FIRST COMMUNITY BANCSHARES INC /NV/
Form 10-K/A
March 07, 2017
Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K/A

Amendment No. 1

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF

THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2016

Commission file number 000-19297

FIRST COMMUNITY BANCSHARES, INC.

(Exact name of registrant as specified in its charter)

Nevada	**55-0694814**
(State or other jurisdiction of	**(I.R.S. Employer**
incorporation or organization)	**Identification No.)**

P.O. Box 989

Bluefield, Virginia 24605-0989

(Address of principal executive offices) (Zip Code)

Registrant s telephone number, including area code: (276) 326-9000

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

Title of each class	**Name of each exchange on which registered**
Common Stock, $1.00 par value	NASDAQ Global Select

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

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

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

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

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

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

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

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

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

As of June 30, 2016, the aggregate market value of the registrant s voting and non-voting common stock held by non-affiliates was $294.92 million.

As of February 28, 2017, there were 16,994,616 shares outstanding of the registrant s Common Stock, $1.00 par value.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Proxy Statement for the Annual Meeting of Stockholders to be held on April 25, 2017, are incorporated by reference in Part III of this Form 10-K.

Table of Contents

EXPLANATORY NOTE

This Amendment No. 1 on Form 10-K/A amends the Annual Report on Form 10-K of First Community Bancshares, Inc. (the Company) for the year ended December 31, 2016, filed with the Securities and Exchange Commission on March 3, 2017 (the Original Form 10-K), solely to correct the date of the Report of Independent Registered Public Accounting Firm on Consolidated Financial Statements of Dixon Hughes Goodman LLP (the Report) from March 4, 2017, to March 3, 2017. The Report of Independent Registered Public Accounting Firm on Consolidated Financial Statements and the Report of Independent Registered Public Accounting Firm on Management s Assessment of Internal Control Over Financial Reporting with the correct date are filed with this Form 10-K/A.

In accordance with Rule 12b-15 under the Securities Exchange Act of 1934, as amended, Part II, Item 8 has been amended and restated in its entirety; however, there have been no changes to the text of such Part II, Item 8 other than the change stated in the preceding paragraph. Further, there have been no changes to the XBRL data filed in Exhibit 101 of the Original Form 10-K. As required by Rule 12b-15, this Form 10-K/A includes a new consent of the independent registered public accounting firm as Exhibit 23 and new certifications pursuant to Sections 302 and 906 of the Sarbanes-Oxley Act of 2002 as Exhibits 31.1, 31.2, and 32.

Except as described above, this Form 10-K/A does not amend, update, or restate the information in any other Item of the Original Form 10-K or reflect any events that have occurred after the filing of the Original Form 10-K.

Table of Contents

PART II

Item 8. Financial Statements and Supplementary Data.

FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA INDEX

Table of Contents

FIRST COMMUNITY BANCSHARES, INC.

CONSOLIDATED BALANCE SHEETS

(Amounts in thousands, except share and per share data)	December 31, 2016	December 31, 2015
Assets		
Cash and due from banks	$ 36,645	$ 37,383
Federal funds sold	38,717	13,498
Interest-bearing deposits in banks	945	906
Total cash and cash equivalents	76,307	51,787
Securities available for sale	165,579	366,173
Securities held to maturity	47,133	72,541
Loans held for investment, net of unearned income		
Non-covered	1,795,954	1,623,506
Covered	56,994	83,035
Allowance for loan losses	(17,948)	(20,233)
Loans held for investment, net	1,835,000	1,686,308
FDIC indemnification asset	12,173	20,844
Premises and equipment, net	50,085	52,756
Other real estate owned, non-covered	5,109	4,873
Other real estate owned, covered	276	4,034
Interest receivable	5,553	6,007
Goodwill	95,779	100,486
Other intangible assets	7,207	5,243
Other assets	86,197	91,224
Total assets	$ 2,386,398	$ 2,462,276
Liabilities		
Deposits		
Noninterest-bearing	$ 427,705	$ 451,511
Interest-bearing	1,413,633	1,421,748
Total deposits	1,841,338	1,873,259
Securities sold under agreements to repurchase	98,005	138,614
FHLB borrowings	65,000	65,000
Other borrowings	15,708	15,756
Interest, taxes, and other liabilities	27,290	26,630
Total liabilities	2,047,341	2,119,259
Stockholders equity		
Preferred stock, undesignated par value; 1,000,000 shares authorized; Series A Noncumulative Convertible Preferred Stock, $0.01 par value; 25,000 shares authorized; none outstanding		
Common stock, $1 par value; 50,000,000 shares authorized; 21,381,779 shares issued at December 31, 2016 and 2015, including 4,387,571 and 3,283,638 shares in treasury, respectively	21,382	21,382
Additional paid-in capital	228,142	227,692
Retained earnings	170,377	155,647
Treasury stock	(78,833)	(56,457)
Accumulated other comprehensive loss	(2,011)	(5,247)
Total stockholders equity	339,057	343,017

Total liabilities and stockholders equity	$ 2,386,398	$ 2,462,276

See Notes to Consolidated Financial Statements.

Table of Contents

FIRST COMMUNITY BANCSHARES, INC.

CONSOLIDATED STATEMENTS OF INCOME

(Amounts in thousands, except share and per share data)	Year Ended December 31, 2016	2015	2014
Interest income			
Interest and fees on loans	$ 87,718	$ 87,632	$ 95,492
Interest on securities taxable	3,229	4,225	5,975
Interest on securities tax-exempt	3,624	3,978	4,350
Interest on deposits in banks	153	267	291
Total interest income	94,724	96,102	106,108
Interest expense			
Interest on deposits	4,479	5,878	7,308
Interest on short-term borrowings	2,101	1,952	2,024
Interest on long-term debt	3,264	3,519	5,958
Total interest expense	9,844	11,349	15,290
Net interest income	84,880	84,753	90,818
Provision for loan losses	1,255	2,191	145
Net interest income after provision for loan losses	83,625	82,562	90,673
Noninterest income			
Wealth management	2,828	2,975	3,030
Service charges on deposits	13,588	13,717	13,828
Other service charges and fees	8,102	8,045	7,581
Insurance commissions	5,442	6,899	6,555
Impairment losses on securities	(4,646)		(737)
Portion of loss recognized in other comprehensive income			
Net impairment losses recognized in earnings	(4,646)		(737)
Net gain (loss) on sale of securities	335	144	(1,385)
Net FDIC indemnification asset amortization	(5,474)	(6,379)	(3,979)
Net gain on divestitures	3,682		755
Other operating income	3,209	4,129	4,355
Total noninterest income	27,066	29,530	30,003
Noninterest expense			
Salaries and employee benefits	39,912	39,625	40,713
Occupancy expense	5,297	5,817	6,338
Furniture and equipment expense	4,341	5,199	4,952
Amortization of intangibles	1,136	1,118	787
FDIC premiums and assessments	1,383	1,513	1,672
FHLB debt prepayment fees		1,702	5,008
Merger, acquisition, and divestiture expense	730	86	1,150
Other operating expense	19,947	21,111	22,242
Total noninterest expense	72,746	76,171	82,862
Income before income taxes	37,945	35,921	37,814
Income tax expense	12,819	11,381	12,324

Net income		25,126		24,540		25,490
Dividends on preferred stock				105		910
Net income available to common shareholders	$	25,126	$	24,435	$	24,580
Earnings per common share						
Basic	$	1.45	$	1.32	$	1.34
Diluted		1.45		1.31		1.31
Cash dividends per common share		0.60		0.54		0.50
Weighted average shares outstanding						
Basic		17,319,689		18,531,039		18,406,363
Diluted		17,365,524		18,727,464		19,483,054

See Notes to Consolidated Financial Statements.

Table of Contents

FIRST COMMUNITY BANCSHARES, INC

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

	Year Ended December 31,		
(Amounts in thousands)	**2016**	**2015**	**2014**
Net income	$ 25,126	$ 24,540	$ 25,490
Other comprehensive income, before tax			
Available-for-sale securities			
Change in net unrealized losses on securities with other-than-temporary impairment			(1)
Change in net unrealized gains on securities without other-than-temporary impairment	1,035	755	12,914
Reclassification adjustment for net (gains) losses recognized in net income	(335)	(144)	1,385
Reclassification adjustment for other-than-temporary impairment losses recognized in net income	4,646		737
Net unrealized gains on available-for-sale securities	5,346	611	15,035
Employee benefit plans			
Net actuarial loss	(367)	(363)	(642)
Plan change	(69)		
Reclassification adjustment for amortization of prior service cost and net actuarial loss recognized in net income	273	326	260
Net unrealized losses on employee benefit plans	(163)	(37)	(382)
Other comprehensive income, before tax	5,183	574	14,653
Income tax expense	(1,947)	(216)	(5,518)
Other comprehensive income, net of tax	3,236	358	9,135
Total comprehensive income	$ 28,362	$ 24,898	$ 34,625

See Notes to Consolidated Financial Statements.

6

Table of Contents

FIRST COMMUNITY BANCSHARES, INC.

CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS EQUITY

(Amounts in thousands, except share and per share data)	Preferred Stock	Common Stock	Additional Paid-in Capital	Retained Earnings	Treasury Stock	Accumulated Other Comprehensive Income (Loss)	Total
Balance January 1, 2014	$ 15,251	$ 20,493	$ 215,663	$ 125,826	$ (33,887)	$ (14,740)	$ 328,606
Net income				25,490			25,490
Other comprehensive income						9,135	9,135
Common dividends declared $0.50 per share				(9,200)			(9,200)
Preferred dividends declared $60.00 per share				(910)			(910)
Preferred stock converted to common stock 6,900 shares	(100)	7	93				
Equity-based compensation expense			332				332
Common stock options exercised 3,854 shares			(13)		66		53
Restricted stock awards 13,933 shares			(202)		238		36
Purchase of treasury shares 132,773 shares at $16.29 per share					(2,168)		(2,168)
Balance December 31, 2014	$ 15,151	$ 20,500	$ 215,873	$ 141,206	$ (35,751)	$ (5,605)	$ 351,374
Balance January 1, 2015	$ 15,151	$ 20,500	$ 215,873	$ 141,206	$ (35,751)	$ (5,605)	$ 351,374
Net income				24,540			24,540
Other comprehensive income						358	358
Common dividends declared $0.54 per share				(9,994)			(9,994)
Preferred dividends declared $15.00 per share				(105)			(105)
Preferred stock converted to common stock 882,096 shares	(12,784)	882	11,902				
Redemption of preferred stock 2,367 shares	(2,367)						(2,367)
Equity-based compensation expense			110				110
Common stock options exercised 4,323 shares			(11)		74		63
Restricted stock awards 23,057 shares			(191)		391		200
Issuance of treasury stock to 401(k) plan 20,745 shares			9		354		363
Purchase of treasury shares 1,238,299 shares at $17.35 per share					(21,525)		(21,525)
Balance December 31, 2015	$	$ 21,382	$ 227,692	$ 155,647	$ (56,457)	$ (5,247)	$ 343,017
Balance January 1, 2016	$	$ 21,382	$ 227,692	$ 155,647	$ (56,457)	$ (5,247)	$ 343,017
Net income				25,126			25,126
Other comprehensive income						3,236	3,236
Common dividends declared $0.60 per share				(10,396)			(10,396)
Equity-based compensation expense			209				209
Common stock options exercised 43,463 shares			146		775		921
Restricted stock awards 16,680 shares			32		290		322
Issuance of treasury stock to 401(k) plan 18,218 shares			63		321		384
Purchase of treasury shares 1,182,294 shares at $20.06 per share					(23,762)		(23,762)
Balance December 31, 2016	$	$ 21,382	$ 228,142	$ 170,377	$ (78,833)	$ (2,011)	$ 339,057

See Notes to Consolidated Financial Statements.

Table of Contents

FIRST COMMUNITY BANCSHARES, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Amounts in thousands)	Year Ended December 31, 2016	2015	2014
Operating activities			
Net income	$ 25,126	$ 24,540	$ 25,490
Adjustments to reconcile net income to net cash provided by operating activities			
Provision for loan losses	1,255	2,191	145
Depreciation and amortization of property, plant, and equipment	3,563	4,135	4,405
Amortization of premiums on investments, net	1,066	1,375	961
Amortization of FDIC indemnification asset, net	5,474	6,379	3,979
Amortization of intangible assets	1,136	1,118	787
Accretion on acquired loans	(4,766)	(7,109)	(9,645)
Gain on divestiture, net	(3,682)		(755)
Gain on sale of loans, net		(501)	(671)
Equity-based compensation expense	209	110	332
Restricted stock awards	322	200	36
Issuance of treasury stock to 401(k) plan	384	363	
Loss (gain) on sale of property, plant, and equipment, net	238	23	(113)
Loss on sale of other real estate	1,495	3,002	3,227
(Gain) loss on sale of securities	(335)	(144)	1,385
Net impairment losses recognized in earnings	4,646		737
FHLB debt prepayment fees		1,702	5,008
Proceeds from sale of mortgage loans		21,993	28,443
Originations of mortgage loans		(19,700)	(28,681)
Decrease in accrued interest receivable	454	308	1,206
Decrease in other operating activities	6,503	18,534	5,413
Net cash provided by operating activities	43,088	58,519	41,689
Investing activities			
Proceeds from sale of securities available for sale	104,928	10,999	162,443
Proceeds from maturities, prepayments, and calls of securities available for sale	99,906	29,931	48,915
Proceeds from maturities and calls of securities held to maturity	25,190	190	190
Payments to acquire securities available for sale	(1,174)	(81,540)	(6,047)
Payments to acquire securities held to maturity		(15,003)	(57,675)
Originations of loans, net	(159,243)	(24,719)	(64,115)
Proceeds from FHLB stock, net	130	1,279	4,349
Cash proceeds from (paid in) mergers, acquisitions, and divestitures, net *(See Note 2)*	29,716	(88)	178,604
Proceeds from the FDIC	4,403	2,683	4,770
Payments to acquire property, plant, and equipment, net	(793)	(1,239)	(1,098)
Proceeds from sale of other real estate	7,147	6,722	10,619
Net cash provided by (used in) investing activities	110,210	(70,785)	280,955
Financing activities			
(Decrease) increase in noninterest-bearing deposits, net	(17,482)	33,782	68,246
Decrease in interest-bearing deposits, net	(37,576)	(161,282)	(121,912)
Decrease in federal funds purchased			(16,000)
(Repayments of) proceeds from securities sold under agreements to repurchase, net	(40,609)	16,872	3,432
Repayments of FHLB and other borrowings, net	(48)	(28,945)	(63,097)
Redemption of preferred stock		(2,367)	
Proceeds from stock options exercised	921	63	53
Excess tax benefit from equity-based compensation	174	8	5
Payments for repurchase of treasury stock	(23,762)	(21,525)	(2,168)
Payments of common dividends	(10,396)	(9,994)	(9,200)
Payments of preferred dividends		(219)	(910)
Net cash used in financing activities	(128,778)	(173,607)	(141,551)

Net increase (decrease) in cash and cash equivalents	24,520	(185,873)	181,093
Cash and cash equivalents at beginning of period	51,787	237,660	56,567
Cash and cash equivalents at end of period	$ 76,307	$ 51,787	$ 237,660
Supplemental disclosure cash flow information			
Cash paid for interest	$ 9,845	$ 11,757	$ 15,791
Cash paid for income taxes	6,588	6,900	12,552
Supplemental transactions noncash items			
Transfer of loans to other real estate	5,162	6,317	12,620
Loans originated to finance other real estate	57	649	671

See Notes to Consolidated Financial Statements.

8

Table of Contents

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 1. Basis of Presentation and Significant Accounting Policies

Basis of Presentation

First Community Bancshares, Inc. (the Company) is a financial holding company headquartered in Bluefield, Virginia that provides banking products and services to individuals and commercial customers through its wholly owned subsidiary First Community Bank (the Bank). The Bank offers insurance products and services through First Community Insurance Services (FCIS) and trust and wealth management services through its Trust Division and wholly owned subsidiary First Community Wealth Management. Unless the context suggests otherwise, the term Company refers to First Community Bancshares, Inc. and its subsidiaries as a consolidated entity.

Principles of Consolidation

The Company s accounting and reporting policies conform with U.S. generally accepted accounting principles (GAAP) and prevailing practices in the banking industry. The consolidated financial statements include all accounts of the Company and its wholly owned subsidiaries and eliminate all intercompany balances and transactions. The Company operates in one business segment, Community Banking, which consists of all operations, including commercial and consumer banking, lending activities, wealth management, and insurance services.

The Company maintains investments in variable interest entities (VIEs). VIEs are legal entities in which equity investors do not have sufficient equity at risk for the entity to independently finance its activities, or as a group, the holders of the equity investment at risk lack the power through voting or similar rights to direct the activities of the entity that most significantly impact its economic performance, or do not have the obligation to absorb the expected losses of the entity or the right to receive expected residual returns of the entity. Consolidation of a VIE is required if a reporting entity is the primary beneficiary of the VIE. The Company periodically reviews its VIEs and has determined that it is not the primary beneficiary of any VIE; therefore, the assets and liabilities of these entities are not consolidated into the financial statements.

Use of Estimates

Preparation of the consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the balance sheet and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that require the most subjective or complex judgments relate to fair value measurements, investment securities, the allowance for loan losses, the Federal Deposit Insurance Corporation (FDIC) indemnification asset, goodwill and other intangible assets, and income taxes.

Reclassification

Certain amounts reported in prior years have been reclassified to conform to the current year s presentation. These reclassifications had no effect on the Company s results of operations, financial position, or cash flow.

Summary of Significant Accounting Policies

Fair Value Measurements

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability, in the principal or most advantageous market for the asset or liability, in an orderly transaction between market participants. Market participants are buyers and sellers in the principal market that are independent,

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

knowledgeable, able to transact, and willing to transact. The fair value hierarchy ranks the inputs used in measuring fair value as follows:

Level 1 Observable, unadjusted quoted prices in active markets

Level 2 Inputs other than quoted prices included in Level 1 that are directly or indirectly observable for the asset or liability

Level 3 Unobservable inputs with little or no market activity that require the Company to use reasonable inputs and assumptions

These valuation methodologies are applied to all the Company s assets and liabilities carried at fair value. Methodologies used to determine fair value might be highly subjective and judgmental in nature. The Company may record adjustments to certain financial assets and liabilities on a recurring basis. The Company may be required to record certain assets at fair value on a nonrecurring basis in specific circumstances, such as evidence of impairment. If the Company determines that a valuation technique change is necessary, the change is assumed to have occurred at the end of the respective reporting period.

Cash and Cash Equivalents

Cash and cash equivalents include cash and due from banks, federal funds sold, and interest-bearing balances on deposit with the Federal Home Loan Bank (FHLB), the Federal Reserve Bank (FRB), and correspondent banks that are available for immediate withdrawal.

Investment Securities

Management classifies debt and marketable equity securities as held-to-maturity or available-for-sale based on the intent and ability to hold the securities to maturity. Debt securities that the Company has the intent and ability to hold to maturity are classified as held-to-maturity securities and carried at amortized cost. Debt securities not classified as held to maturity and marketable equity securities are classified as available-for-sale securities and carried at estimated fair value. Available-for-sale securities consist of securities the Company intends to hold for indefinite periods of time including securities to be used as part of the Company s asset/liability management strategy and securities that may be sold in response to changes in interest rates, prepayment risk, or other similar factors. Unrealized gains and losses on available-for-sale securities are included in accumulated other comprehensive income (AOCI), net of income taxes, in stockholders equity. Gains or losses on calls, maturities, or sales of investment securities are recorded based on the specific identification method and included in noninterest income. Premiums and discounts are amortized or accreted over the life of a security into interest income. Nonmarketable equity investments are reported in other assets. The Company performs extensive quarterly reviews of held-to-maturity and available-for-sale securities to determine if unrealized losses are temporary or other than temporary. If the security is deemed to have other-than-temporary impairment (OTTI), the amount representing the credit loss is recognized as a charge to noninterest income and the amount representing all other factors is recognized in other comprehensive income (OCI).

