn Laird, Virginia; at year end this Division had a loan portfolio of $65,495,000. Credit card balances increased $77,000 to $2,822,000, but are a minor component of the loan portfolio. The following table presents the changes in the loan portfolio over the previous five years.

| | December 31 | | | | |
|---|---|---|---|---|---|
| (Dollars in thousands) | 2016 | 2015 | 2014 | 2013 | 2012 |
| Real estate – mortgage | $238,631 | $232,321 | $223,824 | $212,630 | $204,812 |
| Real estate – construction | 76,172 | 69,759 | 67,180 | 68,512 | 71,251 |
| Consumer installment | 72,048 | 62,239 | 49,615 | 30,643 | 15,753 |
| Commercial | 178,392 | 153,691 | 147,599 | 135,835 | 147,089 |
| Agricultural | 15,876 | 15,672 | 15,374 | 16,265 | 14,099 |
| Multi-family residential | 7,605 | 7,559 | 11,775 | 11,797 | 9,357 |
| Credit cards | 2,822 | 2,745 | 2,705 | 2,680 | 2,788 |
| Other | 90 | 67 | 130 | 91 | 670 |
| Total Loans | $591,636 | $544,053 | $518,202 | $478,453 | $465,819 |

The following table shows the Company's loan maturity and interest rate sensitivity as of December 31, 2016:

| (Dollars in thousands) | Less Than 1 Year | 1-5 Years | Over 5 Years | Total |
|---|---|---|---|---|
| Commercial and agricultural loans | $54,020 | $116,099 | $24,149 | $194,268 |
| Multi-family residential | 1,906 | 4,373 | 1,326 | 7,605 |
| Real Estate – mortgage | 96,512 | 139,298 | 2,821 | 238,631 |
| Real Estate – construction | 60,378 | 15,455 | 339 | 76,172 |
| Consumer – installment/other | 8,099 | 53,360 | 13,501 | 74,960 |
| Total | $220,915 | $328,585 | $42,136 | $591,636 |
| Loans with predetermined rates | $40,749 | $70,009 | $27,847 | $138,605 |
| Loans with variable or adjustable rates | 180,166 | 258,576 | 14,289 | 453,031 |
| Total | $220,915 | $328,585 | $42,136 | $591,636 |

PART II, Continued

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

Analysis of Loan Portfolio, continued

Residential real estate loans are generally made for a period not to exceed 25 years and are secured by a first deed of trust which normally does not exceed 90% of the appraised value. If the loan to value ratio exceeds 90%, the Company requires additional collateral, guarantees or mortgage insurance. On approximately 97% of the real estate loans, interest is adjustable after each one, three or five-year period. The remainder of the portfolio is comprised of fixed rate loans that are generally made for a fifteen-year or a twenty-year period with an interest rate adjustment after ten years.

Since 1992, fixed rate real estate loans have been funded with fixed rate borrowings from the Federal Home Loan Bank, which allows the Company to control its interest rate risk. In addition, the Company makes home equity loans secured by second deeds of trust with total indebtedness not to exceed 90% of the appraised value. Home equity loans are made for three, five or ten year periods at a fixed rate or as a revolving line of credit.

Construction loans may be made to individuals, who have arranged with a contractor for the construction of a residence, or to contractors that are involved in building pre-sold, spec-homes or subdivisions. The majority of commercial loans are made to small retail, manufacturing and service businesses. Consumer loans are made for a variety of reasons; however, approximately 76% of the loans are secured by automobiles and trucks.

Prior to the recession, real estate values in the Company's market area for commercial, agricultural and residential property increased, on the average, between 5% and 8% annually depending on the location and type of property. However, due to the slowing economy and declining real estate sales it is estimated that values peaked in 2007 or 2008. Depending on a number of factors, including property type, location and price point, the decline in value ranges from relatively modest, perhaps 10%, to more severe, up to 30%. Values appear to have bottomed out in 2011, with modest increases in 2014, 2015 and 2016. Approximately 82% of the Company's loans are secured by real estate; however, policies relating to appraisals and loan to value ratios are adequate to control the related risk. Unemployment rates in the Company's market area continue to be below both the national and state averages.

The Bank has identified loan concentrations of greater than 25% of capital in the real estate development category. While the Bank has not developed a formal policy limiting the concentration level to any particular loan type or industry segment, it has established target limits on both a nominal and percentage of capital basis. Concentrations are monitored and reported to the board of directors quarterly. Concentration levels have been used by management to determine how aggressively we may price or pursue new loan requests. At December 31, 2016, there are no industry categories of loans that exceed 10% of total loans.

Nonaccrual and Past Due Loans

Nonperforming loans include nonaccrual loans and loans 90 days or more past due. Nonaccrual loans are loans on which interest accruals have been suspended or discontinued permanently. The Company would have earned approximately $102,000 in additional interest income had the loans on nonaccrual status been current and performing. Nonperforming loans totaled $4,870,000 at December 31, 2016 compared to $6,526,000 at December 31, 2015. At December 31, 2016 $107,000 of loans 90 days or more past due were not on nonaccrual status. Approximately 94% of these nonperforming loans are secured by real estate. Although management expects that there may be additional loan losses, the bank is generally well secured and continues to actively work with its customers to effect payment. As of December 31, 2016, the Company holds $2,076,000 of real estate which was acquired through foreclosure.

Nonperforming loans have decreased approximately $1,656,000 since December 31, 2015.

PART II, Continued

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

Nonaccrual and Past Due Loans, continued

The following is a summary of information pertaining to nonperforming loans:

| (Dollars in thousands) | 2016 | 2015 | 2014 | 2013 | 2012 |
|---|---|---|---|---|---|
| Nonaccrual Loans: | | | | | |
| Real Estate | $4,204 | $5,698 | $5,481 | $9,963 | $9,611 |
| Commercial | 70 | 109 | 1,179 | 1,890 | 2,914 |
| Home Equity | 311 | 40 | 153 | 402 | 740 |
| Other | 178 | 108 | 161 | - | 121 |
| Loans past due 90 days or more: | | | | | |
| Real Estate | 81 | 272 | 0 | 246 | - |
| Commercial | - | 25 | 0 | 4 | - |
| Home Equity | - | 107 | 0 | 61 | - |
| Other | 26 | 167 | 1 | 16 | - |
| Total Nonperforming loans | $4,870 | $6,526 | $6,975 | $12,582 | $13,386 |
| Restructured Loans current and performing: | | | | | |
| Real Estate | 8,641 | 8,713 | 3,913 | 7,484 | 6,572 |
| Commercial | 1,121 | 1,463 | 518 | 3,989 | 3,753 |
| Home Equity | - | 1,414 | 290 | 727 | 450 |
| Other | 76 | 91 | 22 | - | - |
| Nonperforming loans as a percentage of loans held for investment | .82% | 1.20% | 1.35% | 2.63% | 2.87% |
| Net Charge Offs to Total Loans Held for Investment | .21% | .04% | .33% | .78% | .64% |
| Allowance for loan and lease losses to nonperforming loans | 154.89% | 134.55% | 125.09% | 65.04% | 60.91% |

Potential Problem Loans

Loans classified for regulatory purposes as loss, doubtful, substandard, or special mention do not represent or result from trends or uncertainties which management reasonably expects will materially impact future operating results, liquidity or capital resources. Nor do they represent material credits about which management is aware of any information which causes it to have serious doubts as to the ability of such borrowers to comply with the loan repayment terms. As of December 31, 2016, management is not aware of any potential problem loans which are not already classified for regulatory purposes or on the watch list as part of the Bank's internal grading system.

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PART II, Continued

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

Loan Losses and the Allowance for Loan Losses

In evaluating the portfolio, loans are segregated into loans with identified potential losses, pools of loans by type, with separate weighting for past dues and a general allowance based on a variety of criteria. Loans with identified potential losses include examiner and bank classified loans. Classified relationships in excess of $500,000 and loans identified as troubled debt restructurings are reviewed individually for impairment under ASC 310. A variety of factors are considered when reviewing these credits, including borrower cash flow, payment history, fair value of collateral, company management, industry and economic factors.

Loans that are not impaired are categorized by call report code and an estimate is calculated based on actual loss experience over the last five years, for loans of that type. Due to the amount of loan losses in the past two years, during 2015 the Company felt the two-year lost history utilized in 2014 and prior would not be indicative of the amount of losses that could occur in our current economic cycle, therefore the loss history was expanded to five years to capture a more representative loss history. Dealer finance loans utilize a two-year loss history. The Company monitors the net losses for this division and adjusts based on how the portfolio performs since the department was established in 2012. A general allowance for inherent losses has been established to reflect other unidentified losses within the portfolio. The general allowance is calculated using nine qualitative factors identified in the 2006 Interagency Policy Statement on the allowance for loan losses. The general allowance assists in managing recent changes in portfolio risk that may not be captured in individually impaired loans, or in the homogeneous pools based on loss histories. The Board approves the loan loss provision for each quarter based on this evaluation.

The allowance for loan losses of $7,543,000 at December 31, 2016 is equal to 1.27% of total loans held for investment. This compares to an allowance of $8,781,000 or 1.61% at December 31, 2015 and 1.68% at December 31, 2014. Management and the Board of Directors feel that the current reserve level is appropriate. Management has reached this conclusion based on an analysis of historical losses, delinquency rates, collateral values of delinquent loans and a thorough review of the loan portfolio.

Loan losses, net of recoveries, totaled $1,238,000 in 2016 which is equivalent to .21% of total loans outstanding. Over the preceding three years, the Company has had an average loss rate of .19%, compared to a .14% loss rate for its peer group.

PART II, Continued

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

Loan Losses and the Allowance for Loan Losses, continued

A summary of the activity in the allowance for loan losses follows:

| (Dollars in thousands) | 2016 | 2015 | 2014 | 2013 | 2012 |
|---|---|---|---|---|---|
| Balance at beginning of period | $8,781 | $8,725 | $8,184 | $8,154 | $6,937 |
| Provision charged to expenses | - | 300 | 2,250 | 3,775 | 4,200 |
| Loan losses: | | | | | |
| Construction/land development | 356 | 156 | 1,611 | 2,127 | 1,480 |
| Farmland | - | - | - | - | - |
| Real Estate | 23 | 25 | 208 | 173 | 482 |
| Multi-family | - | - | - | - | - |
| Commercial Real Estate | 19 | - | - | 201 | 424 |
| Home Equity – closed end | 8 | 26 | - | 159 | 69 |
| Home Equity – open end | 370 | 51 | 80 | 68 | - |
| Commercial & Industrial – Non Real Estate | 293 | - | 385 | 986 | 776 |
| Consumer | 37 | 32 | 33 | 173 | 45 |
| Dealer Finance | 1,081 | 251 | 107 | 17 | - |
| Credit Cards | 74 | 60 | 46 | 121 | 71 |
| Total loan losses | 2,261 | 601 | 2,470 | 4,025 | 3,347 |
| Recoveries: | | | | | |
| Construction/land development | 7 | 85 | 223 | 40 | 192 |
| Farmland | - | - | - | - | 3 |
| Real Estate | 4 | 37 | - | - | - |
| Multi-family | - | - | - | - | - |
| Commercial Real Estate | 135 | 65 | 108 | 42 | 48 |
| Home Equity – closed end | - | 6 | - | - | - |
| Home Equity – open end | 120 | - | - | 29 | - |
| Commercial & Industrial – Non Real Estate | 267 | 62 | 356 | 127 | 62 |
| Consumer | 19 | 32 | 33 | 14 | 27 |
| Dealer Finance | 417 | 24 | 6 | - | - |
| Credit Cards | 54 | 46 | 35 | 28 | 32 |
| Total recoveries | 1,023 | 357 | 761 | 280 | 364 |
| Net loan losses | (1,238) | (244) | (1,709) | (3,745) | (2,983) |
| Balance at end of period | $7,543 | $8,781 | $8,725 | $8,184 | $8,154 |
| Allowance for loan losses as a percentage of loans | 1.27% | 1.61% | 1.68% | 1.71% | 1.75% |
| Net loan losses to loans held for investment | .21% | .04% | .33% | .78% | .64% |

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PART II, Continued

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

Loan Losses and the Allowance for Loan Losses, continued

ALLOCATION OF THE ALLOWANCE FOR LOAN LOSSES

| | 2016 | | 2015 | | 2014 | | 2013 | | 2012 | |
|---|---|---|---|---|---|---|---|---|---|---|
| Allowance for loan losses: (in thousands) | Balance | Percentage of Loans in Each Category | Balance | Percentage of Loans in Each Category | Balance | Percentage of Loans in Each Category | Balance | Percentage of Loans in Each Category | Balance | Percentage of Loans in Each Category |
| Construction/Land Development | $3,381 | 44.82% | $4,442 | 50.59% | $4,738 | 54.30% | $4,007 | 48.96% | $2,771 | 33.98% |
| Real Estate | 843 | 11.18% | 806 | 9.18% | 623 | 7.14% | 400 | 4.89% | 924 | 11.33% |
| Commercial, Financial and Agricultural | 1,348 | 17.88% | 1,666 | 18.97% | 1,337 | 15.33% | 2,239 | 27.36% | 3,187 | 39.09% |
| Consumer | 1,426 | 18.90% | 1,059 | 12.06% | 1,685 | 19.31% | 905 | 11.06% | 253 | 3.10% |
| Home Equity | 545 | 7.22% | 808 | 9.20% | 342 | 3.92% | 633 | 7.73% | 1,019 | 12.50% |
| Total | $7,543 | 100.00% | $8,781 | 100.00% | $8,725 | 100.00% | $8,184 | 100.00% | $8,154 | 100.00% |

PART II, Continued

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

Deposits and Borrowings

The average deposit balances and average rates paid for 2016, 2015 and 2014 were as follows:

Average Deposits and Rates Paid (Dollars in thousands)

| | December 31, | | | | | |
|---|---|---|---|---|---|---|
| | 2016 | | 2015 | | 2014 | |
| | Amount | Rate | Amount | Rate | Amount | Rate |
| Noninterest-bearing | $141,180 | | $125,665 | | $107,647 | |
| Interest-bearing: | | | | | | |
| Interest Checking | $113,525 | .44% | $112,334 | .48% | $117,396 | .57% |
| Savings Accounts | 100,298 | .44% | 76,491 | .28% | 60,460 | .20% |
| Time Deposits: | | | | | | |
| CDARS | 3,317 | .33% | 11,247 | .18% | 19,771 | .21% |
| $100,000 or more | 51,048 | 1.00% | 66,719 | .55% | 74,743 | .61% |
| Less than $100,000 | 105,856 | .87% | 93,863 | 1.08% | 101,419 | 1.19% |
| Total interest-bearing | 374,044 | .64% | 360,654 | .60% | 373,789 | .67% |
| Total deposits | $515,224 | .46% | $486,319 | .44% | $481,436 | .52% |

Average noninterest-bearing demand deposits, which are comprised of checking accounts, increased $15,515,000 or 12.35% from $125,665,000 at during 2015 to $141,180,000 during 2016. Average interest-bearing deposits, which include interest checking accounts, money market accounts, regular savings accounts and time deposits, increased $13,390,000 or 3.71% from $360,654,000 at December 31, 2015 to $374,044,000 at December 31, 2016. Total average interest checking (including money market) account balances increased $1,191,000 or 1.06% from $112,334,000 at December 31, 2015 to $113,525,000 at December 31, 2016. Total average savings account balances increased $23,807,000 or 31.12% from $76,491,000 at December 31, 2015 to $100,298,000 at December 31, 2016.

Average time deposits decreased $11,608,000 or 6.76% from $171,829,000 at December 31, 2015 to $160,221,000 at December 31, 2016.

The maturity distribution of certificates of deposit of $100,000 or more is as follows:

| (Actual Dollars in thousands) | 2016 | 2015 |
|---|---|---|
| Less than 3 months | $2,379 | $5,238 |
| 3 to 6 months | 4,332 | 12,478 |
| 6 to 12 months | 7,624 | 8,008 |
| 1 year to 5 years | 36,534 | 27,901 |
| Total | $50,869 | $53,625 |

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PART II, Continued

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

Deposits and Borrowings, continued

Non-deposit borrowings include federal funds purchased and Federal Home Loan Bank (FHLB) borrowings, (both short term and long term). Non-deposit borrowings are an important source of funding for the Bank. These sources assist in managing short and long term funding needs, often at rates that are more favorable than raising additional funds within the deposit portfolio.

Borrowings from the Federal Home Loan Bank are used to support the Bank's lending program and allow the Bank to manage interest rate risk by laddering maturities and matching funding terms to the terms of various loan types in the loan portfolio. The Company borrowed $20,000,000 during 2016, with maturities ranging from 5 to 10 years, to replace maturities and lock in lower rates. This compares to $40,000,000 borrowed in 2015 and $10,000,000 in 2014. Repayment of amortizing and fixed maturity loans through FHLB totaled $3,923,000 during 2016. These long-term loans carry an average rate of 1.80% at December 31, 2016.

Contractual Obligations and Scheduled Payments (dollars in thousands)

| | December 31, 2016 | | | | |
|---|---|---|---|---|---|
| | Less than One Year | One Year Through Three Years | Three Years Through Five Years | More than Five Years | Total |
| Federal funds purchased | $- | $- | $- | $- | $- |
| FHLB Short term advances | 40,000 | - | - | - | 40,000 |
| FHLB long term advances | 3,321 | 16,357 | 25,862 | 18,697 | 64,237 |
| Total | $43,321 | $16,357 | $25,862 | $18,697 | $104,237 |

See Note 11 (Short Term Debt) and Note 12 (Long Term Debt) to the Consolidated Financial Statements for a discussion of the rates, terms, and conversion features on these advances.

Stockholders' Equity

Total stockholders' equity increased $3,732,000 or 4.50% in 2016. Net income totaled $9,568,000, noncontrolling interest net income totaled $194,000, issuance of common stock totaled $183,000, changes in other comprehensive income decreased $485,000, and capital was reduced by dividends ($3.114 million), repurchases of common stock of $578,000, repurchase of preferred stock $1,961,000 and minority interest distributions of $74,000. As of December 31, 2016, book value per common share was $24.18 compared to $22.38 as of December 31, 2015. Dividends are paid to stockholders on a quarterly basis in uniform amounts unless unexpected fluctuations in net income indicate a change to this policy is needed.

Banking regulators have established a uniform system to address the adequacy of capital for financial institutions. The rules require minimum capital levels based on risk-adjusted assets. Simply stated, the riskier an entity's investments, the more capital it is required to maintain. The Bank is required to maintain these minimum capital levels. In March 2015, the Bank implemented the Basel III capital requirements, which introduced the Common Equity Tier I ratio in addition to the two previous capital guidelines of Tier I capital (referred to as core capital) and Tier II capital (referred to as supplementary capital). At December 31, 2016, the Bank had Common Equity Tier I capital of 13.86%, Tier I capital of 13.86% of risk weighted assets and combined Tier I and II capital of 15.08% of risk weighted assets. Regulatory minimums at this date were 4.5%, 6% and 8%, respectively. The Bank has maintained capital levels far above the minimum requirements throughout the year. In the unlikely event that such capital levels are not met, regulatory agencies are empowered to require the Bank to raise additional capital and/or reallocate present capital.

In addition, the regulatory agencies have issued guidelines requiring the maintenance of a capital leverage ratio. The leverage ratio is computed by dividing Tier I capital by average total assets. The regulators have established a minimum of 4% for this ratio, but can increase the minimum requirement based upon an institution's overall financial condition. At December 31, 2016, the Bank reported a leverage ratio of 11.83%. The Bank's leverage ratio was also substantially above the minimum.

PART II, Continued

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

Market Risk Management

Most of the Company’s net income is dependent on the Bank’s net interest income. Rapid changes in short-term interest rates may lead to volatility in net interest income resulting in additional interest rate risk to the extent that imbalances exist between the maturities or repricing of interest bearing liabilities and interest earning assets. The Company’s net interest margin decreased .09% in 2016 following an increase of .13% in 2015. This decrease can be attributed to the growth in savings accounts in 2016. These borrowings were added to support loan growth and lock in lower rates for the future. In December 2016, the Federal Open Market Committee elected to raise the short-term rates target .25% to .50 to .75% due to expanding economic activity.