Nonmarketable Equity Investments

As a condition of membership in the FHLB and the FRB, the Company is required to hold a minimum level of stock in the FHLB of Atlanta and the FRB of Richmond. These nonmarketable securities are carried at cost and periodically reviewed for impairment. When evaluating these investments, managements considers publicly available information about the profitability and asset quality of the issuer, dividend payment history, and redemption experience in determining the recoverability of the investment. The investment in FHLB and FRB stock was $10.60 million as of December 31, 2016, and $10.73 million as of December 31, 2015.

Table of Contents

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Other Investments

The Company has certain long-term investments that are considered VIEs, including its subsidiary FCBI Capital Trust (the Trust), certain tax credit limited partnerships, and various limited liability companies that manage real estate investments, facilitate tax credits, and provide title insurance and other related financial services. The Company uses the equity method of accounting if it is able to exercise significant influence over the entity and records its share of the entity s earnings or losses in noninterest income. The Company uses the cost method of accounting if it is not able to exercise significant influence over the entity. There were no equity investments as of December 31, 2016, or December 31, 2015. The carrying value and maximum potential loss exposure of VIEs totaled $1.14 million as of December 31, 2016, and $934 thousand as of December 31, 2015.

Business Combinations

The Company accounts for business combinations using the acquisition method of accounting as outlined in using Topic 805 of the Financial Accounting Standards Board s (FASB) Accounting Standards Codification (ASC). Under this method, all identifiable assets acquired, including purchased loans, and liabilities assumed are recorded at fair value. Any excess of the purchase price over the fair value of net assets acquired is recorded as goodwill. In instances where the price of the acquired business is less than the net assets acquired, a gain on the purchase is recorded. Fair values are assigned based on quoted prices for similar assets, if readily available, or appraisals by qualified independent parties for relevant asset and liability categories. Certain financial assets and liabilities are valued using discount models that apply current discount rates to streams of cash flow. Valuation methods require assumptions, which can result in alternate valuations, varying levels of goodwill or bargain purchase gains, or amortization expense or accretion income. Management must make estimates for the useful or economic lives of certain acquired assets and liabilities that are used to establish the amortization or accretion of some intangible assets and liabilities, such as core deposits. Fair values are subject to refinement for up to one year after the closing date of the acquisition as additional information about the closing date fair values becomes available. Acquisition and divestiture activities are included in the Company s consolidated results of operations from the closing date of the transaction. Acquisition and divestiture related costs are recognized in noninterest expense as incurred. For additional information, see Purchased Credit Impaired Loans and Intangible Assets below.

Loans Held for Investment

Loans classified as held for investment are originated with the intent to hold indefinitely, until maturity, or until pay-off. Loans held for investment are carried at the principal amount outstanding, net of unearned income and any necessary write-downs to reduce individual loans to net realizable value. Interest income on performing loans is recognized as interest income at the contractual rate of interest. Loan origination fees, including loan commitment and underwriting fees, are reduced by direct costs associated with loan processing, including salaries, legal review, and appraisal fees. Net deferred loan fees are deferred and amortized over the life of the related loan or commitment period.

Purchased Performing Loans. Purchased loans that are deemed to be performing at the acquisition date are accounted for using the contractual cash flow method of accounting, which results in the loans being recorded at fair value with a credit discount. The fair value discount is accreted as an adjustment to yield over the estimated contractual lives of the loans. No allowance for loan losses is recorded at acquisition for purchased loans because the fair values of the acquired loans incorporate credit risk assumptions.

Purchased Credit Impaired (PCI) Loans. When purchased loans exhibit evidence of credit deterioration after the acquisition date, and it is probable at acquisition the Company will not collect all contractually required principal and interest payments, the loans are referred to as PCI loans. PCI loans are accounted for using Topic

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

310-30 of the FASB ASC, formerly the American Institute of Certified Public Accountants Statement of Position 03-3, Accounting for Certain Loans or Debt Securities Acquired in a Transfer. PCI loans are initially measured at fair value, which includes estimated future credit losses expected to be incurred over the life of the loans. Per the guidance, the Company groups PCI loans that have common risk characteristics into loan pools. Evidence of credit quality deterioration at acquisition may include measures such as nonaccrual status, credit scores, declines in collateral value, current loan to value percentages, and days past due. The Company considers expected prepayments and estimates the amount and timing of expected principal, interest, and other cash flows for each loan or pool of loans identified as credit impaired. If contractually required payments at acquisition exceed cash flows expected to be collected, the excess is the non-accretable difference, which is available to absorb credit losses on those loans or pools of loans. If the cash flows expected at acquisition exceed the estimated fair values, the excess is the accretable yield, which is recognized in interest income over the remaining lives of those loans or pools of loans when there is a reasonable expectation about the amount and timing of such cash flows.

Impaired Loans and Nonperforming Assets. The Company maintains an active and robust problem credit identification system through its ongoing credit review function. When a credit is identified as exhibiting characteristics of weakening, the Company assesses the credit for potential impairment. Loans are considered impaired when, in the opinion of management and based on current information and events, the collection of principal and interest payments due under the contractual terms of the loan agreements are uncertain. The Company conducts quarterly reviews of loans with balances of $250 thousand or greater that are deemed to be impaired. Factors considered in determining impairment include, but are not limited to, the borrower s cash flow and capacity for debt repayment, the valuation of collateral, historical loss percentages, and economic conditions. Impairment allowances allocated to individual loans, including individual credit relationships and loan pools grouped by similar risk characteristics, are reviewed quarterly by management. Interest income realized on impaired loans in nonaccrual status, if any, is recognized upon receipt. The accrual of interest, which is based on the daily amount of principal outstanding, on impaired loans is generally continued unless the loan becomes delinquent 90 days or more.

Loans are considered past due when either principal or interest payments become contractually delinquent by 30 days or more. The Company s policy is to discontinue the accrual of interest, if warranted, on loans based on the payment status, evaluation of the related collateral, and the financial strength of the borrower. Loans that are 90 days or more past due are placed on nonaccrual status. Management may elect to continue the accrual of interest when the loan is well secured and in process of collection. When interest accruals are discontinued, interest accrued and not collected in the current year is reversed from income, and interest accrued and not collected from prior years is charged to the allowance for loan losses. Nonaccrual loans may be returned to accrual status when all principal and interest amounts contractually due, including past due payments, are brought current; the ability of the borrower to repay the obligation is reasonably assured; and there is generally a period of at least six months of repayment performance by the borrower in accordance with the contractual terms.

Seriously delinquent loans are evaluated for loss mitigation options, including charge-off. Closed-end retail loans are generally charged off against the allowance for loan losses when the loans become 120 days past due. Open-end retail loans and residential real estate secured loans are generally charged off when the loans become 180 days past due. Unsecured loans are generally charged off when the loans become 90 days past due. All other loans are charged off against the allowance for loan losses after collection attempts have been exhausted, which generally is within 120 days. Recoveries of loans previously charged off are credited to the allowance for loan losses in the period received.

Loans are considered troubled debt restructurings (TDRs) when the Company grants concessions, for legal or economic reasons, to borrowers experiencing financial difficulty that would not otherwise be considered. The

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Company generally makes concessions in interest rates, loan terms, and/or amortization terms. All TDRs $250 thousand or greater are evaluated for a specific reserve based on either the collateral or net present value method, whichever is most applicable. TDRs under $250 thousand are subject to the reserve calculation for classified loans based primarily on the historical loss rate. At the date of modification, nonaccrual loans are classified as nonaccrual TDRs. TDRs classified as nonperforming at the date of modification are returned to performing status after six months of satisfactory payment performance; however, these loans remain identified as impaired until full payment or other satisfaction of the obligation occurs.

Other real estate owned (OREO) acquired through foreclosure, or other settlement, is carried at the lower of cost or fair value less estimated selling costs. The fair value is generally based on current third-party appraisals. When a property is transferred into OREO, any excess of the loan balance over the net realizable fair value is charged against the allowance for loan losses. Operating expenses, gains, and losses on the sale of OREO are included in other noninterest expense in the Company s consolidated statements of income after any fair value write-downs are recorded as valuation adjustments.

Allowance for Loan Losses

Management performs quarterly assessments of the allowance for loan losses. The allowance is increased by provisions charged to operations and reduced by net charge-offs. The provision is calculated and charged to earnings to bring the allowance to a level that, through a systematic process of measurement, reflects the amount management estimates is needed to absorb probable losses in the portfolio. The Company s allowance for loan losses is segmented into commercial, consumer real estate, and consumer and other loans with each segment divided into classes with similar characteristics, such as the type of loan and collateral. The allowance for loan losses includes specific allocations related to significant individual loans and credit relationships and general reserves related to loans not individually evaluated. Loans not individually evaluated are grouped into pools based on similar risk characteristics. A loan that becomes adversely classified or graded is moved into a group of adversely classified or graded loans with similar risk characteristics for evaluation. A provision for loan losses is recorded for any credit deterioration in purchased performing loans after the acquisition date.

PCI loans are grouped into pools and evaluated separately from the non-PCI portfolio. The Company estimates cash flows to be collected on PCI loans and discounts those cash flows at a market rate of interest. If cash flows for PCI loans are expected to decline, generally a provision for loan losses is charged to earnings, resulting in an increase to the allowance for loan losses. If cash flows for PCI loans are expected to improve, any previously established allowance is first reversed to the extent of prior charges and then interest income is increased using the prospective yield adjustment over the remaining life of the loan, or pool of loans. Any provision established for PCI loans covered under the FDIC loss share agreements is offset by an adjustment to the FDIC indemnification asset to reflect the indemnified portion, 80%, of the post-acquisition exposure. While allocations are made to various portfolio segments, the allowance for loan losses is available for use against any loan loss management deems appropriate, excluding reserves allocated to specific loans and PCI loan pools.