Net interest income is also affected by changes in the mix of funding that supports earning assets. For example, higher levels of non-interest bearing demand deposits and leveraging earning assets by funding with stockholder’s equity would result in greater levels of net interest income than if most of the earning assets were funded with higher cost interest-bearing liabilities, such as certificates of deposit.

Liquid assets, which include cash and cash equivalents, federal funds sold, interest bearing deposits and short term investments averaged $24,817,000 for 2016. The Bank historically has had a stable core deposit base and, therefore, does not have to rely on volatile funding sources. Because of the stable core deposit base, changes in interest rates should not have a significant effect on liquidity. The Bank's membership in the Federal Home Loan Bank has historically provided liquidity as the Bank borrows money that is repaid over a five to ten-year period and uses the money to make fixed rate loans. The matching of the long-term receivables and liabilities helps the Bank reduce its sensitivity to interest rate changes. The Company reviews its interest rate gap periodically and makes adjustments as needed. There are no off-balance sheet items that will impair future liquidity.

The following table depicts the Company’s interest rate sensitivity, as measured by the repricing of its interest sensitive assets and liabilities as of December 31, 2016. As the notes to the table indicate, the data was based in part on assumptions as to when certain assets or liabilities would mature or reprice. The analysis indicates an asset sensitive one-year cumulative GAP position of 23.71% of total earning assets, compared to 15.59% in 2015. Approximately 45.98% of rate sensitive assets and 30.97% of rate sensitive liabilities are subject to repricing within one year. Short term assets (less than one year) increased $62,185,000 during the year, while total earning assets increased $71,252,000. The increase is attributed to growth in loans held for investment of $47,506,000 as well as investment securities of $11,736,000. Growth in the loans held for investment portfolio was concentrated in real estate secured loans, commercial and the Dealer Finance division. Short term liabilities increased $15,046,000, while total interest bearing liabilities increased $61,707,000. The increase in short term liabilities is largely due to an increase in short term debt to fund Loans Held for Sale. Due to the relatively flat yield curve, management has kept deposit rates low.

PART II, Continued

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

Market Risk Management, continued

The following GAP analysis shows the time frames as of December 31, 2016, in which the Company's assets and liabilities are subject to repricing:

| (Dollars in thousands) | 1-90 Days | 91-365 Days | 1-5 Years | Over 5 Years | Not Classified | Total |
|---|---|---|---|---|---|---|
| Rate Sensitive Assets: | | | | | | |
| Loans held for investment | $92,760 | $125,333 | $328,585 | $42,136 | $- | $588,814 |
| Loans held for sale | 62,735 | - | - | - | - | 62,735 |
| Federal funds sold | 7,926 | - | - | - | - | 7,926 |
| Investment securities | 20,000 | 4,014 | 125 | 634 | 135 | 24,908 |
| Credit cards | 2,822 | - | - | - | - | 2,822 |
| Interest bearing bank deposits | 674 | - | - | - | - | 674 |
| Total | 186,917 | 129,347 | 328,710 | 42,770 | 135 | 687,879 |
| Rate Sensitive Liabilities: | | | | | | |
| Interest bearing demand deposits | - | 33,610 | 70,759 | 18,574 | - | 122,943 |
| Savings deposits | - | 22,060 | 66,178 | 22,059 | - | 110,297 |
| Certificates of deposit $100,000 and over | 2,379 | 11,922 | 36,568 | - | - | 50,869 |
| Other certificates of deposit | 11,624 | 28,275 | 66,460 | - | - | 106,359 |
| Total Deposits | 14,003 | 95,867 | 239,965 | 40,633 | - | 390,468 |
| Short-term debt | 40,000 | - | - | - | - | 40,000 |
| Long-term debt | 1,107 | 2,214 | 42,220 | 18,696 | - | 64,237 |
| Total | 55,110 | 98,081 | 282,185 | 59,329 | - | 494,705 |
| Discrete Gap | 131,807 | 31,266 | 46,525 | (16,559) | 135 | 193,174 |
| Cumulative Gap | 131,807 | 163,073 | 209,598 | 193,039 | 193,174 | |
| As a % of Earning Assets | 19.16% | 23.71% | 30.47% | 28.06% | 28.08% | |

In preparing the above table, no assumptions are made with respect to loan prepayments or deposit run off. Loan principal payments are included in the earliest period in which the loan matures or can be repriced. Principal payments on installment loans scheduled prior to maturity are included in the period of maturity or repricing. Proceeds from the redemption of investments and deposits are included in the period of maturity. Estimated maturities on deposits which have no stated maturity dates were derived from guidance contained in FDICIA 305.

PART II, Continued

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

Quarterly Results (unaudited)

The table below lists the Company's quarterly performance for the years ended December 31, 2016 and 2015:

| | 2016 | | | | |
|---|---|---|---|---|---|
| (Dollars in thousands) | Fourth | Third | Second | First | Total |
| Interest and Dividend Income | 8,332 | 8,198 | 7,931 | 7,634 | 32,095 |
| Interest Expense | 954 | 969 | 862 | 814 | 3,599 |
| Net Interest Income | 7,378 | 7,229 - | 7,069 | 6,820 | 28,496 |
| Provision for Loan Losses | - | | - | - | - |
| Net Interest Income after Provision for Loan Losses | 7,378 | 7,229 | 7,069 | 6,820 | 28,496 |
| Non-Interest Income | 925 | 1,054 | 986 | 699 | 3,664 |
| Non-Interest Expense | 4,833 | 4,962 | 4,772 | 4,732 | 19,299 |
| Income before income taxes | 3,470 | 3,321 | 3,283 | 2,787 | 12,861 |
| Income Tax Expense | 912 | 655 | 839 | 693 | 3,099 |
| Noncontrolling interest | (40) | (64) | (86) | (4) | (194) |
| Net Income | 2,518 | 2,602 | 2,358 | 2,090 | 9,568 |
| Net Income Per Average Common Share Basic | $0.74 | $0.75 | $0.68 | $0.60 | $2.77 |

| | 2015 | | | | |
|---|---|---|---|---|---|
| (Dollars in thousands) | Fourth | Third | Second | First | Total |
| Interest and Dividend Income | 7,518 | 7,451 | 7,373 | 7,011 | 29,353 |
| Interest Expense | 771 | 722 | 698 | 685 | 2,876 |

| | | | | | |
|---|---|---|---|---|---|
| Net Interest Income | 6,747 | 6,729 | 6,675 | 6,326 | 26,477 |
| Provision for Loan Losses | - | - | - | 300 | 300 |
| Net Interest Income after Provision for Loan Losses | 6,747 | 6,729 | 6,675 | 6,026 | 26,177 |
| Non-Interest Income | 862 | 836 | 833 | 745 | 3,276 |
| Non-Interest Expense | 4,614 | 4,494 | 4,496 | 4,382 | 17,986 |
| Income before income taxes | 2,995 | 3,071 | 3,012 | 2,389 | 11,467 |
| Income Tax Expense | 766 | 842 | 786 | 492 | 2,886 |
| Noncontrolling interest | (49) | (39) | (50) | (26) | (164) |
| Net Income | 2,180 | 2,190 | 2,176 | 1,871 | 8,417 |
| Net Income Per Average Common Share Basic | $0.62 | $0.63 | $0.62 | $0.53 | $2.40 |

Item 7A Quantitative and Qualitative Disclosures about Market Risk

Not required.

Item 8. Financial Statements and Supplementary Data

F & M Bank Corp. and Subsidiaries
Consolidated Balance Sheets (dollars in thousands, except share and per share data)
As of December 31, 2016 and 2015

| | 2016 | 2015 |
|---|---|---|
| Assets | | |
| Cash and due from banks | $7,755 | $6,923 |
| Money market funds | 674 | 1,596 |
| Federal funds sold | 7,926 | - |
| Cash and cash equivalents | 16,355 | 8,519 |
| Securities: | | |
| Held to maturity - fair value of $125 in 2016 and 2015 | 125 | 125 |
| Available for sale | 24,783 | 13,047 |
| Other investments | 14,503 | 12,157 |
| Loans held for sale | 62,735 | 57,806 |
| Loans held for investment | 591,636 | 544,053 |
| Less: allowance for loan losses | (7,543) | (8,781) |
| Net loans held for investment | 584,093 | 535,272 |
| Other real estate owned | 2,076 | 2,128 |
| Bank premises and equipment, net | 10,268 | 7,542 |
| Interest receivable | 1,785 | 1,709 |
| Goodwill | 2,670 | 2,670 |
| Bank owned life insurance | 13,513 | 13,046 |
| Other assets | 11,983 | 11,337 |
| Total Assets | $744,889 | $665,357 |
| Liabilities | | |
| Deposits: | | |
| Noninterest bearing | $146,617 | $134,787 |
| Interest bearing | 390,468 | 359,883 |
| Total deposits | 537,085 | 494,670 |
| Short-term debt | 40,000 | 24,954 |
| Accrued liabilities | 16,885 | 14,622 |
| Long-term debt | 64,237 | 48,161 |
| Total Liabilities | 658,207 | 582,406 |
| Commitments and contingencies | | |

| | | |
|---|---|---|
| Stockholders' Equity | | |
| Preferred Stock $25 par value, 400,000 shares authorized, 327,350 and 400,000 shares issued and outstanding at December 31, 2016 and 2015, respectively | 7,609 | 9,425 |
| Common stock $5 par value, 6,000,000 shares authorized, 3,270,315 and 3,285,404 shares issued and outstanding at December 31, 2016 and 2015, respectively | 16,352 | 16,427 |
| Additional paid in capital – common stock | 10,684 | 11,149 |
| Retained earnings | 54,509 | 48,056 |
| Noncontrolling interest in consolidated subsidiaries | 693 | 573 |
| Accumulated other comprehensive loss | (3,165) | (2,680) |
| Total Stockholders' Equity | 86,682 | 82,950 |
| Total Liabilities and Stockholders' Equity | $744,889 | $665,357 |

See accompanying Notes to the Consolidated Financial Statements.

F & M Bank Corp. and Subsidiaries
Consolidated Statements of Income (dollars in thousands, except share and per share data)
For the years ended 2016, 2015 and 2014

| | 2016 | 2015 | 2014 |
|---|---|---|---|
| Interest and Dividend Income | | | |
| Interest and fees on loans held for investment | $29,816 | $27,930 | $26,211 |
| Interest from loans held for sale | 1,888 | 1,100 | 312 |
| Interest from money market funds and federal funds sold | 37 | 21 | 44 |
| Interest from debt securities – taxable | 354 | 302 | 205 |
| Total interest and dividend income | 32,095 | 29,353 | 26,772 |
| Interest Expense | | | |
| Total interest on deposits | 2,380 | 2,153 | 2,490 |
| Interest from short-term debt | 55 | 69 | 9 |
| Interest from long-term debt | 1,164 | 654 | 1,149 |
| Total interest expense | 3,599 | 2,876 | 3,648 |
| Net Interest Income | 28,496 | 26,477 | 23,124 |
| Provision for Loan Losses | - | 300 | 2,250 |
| Net Interest Income After Provision for Loan Losses | 28,496 | 26,177 | 20,874 |
| Noninterest Income | | | |
| Service charges on deposit accounts | 1,174 | 963 | 1,034 |
| Insurance, other commissions and mortgage banking, net | 1,087 | 1,058 | 635 |
| Other operating income | 1,658 | 1,401 | 1,394 |
| Income from bank owned life insurance | 476 | 473 | 467 |
| Low income housing partnership losses | (731) | (619) | (608) |
| Total noninterest income | 3,664 | 3,276 | 2,922 |
| Noninterest Expenses | | | |
| Salaries | 8,570 | 7,816 | 6,898 |
| Employee benefits | 2,552 | 2,239 | 1,911 |
| Occupancy expense | 746 | 679 | 622 |
| Equipment expense | 702 | 651 | 590 |
| FDIC insurance assessment | 388 | 587 | 690 |
| Other real estate owned, net | 86 | 566 | 407 |
| Other operating expenses | 6,255 | 5,447 | 4,538 |
| Total noninterest expenses | 19,299 | 17,986 | 15,656 |
| Income before income taxes | 12,861 | 11,467 | 8,140 |
| Income Tax Expense | 3,099 | 2,886 | 2,293 |
| Net Income | 9,762 | 8,581 | 5,847 |

| | | | |
|---|---|---|---|
| Net Income attributable to Noncontrolling interest | (194) | (164) | (45) |
| Net Income attributable to F & M Bank Corp. | $9,568 | $8,417 | $5,802 |
| | | | |
| Dividends paid/accumulated on preferred stock | 487 | 510 | 128 |
| Net income available to common stockholders | $9,081 | $7,907 | $5,674 |
| | | | |
| Per Common Share Data | | | |
| Net income - basic | 2.77 | 2.40 | 1.82 |
| Net income - diluted | 2.57 | 2.25 | 1.80 |
| Cash dividends on common stock | .80 | .73 | .68 |
| Weighted average common shares outstanding – basic | 3,282,335 | 3,290,812 | 3,119,333 |
| Weighted average common shares outstanding – diluted | 3,716,591 | 3,735,212 | 3,229,942 |

See accompanying Notes to the Consolidated Financial Statements.

F & M BANK CORP.
Consolidated Statements of Comprehensive Income (dollars in thousands)
For the years ended 2016, 2015 and 2014

| | Years Ended December 31, | | |
|---|---|---|---|
| | 2016 | 2015 | 2014 |
| Net Income | 9,762 | 8,581 | 5,847 |
| Other comprehensive income (loss): | | | |
| Pension plan adjustment | (738) | (537) | (2,146) |
| Tax effect | 251 | 183 | 730 |
| Pension plan adjustment, net of tax | (487) | (354) | (1,416) |
| Unrealized holding gains on available-for-sale securities | 3 | 2 | 22 |
| Tax effect | (1) | (1) | (7) |
| Unrealized holding gains, net of tax | 2 | 1 | 15 |
| Total other comprehensive income (loss) | (485) | (353) | (1,401) |
| Total comprehensive income | $9,277 | $8,228 | $4,446 |
| Comprehensive income attributable to noncontrolling interest | $194 | $164 | $45 |
| Comprehensive income attributable to F&M Bank Corp. | $9,083 | $8,064 | $4,401 |

See accompanying Notes to the Consolidated Financial Statements.

F & M Bank Corp. and Subsidiaries
Consolidated Statements of Changes in Stockholders' Equity (dollars in thousands, except share and per share data)
For the years ended December 31, 2016, 2015 and 2014

| | Preferred Stock | Common Stock | Additional Paid in Capital | Retained Earnings | Noncontrolling Interest | Accumulated Other Comprehensive Income (Loss) | Total |
|---|---|---|---|---|---|---|---|
| Balance December 31, 2013 | $- | $12,559 | $3,104 | $38,985 | $419 | $(926) | $54,141 |
| Net income | | | | 5,802 | 45 | | 5,847 |
| Other comprehensive loss | | | | | | (1,401) | (1,401) |
| Distributions to noncontrolling interest | | | | | (38) | | (38) |
| Dividends on preferred stock | | | | (128) | | | (128) |
| Dividends on common stock | | | | (2,105) | | | (2,105) |
| Preferred stock issued (400,000 shares) | 9,425 | | | | | | 9,425 |
| Common stock issued (780,031 shares) | - | 3,900 | 8,156 | - | - | - | 12,056 |
| Balance December 31, 2014 | $9,425 | $16,459 | $11,260 | $42,554 | $426 | $(2,327) | $77,797 |
| Net income | | | | 8,417 | 164 | | 8,581 |
| Other comprehensive loss | | | | | | (353) | (353) |
| Distributions to noncontrolling interest | | | | | (17) | | (17) |
| Dividends on preferred stock | | | | (510) | | | (510) |
| Dividends on common stock | | | | (2,405) | | | (2,405) |
| Common stock repurchased (13,277 shares) | | (67) | (223) | | | | (290) |
| Common stock issued (6,916 shares) | | 35 | 112 | - | - | - | 147 |

| | | | | | | | |
|---|---|---|---|---|---|---|---|
| Balance December 31, 2015 | $9,425 | $16,427 | $11,149 | $48,056 | $573 | $(2,680) | $82,950 |
| Net income | | | | 9,568 | 194 | | 9,762 |
| Other comprehensive loss | | | | | | (485) | (485) |
| Distributions to noncontrolling interest | | | | | (74) | | (74) |
| Dividends on preferred stock | | | | (487) | | | (487) |
| Dividends on common stock | | | | (2,628) | | | (2,628) |
| Common stock repurchased (22,583 shares) | | (112) | (466) | | | | (578) |
| Common stock issued (7,494 shares) | | 37 | 146 | | | | 183 |
| Preferred stock repurchased (72,650 shares) | (1,816) | | (145) | | | | (1,961) |
| Balance, December 31, 2016 | $7,609 | $16,352 | $10,684 | $54,509 | $693 | $(3,165) | $86,682 |

See accompanying Notes to the Consolidated Financial Statements.

F & M Bank Corp. and Subsidiaries
Consolidated Statements of Cash Flows (dollars in thousands)
For the years ended December 31, 2016, 2015 and 2014

| | 2016 | 2015 | 2014 |
|---|---|---|---|
| Cash Flows from Operating Activities | | | |
| Net income | $9,568 | $8,417 | $5,802 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | | |
| Depreciation | 801 | 709 | 612 |
| Amortization of securities | 109 | 147 | 76 |
| Sale of loans held for sale originated | 70,334 | 75,365 | 56,211 |
| Loans held for sale originated | (66,779) | (77,152) | (56,045) |
| Provision for loan losses | - | 300 | 2,250 |
| Benefit (expense) for deferred taxes | 9 | 341 | (515) |
| (Increase) in interest receivable | (76) | (34) | (177) |
| Increase in other assets | (444) | (457) | (1,474) |
| Increase in accrued liabilities | 1,690 | 1,480 | 1,160 |
| Amortization of limited partnership investments | 731 | 627 | 608 |
| Loss on sale and valuation adjustments of other real estate owned | 19 | 489 | 319 |
| Income from life insurance investment | (476) | (473) | (467) |
| Net Cash Provided by Operating Activities | 15,486 | 9,759 | 8,360 |
| Cash Flows from Investing Activities | | | |
| Proceeds from maturities of securities available for sale | 32,218 | 8,243 | 27,495 |
| Proceeds from maturities of securities held to maturity | - | - | 106 |
| Purchases of securities available for sale and other investments | (47,137) | (12,040) | (11,957) |
| Capital improvements to other real estate owned | (24) | - | - |
| Purchases of securities held to maturity | - | - | (125) |
| Net increase in loans held for investment | (49,386) | (25,892) | (43,642) |
| Net (increase) decrease in loans held for sale participations | (8,483) | (42,637) | (9,744) |
| Net purchase of property and equipment | (3,527) | (1,793) | (546) |
| Proceeds from sale of other real estate owned | 623 | 688 | 986 |
| Net Cash Provided by (Used in) Investing Activities | (75,716) | (73,431) | (37,427) |
| Cash Flows from Financing Activities | | | |
| Net change in deposits | 42,415 | 3,165 | 27,356 |
| Net change in short-term debt | 15,046 | 10,596 | 10,935 |
| Dividends paid in cash | (3,115) | (2,915) | (2,232) |
| Proceeds from long-term debt | 20,000 | 40,000 | 10,000 |
| Proceeds from issuance of preferred stock | - | - | 6,831 |
| Proceeds from issuance of common stock | 183 | 146 | 12,056 |
| Repurchase of preferred stock | (1,961) | | |
| Repurchase of common stock | (578) | (289) | |
| Repayments of long-term debt | (3,924) | (1,714) | (19,222) |
| Net Cash Provided by (Used in) Financing Activities | 68,066 | 48,989 | 45,724 |

| | | | |
|---|---|---|---|
| Net Increase (Decrease) in Cash and Cash Equivalents | 7,836 | (14,683) | 16,657 |
| | | | |
| Cash and Cash Equivalents, Beginning of Year | 8,519 | 23,202 | 6,545 |
| Cash and Cash Equivalents, End of Year | $16,355 | $8,519 | $23,202 |
| | | | |
| Supplemental Cash Flow information: | | | |
| Cash paid for: | | | |
| Interest | $3,573 | $2,854 | $3,703 |
| Income taxes | 2,300 | 1,500 | 1,607 |
| Supplemental non-cash disclosures: | | | |
| Transfers from loans to other real estate owned | 566 | 125 | 2,915 |
| Loans originated for the sale of other real estate owned | - | (328) | (780) |
| Conversion of subordinated debt to preferred stock | - | - | 2,594 |

See accompanying Notes to the Consolidated Financial Statements.

F & M Bank Corp. and Subsidiaries
Notes to the Consolidated Financial Statements
December 31, 2016 and 2015

NOTE 1
NATURE OF OPERATIONS:

F & M Bank Corp. (the “Company”), through its subsidiary Farmers & Merchants Bank (the “Bank”), operates under a charter issued by the Commonwealth of Virginia and provides commercial banking services. As a state chartered bank, the Bank is subject to regulation by the Virginia Bureau of Financial Institutions and the Federal Reserve Bank. The Bank provides services to customers located mainly in Rockingham, Shenandoah, Page and Augusta Counties in Virginia, and the adjacent county of Hardy, West Virginia. Services are provided at eleven branch offices, a Dealer Finance Division and a loan production office. The Company offers insurance, mortgage lending and financial services through its subsidiaries, TEB Life Insurance, Inc., Farmers & Merchants Financial Services, Inc, and VBS Mortgage, LLC (VBS). On January 1, 2017, the Company purchased VS Title, a title company headquartered in Harrisonburg, VA with offices in Harrisonburg, Fishersville and Charlottesville, VA.

NOTE 2
SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

The accounting and reporting policies of the Company and its subsidiaries conform to generally accepted accounting principles and to accepted practice within the banking industry. The following is a summary of the more significant policies:

Principles of Consolidation

The consolidated financial statements include the accounts of Farmers and Merchants Bank, TEB Life Insurance Company, Farmers & Merchants Financial Services, Inc. and VBS Mortgage, LLC, (net of noncontrolling interest). Significant inter-company accounts and transactions have been eliminated.

Use of Estimates in the Preparation of Financial Statements

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America ("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, goodwill, other than temporary impairment, the valuation of deferred tax assets and liabilities, pension accounting and the valuation of foreclosed real estate.

Cash and Cash Equivalents

Cash and cash equivalents include cash on hand, money market funds whose initial maturity is ninety days or less and Federal funds sold.

Securities

Certain debt securities that management has the positive intent and ability to hold to maturity are classified as “held to maturity” and recorded at amortized cost. Securities not classified as held to maturity or trading, including equity securities with readily determinable fair values, are classified as “available for sale” and recorded at fair value, with

unrealized gains and losses excluded from earnings and reported in other comprehensive income. Purchase premiums and discounts are recognized in interest income using the interest method over the terms of the securities. Gains and losses on the sale of securities are recorded on the trade date and are determined using the specific identification method. The Company has no securities classified as trading.

The Company follows the accounting guidance related to recognition and presentation of other-than-temporary impairment. The guidance specifies that if (a) an entity does not have the intent to sell a debt security prior to recovery and (b) it is more likely than not that the entity will not have to sell the debt security prior to recovery, the security would not be considered other-than-temporarily impaired, unless there is a credit loss. When criteria (a) and (b) are met, the entity will recognize the credit component of other-than-temporary impairment of a debt security in earnings and the remaining portion in other comprehensive income.

F & M Bank Corp. and Subsidiaries
Notes to the Consolidated Financial Statements
December 31, 2016 and 2015

NOTE 2
SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED):

Securities, continued

For held-to-maturity debt securities, the amount of other-than-temporary impairment recorded in other comprehensive income for the noncredit portion of a previous other-than-temporary impairment is amortized prospectively over the remaining life of the security on the basis of the timing of future estimated cash flows of the security.

For equity securities, when the Company has decided to sell an impaired available-for-sale security and the Company does not expect the fair value of the security to fully recover before the expected time of sale, the security is deemed other-than-temporarily impaired in the period in which the decision to sell is made. The Company recognizes an impairment loss when the impairment is deemed other than temporary even if a decision to sell has not been made.

Other Investments

The Company periodically invests in low income housing partnerships whose primary benefit is the distribution of federal income tax credits to partners. The Company recognizes these benefits and the cost of the investments over the life of the partnership (usually 15 years). In addition, state and federal historic rehabilitation credits are generated from some of the partnerships. Amortization of these investments is prorated based on the amount of benefits received in each year to the total estimated benefits over the life of the projects. The effective yield method is used to record the income statement effects of these investments.

Other Investment Securities
Due to the nature and restrictions placed on the Company's investment in common stock of the Federal Home Loan Bank of Atlanta ("FHLB") and the Federal Reserve Bank of Richmond, these securities are considered restricted and carried at cost.

Income Taxes

Income tax accounting guidance results in two components of income tax expense: current and deferred. Current income tax expense reflects taxes to be paid or refunded for the current period by applying the provisions of the enacted tax law to the taxable income or excess of deductions over revenues. The Company determines deferred income taxes using the liability (or balance sheet) method. Under this method, the net deferred tax asset or liability is based on the tax effects of the differences between the book and tax bases of assets and liabilities, and enacted changes in tax rates and laws are recognized in the period in which they occur.

Deferred income tax expense results from changes in deferred tax assets and liabilities between periods. Deferred tax assets are recognized if it is more likely than not, based on the technical merits, that the tax position will be realized or sustained upon examination. The term more likely than not means a likelihood of more than 50 percent; the terms examined and upon examination also include resolution of the related appeals or litigation processes, if any. A tax position that meets the more-likely-than-not recognition threshold is initially and subsequently measured as the largest amount of tax benefit that has a greater than 50 percent likelihood of being realized upon settlement with a taxing authority that has full knowledge of all relevant information. The determination of whether or not a tax position has met the more-likely-than-not recognition threshold considers the facts, circumstances, and information available at the reporting date and is subject to management’s judgment. Deferred tax assets are reduced by a valuation allowance if,

based on the weight of evidence available, it is more likely than not that some portion or all of a deferred tax asset will not be realized.

The Company recognizes interest and penalties on income taxes as a component of income tax expense.

F & M Bank Corp. and Subsidiaries
Notes to the Consolidated Financial Statements
December 31, 2016 and 2015

NOTE 2
SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED):

Loans Held for Investment

The Company, through its banking subsidiary, provides mortgage, commercial, and consumer loans to customers. A substantial portion of the loan portfolio is represented by mortgage loans, particularly commercial and residential mortgages. The ability of the Company's debtors to honor their contracts is largely dependent upon the real estate and general economic conditions in the Company's market area.

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 outstanding unpaid principal balance adjusted for the allowance for loan losses, and any unearned income. Interest income is accrued on the unpaid principal balance. The accrual of interest on loans is generally discontinued at the time the loan is 90 days delinquent unless the credit is well-secured and in process of collection. Loans are typically charged off when the loan is 120 days past due, unless secured and in process of collection. Loans are placed on nonaccrual status or charged-off at an earlier date if collection of principal or interest is considered doubtful.

The Company's loans are grouped into eleven segments: construction/land development, farmland, real estate, multi-family, commercial real estate, home equity – closed end, home equity – open end, commercial & industrial – non-real estate, consumer, credit cards and dealer finance. Each segment is subject to certain risks that influence the establishment of pricing, loan structures, approval requirements, reserves, and ongoing credit management. The Company does not segregate the portfolio further.

Construction and land development loans are subject to general risks from changing commercial building and housing market trends and economic conditions that may impact demand for completed properties and the costs of completion. Completed properties that do not sell or become leased within originally expected timeframes may impact the borrower's ability to service the debt. These risks are measured by market-area unemployment rates, bankruptcy rates, housing and commercial building market trends, and interest rates. Risks specific to the borrower are also evaluated, including previous repayment history, debt service ability, and current and projected loan-to value ratios for the collateral.

Farmland loans are loans secured by agricultural property. These loans are subject to risks associated with the value of the underlying farmland and the cash flows of the borrower's farming operations.

Multifamily loans are loans secured by multi-unit residential property. These loans are subject to risks associated with the value of the underlying property as well as the successful operation and management of the property.

Real estate loans are for consumer residential real estate where the credit quality is subject to risks associated with the borrower's repayment ability and collateral value, measured generally by analyzing local unemployment and bankruptcy trends, and local housing market trends and interest rates. Risks specific to a borrower are determined by previous repayment history, loan-to-value ratios, and debt-to-income ratios.

The commercial real estate segment includes loans secured by commercial real estate occupied by the owner/borrower, and commercial real estate leased to non-owners. Loans in the commercial real estate segment are impacted by economic risks from changing commercial real estate markets, rental markets for commercial buildings,

business bankruptcy rates, local unemployment rates and interest rate trends that would impact the businesses housed by the commercial real estate.

The Company's home-equity loan portfolios (closed end and open end) carry risks associated with the creditworthiness of the borrower and changes in loan-to-value ratios. The Company manages these risks through policies and procedures such as limiting loan-to-value at origination, experienced underwriting, and requiring standards for appraisers.

F & M Bank Corp. and Subsidiaries
Notes to the Consolidated Financial Statements
December 31, 2016 and 2015

NOTE 2
SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED):

Loans Held for Investment, continued

Commercial and industrial non-real estate loans are secured by collateral other than real estate, or are unsecured. Credit risk for commercial non-real estate loans is subject to economic conditions, generally monitored by local business bankruptcy trends, interest rates, and borrower repayment ability and collateral value (if secured).

Consumer non-real estate includes non-dealer financed automobile loans and other consumer loans. Certain consumer loans are unsecured, while collateral is obtained for automobile loans and other consumer loans. Credit risk stems primarily from the borrower’s ability to repay. If the loan is secured, the Company analyzes loan-to-value ratios. All consumer non-real estate loans are analyzed for debt-to-income ratios and previous credit history, as well as for general risks for the portfolio, including local unemployment rates, personal bankruptcy rates and interest rates.

Credit card loan portfolios carry risks associated with the creditworthiness of the borrower and changes in the economic environment. The Company manages these risks through policies and procedures such as experienced underwriting, maximum debt to income ratios, and minimum borrower credit scores.

Dealer finance lending generally carries certain risks associated with the values of the collateral and borrower’s ability to repay the loan. The Company focuses its dealer finance lending on used vehicles where substantial depreciation has already occurred thereby minimizing the risk of significant loss of collateral values in the future.

Interest accrued but not collected for loans that are placed on nonaccrual status or charged-off is reversed against interest income. The interest on these loans is accounted for on the cash basis or cost recovery method, until qualifying for return to accrual status. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

A loan is considered past due when a payment of principal or interest or both is due but not paid. Management closely monitors past due loans in timeframes of 30-59 days, 60-89 days, and 90 or more days past due.

These policies apply to all loan portfolio segments.

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

Loans Held for Sale

These loans consist of fixed rate loans made through the Company's subsidiary, VBS Mortgage, and loans purchased from Northpointe Bank, Grand Rapids, MI.

F & M Bank Corp. and Subsidiaries
Notes to the Consolidated Financial Statements
December 31, 2016 and 2015

NOTE 2
SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED):

Loans Held for Sale, continued

VBS Mortgage originates conforming mortgage loans for sale in the secondary market. These loans consist primarily of fixed-rate, single-family residential mortgage loans which meet the underwriting characteristics of the investors. VBS enters into mortgage loan commitments whereby the interest rate on the loan is determined prior to funding (rate lock commitments).

The period of time between issuance of a loan commitment and sale of the loan generally ranges from two to three weeks. VBS protects itself from changes in interest rates through the use of best efforts forward delivery contracts, by committing to sell a loan at the time the borrower commits to an interest rate with the intent that the buyer has assumed the interest rate risk on the loan. As a result, the Company is not generally exposed to significant losses nor will it realize significant gains related to its rate lock commitments due to changes in interest rates. The correlation between the rate lock commitments and the best efforts contracts is very high due to their similarity. The market value of rate lock commitments and best efforts contracts is not readily ascertainable with precision because rate lock commitments and best efforts contracts are not actively traded in stand-alone markets. VBS determines the fair value of rate lock commitments and best efforts contracts by measuring the change in the estimated value of the underlying assets while taking into consideration the probability that the loan will be funded. The fair value of rate lock commitments and best efforts contracts was considered immaterial at December 31, 2016 and 2015. The Bank now provides a warehouse line for VBS after closing, until the loan is purchased by the investor. The average time on the line is two or three weeks These loans are pre-sold with servicing released and no interest is retained after the loans are sold. Because of the short holding period, these loans are carried at the lower of cost or market and no market adjustments were necessary in 2016, 2015, or 2014. Gains on sales of loans and commission expense are recognized at the loan closing date and are included in mortgage banking income, net on the Company’s consolidated income statement.

The Bank participates in a Mortgage Purchase Program with Northpointe Bank (Northpointe), a Michigan banking corporation. Pursuant to the terms of a participation agreement, the Bank purchases participation interests in loans made by Northpointe related to fully underwritten and pre-sold mortgage loans originated by various prescreened mortgage loan originators located throughout the United States. A takeout commitment is in place at the time the loans are purchased. The Bank has participated in similar arrangements since 2003 as a higher yielding alternative to federal funds sold or investment securities. These loans are short-term, residential real estate loans that have an average life in our portfolio of approximately two weeks. The Bank holds these loans during the period of time between loan closing and when the loan is paid off by the ultimate secondary market purchaser. As of December 31, 2016, and 2015, there were $62.6 million and $54.1 million of these loans included in loans held for sale on the Company’s consolidated balance sheet.

Troubled Debt Restructuring

In situations where, for economic or legal reasons related to a borrower's financial condition, management may grant a concession to the borrower that it would not otherwise consider, the related loan is classified as a troubled debt restructuring ("TDR"). Management strives to identify borrowers in financial difficulty early and work with them to modify their loan to more affordable terms before their loan reaches nonaccrual status. These modified terms may include rate reductions, principal forgiveness, payment forbearance and other actions intended to minimize the

economic loss and to avoid foreclosure or repossession of the collateral. In cases where borrowers are granted new terms that provide for a reduction of either interest or principal, management measures any impairment on the restructuring as noted above for impaired loans. The Company has $9.8 million in loans classified as TDRs that are current and performing as of December 31, 2016, and $11.7 million as of December 31, 2015.

F & M Bank Corp. and Subsidiaries
Notes to the Consolidated Financial Statements
December 31, 2016 and 2015

NOTE 2
SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED):

Allowance for Loan and Losses

The allowance for loan losses represents management's estimate of probable losses inherent in the Company's loan portfolio. A provision for estimated losses is charged to earnings to establish and maintain the allowance for loan losses at a level reflective of the estimated credit risk. When management determines that a loan balance or portion of a loan balance is not collectible, the loss is charged against the allowance. Subsequent recoveries, if any, are credited to the allowance.

Management's determination of the adequacy of the allowance is based on an evaluation of the composition of the loan portfolio, the value and adequacy of collateral, current economic conditions, historical loan loss experience, and other risk factors. Management evaluates the allowance each quarter through a methodology that estimates losses on individual impaired loans and evaluates the effect of numerous factors on the credit risk of each segment of loans.

The Company's allowance for loan losses has two basic components: the general allowance and the specific allowance. Each of these components is determined based upon estimates and judgments. The general allowance uses historical loss experience as an indicator of future losses, along with various qualitative factors, including levels and trends in delinquencies, nonaccrual loans, charge-offs and recoveries, trends in volume and terms of loans, effects of changes in underwriting standards, experience of lending staff, economic conditions, and portfolio concentrations.

Except for credit card and dealer finance loans, all loans are assigned an internal risk rating based on certain credit quality indicators. Credit card, consumer and dealer finance loans are monitored based on payment activity. Loss rates are amplified for loans with adverse risk ratings that are not considered impaired. In the general allowance, the historical loss rate is combined with the qualitative factors, resulting in an adjusted loss factor for each segment of loans. The period-end balances for each loan segment are multiplied by the adjusted loss factor. Historical loss rates are combined with qualitative factors resulting in an adjusted loss factor for each segment. Specific allowances are established for individually-evaluated impaired loans based on the excess of the loan balance relative to the fair value of the collateral, if the loan is deemed collateral dependent.

Management believes that the allowance for loan losses is adequate. While management uses available information to recognize losses on loans, future additions to the allowance may be necessary based on changes in economic conditions, particularly those affecting real estate values. In addition, regulatory agencies, as an integral part of their examination process, periodically review the Company's allowance for loan losses. Such agencies may require the Company to recognize additions to the allowance based on their judgments about information available to them at the time of their examination.

Other Real Estate Owned (OREO)

OREO is held for sale and represents real estate acquired through or in lieu of foreclosure. OREO is initially recorded at fair value less costs to sell when acquired, establishing a new cost basis. Physical possession of residential real estate property collateralizing a consumer mortgage loan occurs when legal title is obtained upon completion of foreclosure or when the borrower conveys all interest in the property to satisfy the loan through completion of a deed in lieu of foreclosure or through a similar legal agreement. The Company's policy is to carry OREO on its balance sheet at the lower of cost or fair value less estimated costs to sell. If fair value declines subsequent to foreclosure, a

valuation allowance is recorded through expense. Operating costs after acquisition are expensed.

F & M Bank Corp. and Subsidiaries
Notes to the Consolidated Financial Statements
December 31, 2016 and 2015

NOTE 2
SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED):

Bank Premises and Equipment

Land is carried at cost and bank premises and equipment are stated at cost less accumulated depreciation. Depreciation is charged to income over the estimated useful lives of the assets on a combination of the straight-line and accelerated methods. The ranges of the useful lives of the premises and equipment are as follows:

| | |
|---|---|
| Premises and Improvements | 10 - 40 years |
| Furniture and Equipment | 5 - 20 years |

Maintenance, repairs, and minor improvements are charged to operations as incurred. Gains and losses on dispositions are reflected in other income or expense.

Goodwill and Intangible Assets

The Company accounts for goodwill and intangible assets under ASC 805, “Business Combinations” and ASC 350, “Intangibles”, respectively. Goodwill is subject to at least an annual assessment for impairment by applying a fair value based test. Additionally, acquired intangible assets are separately recognized if the benefit of the assets can be sold, transferred, licensed, rented, or exchanged, and amortized over their useful lives. Intangible assets related to branch transactions were fully amortized in 2011. The Company records as goodwill the excess of purchase price over the fair value of the identifiable net assets acquired. Impairment testing is performed annually, as well as when an event triggering impairment may have occurred. The Company performs its annual analysis as of December 31 each fiscal year. Accounting guidance permits preliminary assessment of qualitative factors to determine whether more substantial impairment testing is required. The Company chose to bypass the preliminary assessment and utilized a two-step process for impairment testing of goodwill. The first step tests for impairment, while the second step, if necessary, measures the impairment. No indicators of impairment were identified during the years ended December 31, 2016, 2015, and 2014.

Pension Plans

The Bank has a qualified noncontributory defined benefit pension plan which covers all full-time employees hired prior to April 1, 2012. The benefits are primarily based on years of service and earnings. The Company complies with ASC 325-960 “Defined Benefit Pension Plans” which requires recognition of the over-funded or under-funded status of pension and other postretirement benefit plans on the balance sheet. Under ASC 325-960, gains and losses, prior service costs and credits, and any remaining transition amounts that have not yet been recognized through net periodic benefit cost will be recognized in accumulated other comprehensive income, net of tax effects, until they are amortized as a component of net periodic cost.

Advertising Costs

The Company follows the policy of charging the cost of advertising to expense as incurred. Total advertising costs included in other operating expenses for 2016, 2015, and 2014 were $443,479, $401,138, and $317,780, respectively.

Bank Owned Life Insurance

The Company has purchased life insurance policies on certain employees. Bank owned life insurance is recorded at the amount that can be realized under the insurance contract at the balance sheet date, which is the cash surrender value adjusted for other charges or other amounts due that are probable at settlement.

F & M Bank Corp. and Subsidiaries
Notes to the Consolidated Financial Statements
December 31, 2016 and 2015

NOTE 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED):

Transfers of Financial Assets
Transfers of financial assets are accounted for as sales, when control over the assets has been surrendered. Control over transferred assets is deemed to be surrendered when (1) the assets have been isolated from the Company – put presumptively beyond reach of the transferor and its creditors, even in bankruptcy or other receivership, (2) the transferee obtains the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred assets, and (3) the Company does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity or the ability to unilaterally cause the holder to return specific assets.