FDIC Indemnification Asset

The FDIC indemnification asset represents the carrying amount of the right to receive payments from the FDIC for losses incurred on certain loans and OREO purchased from the FDIC that are covered by loss share agreements. The FDIC indemnification asset is measured separately from related covered assets because it is not contractually embedded in the assets or transferable should the assets be disposed. Under the acquisition method of accounting, the FDIC indemnification asset is recorded at fair value using projected cash flows based on expected reimbursements and applicable loss share percentages as outlined in the loss share agreements. The expected reimbursements do not include reimbursable amounts related to future covered expenditures. The cash

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

flows are discounted to reflect the timing and receipt of reimbursements from the FDIC. The discount is accreted through noninterest income over future periods. Post-acquisition adjustments to the indemnification asset are measured on the same basis as the underlying covered assets. Increases in the cash flows of covered loans reduce the FDIC indemnification asset balance, which is recognized as amortization through noninterest income over the shorter of the remaining life of the FDIC indemnification asset or the underlying loans. Decreases in the cash flows of covered loans increase the FDIC indemnification asset balance, which is recognized as accretion through noninterest income.

Premises and Equipment

Premises, equipment, and capital leases are stated at cost less accumulated depreciation and amortization. Depreciation and amortization are computed using the straight-line method over the estimated useful lives of the respective assets. Useful lives range from 5 to 10 years for furniture, fixtures, and equipment; 3 to 5 years for software, hardware, and data handling equipment; and 10 to 40 years for buildings and building improvements. Land improvements are amortized over a period of 20 years and leasehold improvements are amortized over the lesser of the term of the respective leases plus the first optional renewal period, when renewal is reasonably assured, or the estimated useful lives of the improvements. The Company leases various properties within its branch network. Leases generally have initial terms of up to 20 years and most contain options to renew with reasonable increases in rent. All leases are accounted for as operating leases. Maintenance and repairs are charged to current operations while improvements that extend the economic useful life of the underlying asset are capitalized. Disposition gains and losses are reflected in current operations.

Intangible Assets

Intangible assets consist of goodwill, core deposit intangible assets, and other identifiable intangible assets that result from business combinations. Goodwill represents the excess of the purchase price over the fair value of net assets acquired that is allocated to the appropriate reporting unit when acquired. Core deposit intangible assets represent the future earnings potential of acquired deposit relationships that are amortized over their estimated remaining useful lives. Other identifiable intangible assets primarily represent the rights arising from contractual arrangements that are amortized using the straight-line method.

Goodwill is tested annually, or more frequently if necessary, using a qualitative assessment to determine if it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If the Company concludes that it is more likely than not that the fair value of a reporting unit is less than its carrying amount, the two-step quantitative goodwill impairment test is performed. Step 1 consists of calculating and comparing the fair value of a reporting unit to its carrying amount, including goodwill. If the fair value of a reporting unit is greater than its book value, no goodwill impairment exists. If the carrying amount of a reporting unit is greater than its calculated fair value, goodwill impairment may exist and Step 2 is required to determine the amount of the impairment loss.

Securities Sold Under Agreements to Repurchase

Securities sold under agreements to repurchase are generally accounted for as collateralized financing transactions and recognized as short-term borrowings in the Company s consolidated balance sheets. Securities, generally U.S. government and federal agency securities, pledged as collateral under these arrangements can be sold or repledged only if replaced by the secured party. The fair value of the collateral provided to a third party is continually monitored and additional collateral is provided as appropriate.

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Derivative Instruments

The Company primarily uses derivative instruments to protect against the risk of adverse price or interest rate movements on the value of certain assets and liabilities and on future cash flows. Derivative instruments represent contracts between parties that usually require little or no initial net investment and result in one party delivering cash or another asset to the other party based on a notional amount and an underlying asset as specified in the contract such as interest rates, equity security prices, currencies, commodity prices, or credit spreads. These derivative instruments may consist of interest rate swaps, floors, caps, collars, futures, forward contracts, and written and purchased options. Derivative contracts often involve future commitments to exchange interest payment streams or currencies based on a notional or contractual amount, such as interest rate swaps or currency forwards, or to purchase or sell other financial instruments at specified terms on a specified date, such as options to buy or sell securities or currencies. Derivative instruments are subject to counterparty credit risk due to the possibility that the Company will incur a loss because a counterparty, which may be a bank, a broker-dealer or a customer, fails to meet its contractual obligations. This risk is measured as the expected positive replacement value of contracts. Derivative contracts may be executed only with exchanges or counterparties approved by the Company s Asset/Liability Management Committee.

If certain conditions are met, a derivative may be designated as a hedge related to fair value, cash flow, or foreign exposure risk. The recognition of changes in the fair value of a derivative instrument varies depending on the intended use of the derivative and the resulting designation. The Company accounts for hedges of customer loans as fair value hedges. The change in fair value of the hedging derivative and the change in fair value of the hedged exposure are recorded in earnings. Any hedge ineffectiveness is also reflected in current earnings. Changes in the fair value of derivatives not designated as hedging instruments are recognized as a gain or loss in earnings. The Company formally documents any relationships between hedging instruments and hedged items and the risk management objective and strategy for undertaking each hedged transaction. All derivative instruments are reported at fair value in the consolidated balance sheets.

Equity-Based Compensation

The cost of employee services received in exchange for equity instruments, including stock options and restricted stock awards , is generally measured at fair value on the grant date. The Black-Scholes valuation model is used to estimate the fair value of stock options at the grant date while the fair value of restricted stock awards is based on the market price of the Company s common stock on the grant date. The Black-Scholes model incorporates the following assumptions: the expected volatility is based on the weekly historical volatility of the Company s common stock price over the expected term of the option; the expected term is generally calculated using the shortcut method; the risk-free interest rate is based on the U.S. Department of the Treasury s (Treasury) yield curve on the grant date with a term comparable to the grant; and the dividend yield is based on the Company s dividend yield using the most recent dividend rate paid per share and trading price of the Company s common stock. Compensation cost is recognized over the required service period, generally defined as the vesting period for stock option awards and as the restriction period for restricted stock awards. For awards with graded vesting, compensation cost is recognized on a straight-line basis over the requisite service period for the entire award.

Advertising Expenses

Advertising costs are generally expensed as incurred. The Company may establish accruals for expected advertising expenses in the course of a fiscal year.

Table of Contents

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Income Taxes

Income tax expense is comprised of the current and deferred tax consequences of events and transactions already recognized. The Company includes interest and penalties related to income tax liabilities in income tax expense. The effective tax rate, income tax expense as a percent of pre-tax income, may vary significantly from statutory rates due to tax credits and permanent differences. Deferred tax assets and liabilities are recognized for the estimated future tax consequences attributable to differences between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes. Deferred tax assets and liabilities are adjusted through the provision for income taxes as changes in tax laws or rates are enacted.

Per Share Results

Basic earnings per common share is calculated by dividing net income available to common shareholders by the weighted average number of common shares outstanding during the period. Diluted earnings per common share includes the dilutive effect of potential common stock that could be issued by the Company. Under the treasury stock method of accounting, potential common stock may be issued for stock options, non-vested restricted stock awards, performance based stock awards, and convertible preferred stock. Diluted earnings per common share is calculated by dividing net income by the weighted average number of common shares outstanding for the period plus the number of dilutive potential common shares. The calculation of diluted earnings per common share excludes potential common shares that have an exercise price greater than the average market value of the Company s common stock because the effect would be antidilutive.

Recent Accounting Standards

Standards Adopted

In January 2017, the FASB issued Accounting Standards Update (ASU) 2017-04, Intangibles Goodwill and Other (Topic 350): Simplifying the Accounting for Goodwill Impairment. This ASU removes the requirement to perform a hypothetical purchase price allocation to measure goodwill impairment. A goodwill impairment will now be the amount by which a reporting unit s carrying value exceeds its fair value, not to exceed the carrying amount of goodwill. ASU 2017-04 is effective for fiscal years beginning after December 15, 2019, with early adoption permitted. The update should be applied prospectively. The Company early adopted ASU 2017-04 in the first quarter of 2017. The adoption of the standard did not have an effect on the Company s financial statements.

In January 2017, the FASB issued ASU 2017-03, Accounting Changes and Error Corrections (Topic 250) and Investments Equity Method and Joint Ventures (Topic 323): Amendments to SEC Paragraphs Pursuant to Staff Announcements at the September 22, 2016 and November 17, 2016 EITF Meetings. This ASU requires registrants to disclose the effect that recently issued accounting standards will have on their financial statements when adopted in a future period. In cases where a registrant cannot reasonably estimate the impact of the adoption, additional qualitative disclosures should be considered to assist the reader in assessing the significance of the standard s impact on its financial statements. The Company adopted ASU 2017-03 in the first quarter of 2017. The adoption of the standard resulted in enhanced disclosures regarding the impact that recently issued accounting standards adopted in a future period will have on the Company s financial statements and disclosures. See Standards Not Yet Adopted below.

In September 2015, the FASB issued ASU 2015-16, Simplifying the Accounting for Measurement Period Adjustments. This ASU simplifies the accounting for adjustments made to provisional amounts recognized in a business combination by eliminating the requirement to retrospectively account for those adjustments. The Company adopted ASU 2015-16 in the first quarter of 2016. The adoption of the standard did not have an effect on the Company s financial statements.

Table of Contents

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

In February 2015, the FASB issued ASU 2015-02, Amendments to the Consolidation Analysis. This ASU changes the analysis that an entity performs to determine whether to consolidate certain legal entities. The Company adopted ASU 2015-02 in the first quarter of 2016. The Company evaluated its investments in VIEs under the guidance and concluded that not consolidating these entities was still appropriate; therefore, the adoption of the standard did not have an effect on the Company s financial statements.

In June 2014, the FASB issued ASU 2014-12, Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved after the Requisite Service Period. This ASU requires that a performance target that affects vesting and that could be achieved after the requisite service period be treated as a performance condition. An entity should apply guidance in Topic 718 as it relates to awards with performance conditions that affect vesting to account for such awards. As such, the performance target should not be reflected in estimating the grant-date fair value of the award. Compensation cost should be recognized in the period in which it becomes probable that the performance target will be achieved and should represent the compensation cost attributable to the period for which the service has already been rendered. The Company adopted ASU 2014-12 in the first quarter of 2016. The adoption of the standard did not have an effect on the Company s financial statements.

Standards Not Yet Adopted

In November 2016, the FASB issued ASU 2016-18, Statement of Cash Flows (Topic 230): Restricted Cash. This ASU requires that a statement of cash flows explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. Amounts generally described as restricted cash and restricted cash equivalents should be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown on the statement of cash flows. ASU 2016-18 will be effective for the Company for fiscal years beginning after December 15, 2017. The Company expects to adopt ASU 2016-18 in the first quarter of 2018. The Company is evaluating the impact of the standard and does not expect the guidance to have a material effect on its financial statements.