Comprehensive Income

Comprehensive income is shown in a two-statement approach, the first statement presents total net income and its components followed by a second statement that presents all the components of other comprehensive income such as unrealized gains and losses on available for sale securities and changes in the funded status of a defined benefit pension plan.

Derivative Financial Instruments

Under ASC 815, the gain or loss on a derivative designated and qualifying as a fair value hedging instrument, as well as the offsetting gain or loss on the hedging item attributable to the risk being hedged, is recognized currently in earnings in the same accounting period. The effective portion of the gain or loss on a derivative designated and qualifying as a cash flow hedging instrument is initially reported as a component of other comprehensive income and subsequently reclassified into earnings in the same period or periods during which the hedged transaction affects earnings. The ineffective portion of the gain or loss on the derivative instrument, if any, is recognized currently in earnings.

Interest rate derivative financial instruments receive hedge accounting treatment only if they are designated as a hedge and are expected to be, and are, effective in substantially reducing interest rate risk arising from the assets and liabilities identified as exposing the Company to risk. Those derivative financial instruments that do not meet the hedging criteria discussed below would be classified as trading activities and would be recorded at fair value with changes in fair value recorded in income. Derivative hedge contracts must meet specific effectiveness tests (i.e., over time the change in their fair values due to the designated hedge risk must be within 80 to 125 percent of the opposite change in the fair value of the hedged assets or liabilities). Changes in fair value of the derivative financial instruments must be effective at offsetting changes in the fair value of the hedging items due to the designated hedge risk during the term of the hedge. Further, if the underlying financial instrument differs from the hedged asset or liability, there must be a clear economic relationship between the prices of the two financial instruments. If periodic assessment indicates derivatives no longer provide an effective hedge, the derivatives contracts would be closed out and settled or classified as a trading activity.

Loss Contingencies
Loss contingencies, including claims and legal actions arising in the ordinary course of business, are recorded as liabilities when the likelihood of loss is probable and an amount or range of loss can be reasonably estimated. Management does not believe there now are such matters that will have a material effect on the consolidated financial statements.

Fair Value Measurements

The Company follows the provisions of ASC Topic 820 “Fair Value Measurements and Disclosures,” for financial assets and financial liabilities. ASC 820 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements.

F & M Bank Corp. and Subsidiaries
Notes to the Consolidated Financial Statements
December 31, 2016 and 2015

NOTE 2
SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED):

Reclassifications
Certain reclassifications have been made in prior years' financial statements to conform to classifications used in the current year. There were no material reclassifications.

Earnings per Share
Accounting guidance specifies the computation, presentation and disclosure requirements for earnings per share ("EPS") for entities with publicly held common stock or potential common stock such as options, warrants, convertible securities or contingent stock agreements if those securities trade in a public market. Basic EPS is computed by dividing net income available to common stockholders by the weighted average number of common shares outstanding. Diluted EPS is similar to the computation of basic EPS except that the denominator is increased to include the number of additional common shares that would have been outstanding if the dilutive common shares had been issued. The dilutive effect of conversion of preferred stock is reflected in the diluted earnings per common share calculation.

Net income available to common stockholders represents consolidated net income adjusted for preferred dividends declared.

The following table provides a reconciliation of net income to net income available to common stockholders for the periods presented:

| | For the year ended | | |
|---|---|---|---|
| Dollars in thousands | December 31, 2016 | December 31, 2015 | December 31, 2014 |
| Earnings Available to Common Stockholders: | | | |
| Net Income | $9,762 | $8,581 | $5,847 |
| Minority interest | 194 | 164 | 45 |
| Preferred Stock Dividends | 487 | 510 | 128 |
| Net Income Available to Common Stockholders | $9,081 | $7,907 | $5,674 |

The following table shows the effect of dilutive preferred stock conversion on the Company's earnings per share for the periods indicated:

| Year ended | | |
|---|---|---|
| 12/31/2016 | 12/31/2015 | 12/31/14 |

| Dollars in thousands, except share data | Net Income Available | Weighted Average Shares | Per Share Amounts | Net Income Available | Weighted Average Shares | Per Share Amounts | Net Income Available | Weighted Average Shares | Per Share Amounts |
|---|---|---|---|---|---|---|---|---|---|
| Basic EPS | $9,081 | 3,282,335 | $2.77 | $7,907 | 3,290,812 | $2.40 | $5,674 | 3,119,333 | $1.82 |
| Effect of Dilutive Securities: | | | | | | | | | |
| Convertible Preferred Stock | 487 | 434,256 | (0.20) | 510 | 444,400 | (0.15) | 128 | 110,631 | (0.02) |
| Diluted EPS | $9,568 | 3,716,591 | $2.57 | $8,417 | 3,735,212 | $2.25 | $5,802 | 3,229,942 | $1.80 |

F & M Bank Corp. and Subsidiaries
Notes to the Consolidated Financial Statements
December 31, 2016 and 2015

NOTE 2
SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED):

Recent Accounting Pronouncements

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 Company does not expect the adoption of ASU 2014-15 to have a material impact on its consolidated financial statements.

In January 2016, the FASB issued ASU 2016-01, "Financial Instruments – Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities." The amendments in ASU 2016-01, among other things: 1) Requires equity investments (except those accounted for under the equity method of accounting, or those that result in consolidation of the investee) to be measured at fair value with changes in fair value recognized in net income. 2) Requires public business entities to use the exit price notion when measuring the fair value of financial instruments for disclosure purposes. 3) Requires separate presentation of financial assets and financial liabilities by measurement category and form of financial asset (i.e., securities or loans and receivables). 4) Eliminates the requirement for public business entities to disclose the method(s) and significant assumptions used to estimate the fair value that is required to be disclosed for financial instruments measured at amortized cost. The amendments in this ASU are effective for public companies for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. The Company does not expect the adoption of ASU 2016-01 to have a material impact on its consolidated financial statements.

In February 2016, the FASB issued ASU No. 2016-02, "Leases (Topic 842)." Among other things, in the amendments in ASU 2016-02, lessees will be required to recognize the following for all leases (with the exception of short-term leases) at the commencement date: (1) A lease liability, which is a lessee's obligation to make lease payments arising from a lease, measured on a discounted basis; and (2) A right-of-use asset, which is an asset that represents the lessee's right to use, or control the use of, a specified asset for the lease term. Under the new guidance, lessor accounting is largely unchanged. Certain targeted improvements were made to align, where necessary, lessor accounting with the lessee accounting model and Topic 606, Revenue from Contracts with Customers. The amendments in this ASU are effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. Early application is permitted upon issuance. Lessees (for capital and operating leases) and lessors (for sales-type, direct financing, and operating leases) must apply a modified retrospective transition approach for leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements. The modified retrospective approach would not require any transition accounting for leases that expired before the earliest comparative period presented. Lessees and lessors may not apply a full retrospective transition approach. The Company is currently assessing the impact that ASU 2016-02 will have on its consolidated financial statements.

During March 2016, the FASB issued ASU No. 2016-05, “Derivatives and Hedging (Topic 815): Effect of Derivative Contract Novations on Existing Hedge Accounting Relationships.” The amendments in this ASU clarify that a change in the counterparty to a derivative instrument that has been designated as the hedging instrument does not, in and of itself, require de-designation of that hedging relationship provided that all other hedge accounting criteria remain intact. The amendments in this ASU are effective for financial statements issued for fiscal years beginning after December 15, 2016, and interim periods within those fiscal years. Early adoption is permitted, including adoption in an interim period. The Bank/Company does not expect the adoption of ASU 2016-05 to have a material impact on its (consolidated) financial statements.

F & M Bank Corp. and Subsidiaries
Notes to the Consolidated Financial Statements
December 31, 2016 and 2015

NOTE 2
SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED):

Recent Accounting Pronouncements, continued

In March 2016, the FASB issued ASU No. 2016-07, "Investments – Equity Method and Joint Ventures (Topic 323): Simplifying the Transition to the Equity Method of Accounting." The amendments in this ASU eliminate the requirement that when an investment qualifies for use of the equity method as a result of an increase in the level of ownership interest or degree of influence, an investor must adjust the investment, results of operations, and retained earnings retroactively on a step-by-step basis as if the equity method had been in effect during all previous periods that the investment had been held. The amendments require that the equity method investor add the cost of acquiring the additional interest in the investee to the current basis of the investor's previously held interest and adopt the equity method of accounting as of the date the investment becomes qualified for equity method accounting. Therefore, upon qualifying for the equity method of accounting, no retroactive adjustment of the investment is required. In addition, the amendments in this ASU require that an entity that has an available-for-sale equity security that becomes qualified for the equity method of accounting recognize through earnings the unrealized holding gain or loss in accumulated other comprehensive income at the date the investment becomes qualified for use of the equity method. The amendments are effective for all entities for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2016. The amendments should be applied prospectively upon their effective date to increases in the level of ownership interest or degree of influence that result in the adoption of the equity method. Early Adoption is permitted. The Company does not expect the adoption of ASU 2016-07 to have a material impact on its consolidated financial statements.

During June 2016, the FASB issued ASU No. 2016-13, "Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments." The amendments in this ASU, among other things, require the measurement of all expected credit losses for financial assets held at the reporting date based on historical experience, current conditions, and reasonable and supportable forecasts. Financial institutions and other organizations will now use forward-looking information to better inform their credit loss estimates. Many of the loss estimation techniques applied today will still be permitted, although the inputs to those techniques will change to reflect the full amount of expected credit losses. In addition, the ASU amends the accounting for credit losses on available-for-sale debt securities and purchased financial assets with credit deterioration. The amendments in this ASU are effective for SEC filers for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2019. For public companies that are not SEC filers, the amendments in this ASU are effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2020. The Company is currently assessing the impact that ASU 2016-13 will have on its consolidated financial statements.

During August 2016, the FASB issued ASU No. 2016-15, "Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments", to address diversity in how certain cash receipts and cash payments are presented and classified in the statement of cash flows. The amendments are effective for public business entities for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years. The amendments should be applied using a retrospective transition method to each period presented. If retrospective application is impractical for some of the issues addressed by the update, the amendments for those issues would be applied prospectively as of the earliest date practicable. Early adoption is permitted, including adoption in an interim period. The Company does not expect the adoption of ASU 2016-15 to have a material impact on its consolidated financial statements.

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F & M Bank Corp. and Subsidiaries
Notes to the Consolidated Financial Statements
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NOTE 2
SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED):

Recent Accounting Pronouncements, continued

During January 2017, the FASB issued ASU No. 2017-01, “Business Combinations (Topic 805): Clarifying the Definition of a Business”. The amendments in this ASU clarify the definition of a business with the objective of adding guidance to assist entities with evaluating whether transactions should be accounted for as acquisitions (or disposals) of assets or businesses. Under the current implementation guidance in Topic 805, there are three elements of a business—inputs, processes, and outputs. While an integrated set of assets and activities (collectively referred to as a “set”) that is a business usually has outputs, outputs are not required to be present. In addition, all the inputs and processes that a seller uses in operating a set are not required if market participants can acquire the set and continue to produce outputs. The amendments in this ASU provide a screen to determine when a set is not a business. If the screen is not met, the amendments (1) require that to be considered a business, a set must include, at a minimum, an input and a substantive process that together significantly contribute to the ability to create output and (2) remove the evaluation of whether a market participant could replace missing elements. The ASU provides a framework to assist entities in evaluating whether both an input and a substantive process are present. The amendments in this ASU are effective for annual periods beginning after December 15, 2017, including interim periods within those annual periods. The amendments in this ASU should be applied prospectively on or after the effective date. No disclosures are required at transition. The Company does not expect the adoption of ASU 2017-01 to have a material impact on its consolidated financial statements.

During January 2017, the FASB issued ASU No. 2017-04, “Intangibles – Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment”. The amendments in this ASU simplify how an entity is required to test goodwill for impairment by eliminating Step 2 from the goodwill impairment test. Step 2 measures a goodwill impairment loss by comparing the implied fair value of a reporting unit’s goodwill with the carrying amount of that goodwill. Instead, under the amendments in this ASU, an entity should perform its annual, or interim, goodwill impairment test by comparing the fair value of a reporting unit with its carrying amount. An entity still has the option to perform the qualitative assessment for a reporting unit to determine if the quantitative impairment test is necessary. Public business entities that are U.S. Securities and Exchange Commission (SEC) filers should adopt the amendments in this ASU for annual or interim goodwill impairment tests in fiscal years beginning after December 15, 2019. Public business entities that are not SEC filers should adopt the amendments in this ASU for annual or interim goodwill impairment tests in fiscal years beginning after December 15, 2020. Early adoption is permitted for interim or annual goodwill impairment tests performed on testing dates after January 1, 2017. The Company does not expect the adoption of ASU 2017-04 to have a material impact on its consolidated financial statements.

F & M Bank Corp. and Subsidiaries
Notes to the Consolidated Financial Statements
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NOTE 3
CASH AND DUE FROM BANKS:

The Bank is required to maintain average reserve balances based on a percentage of deposits. Due to the deposit reclassification procedures implemented by the Bank, there is no Federal Reserve Bank reserve requirement for the years ended December 31, 2016 and 2015.

NOTE 4
SECURITIES:

The amortized cost and fair value, with unrealized gains and losses, of securities held to maturity were as follows:

| | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Fair Value |
|---|---|---|---|---|
| December 31, 2016 | | | | |
| U. S. Treasuries | 125,005 | $- | $- | 125,005 |
| December 31, 2015 | | | | |
| U. S. Treasuries | 125,043 | $- | $- | 125,043 |

The amortized cost and fair value of securities available for sale are as follows:

| | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Fair Value |
|---|---|---|---|---|
| December 31, 2016 | | | | |
| U. S. Treasuries | $24,004,705 | $8,668 | $- | $24,013,373 |
| U. S. Government sponsored enterprises | - | - | - | - |
| Mortgage-backed obligations of federal agencies | 634,009 | 123 | - | 634,132 |
| Equity securities | 135,000 | - | - | 135,000 |
| Total Securities Available for Sale | $24,773,714 | $8,791 | $- | $24,782,505 |
| December 31, 2015 | | | | |
| U. S. Treasuries | $4,015,440 | $5,840 | $- | $4,021,280 |

| | | | | |
|---|---|---|---|---|
| U. S. Government sponsored enterprises | 8,080,540 | 3,780 | 10,600 | 8,073,720 |
| Mortgage-backed obligations of federal agencies | 810,802 | 6,143 | - | 816,945 |
| Equity securities | 135,000 | - | - | 135,000 |
| Total Securities Available for Sale | $13,041,782 | $15,763 | $10,600 | $13,046,945 |

F & M Bank Corp. and Subsidiaries
Notes to the Consolidated Financial Statements
December 31, 2016 and 2015

NOTE 4
SECURITIES (CONTINUED):

The amortized cost and fair value of securities at December 31, 2016, by contractual maturity are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

| | Securities Held to Maturity | | Securities Available for Sale | |
|---|---|---|---|---|
| | Amortized Cost | Fair Value | Amortized Cost | Fair Value |
| Due in one year or less | $- | $- | $24,004,705 | $24,013,373 |
| Due after one year through five years | 125,005 | 125,005 | - | - |
| Due after five years through ten years | - | - | 634,009 | 634,132 |
| Due after ten years | - | - | 135,000 | 135,000 |
| Total | $125,005 | $125,005 | $24,773,714 | $24,782,505 |

There were no sales of debt or equity securities during 2016, 2015 or 2014.

There were no pledged securities at December 31, 2016. The carrying value (which approximates fair value) of securities pledged by the Bank to secure deposits and for other purposes amounted to $12,912,000 at December 31, 2015.

Other investments consist of investments in twenty low-income housing and historic equity partnerships (carrying basis of $7,982,000), stock in the Federal Home Loan Bank (carrying basis of $5,018,000), and various other investments (carrying basis of $1,503,000). The interests in the low-income housing and historic equity partnerships have limited transferability and the interests in the other stocks are restricted as to sales. The market values of these securities are estimated to approximate their carrying value as of December 31, 2016. At December 31, 2016, the Company was committed to invest an additional $4,795,251 in eight low-income housing limited partnerships. These funds will be paid as requested by the general partner to complete the projects. This additional investment has been reflected in the above carrying basis and in accrued liabilities on the balance sheet.

The primary purpose of the investment portfolio is to generate income and meet liquidity needs of the Company through readily saleable financial instruments. The portfolio includes fixed rate bonds, whose prices move inversely with rates and variable rate bonds. At the end of any accounting period, the investment portfolio has unrealized gains and losses. The Company monitors the portfolio, which is subject to liquidity needs, market rate changes and credit risk changes for other than temporary impairment. The primary concern in a loss situation is the credit quality of the business behind the instrument. Bonds deteriorate in value due to credit quality of the individual issuer and changes in market conditions.

As of December 31, 2016, there were no securities in an unrealized loss position. A summary of unrealized losses (in thousands) and the length of time in a continuous loss position, by security type of December 31, 2015 were as follows:

| | Less than 12 Months | | More than 12 Months | | Total | |
|---|---|---|---|---|---|---|
| | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses |
| 2015 | | | | | | |
| U. S. Government sponsored enterprises | $6,056 | $(11) | $- | $- | $6,056 | $(11) |

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F & M Bank Corp. and Subsidiaries
Notes to the Consolidated Financial Statements
December 31, 2016 and 2015

NOTE 4
SECURITIES (CONTINUED):

Management evaluates securities for other-than-temporary impairment on at least a quarterly basis, and more frequently when economic or market conditions warrant such evaluation. Consideration is given to (1) the length of time and the extent to which the fair value has been less than the cost, (2) the financial condition and near-term prospects of the issuer, and (3) the intent and ability of the Company to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery of fair value. The Company does not intend to sell these securities and it is more likely than not that the Company will not be required to sell these securities before recovery of their amortized cost. As of December 31, 2016, the Company did not have any securities that were temporarily impaired. There were no securities that had been in an unrealized loss position for more than twelve months. The Company did not recognize any other-than-temporary impairment losses in 2016, 2015 or 2014.

NOTE 5
LOANS:

Loans held for investment as of December 31, 2016, and 2015 were as follows:

| | 2016 | 2015 |
|---|---|---|
| Construction/Land Development | $76,171,890 | $69,759,401 |
| Farmland | 12,901,023 | 13,377,740 |
| Real Estate | 172,758,171 | 166,586,877 |
| Multi-Family | 7,604,876 | 7,558,460 |
| Commercial Real Estate | 150,060,810 | 128,031,686 |
| Home Equity – closed end | 11,452,712 | 9,135,433 |
| Home Equity – open end | 54,419,961 | 56,599,337 |
| Commercial & Industrial – Non-Real Estate | 31,306,361 | 27,954,171 |
| Consumer | 6,643,868 | 8,219,391 |
| Dealer Finance | 65,494,924 | 54,085,791 |
| Credit Cards | 2,821,901 | 2,745,190 |
| Total | $591,636,497 | $544,053,477 |

The Company has pledged loans held for investment as collateral for borrowings with the Federal Home Loan Bank of Atlanta totaling $199,401,000 and $182,312,000 as of December 31, 2016, and 2015, respectively. The Company maintains a blanket lien on its entire residential real estate portfolio and certain commercial and home equity loans.