In August 2016, the FASB issued ASU 2016-15, Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments. This ASU makes eight targeted changes to how cash receipts and cash payments are presented and classified in the statement of cash flows. ASU 2016-15 will be effective for the Company for the fiscal years beginning after December 15, 2017, with early adoption permitted. The update should be applied on a retrospective basis, if practicable. The Company expects to adopt ASU 2016-15 in the first quarter of 2018. The Company is evaluating the impact of the standard and does not expect the guidance to have a material effect on its financial statements.

In June 2016, the FASB issued ASU 2016-13, Financial Instruments Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments. This ASU intends to improve financial reporting by requiring timelier recording of credit losses on loans and other financial instruments held by financial institutions and other organizations. This ASU requires an organization to measure all expected credit losses for financial assets held at the reporting date based on historical experience, current conditions, and reasonable and supportable forecasts and requires enhanced disclosures related to the significant estimates and judgments used in estimating credit losses, as well as the credit quality and underwriting standards of an organization s portfolio. In addition, the update amends the accounting for credit losses on available-for-sale debt securities and purchased financial assets with credit deterioration. ASU 2016-13 will be effective for the Company for the fiscal years beginning after December 15, 2019, with early adoption permitted for fiscal years beginning after December 15, 2018. The Company expects to adopt ASU 2016-13 in the first quarter of 2020 and recognize a cumulative adjustment to retained earnings as of the beginning of the year of adoption. The Company is evaluating the impact of the standard.

Table of Contents

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

In March 2016, the FASB issued ASU 2016-09, Compensation Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting. This ASU simplifies several aspects of the accounting for share-based payment award transactions including income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. ASU 2016-09 will be effective for the Company for fiscal years beginning after December 15, 2016, with early adoption permitted. The Company expects to adopt ASU 2016-09 in the first quarter of 2017. The Company is evaluating the impact of the standard and does not expect the guidance to have a material effect on its financial statements.

In February 2016, the FASB issued ASU 2016-02, Leases (Topic 842). This ASU increases transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet and requiring more disclosures related to leasing transactions. ASU 2016-02 will be effective for the Company for the fiscal years beginning after December 15, 2018, with early adoption permitted. The Company expects to adopt ASU 2016-02 in the first quarter of 2019. The Company is evaluating the impact of the standard and expects a minimal increase in assets and liabilities; however, the Company does not expect the guidance to have a material effect on its 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. This ASU significantly revises an entity s accounting related to (1) the classification and measurement of investments in equity securities and (2) the presentation of certain fair value changes for financial liabilities measured at fair value. The new guidance also amends certain disclosure requirements associated with the fair value of financial instruments. ASU 2016-01 will be effective for the Company for fiscal years beginning after December 15, 2017, with early adoption permitted for the instrument-specific credit risk provision. The Company expects to adopt ASU 2016-01 in the first quarter of 2018. The Company is evaluating the impact of the standard and does not expect to recognize a significant cumulative effect adjustment to retained earnings at the beginning of the year of adoption or expect the guidance to have a material effect on its financial statements. The cumulative-effect adjustment will be dependent on the composition and fair value of the Company s equity securities portfolio at the adoption date.

In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers. This ASU s core principle is that an entity will recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which the company expects to be entitled in exchange for those goods or services. In doing so, companies will need to use more judgment and make more estimates than under existing guidance. These may include identifying performance obligations in the contract, estimating the amount of variable consideration to include in the transaction price and allocating the transaction price to each separate performance obligation. In August 2015, the FASB issued ASU 2015-14, Revenue from Contracts with Customers deferring the effective date of ASU 2014-09 for the Company until fiscal years beginning after December 15, 2017, with early adoption permitted for fiscal years beginning after December 15, 2016. Additional revenue related standards to be adopted concurrently with ASU 2014-09 include ASU 2016-20, ASU 2016-12, ASU 2016-10, and ASU 2016-08. The Company expects to adopt ASU 2014-09, and related updates, in the first quarter of 2018 and recognize a cumulative adjustment to retained earnings as of the beginning of the year of adoption. The Company s primary source of revenue is interest income, which is excluded from the scope of this guidance; however, the Company is evaluating the impact of the standard on other income, which includes fees for services, commissions on sales, and various deposit service charges. The Company does not expect the guidance to have a material effect on its financial statements.

The Company does not expect other recent accounting standards issued by the FASB or other standards-setting bodies to have a material impact on the consolidated financial statements.

Table of Contents

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Note 2. Acquisitions and Divestitures

The following table presents the components of net cash received in, or paid for, acquisitions and divestitures, an investing activity in the Company s consolidated statements of cash flows, for the periods indicated:

	Year Ended December 31,		
(Amounts in thousands)	**2016**	**2015**	**2014**
Acquisitions			
Fair value of assets and liabilities acquired:			
Loans	$ 149,122	$	$ 140
Premises and equipment	4,829		4,547
Other assets	448		4,563
Other intangible assets	3,842		
Deposits	(134,307)		(318,877)
Other liabilities	(75)		(76)
Purchase price in excess of net assets acquired	2,446	88	1,721
Total purchase price	26,305	88	(307,982)
Non-cash purchase price			
Cash acquired			
Net cash paid (received) in acquisitions	26,305	88	(307,982)
Divestitures			
Book value of assets sold	(165,742)	389	(83,283)
Book value of liabilities sold	111,198	(152)	215,268
Sales price in excess of net liabilities assumed	(3,682)	(6)	(755)
Total sales price	(58,226)	231	131,230
Cash sold			(1,852)
Amount due remaining on books	2,205	(231)	
Net cash (received) paid in divestitures	(56,021)		129,378
Net cash (received) paid in acquisitions and divestitures	$ (29,716)	$ 88	$ (178,604)

Ascension Insurance Agency, Inc.

On October 1, 2016, the Company completed the sale of Greenpoint Insurance Group, Inc. (Greenpoint) to Ascension Insurance Agency, Inc. for $7.11 million, including earn-out payments of $2.21 million to be received over the next three years if certain operating targets are met. The divestiture consisted of two North Carolina offices operating as Greenpoint and two Virginia offices operating under the trade name Carr & Hyde Insurance. The Company recorded a net gain of $617 thousand in connection with the divestiture and eliminated $6.49 million in goodwill and other intangible assets. The Company incurred expenses related to the divestiture of $46 thousand in 2016. The transaction did not impact the Company s in-branch insurance offices operating as FCIS in West Virginia and Virginia.

On October 31, 2015, the Company sold one insurance agency for $372 thousand. The Company recorded a net loss of $8 thousand in connection with the sale and eliminated $385 thousand in goodwill and other intangible assets. In addition, the Company recorded additional goodwill of $88 thousand in 2015 related to contingent earn-out payments from acquisitions that occurred before 2009.

Table of Contents

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

First Bank

On July 15, 2016, the Company completed the branch exchange with First Bank, North Carolina, pursuant to which the Bank exchanged a portion of its North Carolina branch network for First Bank s Virginia branch network. Under the agreements, the Bank simultaneously sold six branches in the Winston-Salem and Mooresville areas of North Carolina and acquired seven branches in Southwestern Virginia. The branch acquisition complements the Company s 2014 acquisition of seven branches from Bank of America by expanding the Company s existing presence in Southwest Virginia and affords the opportunity to realize certain operating cost savings.

In connection with the branch exchange, the Company acquired total assets of $160.69 million, including total loans of $149.12 million and goodwill and other intangibles of $6.29 million, and total liabilities of $134.38 million, including total deposits of $134.31 million. The Company did not acquire any PCI loans. The consideration transferred included the net fair value of divested assets and a purchase premium of $3.84 million. The Company divested total assets of $162.17 million, including loans of $155.54 million and goodwill and other intangibles of $2.33 million, and total liabilities of $111.05 million, including deposits of $111.02 million, and received a deposit premium of $4.07 million. In connection with the divestiture, the Company recorded a net gain of $3.07 million. The Company incurred expenses related to the First Bank transaction of $684 thousand in 2016. The estimated fair values, including identifiable intangible assets, are preliminary and subject to refinement for up to one year after the closing date of the acquisition.

CresCom Bank

On December 12, 2014, the Company completed the sale of thirteen branches to CresCom Bank, Charleston, South Carolina. The divestiture consisted of ten branches in the Southeastern, Coastal region of North Carolina and three branches in South Carolina, all of which were previously acquired in the FDIC-assisted acquisition of Waccamaw Bank (Waccamaw) on June 8, 2012. At closing, the Company divested total deposits of $215.19 million and total loans of $70.04 million. The transaction excluded loans covered under FDIC loss share agreements. The Company recorded a net gain of $755 thousand in connection with the divestiture, which included a deposit premium of $6.45 million and goodwill allocation of $6.45 million.

Bank of America

On October 24, 2014, the Company completed the acquisition of seven branches from Bank of America, National Association. The acquisition consisted of six branches in Southwestern Virginia and one branch in Central North Carolina. At acquisition, the Company assumed total deposits of $318.88 million for a premium of $5.79 million. No loans were included in the purchase. The Company purchased the real estate, or assumed the leases, associated with the branches.

Table of Contents

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Note 3. Investment Securities

The following tables present the amortized cost and fair value of available-for-sale securities, including gross unrealized gains and losses, as of the dates indicated:

	December 31, 2016			
(Amounts in thousands)	**Amortized Cost**	**Unrealized Gains**	**Unrealized Losses**	**Fair Value**
U.S. Agency securities	$ 1,342	$ 3	$	$ 1,345
Municipal securities	111,659	2,258	(586)	113,331
Single issue trust preferred securities	22,104		(2,165)	19,939
Mortgage-backed Agency securities	31,290	66	(465)	30,891
Equity securities	55	18		73
Total securities available for sale	$ 166,450	$ 2,345	$ (3,216)	$ 165,579

	December 31, 2015			
(Amounts in thousands)	**Amortized Cost**	**Unrealized Gains**	**Unrealized Losses**	**Fair Value**
U.S. Agency securities	$ 31,414	$ 39	$ (751)	$ 30,702
Municipal securities	124,880	4,155	(357)	128,678
Single issue trust preferred securities	55,882		(8,050)	47,832
Corporate securities	70,571		(238)	70,333
Certificates of deposit	5,000			5,000
Mortgage-backed Agency securities	84,576	155	(1,175)	83,556
Equity securities	66	6		72
Total securities available for sale	$ 372,389	$ 4,355	$ (10,571)	$ 366,173

Table of Contents

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following table presents the amortized cost and fair value of available-for-sale securities, by contractual maturity, as of December 31, 2016. Actual maturities could differ from contractual maturities because issuers may have the right to call or prepay obligations with or without penalties.