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NOTE 5
LOANS (CONTINUED):

The following is a summary of information pertaining to impaired loans (in thousands), as of December 31, 2016 and 2015:

| December 31, 2016 | Recorded Investment | Unpaid Principal Balance | Related Allowance | Average Recorded Investment | Interest Income Recognized |
|---|---|---|---|---|---|
| Impaired loans without a valuation allowance: | | | | | |
| Construction/Land Development | $3,296 | $3,652 | $- | $2,547 | $10 |
| Farmland | - | - | - | - | - |
| Real Estate | 768 | 768 | - | 778 | 10 |
| Multi-Family | - | - | - | - | - |
| Commercial Real Estate | 1,958 | 1,958 | - | 1,087 | 114 |
| Home Equity – closed end | - | - | - | - | - |
| Home Equity – open end | - | 347 | - | 964 | 2 |
| Commercial & Industrial – Non-Real Estate | 170 | 170 | - | 174 | 2 |
| Consumer | 13 | 13 | - | 11 | - |
| Credit Cards | - | - | - | - | - |
| Dealer Finance | - | - | - | 14 | 1 |
| | 6,205 | 6,908 | - | 5,575 | 139 |
| Impaired loans with a valuation allowance | | | | | |
| Construction/Land Development | 6,592 | 6,592 | 1,853 | 8,525 | 291 |
| Farmland | - | - | - | - | - |
| Real Estate | 1,206 | 1,206 | 221 | 1,215 | 10 |
| Multi-Family | - | - | - | - | - |
| Commercial Real Estate | 952 | 952 | 60 | 959 | 57 |
| Home Equity – closed end | - | - | - | - | - |
| Home Equity – open end | - | - | - | 969 | - |
| Commercial & Industrial – Non-Real Estate | - | - | - | 14 | - |
| Consumer | - | - | - | - | - |
| Credit cards | - | - | - | - | - |
| Dealer Finance | 87 | 87 | 20 | 77 | 1 |
| | 8,837 | 8,837 | 2,154 | 11.759 | 359 |
| Total impaired loans | $15,042 | $15,745 | $2,154 | $17,334 | $498 |

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F & M Bank Corp. and Subsidiaries
Notes to the Consolidated Financial Statements
December 31, 2016 and 2015

NOTE 5
LOANS (CONTINUED):

| December 31, 2015 | Recorded Investment | Unpaid Principal Balance | Related Allowance | Average Recorded Investment | Interest Income Recognized |
|---|---|---|---|---|---|
| Impaired loans without a valuation allowance: | | | | | |
| Construction/Land Development | $1,361 | $1,499 | $- | $3,622 | $73 |
| Farmland | - | - | - | - | - |
| Real Estate | 1,097 | 1,097 | - | 734 | 58 |
| Multi-Family | - | - | - | - | - |
| Commercial Real Estate | 307 | 307 | - | 874 | 17 |
| Home Equity – closed end | - | - | - | - | - |
| Home Equity – open end | 1,159 | 1,159 | - | 1,513 | 82 |
| Commercial & Industrial – Non-Real Estate | 181 | 181 | - | 186 | 10 |
| Consumer | 18 | 18 | - | 7 | - |
| Credit cards | - | - | - | - | - |
| Dealer Finance | 4 | 4 | - | 1 | 4 |
| | 4,127 | 4,265 | - | 6,937 | 244 |
| Impaired loans with a valuation allowance | | | | | |
| Construction/Land Development | 11,534 | 11,534 | 2,373 | 12,884 | 299 |
| Farmland | - | - | - | - | - |
| Real Estate | 324 | 324 | 238 | 699 | 46 |
| Multi-Family | - | - | - | - | - |
| Commercial Real Estate | 890 | 890 | 18 | 900 | 15 |
| Home Equity – closed end | - | - | - | - | - |
| Home Equity – open end | 1,414 | 1,414 | 269 | 613 | 75 |
| Commercial & Industrial – Non-Real Estate | - | - | - | - | - |
| Consumer | - | - | - | - | - |
| Credit cards | - | - | - | - | - |
| Dealer Finance | 68 | 68 | 17 | 38 | 5 |
| | 14,230 | 14,230 | 2,915 | 15,134 | 440 |
| Total impaired loans | $18,357 | $18,495 | $2,915 | $22,071 | $684 |

The Recorded Investment is defined as the principal balance less principal payments and charge-offs.

Loans held for sale consists of loans originated by VBS Mortgage for sale in the secondary market, and the Bank's commitment to purchase residential mortgage loan Participations from Northpointe Bank. The volume of loans purchased from Northpointe fluctuates due to a number of factors including changes in secondary market rates, which affects demand for mortgage loans; the number of participating banks involved in the program; the number of mortgage loan originators selling loans to the lead bank and the funding capabilities of the lead bank. Loans held for sale as of December 31, 2016, and 2015 were $62,734,803 and $57,805,529, respectively.

F & M Bank Corp. and Subsidiaries
Notes to the Consolidated Financial Statements
December 31, 2016 and 2015

NOTE 5
LOANS (CONTINUED):

The following table presents the aging of the recorded investment of past due loans (in thousands) as of December 31, 2016 and 2015:

| | 30-59 Days Past due | 60-89 Days Past Due | Greater than 90 Days (excluding non-accrual) | Non-Accrual Loans | Total Past Due | Current | Total Loan Receivable |
|---|---|---|---|---|---|---|---|
| December 31, 2016 | | | | | | | |
| Construction/Land Development | $73 | $101 | $- | $2,805 | $2,979 | $73,193 | $76,172 |
| Farmland | - | - | - | - | - | 12,901 | 12,901 |
| Real Estate | 2,114 | 340 | 81 | 1,399 | 3,934 | 168,824 | 172,758 |
| Multi-Family | - | - | - | - | - | 7,605 | 7,605 |
| Commercial Real Estate | 139 | - | - | - | 139 | 149,922 | 150,061 |
| Home Equity – closed end | 101 | - | - | 32 | 133 | 11,320 | 11,453 |
| Home Equity – open end | 309 | - | - | 279 | 588 | 53,832 | 54,420 |
| Commercial & Industrial – Non- Real Estate | 313 | 5 | - | 70 | 388 | 30,918 | 31,306 |
| Consumer | 35 | 4 | - | - | 39 | 6,604 | 6,643 |
| Dealer Finance | 790 | 187 | 26 | 178 | 1,181 | 64,314 | 65,495 |
| Credit Cards | 18 | 4 | - | - | 22 | 2,800 | 2,822 |
| Total | $3,892 | $641 | $107 | $4,763 | $9,403 | $582,233 | $591,636 |

| | 30-59 Days Past due | 60-89 Days Past Due | Greater than 90 Days (excluding non-accrual) | Non-Accrual Loans | Total Past Due | Current | Total Loan Receivable |
|---|---|---|---|---|---|---|---|
| December 31, 2015 | | | | | | | |
| Construction/Land Development | $104 | $- | $- | $4,688 | $4,792 | $64,967 | $69,759 |
| Farmland | - | - | - | - | - | 13,378 | 13,378 |
| Real Estate | 2,684 | 1,332 | 272 | 1,010 | 5,298 | 161,289 | 166,587 |
| Multi-Family | - | - | - | - | - | 7,559 | 7,559 |
| Commercial Real Estate | 340 | 241 | - | - | 581 | 127,451 | 128,032 |

| | | | | | | | |
|---|---|---|---|---|---|---|---|
| Home Equity – closed end | 41 | 7 | - | - | 48 | 9,087 | 9,135 |
| Home Equity – open end | 918 | 46 | 107 | 40 | 1,111 | 55,488 | 56,599 |
| Commercial & Industrial – Non- Real Estate | 114 | 3 | 25 | 109 | 251 | 27,703 | 27,954 |
| Consumer | 120 | 10 | - | - | 130 | 8,089 | 8,219 |
| Dealer Finance | 905 | 183 | 152 | 108 | 1,348 | 52,738 | 54,086 |
| Credit Cards | 10 | 13 | 15 | - | 38 | 2,707 | 2,745 |
| Total | $5,236 | $1,835 | $571 | $5,955 | $13,597 | $530,456 | $544,053 |

F & M Bank Corp. and Subsidiaries
Notes to the Consolidated Financial Statements
December 31, 2016 and 2015

NOTE 6
ALLOWANCE FOR LOAN LOSSES:

A summary of changes in the allowance for loan losses (in thousands) for the years ended December 31, 2016 and 2015 is as follows:

| December 31, 2016 | Beginning Balance | Charge-offs | Recoveries | Provision for Loan Losses | Ending Balance | Individually Evaluated for Impairment | Collectively Evaluated for Impairment |
|---|---|---|---|---|---|---|---|
| Allowance for loan losses: | | | | | | | |
| Construction/Land Development | $4,442 | $356 | $7 | $(712) | $3,381 | $1,853 | $1,528 |
| Farmland | 95 | - | - | (61) | 34 | - | 34 |
| Real Estate | 806 | 23 | 4 | 56 | 843 | 221 | 622 |
| Multi-Family | 71 | - | - | (48) | 23 | - | 23 |
| Commercial Real Estate | 445 | 19 | 135 | 144 | 705 | - | 705 |
| Home Equity – closed end | 174 | 8 | - | (91) | 75 | - | 75 |
| Home Equity – open end | 634 | 370 | 120 | 86 | 470 | 60 | 410 |
| Commercial & Industrial – Non-Real Estate | 1,055 | 293 | 267 | (443) | 586 | - | 586 |
| Consumer | 108 | 37 | 19 | (12) | 78 | - | 78 |
| Dealer Finance | 836 | 1,081 | 417 | 1,117 | 1,289 | 20 | 1,269 |
| Credit Cards | 115 | 74 | 54 | (36) | 59 | - | 59 |
| Total | $8,781 | $2,261 | $1,023 | $- | $7,543 | $2,154 | $5,389 |

| December 31, 2015 | Beginning Balance | Charge-offs | Recoveries | Provision for Loan Losses | Ending Balance | Individually Evaluated for Impairment | Collectively Evaluated for Impairment |
|---|---|---|---|---|---|---|---|
| Allowance for loan losses: | | | | | | | |
| Construction/Land Development | $4,738 | $156 | $85 | $(225) | $4,442 | $2,373 | $2,069 |
| Farmland | - | - | - | 95 | 95 | - | 95 |
| Real Estate | 623 | 25 | 37 | 171 | 806 | 238 | 568 |
| Multi-Family | - | - | - | 71 | 71 | - | 71 |

| | | | | | | | |
|---|---|---|---|---|---|---|---|
| Commercial Real Estate | 126 | - | 65 | 254 | 445 | 18 | 427 |
| Home Equity – closed end | 188 | 26 | 6 | 6 | 174 | - | 174 |
| Home Equity – open end | 154 | 51 | - | 531 | 634 | 269 | 365 |
| Commercial & Industrial – Non-Real Estate | 1,211 | - | 62 | (218) | 1,055 | - | 1,055 |
| Consumer | 214 | 32 | 32 | (106) | 108 | - | 108 |
| Dealer Finance | 1,336 | 251 | 24 | (273) | 836 | 17 | 819 |
| Credit Cards | 135 | 60 | 46 | (6) | 115 | - | 115 |
| Total | $8,725 | $601 | $357 | $300 | $8,781 | $2,915 | $5,866 |

F & M Bank Corp. and Subsidiaries
Notes to the Consolidated Financial Statements
December 31, 2016 and 2015

NOTE 6
ALLOWANCE FOR LOAN LOSSES (CONTINUED):

The following table presents the recorded investment in loans (in thousands) based on impairment method as of December 31, 2016 and 2015:

| December 31, 2016 | Loan Receivable | Individually Evaluated for Impairment | Collectively Evaluated for Impairment |
|---|---|---|---|
| Construction/Land Development | $76,172 | $9,888 | $66,284 |
| Farmland | 12,901 | - | 12,901 |
| Real Estate | 172,758 | 1,974 | 170,784 |
| Multi-Family | 7,605 | - | 7,605 |
| Commercial Real Estate | 150,061 | 2,910 | 147,151 |
| Home Equity – closed end | 11,453 | - | 11,453 |
| Home Equity –open end | 54,420 | - | 54,420 |
| Commercial & Industrial – Non-Real Estate | 31,306 | 170 | 31,136 |
| Consumer | 6,643 | 13 | 6,630 |
| Dealer Finance | 65,495 | 87 | 65,408 |
| Credit Cards | 2,822 | - | 2,822 |
| Total | $591,636 | $15,042 | $576,594 |

| December 31, 2015 | Loan Receivable | Individually Evaluated for Impairment | Collectively Evaluated for Impairment |
|---|---|---|---|
| Construction/Land Development | $69,759 | $12,895 | $56,864 |
| Farmland | 13,378 | - | 13,378 |
| Real Estate | 166,587 | 1,421 | 165,167 |
| Multi-Family | 7,559 | - | 7,559 |
| Commercial Real Estate | 128,032 | 1,197 | 126,835 |
| Home Equity – closed end | 9,135 | - | 9,135 |
| Home Equity –open end | 56,599 | 2,573 | 54,026 |
| Commercial & Industrial – Non-Real Estate | 27,954 | 181 | 27,773 |
| Consumer | 8,219 | 18 | 8,201 |
| Dealer Finance | 54,086 | 72 | 54,013 |

| | | | |
|---|---|---|---|
| Credit Cards | 2,745 | - | 2,745 |
| Total | $544,053 | $18,357 | $525,696 |

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F & M Bank Corp. and Subsidiaries
Notes to the Consolidated Financial Statements
December 31, 2016 and 2015

NOTE 6
ALLOWANCE FOR LOAN LOSSES (CONTINUED):

The following table shows the Company's loan portfolio broken down by internal loan grade (in thousands) as of December 31, 2016 and 2015:

| December 31, 2016 | Grade 1 Minimal Risk | Grade 2 Modest Risk | Grade 3 Average Risk | Grade 4 Acceptable Risk | Grade 5 Marginally Acceptable | Grade 6 Watch | Grade 7 Substandard | Grade 8 Doubtful | Total |
|---|---|---|---|---|---|---|---|---|---|
| Construction/Land Development | $- | $1,478 | $10,870 | $43,863 | $8,399 | $2,473 | $9,089 | $- | $76,172 |
| Farmland | 65 | - | 3,073 | 3,456 | 4,446 | 1,861 | - | - | 12,901 |
| Real Estate | - | 1,149 | 62,168 | 74,242 | 28,266 | 4,680 | 2,253 | - | 172,758 |
| Multi-Family | - | 311 | 3,009 | 4,099 | 186 | - | - | - | 7,605 |
| Commercial Real Estate | - | 2,793 | 32,986 | 91,157 | 19,181 | 1,840 | 2,104 | - | 150,061 |
| Home Equity – closed end | - | 150 | 3,966 | 4,139 | 1,746 | 1,414 | 38 | - | 11,453 |
| Home Equity – open end | 124 | 1,724 | 16,415 | 30,974 | 4,547 | 125 | 511 | - | 54,420 |
| Commercial & Industrial (Non-Real Estate) | 1,375 | 1,267 | 6,827 | 19,530 | 2,198 | 39 | 70 | - | 31,306 |
| Consumer (excluding dealer) | 67 | 174 | 1,837 | 607 | 1,242 | 2,252 | 466 | - | 6,643 |
| Total | $1,631 | $9,046 | $141,151 | $272,065 | $70,211 | $14,684 | $14,531 | $- | $523,319 |

| | Credit Cards | Dealer Finance |
|---|---|---|
| Performing | $2,822 | $65,291 |
| Non performing | - | 204 |
| Total | $2,822 | $65,495 |

F & M Bank Corp. and Subsidiaries
Notes to the Consolidated Financial Statements
December 31, 2016 and 2015

NOTE 6
ALLOWANCE FOR LOAN LOSSES (CONTINUED):

| December 31, 2015 | Grade 1 Minimal Risk | Grade 2 Modest Risk | Grade 3 Average Risk | Grade 4 Acceptable Risk | Grade 5 Marginally Acceptable | Grade 6 Watch | Grade 7 Substandard | Grade 8 Doubtful | Total |
|---|---|---|---|---|---|---|---|---|---|
| Construction/Land Development | $- | $485 | $8,410 | $31,783 | $14,260 | $3,216 | $11,605 | $- | $69,759 |
| Farmland | 66 | - | 2,615 | 3,768 | 4,952 | 1,977 | - | - | 13,378 |
| Real Estate | - | 955 | 54,400 | 76,545 | 23,695 | 8,334 | 2,658 | - | 166,587 |
| Multi-Family | - | 391 | 3,925 | 3,046 | 197 | - | - | - | 7,559 |
| Commercial Real Estate | - | 2,087 | 25,889 | 74,337 | 20,271 | 4,149 | 1,299 | - | 128,032 |
| Home Equity – closed end | - | - | 3,549 | 3,792 | 1,661 | 114 | 19 | - | 9,135 |
| Home Equity – open end | - | 1,657 | 15,043 | 31,455 | 4,827 | 398 | 3,219 | - | 56,599 |
| Commercial & Industrial (Non-Real Estate) | 896 | 646 | 6,423 | 17,053 | 2,281 | 517 | 138 | - | 27,954 |
| Consumer (excluding dealer) | 83 | 215 | 2,273 | 750 | 1,536 | 2,786 | 576 | - | 8,219 |
| Total | $1,045 | $6,436 | $122,527 | $242,529 | $73,680 | $21,491 | $19,514 | $- | $487,222 |

| | Credit Cards | Dealer Finance |
|---|---|---|
| Performing | $2,730 | $53,826 |
| Non performing | 15 | 260 |
| Total | $2,745 | $54,086 |

Description of internal loan grades:

Grade 1 – Minimal Risk: Excellent credit, superior asset quality, excellent debt capacity and coverage, and recognized management capabilities.

Grade 2 – Modest Risk: Borrower consistently generates sufficient cash flow to fund debt service, excellent credit, above average asset quality and liquidity.

Grade 3 – Average Risk: Borrower generates sufficient cash flow to fund debt service. Employment (or business) is stable with good future trends. Credit is very good.

Grade 4 – Acceptable Risk: Borrower’s cash flow is adequate to cover debt service; however, unusual expenses or capital expenses must by covered through additional long term debt. Employment (or business) stability is reasonable, but future trends may exhibit slight weakness. Credit history is good. No unpaid judgments or collection items

appearing on credit report.

Grade 5 – Marginally acceptable: Credit to borrowers who may exhibit declining earnings, may have leverage that is materially above industry averages, liquidity may be marginally acceptable. Employment or business stability may be weak or deteriorating. May be currently performing as agreed, but would be adversely affected by developing factors such as layoffs, illness, reduced hours or declining business prospects. Credit history shows weaknesses, past dues, paid or disputed collections and judgments, but does not include borrowers that are currently past due on obligations or with unpaid, undisputed judgments.

F & M Bank Corp. and Subsidiaries
Notes to the Consolidated Financial Statements
December 31, 2016 and 2015

NOTE 6
ALLOWANCE FOR LOAN LOSSES (CONTINUED):

Grade 6 – Watch: Loans are currently protected, but are weak due to negative balance sheet or income statement trends. There may be a lack of effective control over collateral or the existence of documentation deficiencies. These loans have potential weaknesses that deserve management's close attention. Other reasons supporting this classification include adverse economic or market conditions, pending litigation or any other material weakness. Existing loans that become 60 or more days past due are placed in this category pending a return to current status.

Grade 7 – Substandard: Loans having well-defined weaknesses where a payment default and or loss is possible, but not yet probable. Cash flow is inadequate to service the debt under the current payment, or terms, with prospects that the condition is permanent. Loans classified as substandard are inadequately protected by the current net worth and paying capacity of the borrower and there is the likelihood that collateral will have to be liquidated and/or guarantor(s) called upon to repay the debt. Generally, the loan is considered collectible as to both principal and interest, primarily because of collateral coverage, however, if the deficiencies are not corrected quickly; there is a probability of loss.

Grade 8 – Doubtful: The loan has all the characteristics of a substandard credit, but available information indicates it is unlikely the loan will be repaid in its entirety. Cash flow is insufficient to service the debt. It may be difficult to project the exact amount of loss, but the probability of some loss is great. Loans are to be placed on non-accrual status when any portion is classified doubtful.

Credit card and dealer finance loans are classified as performing or nonperforming. A loan is nonperforming when payments of principal and interest are past due 90 days or more.

NOTE 7
TROUBLED DEBT RESTRUCTURING:

In the determination of the allowance for loan losses, management considers troubled debt restructurings and subsequent defaults in these restructurings by adjusting the loan grades of such loans, which are considered in the qualitative factors within the allowance for loan loss methodology. Defaults resulting in charge-offs affect the historical loss experience ratios which are a component of the allowance calculation. Additionally, specific reserves may be established on restructured loans which are evaluated individually for impairment.

During the twelve months ended December 31, 2016, the Bank modified 6 loans that were considered to be troubled debt restructurings. These modifications include rate adjustments, revisions to amortization schedules, suspension of principal payments for a temporary period, re-advancing funds to be applied as payments to bring the loan(s) current, or any combination thereof.

| | December 31, 2016 | |
|---|---|---|
| | Pre-Modification | Post-Modification |
| (in thousands) | Outstanding | Outstanding |

| Troubled Debt Restructurings | Number of Contracts | Recorded Investment | Recorded Investment |
|---|---|---|---|
| Real Estate | 2 | $141 | $141 |
| Consumer | 4 | 39 | 39 |
| Total | 6 | $180 | $180 |

As of December 31, 2016, there were no loans restructured in the previous twelve months, in default. A restructured loan is considered in default when it becomes 90 days past due.

F & M Bank Corp. and Subsidiaries
Notes to the Consolidated Financial Statements
December 31, 2016 and 2015

NOTE 7
TROUBLED DEBT RESTRUCTURING (CONTINUED):

During the twelve months ended December 31, 2015, the Bank modified 16 loans that were considered to be troubled debt restructurings. These modifications included rate adjustments, revisions to amortization schedules, suspension of principal payments for a temporary period, re-advancing funds to be applied as payments to bring the loan(s) current, or any combination thereof.

| | December 31, 2015 | | |
|---|---|---|---|
| | | Pre-Modification | Post-Modification |
| (in thousands) | | Outstanding | Outstanding |
| Troubled Debt Restructurings | Number of Contracts | Recorded Investment | Recorded Investment |
| Commercial | 1 | $974 | $974 |
| Real Estate | 5 | 1,408 | 1,408 |
| Home Equity | 4 | 1,414 | 1,414 |
| Consumer | 6 | 73 | 73 |
| Total | 16 | $3,869 | $3,869 |

As of December 31, 2015, there were no loans restructured in the previous twelve months, in default. A restructured loan is considered in default when it becomes 90 days past due.

NOTE 8
BANK PREMISES AND EQUIPMENT:

Bank premises and equipment as of December 31 are summarized as follows:

| | 2016 | 2015 |
|---|---|---|
| Land | $3,090,632 | $1,868,709 |
| Buildings and improvements | 9,404,429 | 7,209,427 |
| Furniture and equipment | 6,560,956 | 7,397,173 |

| | | |
|---|---|---|
| | 19,056,017 | 16,475,309 |
| Less - accumulated depreciation | (8,788,082) | (8,933,231) |
| Net | $10,267,935 | $7,542,078 |

Provisions for depreciation of $801,093 in 2016, $709,237 in 2015, and $612,116 in 2014 were charged to operations.

F & M Bank Corp. and Subsidiaries
Notes to the Consolidated Financial Statements
December 31, 2016 and 2015

NOTE 9
OTHER REAL ESTATE OWNED:

The table below reflects other real estate owned (OREO) activity for 2016 and 2015:

Other Real Estate Owned

| | 2016 | 2015 |
|---|---|---|
| Balance as of January 1 | $2,127,685 | $3,507,153 |
| Loans transferred to OREO | 566,272 | 125,000 |
| Capital improvements | 24,335 | 98,929 |
| Sale of OREO | (623,249) | (1,065,792) |
| Write down of OREO or losses on sale | (19,074) | (537,605) |
| Balance as of December 31 | $2,075,969 | $2,127,685 |

At December 31, 2016, the balance of real estate owned includes $121,450 of foreclosed residential real estate properties recorded as a result of obtaining physical possession of the property. At December 31, 2016, the recorded investment of consumer mortgage loans secured by residential real estate properties for which formal foreclosure procedures are in process is $40,377.

NOTE 10
DEPOSITS:

Time deposits that meet or exceed the FDIC insurance limit of $250,000 at year end 2016 and 2015 were $7,841,553 and $6,605,644. At December 31, 2016, the scheduled maturities of time deposits are as follows:

| | |
|---|---|
| 2017 | $53,013,651 |
| 2018 | 57,544,691 |
| 2019 | 25,625,074 |
| 2020 | 12,136,116 |
| 2021 and after | 8,908,548 |
| Total | $157,228,080 |

NOTE 11
SHORT-TERM DEBT:

Short-term debt, all maturing within 12 months, as of December 31, 2016 and 2015 is summarized as follows:

| | Outstanding | Average | Weighted |
|---|---|---|---|

| | Maximum Outstanding at any Month End | At Year End | Balance Outstanding | Average Interest Rate | Yield |
|---|---|---|---|---|---|
| 2016 | | | | | |
| Federal funds purchased | $11,421,000 | $- | $635,653 | .02% | .98% |
| FHLB short term | 50,000,000 | 40,000,000 | 34,740,437 | .11% | .12% |
| Securities sold under agreements to repurchase | 4,272,235 | - | 2,133,239 | .55% | .25% |
| Totals | | $40,000,000 | $37,509,329 | .15% | .15% |
| 2015 | | | | | |
| Federal funds purchased | $8,843,000 | $959,217 | $833,907 | .02% | .78% |
| FHLB short term | 45,000,000 | 20,000,000 | 26,739,726 | .16% | .19% |
| Securities sold under agreements to repurchase | 4,697,341 | 3,994,834 | 4,443,753 | .04% | .25% |
| Totals | | $24,954,051 | $32,017,386 | .21% | .22% |

F & M Bank Corp. and Subsidiaries
Notes to the Consolidated Financial Statements
December 31, 2016 and 2015

NOTE 11
SHORT-TERM DEBT (CONTINUED)

Securities sold under repurchase agreements are secured transactions with customers and generally mature the day following the date sold. Federal funds purchased are unsecured overnight borrowings from other financial institutions. FHLB short term debt, which is secured by the loan portfolio, is a daily rate variable loan that acts as a line of credit to meet financing needs.

As of December 31, 2016, the Company had unsecured lines of credit with correspondent banks totaling $26,000,000, which may be used in the management of short-term liquidity, in which no balances were outstanding.

NOTE 12
LONG-TERM DEBT:

The Company borrowed $20,000,000 from the Federal Home Loan Bank of Atlanta (FHLB) in 2016 to fund loan growth and extend maturities of long term debt at lower rates. The Company borrowed $40,000,000 in 2015. The interest rates on the long-term debt were fixed at the time of the advance and ranged from 1.16% to 2.56%; the weighted average interest rate was 1.80% and 1.86% at December 31, 2016 and 2015, respectively. The balance of these obligations at December 31, 2016 and December 31, 2015 were $63,982,000 and $48,161,000, respectively. The long-term debt is secured by qualifying mortgage loans held for investment by the Company.

The maturities of long-term Federal Home Loan Bank long term debt as of December 31, 2016, were as follows:

| | |
|---|---|
| 2017 | $4,429,000 |
| 2018 | 9,429,000 |
| 2019 | 6,929,000 |
| 2020 | 14,429,000 |
| 2021 | 10,929,000 |
| Thereafter | 17,837,000 |
| Total | $63,982,000 |

The Company has a small note payable to purchase a lot adjacent to one of its branches in the amount of $255,000 payable in three annual installments.

NOTE 13
INCOME TAX EXPENSE:

The components of income tax expense were as follows:

| | 2016 | 2015 | 2014 |
|---|---|---|---|
| Current expense | | | |
| Federal | $3,108,055 | $3,227,013 | $1,777,598 |

| | | | |
|---|---|---|---|
| Deferred (benefit) expense | | | |
| Federal | (8,751) | (340,941) | 505,684 |
| State | - | - | 9,854 |
| Total Deferred (benefit) expense | (8,751) | (340,941) | 515,538 |
| Total Income Tax Expense | $3,099,305 | $2,886,072 | $2,293,136 |

F & M Bank Corp. and Subsidiaries
Notes to the Consolidated Financial Statements
December 31, 2016 and 2015

NOTE 13
INCOME TAX EXPENSE (CONTINUED):

The components of deferred taxes as of December 31, were as follows:

| | 2016 | 2015 |
|---|---|---|
| Deferred Tax Assets: | | |
| Allowance for loan losses | $2,353,979 | $2,564,214 |
| Split Dollar Life Insurance | 4,440 | 4,440 |
| Nonqualified deferred compensation | 855,635 | 702,440 |
| Low income housing partnerships losses | 93,561 | 210,107 |
| Core deposit amortization | 165,124 | 176,605 |
| Other real estate owned | 280,248 | 269,610 |
| Unfunded pension benefit obligation | 1,633,388 | 1,382,268 |
| Total Assets | $5,386,375 | $5,309,684 |

| | 2016 | 2015 |
|---|---|---|
| Deferred Tax Liabilities: | | |
| Unearned low income housing credits | $307,042 | $418,416 |
| Depreciation | 437,253 | 359,406 |
| Prepaid pension | 1,839,781 | 1,988,736 |
| Goodwill tax amortization | 900,641 | 901,340 |
| Net unrealized gain on securities available for sale | 2,989 | 1,757 |
| Total Liabilities | 3,487,706 | 3,669,655 |
| Net Deferred Tax Asset (included in Other Assets on Balance Sheet) | $1,898,668 | $1,640,029 |

The following table summarizes the differences between the actual income tax expense and the amounts computed using the federal statutory tax rates:

| | 2016 | 2015 | 2014 |
|---|---|---|---|
| Tax expense at federal statutory rates | $4,306,709 | $3,843,048 | $2,959,056 |
| Increases (decreases) in taxes resulting from: | | | |
| State income taxes, net of federal benefit | 5,882 | 8,087 | 8,659 |

| | | | |
|---|---|---|---|
| Partially tax-exempt income | (41,135) | (46,348) | (54,529) |
| Tax-exempt income | (216,999) | (222,672) | (190,192) |
| LIH and historic credits | (896,063) | (700,882) | (506,742) |
| Deferred Tax Asset Valuation Allowance – reversal | - | - | 396,440 |
| Other | (59,088) | 4,840 | (112,714) |
| Total Income Tax Expense | $3,099,305 | $2,886,072 | $2,293,136 |

The Company has analyzed the tax positions taken or expected to be taken in its tax returns and concluded it has no liability related to uncertain tax positions in accordance with accounting guidance related to income taxes.

The Company and its subsidiaries file federal income tax returns and state income tax returns. With few exceptions, the Company is no longer subject to federal or state income tax examinations by tax authorities for years before 2013.

F & M Bank Corp. and Subsidiaries
Notes to the Consolidated Financial Statements
December 31, 2016 and 2015

NOTE 14
EMPLOYEE BENEFITS:

Defined Benefit Pension Plan

The Company has a qualified noncontributory defined benefit pension plan which covers substantially all of its employees hired before April 1, 2012. The benefits are primarily based on years of service and earnings. The Company uses December 31st as the measurement date for the defined benefit pension plan.

The following table provides a reconciliation of the changes in the benefit obligations and fair value of plan assets for 2016, 2015 and 2014:

| | 2016 | 2015 | 2014 |
|---|---|---|---|
| Change in Benefit Obligation | | | |
| Benefit obligation, beginning | $10,944,658 | $10,777,415 | $7,933,568 |
| Service cost | 631,874 | 648,334 | 501,032 |
| Interest cost | 452,896 | 410,944 | 377,706 |
| Actuarial (gain) loss | 872,245 | (137,048) | 2,030,583 |
| Benefits paid | (426,628) | (754,987) | (65,474) |
| Benefit obligation, ending | $12,475,045 | $10,944,658 | $10,777,415 |
| Change in Plan Assets | | | |
| Fair value of plan assets, beginning | $11,678,218 | $11,683,845 | $9,687,226 |
| Actual return on plan assets | 780,160 | (640) | 562,093 |
| Employer contribution | - | 750,000 | 1,500,000 |
| Benefits paid | (426,628) | (754,987) | (65,474) |
| Fair value of plan assets, ending | $12,031,750 | $11,678,218 | $11,683,845 |
| Funded status at the end of the year | $(443,295) | $733,560 | $906,430 |

The fair value of plan assets is measured based on the fair value hierarchy as discussed in Note 20, “Fair Value Measurements” to the Consolidated Financial Statements. The valuations are based on third party data received as of the balance sheet date. All plan assets are considered Level 1 assets, as quoted prices exist in active markets for identical assets.

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NOTE 14
EMPLOYEE BENEFITS (CONTINUED):

Defined Benefit Pension Plan, continued

| | 2016 | 2015 | 2014 |
|---|---|---|---|
| Amount recognized in the Consolidated Balance Sheet | | | |
| Prepaid benefit cost | $4,360,788 | $4,799,051 | $4,434,917 |
| Unfunded pension benefit obligation under ASC 325-960 | (4,804,083) | (4,065,491) | (3,528,487) |
| Deferred taxes | 1,633,388 | 1,382,267 | 1,199,686 |
| Amount recognized in accumulated other comprehensive income (loss) | | | |
| Net loss | $(4,861,211) | $(4,137,855) | $(3,616,087) |
| Prior service cost | 57,128 | 72,364 | 87,600 |
| Amount recognized | (4,804,083) | (4,065,491) | (3,528,487) |
| Deferred Taxes | 1,633,388 | 1,382,267 | 1,199,686 |
| Amount recognized in accumulated comprehensive income | $(3,170,695) | $(2,683,224) | $(2,328,801) |
| Prepaid benefit detail | | | |
| Benefit obligation | $(12,475,045) | $(10,944,658) | $(10,777,415) |
| Fair value of assets | 12,031,750 | 11,678,218 | 11,683,845 |
| Unrecognized net actuarial loss | 4,861,211 | 4,137,855 | 3,616,087 |
| Unrecognized prior service cost | (57,128) | (72,364) | (87,600) |
| Prepaid (accrued) benefits | $4,360,788 | $4,799,051 | $4,434,917 |
| Components of net periodic benefit cost | | | |
| Service cost | $631,874 | $648,334 | $501,032 |
| Interest cost | 452,896 | 410,944 | 377,706 |
| Expected return on plan assets | (854,414) | (838,818) | (698,252) |
| Amortization of prior service cost | (15,236) | (15,236) | (15,236) |
| Recognized net actuarial (gain) loss | 223,143 | 180,642 | 36,110 |
| Net periodic benefit cost | $438,263 | $385,866 | $201,360 |
| Other changes in plan assets and benefit obligations recognized in other comprehensive income (loss) | | | |
| Net (gain) loss | $723,356 | $521,768 | $2,130,632 |
| Amortization of prior service cost | 15,236 | 15,236 | 15,236 |
| Total recognized in other comprehensive income | $738,592 | $537,004 | $2,145,868 |
| Total recognized in net periodic benefit cost and other Comprehensive income (loss) | $1,176,855 | $922,870 | $2,347,228 |

| | | | |
|---|---|---|---|
| Additional disclosure information | | | |
| Accumulated benefit obligation | $8,788,626 | $7,601,249 | $7,543,340 |
| Vested benefit obligation | $8,780,087 | $7,539,365 | $7,408,014 |
| Discount rate used for net pension cost | 4.25% | 4.00% | 5.00% |
| Discount rate used for disclosure | 4.00% | 4.25% | 4.00% |
| Expected return on plan assets | 7.50% | 7.50% | 7.50% |
| Rate of compensation increase | 3.00% | 3.00% | 3.00% |
| Average remaining service (years) | 13 | 13 | 14 |

F & M Bank Corp. and Subsidiaries
Notes to the Consolidated Financial Statements
December 31, 2016 and 2015

NOTE 14
EMPLOYEE BENEFITS (CONTINUED):

Funding Policy

The Company's contributions for 2015 and 2014 were $750,000, and $1,500,000, respectively. Due to the current funding status of the plan, the Company did not make a contribution in 2016. The net periodic pension cost of the plan for 2017 will be approximately $601,000.

Long-Term Rate of Return

The Company, as plan sponsor, selects the expected long-term rate of return on assets assumption in consultation with investment advisors and the plan 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. Undue weight is not given to recent experience, which may not continue over the measurement period, with higher significance 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, and solely for this purpose, the plan is assumed to continue in force and not terminate during the period during which the 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 estimated within periodic cost).

Asset Allocation

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% equity. The Investment Manager 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. The pension plan's allocations as of December 31, 2016, and 2015 were 61% equity and 39% fixed and 60% equity and 40% fixed, respectively.

Estimated Future Benefit Payments, which reflect expected future service, as appropriate, as of December 31, 2016, are as follows:

| | |
|---|---|
| 2017 | $595,435 |
| 2018 | 1,284,377 |
| 2019 | 669,286 |
| 2020 | 549,902 |
| 2021 | 152,296 |
| 2022-2026 | 5,655,187 |
| | $8,906,483 |

Employee Stock Ownership Plan (ESOP)

The Company sponsors an ESOP which provides stock ownership to substantially all employees of the Company. The Plan provides total vesting upon the attainment of five years of service. Contributions to the plan are made at the discretion of the Board of Directors and are allocated based on the compensation of each employee relative to total compensation paid by the Company. All shares issued and held by the Plan are considered outstanding in the computation of earnings per share. Dividends on Company stock are allocated and paid to participants at least annually. Shares of Company stock, when distributed, have restrictions on transferability. The Company contributed $470,000 in 2016, $420,000 in 2015, and $360,000 in 2014 to the Plan and charged this expense to operations. The shares held by the ESOP totaled 190,271 and 188,596 at December 31, 2016 and 2015, respectively.

F & M Bank Corp. and Subsidiaries
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NOTE 14
EMPLOYEE BENEFITS (CONTINUED):

401(K) Plan

The Company sponsors a 401(k) savings plan under which eligible employees may choose to save up to 20 percent of their salary on a pretax basis, subject to certain IRS limits. Under the Federal Safe Harbor rules employees are automatically enrolled at 3% (in the third year this increases by 1% per year up to 6%) of their salary unless elected otherwise. The Company matches a hundred percent of the first 1% contributed by the employee and fifty percent from 2% to 6% of employee contributions. Vesting in the contributions made by the Company is 100% after two years of service. Contributions under the plan amounted to $242,415, $211,987 and $190,057 in 2016, 2015 and 2014, respectively.

Deferred Compensation Plan

The Company has a nonqualified deferred compensation plan for several of its key employees and directors. The Company may make annual contributions to the plan, and the employee or director has the option to defer a portion of their salary or bonus based on qualifying annual elections. Contributions to the plan totaled $110,000 in 2016, $110,000 in 2015 and $100,000 in 2014. A liability is accrued for the obligation under the plan and totaled $2,766,902 and $2,423,358 at December 31, 2016 and 2015, respectively.

Investments in Life Insurance Contracts

The Bank currently offers a variety of benefit plans to all full-time employees. While the costs of these plans are generally tax deductible to the Bank, the cost has been escalating greatly in recent years. To help offset escalating benefit costs and to attract and retain qualified employees, the Bank purchased Bank Owned Life Insurance (BOLI) contracts that will provide benefits to employees during their lifetime. Dividends received on these policies are tax-deferred and the death benefits under the policies are tax exempt. Rates of return on a tax-equivalent basis are very favorable when compared to other long-term investments which the Bank might make. The accrued liability related to the BOLI contracts was $412,142 and $393,405 for December 31, 2016 and 2015, respectively.

NOTE 15
CONCENTRATIONS OF CREDIT:

The Company had cash deposits in other commercial banks in excess of FDIC insurance limits totaling $680,021 and $1,596,382 at December 31, 2016 and 2015, respectively.

The Company grants commercial, residential real estate and consumer loans to customers located primarily in the northwestern portion of the State of Virginia. Loan concentration areas greater than 25% of capital include land development. Collateral required by the Company is determined on an individual basis depending on the purpose of the loan and the financial condition of the borrower. As of December 31, 2016, approximately 82% of the loan portfolio was secured by real estate.

NOTE 16
COMMITMENTS:

The Company makes commitments to extend credit in the normal course of business and issues standby letters of credit to meet the financing needs of its customers. The amount of the commitments represents the Company's exposure to credit loss that is not included in the consolidated balance sheet. As of the December 31, 2016 and 2015, the Company had the following commitments outstanding:

| | 2016 | 2015 |
|---|---|---|
| Commitments to extend credit | $148,060,176 | $135,138,834 |
| Standby letters of credit | 1,089,117 | 1,344,191 |

The Company uses the same credit policies in making commitments to extend credit and issue standby letters of credit as it does for the loans reflected in the consolidated balance sheet.

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December 31, 2016 and 2015

NOTE 16
COMMITMENTS (CONTINUED):

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Company evaluates each customer's creditworthiness on a case-by-case basis. Collateral required, if any, upon extension of credit is based on management's credit evaluation of the borrower’s ability to pay. Collateral held varies but may include accounts receivable, inventory, property, plant and equipment.