(Amounts in thousands)	U.S. Agency Securities	Municipal Securities	Corporate Notes	Total
Amortized cost maturity:				
One year or less	$	$ 1,135	$	$ 1,135
After one year through five years	1	1,035		1,036
After five years through ten years		88,449		88,449
After ten years	1,341	21,040	22,104	44,485
Amortized cost	$ 1,342	$ 111,659	$ 22,104	135,105
Mortgage-backed securities				31,290
Equity securities				55
Total amortized cost				$ 166,450
Fair value maturity:				
One year or less	$	$ 1,141	$	$ 1,141
After one year through five years	1	1,059		1,060
After five years through ten years		90,360		90,360
After ten years	1,344	20,771	19,939	42,054
Fair value	$ 1,345	$ 113,331	$ 19,939	134,615
Mortgage-backed securities				30,891
Equity securities				73
Total fair value				$ 165,579

The following tables present the amortized cost and fair value of held-to-maturity securities, including gross unrealized gains and losses, as of the dates indicated:

	December 31, 2016			
(Amounts in thousands)	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
U.S. Agency securities	$ 36,741	$ 124	$	$ 36,865
Corporate securities	10,392	11	(2)	10,401
Total securities held to maturity	$ 47,133	$ 135	$ (2)	$ 47,266

	December 31, 2015			
(Amounts in thousands)	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
U.S. Agency securities	$ 61,863	$ 75	$ (106)	$ 61,832
Municipal securities	190	3		193
Corporate securities	10,488		(23)	10,465
Total securities held to maturity	$ 72,541	$ 78	$ (129)	$ 72,490

22

Table of Contents

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following table presents the amortized cost and fair value of held-to-maturity securities, by contractual maturity, as of December 31, 2016. Actual maturities could differ from contractual maturities because issuers may have the right to call or prepay obligations with or without penalties.

(Amounts in thousands)	U.S. Agency Securities	Corporate Notes	Total
Amortized cost maturity:			
One year or less	$ 18,756	$ 3,095	$ 21,851
After one year through five years	17,985	7,297	25,282
After five years through ten years			
After ten years			
Total amortized cost	$ 36,741	$ 10,392	$ 47,133
Fair value maturity:			
One year or less	$ 18,768	$ 3,096	$ 21,864
After one year through five years	18,097	7,305	25,402
After five years through ten years			
After ten years			
Total fair value	$ 36,865	$ 10,401	$ 47,266

23

Table of Contents

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following tables present municipal securities, by state, for the states where the largest volume of these securities are held in the Company s portfolio. The tables also present the amortized cost and fair value of the municipal securities, including gross unrealized gains and losses, as of the dates indicated.

	December 31, 2016				
(Amounts in thousands)	**Percent of Municipal Portfolio**	**Amortized Cost**	**Unrealized Gains**	**Unrealized Losses**	**Fair Value**
New York	11.66%	$ 12,876	$ 334	$	$ 13,210
Minnesota	9.70%	10,796	232	(40)	10,988
Wisconsin	8.66%	9,786	74	(42)	9,818
Ohio	8.50%	9,599	125	(88)	9,636
Massachusetts	8.45%	9,355	229	(10)	9,574
New Jersey	7.14%	7,891	202		8,093
Connecticut	6.90%	7,628	190		7,818
Texas	6.55%	7,397	130	(103)	7,424
Iowa	5.66%	6,467	36	(88)	6,415
Other	26.78%	29,864	706	(215)	30,355
Total	100.00%	$ 111,659	$ 2,258	$ (586)	$ 113,331

	December 31, 2015				
(Amounts in thousands)	**Percent of Municipal Portfolio**	**Amortized Cost**	**Unrealized Gains**	**Unrealized Losses**	**Fair Value**
New York	11.38%	$ 14,062	$ 602	$	$ 14,664
Minnesota	8.72%	11,011	283	(64)	11,230
Wisconsin	8.69%	10,797	420	(14)	11,203
Ohio	8.38%	10,416	388		10,804
Connecticut	7.76%	9,786	217	(5)	9,998
New Jersey	7.69%	9,554	378	(22)	9,910
Massachusetts	7.60%	9,479	315		9,794
Texas	6.04%	7,651	208	(75)	7,784
Other	5.03%	6,471	75	(60)	6,486
Total	28.71%	35,843	1,272	(117)	36,998
	100.00%	$ 125,070	$ 4,158	$ (357)	$ 128,871

Table of Contents

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following tables present the fair values and unrealized losses for available-for-sale securities in a continuous unrealized loss position for less than 12 months and for 12 months or longer as of the dates indicated:

	December 31, 2016					
	Less than 12 Months		12 Months or Longer		Total	
(Amounts in thousands)	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Municipal securities	$ 24,252	$ (527)	$ 715	$ (59)	$ 24,967	$ (586)
Single issue trust preferred securities			19,939	(2,165)	19,939	(2,165)
Mortgage-backed Agency securities	12,834	(166)	11,851	(299)	24,685	(465)
Total	$ 37,086	$ (693)	$ 32,505	$ (2,523)	$ 69,591	$ (3,216)

	December 31, 2015					
	Less than 12 Months		12 Months or Longer		Total	
(Amounts in thousands)	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
U.S. Agency securities	$ 4,441	$ (5)	$ 23,922	$ (746)	$ 28,363	$ (751)
Municipal securities	8,126	(48)	10,393	(309)	18,519	(357)
Single issue trust preferred securities			47,832	(8,050)	47,832	(8,050)
Corporate securities	70,333	(238)			70,333	(238)
Mortgage-backed Agency securities	27,050	(253)	37,291	(922)	64,341	(1,175)
Total	$ 109,950	$ (544)	$ 119,438	$ (10,027)	$ 229,388	$ (10,571)

The following tables present the fair values and unrealized losses for held-to-maturity securities in a continuous unrealized loss position for less than 12 months and for 12 months or longer as of the dates indicated:

	December 31, 2016					
	Less than 12 Months		12 Months or Longer		Total	
(Amounts in thousands)	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Corporate securities	$ 3,533	$ (2)	$	$	$ 3,533	$ (2)
Total	$ 3,533	$ (2)	$	$	$ 3,533	$ (2)

	December 31, 2015					
	Less than 12 Months		12 Months or Longer		Total	
(Amounts in thousands)	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
U.S. Agency securities	$ 43,723	$ (106)	$	$	$ 43,723	$ (106)
Corporate securities	6,851	(23)			6,851	(23)

Total	$ 50,574	$ (129)	$	$	$ 50,574	$ (129)

There were 82 individual securities in an unrealized loss position as of December 31, 2016, and their combined depreciation in value represented 1.51% of the investment securities portfolio. These securities included 15 securities in a continuous unrealized loss position for 12 months or longer that the Company does not intend to

Table of Contents

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

sell, and that it has determined is not more likely than not going to be required to sell, prior to maturity or recovery. There were 107 individual securities in an unrealized loss position as of December 31, 2015, and their combined depreciation in value represented 2.44% of the investment securities portfolio.

The Company reviews its investment portfolio quarterly for indications of OTTI. The initial indicator of OTTI for both debt and equity securities is a decline in fair value below book value and the severity and duration of the decline. For debt securities, the credit-related OTTI is recognized as a charge to noninterest income and the noncredit-related OTTI is recognized in OCI. The Company incurred credit-related OTTI charges on debt securities of $4.64 million in 2016 related to the Company s change in intent to hold certain securities to recovery. The intent was changed to sell specific trust preferred securities in the Company s investment portfolio primarily to reduce credit concentrations with two issuers. The Company incurred credit-related OTTI charges on debt securities of $705 thousand in 2014 related to a non-Agency mortgage-backed security that was sold in November 2014. Temporary impairment on debt securities is primarily related to changes in benchmark interest rates, changes in pricing in the credit markets, and other current economic factors. For equity securities, the OTTI is recognized as a charge to noninterest income. The Company incurred OTTI charges related to equity securities of $11 thousand in 2016 and $32 thousand in 2014. There were no OTTI charges recognized in 2015.

The following table presents the changes in credit-related losses recognized in earnings on debt securities where a portion of the impairment was recognized in OCI during the periods indicated:

	Year Ended December 31,		
(Amounts in thousands)	**2016**	**2015**	**2014**
Beginning balance [1]	$	$	$ 7,798
Additions for credit losses on securities not previously recognized	4,646		
Additions for credit losses on securities previously recognized			705
Reduction for securities sold/realized losses	(4,646)		(8,503)
Ending balance	$	$	$

(1) The beginning balance includes credit-related losses included in OTTI charges recognized on debt securities in prior periods.

The carrying amount of securities pledged for various purposes totaled $139.75 million as of December 31, 2016, and $236.73 million as of December 31, 2015.

The following table presents the gross realized gains and losses from the sale of available-for-sale securities for the periods indicated:

	Year Ended December 31,		
(Amounts in thousands)	**2016**	**2015**	**2014**
Gross realized gains	$ 757	$ 363	$ 2,257
Gross realized losses	(422)	(219)	(3,642)
Net gain (loss) on sale of securities	$ 335	$ 144	$ (1,385)

Table of Contents

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Note 4. Loans

The Company groups loans held for investment into three segments (commercial loans, consumer real estate loans, and consumer and other loans) with each segment divided into various classes. Covered loans are those loans acquired in FDIC assisted transactions that are covered by loss share agreements. Customer overdrafts reclassified as loans totaled $1.41 million as of December 31, 2016, and $1.24 million as of December 31, 2015. Deferred loan fees totaled $3.90 million in 2016, $3.78 million in 2015, and $3.39 million in 2014. For information about off-balance sheet financing, see Note 20, Litigation, Commitments, and Contingencies, to the Consolidated Financial Statements of this report.