The Bank leases four of its branch offices and both of its loan production offices under long term lease arrangements which had initial terms of either three, five or ten years. Lease expense was $173,777, $164,294 and $120,728 for 2016, 2015 and 2014, respectively. As of December 31, 2016, the required lease payments for the next five years were as follows:

| | |
|---|---|
| 2017 | $145,099 |
| 2018 | 102,726 |
| 2019 | 74,349 |
| 2020 | 75,500 |
| 2021 | 55,439 |

NOTE 17
ON BALANCE SHEET DERIVATIVE INSTRUMENTS AND HEDGING ACTIVITIES:

Derivative Financial Instruments

The Company has stand alone derivative financial instruments in the form of forward option contracts. These transactions involve both credit and market risk. The notional amounts are amounts on which calculations, payments, and the value of the derivative are based. Notional amounts do not represent direct credit exposures. Direct credit exposure is limited to the net difference between the calculated amounts to be received and paid, if any. Such difference, which represents the fair value of the derivative instruments, is reflected on the Company’s balance sheet as derivative assets and derivative liabilities.

The Company is exposed to credit-related losses in the event of nonperformance by the counterparties to these agreements. The Company controls the credit risk of its financial contracts through credit approvals, limits and monitoring procedures, and does not expect any counterparties to fail their obligations. The Company deals only with primary dealers.

Derivative instruments are generally either negotiated Over-the-Counter (OTC) contracts or standardized contracts executed on a recognized exchange. Negotiated OTC derivative contracts are generally entered into between two counterparties that negotiate specific agreement terms, including the underlying instrument, amount, exercise prices and maturity.

The Company issues to customer’s certificates of deposit with an interest rate that is derived from the rate of return on the stock of the companies that comprise The Dow Jones Industrial Average. In order to manage the interest rate risk

associated with this deposit product, the Company has purchased a series of forward option contracts. These contracts provide the Company with a rate of return commensurate with the return of The Dow Jones Industrial Average from the time of the contract until maturity of the related certificates of deposit. These contracts are accounted for as fair value hedges. Because the certificates of deposit can be redeemed by the customer at any time and the related forward options contracts cannot be cancelled by the Company, the hedge is not considered effective. The ineffective portion of the gain or loss on the derivative instrument, if any, is recognized currently in earnings. There was no ineffective portion included in the consolidated income statement for the years ended December 31, 2016, 2015 and 2014.

F & M Bank Corp. and Subsidiaries
Notes to the Consolidated Financial Statements
December 31, 2016 and 2015

NOTE 17
ON BALANCE SHEET DERIVATIVE INSTRUMENTS AND HEDGING ACTIVITIES (CONTINUED):

At December 31, the information pertaining to the forward option contracts, included in other assets and other liabilities on the balance sheet, is as follows:

| | 2016 | 2015 |
|---|---|---|
| Notional amount | $189,629 | $189,629 |
| Fair market value of contracts, included in other assets | 26,327 | 15,162 |

Mortgage Banking Derivatives

Commitments to fund certain mortgage loans originated by VBS (rate lock commitments) to be sold into the secondary market and best efforts commitments for the future delivery of mortgage loans to third party investors are considered derivatives. It is the practice of VBS to enter into best efforts commitments for the future delivery of residential mortgage loans when interest rate lock commitments are entered into in order to economically hedge the effect of changes in interest rates resulting from its commitments to fund the loans. These mortgage banking derivatives are not designated hedge relationships. The fair value of the mortgage banking derivatives were estimated based on changes in interest rates from the date of the commitments and were considered immaterial at December 31, 2016 and 2015.

NOTE 18
TRANSACTIONS WITH RELATED PARTIES:

During the year, executive officers and directors (and companies controlled by them) were customers of and had transactions with the Company in the normal course of business. Management believes these transactions were made on substantially the same terms as those prevailing for other customers and did not involve any abnormal risk.

Loan transactions with related parties are shown in the following schedule:

| | 2016 | 2015 |
|---|---|---|
| Total loans, beginning of year | $7,180,104 | $7,449,140 |
| New loans | 4,701,094 | 5,226,432 |
| Relationship change | 611,415 | (44,948) |
| Repayments | (5,006,226) | (5,450,520) |
| Total loans, end of year | $7,486,387 | $7,180,104 |

Deposit of executive officers and directors and their affiliates were $4,523,561 and $4,529,503 on December 31, 2016 and 2015 respectively. Management believes these deposits were made under the same terms available to other customers of the bank.

NOTE 19
DIVIDEND LIMITATIONS ON SUBSIDIARY BANK:

The principal source of funds of F & M Bank Corp. is dividends paid by the Farmers and Merchants Bank. The Federal Reserve Act restricts the amount of dividends the Bank may pay. Approval by the Board of Governors of the Federal Reserve System is required if the dividends declared by a state member bank, in any year, exceed the sum of (1) net income of the current year and (2) income net of dividends for the preceding two years. As of January 1, 2016, approximately $14,814,000 was available for dividend distribution without permission of the Board of Governors. Dividends paid by the Bank to the Company totaled $5,000,000 in 2016, $2,500,000 in 2015 and $1,300,000 in 2014.

F & M Bank Corp. and Subsidiaries
Notes to the Consolidated Financial Statements
December 31, 2016 and 2015

NOTE 20
FAIR VALUE MEASUREMENTS:

The fair value of a financial instrument is the current amount that would be exchanged between willing parties, other than in a forced liquidation. Fair value is best determined based upon quoted market prices. However, in many instances, there are no quoted market prices for the Company's various financial instruments. In cases where quoted market prices are not available, fair values are based on estimates using present value or other valuation techniques.

Those techniques are significantly affected by the assumptions used, including the discount rate and estimates of future cash flows. Accordingly, the fair value estimates may not be realized in an immediate settlement of the instrument. Accounting guidance for fair value 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 Company.

The Company records fair value adjustments to certain assets and liabilities and determines fair value disclosures utilizing a definition of fair value of assets and liabilities that states that fair value is an exit price, representing the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. Additional considerations are involved to determine the fair value of financial assets in markets that are not active.

The Company uses a hierarchy of valuation techniques based on whether the inputs to those valuation techniques are observable or unobservable. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect the Company's market assumptions. The three levels of the fair value hierarchy based on these two types of inputs are as follows:

| | |
|---|---|
| Level 1 – | Valuation is based on quoted prices in active markets for identical assets and liabilities. |
| Level 2 – | Valuation is based on observable inputs including quoted prices in active markets for similar assets and liabilities, quoted prices for identical or similar assets and liabilities in less active markets, and model-based valuation techniques for which significant assumptions can be derived primarily from or corroborated by observable data in the market. |
| Level 3 – | Valuation is based on model-based techniques that use one or more significant inputs or assumptions that are unobservable in the market. |

The following describes the valuation techniques used by the Company to measure certain financial assets and liabilities recorded at fair value on a recurring basis in the financial statements:

Securities

Where quoted prices are available in an active market, securities are classified within Level 1 of the valuation hierarchy. Level 1 securities would include highly liquid government bonds, mortgage products and exchange traded equities. If quoted market prices are not available, then fair values are estimated by using pricing models, quoted prices of securities with similar characteristics, or discounted cash flow. Level 2 securities would include U.S. agency securities, mortgage-backed agency securities, obligations of states and political subdivisions and certain corporate, asset backed and other securities. In certain cases where there is limited activity or less transparency around inputs to the valuation, securities are classified within Level 3 of the valuation hierarchy. The carrying value of restricted

Federal Reserve Bank and Federal Home Loan Bank stock approximates fair value based upon the redemption provisions of each entity and is therefore excluded from the following table.

Derivatives

The Company's derivatives are recorded at fair value based on third party vendor supplied information using discounted cash flow analysis from observable-market based inputs, which are considered Level 2 inputs.

F & M Bank Corp. and Subsidiaries
Notes to the Consolidated Financial Statements
December 31, 2016 and 2015

NOTE 20
FAIR VALUE MEASUREMENTS (CONTINUED):

The following tables present the balances of financial assets measured at fair value on a recurring basis as of December 31, 2016, and 2015 (dollars in thousands):

| December 31, 2016 | Total | Level 1 | Level 2 | Level 3 |
|---|---|---|---|---|
| U. S. Treasuries | $24,014 | $- | $24,014 | $- |
| Mortgage-backed obligations of federal agencies | 634 | - | 634 | - |
| Equity securities | 135 | - | 135 | - |
| Total securities available for sale | $24,783 | - | $24,783 | - |

| December 31, 2015 | Total | Level 1 | Level 2 | Level 3 |
|---|---|---|---|---|
| U. S. Treasuries | $4,021 | $- | $4,021 | $- |
| U. S. Government sponsored enterprises | 8,074 | - | 8,074 | - |
| Mortgage-backed obligations of federal agencies | 817 | - | 817 | - |
| Equity securities | 135 | - | 135 | - |
| Total securities available for sale | $13,047 | - | $13,047 | - |

Certain financial assets are measured at fair value on a nonrecurring basis in accordance with GAAP. Adjustments to the fair value of these assets usually result from the application of lower-of-cost-or-market accounting or write-downs of individual assets.

The following describes the valuation techniques used by the Company to measure certain financial assets recorded at fair value on a nonrecurring basis in the financial statements:

Loans Held for Sale

Loans held for sale are short-term loans purchased at par for resale to investors at the par value of the loan and loans originated by VBS for sale in the secondary market. Loan participations are generally repurchased within 15 days. Loans originated for sale by VBS are recorded at lower of cost or market. No market adjustments were required at December 31, 2016 or 2015; therefore, loans held for sale were carried at cost. Because of the short-term nature and fixed repurchased price, the book value of these loans approximates fair value at December 31, 2016, and 2015.

Impaired Loans

Loans are designated as impaired when, in the judgment of management based on current information and events, it is probable that all amounts due will not be collected according to the contractual terms of the loan agreement. Troubled debt restructurings are impaired loans. Impaired loans are measured at fair value on a nonrecurring basis. If an individually-evaluated impaired loan's balance exceeds fair value, the amount is allocated to the allowance for loan losses. Any fair value adjustments are recorded in the period incurred as provision for loan losses on the Consolidated Statements of Income.

The fair value of an impaired loan and measurement of associated loss is based on one of three methods: the observable market price of the loan, the present value of projected cash flows, or the fair value of the collateral. The observable market price of a loan is categorized as a Level 1 input. The present value of projected cash flows method results in a Level 3 categorization because the calculation relies on the Company's judgment to determine projected cash flows, which are then discounted at the current rate of the loan, or the rate prior to modification if the loan is a troubled debt restructure.

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Notes to the Consolidated Financial Statements
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NOTE 20 FAIR VALUE MEASUREMENTS (CONTINUED):

Loans measured using the fair value of collateral method are categorized in Level 3. Collateral may be in the form of real estate or business assets including equipment, inventory, and accounts receivable. Most collateral is real estate. The Company bases collateral method fair valuation upon the "as-is" value of independent appraisals or evaluations.

The value of real estate collateral is determined by an independent appraisal utilizing an income or market valuation approach. Appraisals conducted by an independent, licensed appraiser outside of the Company using observable market data is categorized as Level 3. The value of business equipment is based upon an outside appraisal (Level 3) if deemed significant, or the net book value on the applicable business' financial statements (Level 3) if not considered significant. Likewise, values for inventory and accounts receivables collateral are based on financial statement balances or aging reports (Level 3).

As of December 31, 2016, and 2015, the fair value measurements for impaired loans with specific allocations were primarily based upon the fair value of the collateral.

The following table summarizes the Company's financial assets that were measured at fair value on a nonrecurring basis during the period (dollars in thousands):

| December 31, 2016 | Total | Level 1 | Level 2 | Level 3 |
|---|---|---|---|---|
| Construction/Land Development | $4,739 | - | - | $4,739 |
| Real Estate | 985 | - | - | 985 |
| Commercial Real Estate | 892 | - | - | 892 |
| Dealer Finance | 67 | - | - | 67 |
| Impaired loans | $6,683 | - | - | $6,683 |

| December 31, 2015 | Total | Level 1 | Level 2 | Level 3 |
|---|---|---|---|---|
| Construction/Land Development | $9,161 | - | - | $9,161 |
| Real Estate | 86 | - | - | 86 |
| Commercial Real Estate | 872 | - | - | 872 |
| Home Equity – open end | 1,145 | - | - | 1,145 |
| Dealer Finance | 51 | - | - | 51 |
| Impaired loans | $11,315 | - | - | $11,315 |

The following table presents information about Level 3 Fair Value Measurements for December 31, 2016:

| | Fair Value at December 31, 2016 | Valuation Technique | Significant Unobservable Inputs | Range |
|---|---|---|---|---|
| Impaired Loans | $6,683 | Discounted appraised value | Discount for selling costs and marketability | 2%-50% (Average 4.7%) |

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F & M Bank Corp. and Subsidiaries
Notes to the Consolidated Financial Statements
December 31, 2016 and 2015

NOTE 20 FAIR VALUE MEASUREMENTS (CONTINUED):

Other Real Estate Owned

Certain assets such as other real estate owned (OREO) are measured at fair value less cost to sell. Valuation of other real estate owned is determined using current appraisals from independent parties, a level two input. If current appraisals cannot be obtained prior to reporting dates, or if declines in value are identified after a recent appraisal is received, appraisal values are discounted, resulting in Level 3 estimates. If the Company markets the property with a realtor, estimated selling costs reduce the fair value, resulting in a valuation based on Level 3 inputs.

The Company markets other real estate owned both independently and with local realtors. Properties marketed by realtors are discounted by selling costs. Properties that the Company markets independently are not discounted by selling costs.

The following table summarizes the Company's other real estate owned that were measured at fair value on a nonrecurring basis during the period.

| December 31, 2016 | Total | Level 1 | Level 2 | Level 3 |
|---|---|---|---|---|
| Other real estate owned | $2,076 | - | - | $2,076 |

| December 31, 2015 | Total | Level 1 | Level 2 | Level 3 |
|---|---|---|---|---|
| Other real estate owned | $2,128 | - | - | $2,128 |

The following table presents information about Level 3 Fair Value Measurements for December 31, 2016:

| | Fair Value at December 31, 2016 | Valuation Technique | Significant Unobservable Inputs | Range |
|---|---|---|---|---|
| Other real estate owned | $2,076 | Discounted appraised value | Discount for selling costs | 5%-15% (Average 8%) |

The following methods and assumptions were used by the Company in estimating fair value disclosures for financial instruments:

Cash and Due from Bank, and Interest-Bearing Deposits
The carrying amounts approximate fair value.

Securities
The fair values of securities, excluding restricted stock, are determined by quoted market prices or dealer quotes. The fair value of certain state and municipal securities is not readily available through market sources other than dealer quotations, so fair value estimates are based on quoted market prices of similar instruments adjusted for differences between the quoted instruments and the instruments being valued. The carrying value of restricted securities and other investments approximates fair value and are therefore excluded from the following table.

Loans Held for Sale
Fair values of loans held for sale are based on commitments on hand from investors or prevailing market prices.

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Notes to the Consolidated Financial Statements
December 31, 2016 and 2015

NOTE 20 FAIR VALUE (CONTINUED):

Loans
Fair values are estimated for portfolios of loans with similar financial characteristics. Loans are segregated by type such as commercial, real estate – commercial, real estate – construction, real estate – mortgage, credit card and other consumer loans. Each loan category is further segmented into fixed and adjustable rate interest terms and by performing and nonperforming categories.

The fair value of performing loans is calculated by discounting scheduled cash flows through the estimated maturity using estimated market discount rates that reflect the credit and interest rate risk inherent in the loan, as well as estimates for prepayments. The estimate of maturity is based on the Company's historical experience with repayments for loan classification, modified, as required, by an estimate of the effect of economic conditions on lending.

Fair value for significant nonperforming loans is based on estimated cash flows which are discounted using a rate commensurate with the risk associated with the estimated cash flows. Assumptions regarding credit risk, cash flows and discount rates are determined within management's judgment, using available market information and specific borrower information.

Bank-Owned Life Insurance
Bank-owned life insurance represents insurance policies on officers of the Company. The cash values of the policies are estimates using information provided by insurance carriers. These policies are carried at their cash surrender value, which approximates fair value.

Deposits
The fair value of demand and savings deposits is the amount payable on demand. The fair value of fixed maturity term deposits and certificates of deposit is estimated using the rates currently offered for deposits with similar remaining maturities.

Short-Term Debt
The carrying amounts of short-term debt maturing within 90 days approximate their fair values. Fair values of any other short-term debt are estimated using discounted cash flow analyses based on the current incremental borrowing rates for similar types of debt.

Long-Term Debt
The fair value of the Company's long-term debt is estimated using discounted cash flow analyses based on the Company's incremental borrowing rates for similar types of debt arrangements.

Accrued Interest
The carrying amounts of accrued interest approximate fair value.

F & M Bank Corp. and Subsidiaries
Notes to the Consolidated Financial Statements
December 31, 2016 and 2015

NOTE 20 FAIR VALUE (CONTINUED):

The estimated fair values, and related carrying amounts (in thousands), of the Company's financial instruments are as follows:

Fair Value Measurements at December 31, 2016 Using

| (dollars in thousands) | Carrying Amount | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) | Fair Value at December 31, 2016 |
|---|---|---|---|---|---|
| Assets: | | | | | |
| Cash and cash equivalents | $16,355 | $16,355 | $- | $- | $16,355 |
| Securities | 24,908 | - | 24,908 | - | 24,908 |
| Loans held for sale | 62,735 | - | 62,735 | - | 62,735 |
| Loans held for investment, net | 584,093 | - | - | 598,991 | 598,991 |
| Interest receivable | 1,785 | - | 1,785 | - | 1,785 |
| Bank owned life insurance | 13,513 | - | 13,513 | - | 13,513 |
| Total | $703,389 | $16,355 | $102,941 | $598,991 | $718,287 |
| Liabilities: | | | | | |
| Deposits | $537,085 | $- | $379,857 | $158,073 | $537,930 |
| Short-term debt | 40,000 | - | 40,000 | - | 40,000 |
| Long-term debt | 64,237 | - | - | 63,945 | 63,945 |
| Interest payable | 228 | - | 228 | - | 228 |
| Total | $641,550 | $- | $420,085 | $222,018 | $642,103 |

Fair Value Measurements at December 31, 2015 Using

| (dollars in thousands) | Carrying Amount | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) | Fair Value at December 31, 2015 |
|---|---|---|---|---|---|
| Assets: | | | | | |

| | | | | | |
|---|---|---|---|---|---|
| Cash and cash equivalents | $8,519 | $8,519 | $- | $- | $8,519 |
| Securities | 13,172 | - | 13,172 | - | 13,172 |
| Loans held for sale | 57,806 | - | 57,806 | - | 57,806 |
| Loans held for investment, net | 535,272 | - | - | 546,792 | 546,792 |
| Interest receivable | 1,709 | - | 1,709 | - | 1,709 |
| Bank owned life insurance | 13,046 | - | 13,046 | - | 13,046 |
| Total | $629,524 | $8,519 | $85,733 | $546,792 | $641,044 |
| Liabilities: | | | | | |
| Deposits | $494,670 | $- | $333,630 | $162,524 | $496,154 |
| Short-term debt | 24,954 | - | 24,954 | - | 24,954 |
| Long-term debt | 48,161 | - | - | 48,565 | 48,565 |
| Interest payable | 203 | - | 203 | - | 203 |
| Total | $567,988 | $- | $358,787 | $210,685 | $569,472 |

F & M Bank Corp. and Subsidiaries
Notes to the Consolidated Financial Statements
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NOTE 21
REGULATORY MATTERS

The Company meets the eligibility criteria of a small bank holding company in accordance with the Federal Reserve's Small Bank Holding Company Policy Statement issued in February 2015, and is no longer obligated to report consolidated regulatory capital. The Bank is 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 Bank's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Bank must meet specific capital guidelines that involve quantitative measures of the Bank's assets, liabilities, and certain off balance-sheet items as calculated under regulatory accounting practices. The Bank's capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

The final rules implementing the Basel Committee on Banking Supervision's capital guidelines for U.S. Banks (Basel III rules) became effective January 1, 2015, with full compliance of all the requirements being phased in over a multi-year schedule, and becoming fully phased in by January 1, 2019. Under the Basel III rules, the Company must hold a capital conservation buffer above the adequately capitalized risk-based capital ratios. The capital conservation buffer is being phased in from 0.0% for 2015 to 2.50% by 2019. The capital conservation buffer for 2016 is 0.625%. The net unrealized gain on securities available for sale and the unfunded pension liability are not included in computing regulatory capital.

Quantitative measures established by regulation, to ensure capital adequacy, require the Bank to maintain minimum amounts and ratios. These ratios are defined in the regulations and the amounts are set forth in the table below. Management believes, as of December 31, 2016, that the Bank meet all capital adequacy requirements to which they are subject.

As of the most recent notification from the Federal Reserve Bank Report of Examination, the subsidiary bank was categorized as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized, the Bank must maintain minimum total risk based, Tier I risk-based, and Tier I leverage ratios as set forth in the table. There are no conditions or events since that notification that management believes have changed the institution's category.

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NOTE 21
REGULATORY MATTERS (CONTINUED):

The actual capital ratios for the Bank are presented in the following table (dollars in thousands):

| | Actual | | Minimum Capital Requirement | | Minimum to be Well Capitalized Under Prompt Corrective Action Provisions | |
|---|---|---|---|---|---|---|
| December 31, 2016 | Amount | Ratio | Amount | Ratio | Amount | Ratio |
| Total risk-based ratio | $93,519 | 15.08% | $49,615 | 8.00% | $62,019 | 10.00% |
| Tier 1 risk-based ratio | 85,976 | 13.86% | 37,212 | 6.00% | 49,615 | 8.00% |
| Common equity tier 1 | 85,976 | 13.86% | 27,909 | 4.50% | 40,312 | 6.50% |
| Total assets leverage ratio | 85,976 | 11.83% | 29,065 | 4.00% | 36,331 | 5.00% |

| | Actual | | Minimum Capital Requirement | | Minimum to be Well Capitalized Under Prompt Corrective Action Provisions | |
|---|---|---|---|---|---|---|
| December 31, 2015 | Amount | Ratio | Amount | Ratio | Amount | Ratio |
| Total risk-based ratio | $86,053 | 15.24% | $45,157 | 8.00% | 56,447 | 10.00% |
| Tier 1 risk-based ratio | 78,976 | 13.99% | 33,868 | 6.00% | 45,157 | 8.00% |
| Common equity tier 1 | 78,976 | 13.99% | 25,401 | 4.50% | 36,690 | 6.50% |
| Total assets leverage ratio | 78,976 | 12.06% | 26,185 | 4.00% | 32,731 | 5.00% |

F & M Bank Corp. and Subsidiaries
Notes to the Consolidated Financial Statements
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NOTE 22
PARENT COMPANY ONLY FINANCIAL STATEMENTS:
Balance Sheets
December 31, 2016 and 2015

| | 2016 | 2015 |
|---|---|---|
| Assets | | |
| Cash and cash equivalents | $1,154,650 | $1,907,581 |
| Investment in subsidiaries | 85,480,954 | 81,646,312 |
| Securities available for sale | 135,000 | 135,000 |
| Total Assets | $86,770,604 | $83,688,893 |
| Liabilities | | |
| Income tax payable (including due form subsidiary) | $312,087 | $847,001 |
| Deferred income taxes | 307,042 | 301,870 |
| Demand obligations for low income housing investment | 162,290 | 162,290 |
| Total Liabilities | $781,419 | $1,311,161 |
| Stockholders' Equity | | |
| Preferred stock par value $5 per share, 400,000 shares authorized, issued and outstanding | $7,608,873 | $9,425,123 |
| Common stock par value $5 per share, 6,000,000 shares authorized, 3,270,315 and 3,285,404 shares issued and outstanding for 2016 and 2015, respectively | 16,351,575 | 16,427,020 |
| Additional paid in capital | 10,683,583 | 11,149,104 |
| Retained earnings | 54,510,046 | 48,056,300 |
| Accumulated other comprehensive income (loss) | (3,164,892) | (2,679,815) |
| Total Stockholders' Equity | 85,989,185 | 82,377,732 |
| Total Liabilities and Stockholders' Equity | $86,770,604 | $83,688,893 |

Statements of Income
For the years ended December 31, 2016, 2015 and 2014

| | 2016 | 2015 | 2014 |
|---|---|---|---|
| Income | | | |
| Dividends from affiliate | $5,000,000 | $2,500,000 | $1,300,000 |
| Net limited partnership income (loss) | - | 4,792 | - |
| Total Income | 5,000,000 | 2,504,792 | 1,300,000 |
| Expenses | | | |

| | | | |
|---|---|---|---|
| Total Expenses | 1,070 | 21,316 | 7,100 |
| Net income before income tax expense (benefit) and undistributed subsidiary net income | 4,998,930 | 2,483,476 | 1,292,900 |
| Income Tax Expense (Benefit) | (248,836) | (191,494) | 243,492 |
| Income before undistributed subsidiary net income | 5,247,766 | 2,674,970 | 1,049,408 |
| Undistributed subsidiary net income | 4,319,719 | 5,742,039 | 4,752,201 |
| Net Income F&M Bank Corp. | $9,567,485 | $8,417,009 | $5,801,609 |

F & M Bank Corp. and Subsidiaries
Notes to the Consolidated Financial Statements
December 31, 2016 and 2015

NOTE 22
PARENT COMPANY ONLY FINANCIAL STATEMENTS (CONTINUED):

Statements of Cash Flows
For the years ended December 31, 2016, 2015 and 2014

| | 2016 | 2015 | 2014 |
|---|---|---|---|
| Cash Flows from Operating Activities | | | |
| Net income | $9,567,485 | $8,417,009 | $5,801,609 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | | |
| Undistributed subsidiary income | (4,319,719) | (5,742,039) | (4,752,201) |
| Deferred tax (benefit) expense | 5,172 | (81,256) | 279,928 |
| Decrease (increase) in other assets | - | 1,300,586 | (444,885) |
| Increase (decrease) in other liabilities | (534,914) | (143,028) | 137,817 |
| Net Cash Provided by Operating Activities | 4,718,024 | 3,751,272 | 1,022,268 |
| Cash Flows from Investing Activities | | | |
| Purchase of securities available for sale | - | - | (135,000) |
| Net Cash Used in Investing Activities | - | - | (135,000) |
| Cash Flows from Financing Activities | | | |
| Capital contributed to subsidiary | - | - | (19,000,000) |
| Proceeds from issuance of preferred stock | - | - | 9,425,123 |
| Repurchase of preferred stock | (1,961,550) | | |
| Repurchase of common stock | (578,711) | (289,119) | - |
| Proceeds from issuance of common stock | 183,045 | 146,418 | 12,055,709 |
| Dividends paid in cash | (3,113,739) | (2,915,130) | (2,231,912) |
| Net Provided by (Cash Used) in Financing Activities | (5,470,955) | (3,057,831) | 248,920 |
| Net Increase (decrease) in Cash and Cash Equivalents | (752,931) | 693,441 | 1,136,188 |
| Cash and Cash Equivalents, Beginning of Year | 1,907,581 | 1,214,140 | 77,952 |
| Cash and Cash Equivalents, End of Year | $1,154,650 | $1,907,581 | $1,214,140 |

F & M Bank Corp. and Subsidiaries
Notes to the Consolidated Financial Statements
December 31, 2016 and 2015

NOTE 23
INVESTMENT IN VBS MORTGAGE, LLC

On November 3, 2008, the Bank acquired a 70% ownership interest in VBS Mortgage, LLC (formerly Valley Broker Services, DBA VBS Mortgage). VBS originates both conventional and government sponsored mortgages for sale in the secondary market. As of December 31, 2016, and 2015, VBS' summarized balance sheet and income statement were as follows:

Balance Sheets
December 31, 2016 and 2015

| | 2016 | 2015 |
|---|---|---|
| Assets | | |
| Cash and cash equivalents | $1,397,411 | $1,071,293 |
| Loans Receivable | 5,749,139 | 763,534 |
| Property and equipment, net | 72,120 | 79,038 |
| Other Assets | 268,346 | 266,073 |
| Total Assets | $7,487,016 | $2,179,938 |
| Liabilities | | |
| Lind of credit | 4,713,054 | - |
| Other liabilities | 465,183 | 271,004 |
| Total Liabilities | $5,178,237 | $271,004 |
| Equity | | |
| Capital | 219,634 | 219,634 |
| Retained earnings | 2,089,145 | 1,689,300 |
| Total Equity | $2,308,779 | $1,908,934 |
| Total Liabilities and Equity | $7,487,016 | $2,179,938 |

Statements of Income
For the years ended December 31, 2016, 2015 and 2014

| | 2016 | 2015 | 2014 |
|---|---|---|---|
| Income | | | |
| Mortgage origination income | $3,314,350 | $2,645,235 | $1,907,804 |
| Other Income | 38,647 | 51,175 | 53,528 |
| Total Income | 3,352,997 | 2,696,410 | 1,961,332 |

| | | | |
|---|---|---|---|
| Expenses | | | |
| Salaries and employee benefits | 1,819,537 | 1,413,107 | 1,105,902 |
| Occupancy and equipment expense | 223,698 | 212,858 | 177,014 |
| Management and professional fees | 337,605 | 290,102 | 321,053 |
| Other | 325,449 | 231,757 | 205,188 |
| Total Expenses | 2,706,289 | 2,147,824 | 1,809,157 |
| Net income | $646,708 | $548,586 | $152,175 |

F & M Bank Corp. and Subsidiaries
Notes to the Consolidated Financial Statements
December 31, 2016 and 2015

NOTE 24 ACCUMULATED OTHER COMPREHENSIVE LOSS

The balances in accumulated other comprehensive loss are shown in the following table:

| dollars in thousands | Unrealized Securities Gains (Losses) | Adjustments Related to Pension Plan | Accumulated Other Comprehensive Loss |
|---|---|---|---|
| Balance at December, 31, 2013 | $(12) | $(914) | $(926) |
| Change in unrealized securities gains (losses), net of tax | 15 | - | 15 |
| Change in unfunded pension liability, net of tax | - | (1,416) | (1,416) |
| Balance at December, 31, 2014 | 3 | (2,330) | (2,327) |
| Change in unrealized securities gains (losses), net of tax | 1 | - | 1 |
| Change in unfunded pension liability, net of tax | - | (354) | (354) |
| Balance at December, 31, 2015 | 4 | (2,684) | (2,680) |
| Change in unrealized securities gains (losses), net of tax | 2 | - | 2 |
| Change in unfunded pension liability, net of tax | - | (487) | (487) |
| Balance at December, 31, 2016 | $6 | $(3,171) | $(3,165) |

There were no reclassifications adjustments reported on the consolidated statements of income during 2014, 2015 or 2016.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders
F&M Bank Corp.
Timberville, Virginia

We have audited the accompanying consolidated balance sheet of F&M Bank Corp. and subsidiaries (the Company) as of December 31, 2016, and the related consolidated statement of income, comprehensive income, stockholders' equity and cash flow for the year then ended (collectively, the financial statements). These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements 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 the financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides 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 F&M Bank Corp. and subsidiaries as of December 31, 2016, and the results of their operations and their cash flows for the year then ended in conformity with U.S. generally accepted accounting principles.

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

Winchester, Virginia
March 28, 2017

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Stockholders
F & M Bank Corp. and Subsidiaries
Timberville, Virginia

We have audited the accompanying consolidated balance sheets of F&M Bank Corp. and Subsidiaries (the "Company") as of December 31, 2015 and 2014, and the related consolidated statements of income, comprehensive income, changes in stockholders' equity and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of F&M Bank Corp. and Subsidiaries as of December 31, 2015 and 2014, and the results of their operations and their cash flows for the years then ended, in conformity with generally accepted accounting principles in the United States of America.

/s/ Elliott Davis Decosimo, PLLC

Raleigh, North Carolina
March 28, 2017

Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure

Information required by this item is in our form 8-K dated October 17, 2016 and is incorporated by reference herein.

Item 9A. Controls and Procedures

Disclosure Controls and Procedures. The Company, under the supervision and with the participation of management, including the Company's Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of the design and operation of its disclosure controls and procedures as of the end of the period covered by this Annual Report on Form 10-K. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer have concluded that the Company's disclosure controls and procedures were effective as of December 31, 2016 to ensure that information required to be disclosed by the Company in reports that it files or submits under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms and is accumulated and communicated to the Company's management, including its Chief Executive Officer and Chief Financial Officer as appropriate to allow timely decisions regarding required disclosures.

Management's Report on Internal Control over Financial Reporting. Management is responsible for establishing and maintaining adequate internal control over financial reporting (as such term is defined in Rule 13a-15(f) and Rule 15d – 15(f) under the Exchange Act). Our internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of our assets; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that our receipts and expenditures are being made only in accordance with authorizations of our management and directors; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of our assets that could have a material effect on the financial statements.

Because of the inherent limitations in any internal control, no matter how well designed, misstatements may occur and not be prevented or detected. Accordingly, even effective internal control over financial reporting can provide only reasonable assurance with respect to financial statement preparation. Further, the evaluation of the effectiveness of internal control over financial reporting was made as of a specific date, and continued effectiveness in future periods is subject to the risks that controls may become inadequate because of changes in conditions or that the degree of compliance with the policies and procedures may decline.

Management conducted an evaluation of the effectiveness of our system of internal control over financial reporting as of December 31, 2016 based on the framework set forth in "Internal Control - Integrated Framework" issued by the Committee of Sponsoring Organizations of the Treadway Commission in 2013. Based on its evaluation, management concluded that, as of December 31, 2016, F&M's internal control over financial reporting was effective.

This annual report does not include an attestation report of the Company's registered public accounting firm regarding internal control over financial reporting. Management's report was not subject to attestation by the Company's registered public accounting firm pursuant to rules of the Securities and Exchange Commission that permit the Company to provide only management's report in this annual report.

Changes in Internal Control over Financial Reporting. There were no changes in the Company's internal control over financial reporting during the Company's quarter ended December 31, 2016 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

Item 9B. Other Information

None.

PART III

Item 10. Directors, Executive Officers and Corporate Governance

Information regarding directors, executive officers and the audit committee financial expert is incorporated by reference from the Company's definitive proxy statement for the Company's 2017 Annual Meeting of Shareholders to be held May 13, 2017 ("Proxy Statement"), under the captions "Election of Directors," "Board of Directors and Committees," and "Executive Officers."

Information on Section 16(a) beneficial ownership reporting compliance for the directors and executive officers of the Company is incorporated by reference from the Proxy Statement under the caption "Section 16(a) Beneficial Ownership Reporting Compliance."

The Company has adopted a broad based code of ethics for all employees and directors. The Company has also adopted a code of ethics tailored to senior officers who have financial responsibilities. A copy of the codes may be obtained without charge by request from the corporate secretary.

Item 11. Executive Compensation

This information is incorporated by reference from the Proxy Statement under the caption "Executive Compensation."

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

This information is incorporated by reference from the Proxy Statement under the caption "Ownership of Company Common Stock" and "Executive Compensation" and from Item 5 of this 10-K.

Item 13. Certain Relationships and Related Transactions, and Directors Independence

This information is incorporated by reference from the Proxy Statement under the caption "Interest of Directors and Officers in Certain Transactions."

Item 14. Principal Accounting Fees and Services

This information is incorporated by reference from the Proxy Statement under the caption "Principal Accounting Fees."

PART IV

Item 15. Exhibits and Financial Statement Schedules

The following financial statements are filed as a part of this report:

(a)(1) Financial Statements

The following consolidated financial statements and reports of independent auditors of the Company are in Part II, Item 8 on pages 38 thru 89:


| | |
|---|---|
| Consolidated Balance Sheets - December 31, 2016 and 2015 | 38 |
| Consolidated Statements of Income - Years ended December 31, 2016, 2015 and 2014 | 39 |
| Consolidated Statements of Comprehensive Income - Years ended December 31, 2016, 2015 and 2014 | 40 |
| Consolidated Statements of Changes in Stockholders' Equity – Years ended December 31, 2016, 2015 and 2014 | 41 |

Consolidated Statements of Cash Flows - Years ended December 31, 2016, 2015 and 2014 42
Notes to the Consolidated Financial Statements 43
Reports of Independent Registered Public Accounting Firms 88

PART IV

Item 15. Exhibits and Financial Statement Schedules, continued

(a)(2) Financial Statement Schedules

All schedules are omitted since they are not required, are not applicable, or the required information is shown in the consolidated financial statements or notes thereto.

(a)(3) Exhibits

The following exhibits are filed as a part of this form 10-K:

Exhibit No.
3.1
Restated Articles of Incorporation of F & M Bank Corp., incorporated herein by reference from F & M Bank Corp.'s, Quarterly Report on Form 10-Q, filed November 14, 2013.
3.2
Amended and Restated Bylaws of F & M Bank Corp., incorporated herein by reference from F & M Bank Corp.'s, Annual Report on Form 10-K, filed March 8, 2002.
3.2
Articles of Amendment to the Articles of Incorporation of F&M Bank Corp. designating the Series A Preferred Stock incorporated herein by reference from F&M Bank Corp,'s current report on Form 8-K filed December 4, 2014.
10.1
Change in Control Severance Plan, incorporated herein by reference from Exhibit 10.1 to F&M Bank Corp.'s Registration Statement on Form S-1, filed December 22, 2010.
10.2
VBA Executives Deferred Compensation Plan for Farmers & Merchants Bank, incorporated herein by reference from F & M Bank Corp.'s Annual Report on Form 10-K, filed March 28, 2014.
10.3
VBA Directors Non-Qualified Deferred Compensation Plan for Farmers & Merchants Bank, incorporated herein by reference from F & M Bank Corp.'s Annual Report on Form 10-K, filed March 28, 2014.
21.0
Subsidiaries of the Registrant
23.1
Consent of Yount, Hyde & Barbour, P.C.
23.2
Consent of Elliott Davis Decosimo, PLLC
31.1
Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2
Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1
Certification of Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101
The following materials from F&M Bank Corp.'s Annual Report on Form 10-K for the year ended December 31, 2016, formatted in Extensible Business Reporting Language (XBRL), include: (i) Consolidated Balance Sheets, (ii) Consolidated Statements of Income, (iii) Consolidated Statements of Comprehensive Income, (iv) Consolidated

Statements of Changes in Stockholders' Equity, (v) Consolidated Statements of Cash Flows and (vi) related notes (furnished herewith).

Item 16 Form 10-K Summary

Not Required

Shareholders may obtain, free of charge, a copy of the exhibits to this Report on Form 10-K by writing Larry A. Caplinger, Corporate Secretary, at F & M Bank Corp., P.O. Box 1111, Timberville, VA 22853 or our website at www.fmbankva.com.

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.

F & M Bank Corp.
(Registrant)

| | |
|---|---|
| By: /s/ Dean W. Withers | March 28, 2017 |
| Dean W. Withers<br>Director, President and Chief Executive Officer | Date |

| | |
|---|---|
| By: /s/ Carrie A. Comer | March 28, 2017 |
| Carrie A. Comer<br>Senior Vice President and Chief Financial Officer | Date |

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 as of the date indicated.

| Signature | Title | Date |
|---|---|---|
| /s/ Larry A. Caplinger<br>Larry A. Caplinger | Director | March 28, 2017 |
| /s/ John N. Crist<br>John N. Crist | Director | March 28, 2017 |
| /s/ Ellen R. Fitzwater<br>Ellen R. Fitzwater | Director, Chair | March 28, 2017 |
| /s/ Daniel J. Harshman<br>Daniel J. Harshman | Director | March 28, 2017 |
| /s/ Richard S. Myers<br>Richard S. Myers | Director | March 28, 2017 |
| /s/ Michael W. Pugh<br>Michael W. Pugh | Director | March 28, 2017 |

| | | |
|---|---|---|
| /s/ Christopher S. Runion<br>Christopher S. Runion | Director | March 28, 2017 |
| /s/ Ronald E. Wampler<br>Ronald E. Wampler | Director | March 28, 2017 |
| /s/ E. Ray Burkholder<br>E. Ray Burkholder | Director | March 28, 2017 |

Exhibit Index:

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The following materials from F&M Bank Corp.'s Annual Report on Form 10-K for the year ended December 31, 2016, formatted in Extensible Business Reporting Language (XBRL), include: (i) Consolidated Balance Sheets, (ii) Consolidated Statements of Income, (iii) Consolidated Statements of Comprehensive Income, (iv) Consolidated Statements of Changes in Stockholders' Equity, (v) Consolidated Statements of Cash Flows and (vi) related notes (furnished herewith).