The following table presents loans, net of unearned income with non-covered loans and by loan class, as of the dates indicated:

	December 31,			
	2016		2015	
(Amounts in thousands)	**Amount**	**Percent**	**Amount**	**Percent**
Non-covered loans held for investment				
Commercial loans				
Construction, development, and other land	$ 56,948	3.07%	$ 48,896	2.86%
Commercial and industrial	92,204	4.98%	88,903	5.21%
Multi-family residential	134,228	7.24%	95,026	5.57%
Single family non-owner occupied	142,965	7.72%	149,351	8.75%
Non-farm, non-residential	598,674	32.31%	485,460	28.45%
Agricultural	6,003	0.32%	2,911	0.17%
Farmland	31,729	1.71%	27,540	1.61%
Total commercial loans	1,062,751	57.35%	898,087	52.62%
Consumer real estate loans				
Home equity lines	106,361	5.74%	107,367	6.29%
Single family owner occupied	500,891	27.03%	495,209	29.02%
Owner occupied construction	44,535	2.41%	43,505	2.55%
Total consumer real estate loans	651,787	35.18%	646,081	37.86%
Consumer and other loans				
Consumer loans	77,445	4.18%	72,000	4.22%
Other	3,971	0.21%	7,338	0.43%
Total consumer and other loans	81,416	4.39%	79,338	4.65%
Total non-covered loans	1,795,954	96.92%	1,623,506	95.13%
Total covered loans	56,994	3.08%	83,035	4.87%
Total loans held for investment, net of unearned income	$ 1,852,948	100.00%	$ 1,706,541	100.00%

27

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following table presents the covered loan portfolio, by loan class, as of the dates indicated:

(Amounts in thousands)	December 31, 2016	2015
Covered loans		
Commercial loans		
Construction, development, and other land	$ 4,570	$ 6,303
Commercial and industrial	895	1,170
Multi-family residential	8	640
Single family non-owner occupied	962	2,674
Non-farm, non-residential	7,512	14,065
Agricultural	25	34
Farmland	397	643
Total commercial loans	14,369	25,529
Consumer real estate loans		
Home equity lines	35,817	48,565
Single family owner occupied	6,729	8,595
Owner occupied construction		262
Total consumer real estate loans	42,546	57,422
Consumer and other loans		
Consumer loans	79	84
Total covered loans	$ 56,994	$ 83,035

The Company identifies certain purchased loans as impaired when fair values are established at acquisition and groups those PCI loans into loan pools with common risk characteristics. The Company estimates cash flows to be collected on PCI loans and discounts those cash flows at a market rate of interest. The following table presents the recorded investment and contractual unpaid principal balance of PCI loans, by acquisition, as of the dates indicated:

	December 31, 2016		2015	
(Amounts in thousands)	Recorded Investment	Unpaid Principal Balance	Recorded Investment	Unpaid Principal Balance
PCI Loans, by acquisition				
Peoples	$ 5,576	$ 9,397	$ 6,681	$ 11,249
Waccamaw	21,758	45,030	34,707	63,151
Other acquired	1,095	1,121	1,254	1,297
Total PCI Loans	$ 28,429	$ 55,548	$ 42,642	$ 75,697

Table of Contents

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following table presents the changes in the accretable yield on PCI loans, by acquisition, during the periods indicated:

(Amounts in thousands)	**Peoples**	**Waccamaw**	**Other**	**Total**
Balance January 1, 2014	$ 5,294	$ 10,338	$ 8	$ 15,640
Additions	267	26		293
Accretion	(2,147)	(6,118)	(37)	(8,302)
Reclassifications from nonaccretable difference	1,912	16,400	29	18,341
Other changes, net	(581)	(1,598)		(2,179)
Balance December 31, 2014	$ 4,745	$ 19,048	$	$ 23,793
Balance January 1, 2015	$ 4,745	$ 19,048	$	$ 23,793
Additions		2		2
Accretion	(2,712)	(6,459)		(9,171)
Reclassifications from nonaccretable difference	1,283	6,564		7,847
Other changes, net	273	6,954		7,227
Balance December 31, 2015	$ 3,589	$ 26,109	$	$ 29,698
Balance January 1, 2016	$ 3,589	$ 26,109	$	$ 29,698
Accretion	(1,237)	(5,380)		(6,617)
Reclassifications from nonaccretable difference	287	1,620		1,907
Other changes, net	1,753	(515)		1,238
Balance December 31, 2016	$ 4,392	$ 21,834	$	$ 26,226

Note 5. Credit Quality

The Company uses a risk grading matrix to assign a risk grade to each loan in its portfolio. Loan risk ratings may be upgraded or downgraded to reflect current information identified during the loan review process. The general characteristics of each risk grade are as follows:

Pass This grade is assigned to loans with acceptable credit quality and risk. The Company further segments this grade based on borrower characteristics that include capital strength, earnings stability, liquidity, leverage, and industry conditions.

Special Mention This grade is assigned to loans that require an above average degree of supervision and attention. These loans have the characteristics of an asset with acceptable credit quality and risk; however, adverse economic or financial conditions exist that create potential weaknesses deserving of management s close attention. If potential weaknesses are not corrected, the prospect of repayment may worsen.

Substandard This grade is assigned to loans that have well defined weaknesses that may make payment default, or principal exposure, possible. These loans will likely be dependent on collateral liquidation, secondary repayment sources, or events outside the normal course of business to meet repayment terms.

Doubtful This grade is assigned to loans that have the weaknesses inherent in substandard loans; however, the weaknesses are so severe that collection or liquidation in full is unlikely based on current facts, conditions, and values. Due to certain specific pending factors, the amount of loss cannot yet be determined.

Loss This grade is assigned to loans that will be charged off or charged down when payments, including the timing and value of payments, are uncertain. This risk grade does not imply that the asset has no recovery or salvage value, but simply means that it is not practical or desirable to defer writing off, either all or a portion of, the loan balance even though partial recovery may be realized in the future.

Table of Contents

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following tables present the recorded investment of the loan portfolio, by loan class and credit quality, as of the dates indicated. Losses on covered loans are generally reimbursable by the FDIC at the applicable loss share percentage, 80%; therefore, covered loans are disclosed separately.

	December 31, 2016					
(Amounts in thousands)	Pass	Special Mention	Substandard	Doubtful	Loss	Total
Non-covered loans						
Commercial loans						
Construction, development, and other land	$ 55,188	$ 980	$ 780	$	$	$ 56,948
Commercial and industrial	87,581	3,483	1,137		3	92,204
Multi-family residential	126,468	6,992	768			134,228
Single family non-owner occupied	131,934	5,466	5,565			142,965
Non-farm, non-residential	579,134	10,236	9,102	202		598,674
Agricultural	5,839	164				6,003
Farmland	28,887	1,223	1,619			31,729
Consumer real estate loans						
Home equity lines	104,033	871	1,457			106,361
Single family owner occupied	475,402	4,636	20,381	472		500,891
Owner occupied construction	43,833		702			44,535
Consumer and other loans						
Consumer loans	77,218	11	216			77,445
Other	3,971					3,971
Total non-covered loans	1,719,488	34,062	41,727	674	3	1,795,954
Covered loans						
Commercial loans						
Construction, development, and other land	2,768	803	999			4,570
Commercial and industrial	882		13			895
Multi-family residential			8			8
Single family non-owner occupied	796	63	103			962
Non-farm, non-residential	6,423	537	552			7,512
Agricultural	25					25
Farmland	132		265			397
Consumer real estate loans						
Home equity lines	14,283	20,763	771			35,817
Single family owner occupied	4,601	928	1,200			6,729
Consumer and other loans						
Consumer loans	79					79
Total covered loans	29,989	23,094	3,911			56,994
Total loans	$ 1,749,477	$ 57,156	$ 45,638	$ 674	$ 3	$ 1,852,948

30

Table of Contents

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	December 31, 2015					
(Amounts in thousands)	**Pass**	**Special Mention**	**Substandard**	**Doubtful**	**Loss**	**Total**
Non-covered loans						
Commercial loans						
Construction, development, and other land	$ 46,816	$ 974	$ 1,106	$	$	$ 48,896
Commercial and industrial	87,223	663	1,017			88,903
Multi-family residential	81,168	12,969	889			95,026
Single family non-owner occupied	139,680	3,976	5,695			149,351
Non-farm, non-residential	454,906	15,170	15,384			485,460
Agricultural	2,886	25				2,911
Farmland	25,855	1,427	258			27,540
Consumer real estate loans						
Home equity lines	104,897	1,083	1,387			107,367
Single family owner occupied	468,155	6,686	20,368			495,209
Owner occupied construction	42,783		722			43,505
Consumer and other loans						
Consumer loans	71,685	61	254			72,000
Other	7,338					7,338
Total non-covered loans	1,533,392	43,034	47,080			1,623,506
Covered loans						
Commercial loans						
Construction, development, and other land	3,908	1,261	1,134			6,303
Commercial and industrial	1,144	4	22			1,170
Multi-family residential	460		180			640
Single family non-owner occupied	1,808	457	409			2,674
Non-farm, non-residential	9,192	2,044	2,829			14,065
Agricultural	34					34
Farmland	364		279			643
Consumer real estate loans						
Home equity lines	17,893	29,823	849			48,565
Single family owner occupied	5,102	1,963	1,530			8,595
Owner occupied construction	112	51	99			262
Consumer and other loans						
Consumer loans	84					84
Total covered loans	40,101	35,603	7,331			83,035
Total loans	$ 1,573,493	$ 78,637	$ 54,411	$	$	$ 1,706,541

The Company identifies loans for potential impairment through a variety of means, including, but not limited to, ongoing loan review, renewal processes, delinquency data, market communications, and public information. If the Company determines that it is probable all principal and interest amounts contractually due will not be collected, the loan is generally deemed impaired.

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following table presents the recorded investment, unpaid principal balance, and related allowance for loan losses for impaired loans, excluding PCI loans, as of the dates indicated:

(Amounts in thousands)	December 31, 2016 Recorded Investment	December 31, 2016 Unpaid Principal Balance	December 31, 2016 Related Allowance	December 31, 2015 Recorded Investment	December 31, 2015 Unpaid Principal Balance	December 31, 2015 Related Allowance
Impaired loans with no related allowance						
Commercial loans						
Construction, development, and other land	$ 33	$ 35	$	$ 57	$ 57	$
Commercial and industrial	346	383		16	23	
Multi-family residential	294	369		84	94	
Single family non-owner occupied	3,084	3,334		2,095	2,239	
Non-farm, non-residential	3,829	4,534		10,369	11,055	
Agricultural						
Farmland	1,161	1,188		310	326	
Consumer real estate loans						
Home equity lines	913	968		868	898	
Single family owner occupied	11,779	12,630		11,289	11,996	
Owner occupied construction	573	589		243	243	
Consumer and other loans						
Consumer loans	62	103		71	74	
Other						
Total impaired loans with no allowance	22,074	24,133		25,402	27,005	
Impaired loans with a related allowance						
Commercial loans						
Single family non-owner occupied	351	351	31	619	623	124
Non-farm, non-residential				5,667	5,673	1,568
Farmland	430	430	18			
Consumer real estate loans						
Single family owner occupied	4,118	4,174	770	4,899	4,907	672
Owner occupied construction				349	355	7
Total impaired loans with an allowance	4,899	4,955	819	11,534	11,558	2,371
Total impaired loans[(1)]	$ 26,973	$ 29,088	$ 819	$ 36,936	$ 38,563	$ 2,371

(1) Includes loans totaling $16.89 million as of December 31, 2016, and $14.22 million as of December 31, 2015, that do not meet the Company s evaluation threshold for individual impairment and are therefore collectively evaluated for impairment

Table of Contents

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following table presents the average recorded investment and interest income recognized on impaired loans, excluding PCI loans, for the periods indicated:

	Year Ended December 31,					
	2016		**2015**		**2014**	
(Amounts in thousands)	**Interest Income Recognized**	**Average Recorded Investment**	**Interest Income Recognized**	**Average Recorded Investment**	**Interest Income Recognized**	**Average Recorded Investment**
Impaired loans with no related allowance:						
Commercial loans						
Construction, development, and other land	$ 22	$ 344	$ 5	$ 481	$ 8	$ 607
Commercial and industrial	16	646		324	18	1,627
Multi-family residential	21	308	4	269	21	162
Single family non-owner occupied	178	3,076	88	2,140	60	1,629
Non-farm, non-residential	307	8,573	312	11,677	353	8,248
Agricultural						1
Farmland	55	437	16	195	6	315
Consumer real estate loans						
Home equity lines	30	1,223	36	813	22	686
Single family owner occupied	343	12,330	356	12,708	404	11,486
Owner occupied construction	9	497	10	359	5	259
Consumer and other loans						
Consumer loans	5	60	8	98	5	108
Total impaired loans with no related allowance	986	27,494	835	29,064	902	25,128
Impaired loans with a related allowance:						
Commercial loans						
Commercial and industrial					47	2,199
Multi-family residential					23	4,190
Single family non-owner occupied	23	518	25	575	2	369
Non-farm, non-residential	215	3,831	65	4,987	31	3,386
Farmland	14	108				
Consumer real estate loans						
Home equity lines					1	57
Single family owner occupied	118	4,452	26	3,731	48	3,897
Owner occupied construction		87	1	178		
Total impaired loans with a related allowance	370	8,996	117	9,471	152	14,098
Total impaired loans	$ 1,356	$ 36,490	$ 952	$ 38,535	$ 1,054	$ 39,226

The following tables provide information on impaired PCI loan pools as of and for the dates indicated:

	December 31,	
(Amounts in thousands, except impaired loan pools)	**2016**	**2015**

Unpaid principal balance	$ 1,086	$ 3,759
Recorded investment	1,085	2,834
Allowance for loan losses related to PCI loan pools	12	54
Impaired PCI loan pools	1	2

	Year Ended December 31,		
(Amounts in thousands)	**2016**	**2015**	**2014**
Interest income recognized	$ 142	$ 364	$ 3,081
Average recorded investment	1,929	3,309	30,007

Table of Contents

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The Company generally places a loan on nonaccrual status when it is 90 days or more past due. PCI loans are generally not classified as nonaccrual due to the accrual of interest income under the accretion method of accounting. The following table presents nonaccrual loans, by loan class, as of the dates indicated:

	December 31,					
	2016			2015		
(Amounts in thousands)	**Non-covered**	**Covered**	**Total**	**Non-covered**	**Covered**	**Total**
Commercial loans						
Construction, development, and other land	$ 72	$ 32	$ 104	$ 39	$ 54	$ 93
Commercial and industrial	332	13	345		16	16
Multi-family residential	294		294	84		84
Single family non-owner occupied	1,242	24	1,266	1,850	29	1,879
Non-farm, non-residential	3,295	30	3,325	7,150	39	7,189
Farmland	1,591		1,591	234		234
Consumer real estate loans						
Home equity lines	705	400	1,105	825	413	1,238
Single family owner occupied	7,924	109	8,033	7,245	96	7,341
Owner occupied construction	336		336	349		349
Consumer and other loans						
Consumer loans	63		63	71		71
Total nonaccrual loans	$ 15,854	$ 608	$ 16,462	$ 17,847	$ 647	$ 18,494

Table of Contents

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following tables present the aging of past due loans, by loan class, as of the dates indicated. Nonaccrual loans 30 days or more past due are included in the applicable delinquency category. Loans acquired with credit deterioration, with a discount, continue to accrue interest based on expected cash flows; therefore, PCI loans are not generally considered nonaccrual. There were no non-covered accruing loans contractually past due 90 days or more as of December 31, 2016, or December 31, 2015.

	December 31, 2016					
(Amounts in thousands)	**30 - 59 Days Past Due**	**60 - 89 Days Past Due**	**90+ Days Past Due**	**Total Past Due**	**Current Loans**	**Total Loans**
Non-covered loans						
Commercial loans						
Construction, development, and other land	$ 33	$ 5	$ 17	$ 55	$ 56,893	$ 56,948
Commercial and industrial	174	30	149	353	91,851	92,204
Multi-family residential	163		281	444	133,784	134,228
Single family non-owner occupied	1,302	159	835	2,296	140,669	142,965
Non-farm, non-residential	1,235	332	2,169	3,736	594,938	598,674
Agricultural		5		5	5,998	6,003
Farmland	224	343	565	1,132	30,597	31,729
Consumer real estate loans						
Home equity lines	78	136	658	872	105,489	106,361
Single family owner occupied	4,777	2,408	3,311	10,496	490,395	500,891
Owner occupied construction	342	336		678	43,857	44,535
Consumer and other loans						
Consumer loans	371	90	15	476	76,969	77,445
Other					3,971	3,971
Total non-covered loans	8,699	3,844	8,000	20,543	1,775,411	1,795,954
Covered loans						
Commercial loans						
Construction, development, and other land	434		32	466	4,104	4,570
Commercial and industrial					895	895
Multi-family residential					8	8
Single family non-owner occupied	24			24	938	962
Non-farm, non-residential	32			32	7,480	7,512
Agricultural					25	25
Farmland					397	397
Consumer real estate loans						
Home equity lines	108	146	62	316	35,501	35,817
Single family owner occupied	58		39	97	6,632	6,729
Owner occupied construction						
Consumer and other loans						
Consumer loans					79	79
Total covered loans	656	146	133	935	56,059	56,994
Total loans	$ 9,355	$ 3,990	$ 8,133	$ 21,478	$ 1,831,470	$ 1,852,948

Table of Contents

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	December 31, 2015					
(Amounts in thousands)	30 - 59 Days Past Due	60 - 89 Days Past Due	90+ Days Past Due	Total Past Due	Current Loans	Total Loans
Non-covered loans						
Commercial loans						
Construction, development, and other land	$	$	$ 39	$ 39	$ 48,857	$ 48,896
Commercial and industrial	281	66		347	88,556	88,903
Multi-family residential	302	76	84	462	94,564	95,026
Single family non-owner occupied	748	120	929	1,797	147,554	149,351
Non-farm, non-residential	347	676	4,940	5,963	479,497	485,460
Agricultural					2,911	2,911
Farmland	585	11	234	830	26,710	27,540
Consumer real estate loans						
Home equity lines	668	195	468	1,331	106,036	107,367
Single family owner occupied	6,122	1,943	3,191	11,256	483,953	495,209
Owner occupied construction					43,505	43,505
Consumer and other loans						
Consumer loans	278	71	23	372	71,628	72,000
Other					7,338	7,338
Total non-covered loans	9,331	3,158	9,908	22,397	1,601,109	1,623,506
Covered loans						
Commercial loans						
Construction, development, and other land	96		42	138	6,165	6,303
Commercial and industrial			16	16	1,154	1,170
Multi-family residential					640	640
Single family non-owner occupied	1,422			1,422	1,252	2,674
Non-farm, non-residential			39	39	14,026	14,065
Agricultural					34	34
Farmland					643	643
Consumer real estate loans						
Home equity lines	489	37	225	751	47,814	48,565
Single family owner occupied	274		42	316	8,279	8,595
Owner occupied construction					262	262
Consumer and other loans						
Consumer loans					84	84
Total covered loans	2,281	37	364	2,682	80,353	83,035
Total loans	$ 11,612	$ 3,195	$ 10,272	$ 25,079	$ 1,681,462	$ 1,706,541

Table of Contents

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The Company may make concessions in interest rates, loan terms and/or amortization terms when restructuring loans for borrowers experiencing financial difficulty. Restructured loans in excess of $250 thousand are evaluated for a specific reserve based on either the collateral or net present value method, whichever is most applicable. Restructured loans under $250 thousand are subject to the reserve calculation at the historical loss rate for classified loans. Certain TDRs are classified as nonperforming at the time of restructuring and are returned to performing status after six months of satisfactory payment performance; however, these loans remain identified as impaired until full payment or other satisfaction of the obligation occurs. PCI loans are generally not considered TDRs as long as the loans remain in the assigned loan pool. No covered loans were recorded as TDRs as of December 31, 2016, or December 31, 2015.

The following table presents loans modified as TDRs, by loan class and accrual status, as of the dates indicated:

	December 31, 2016			December 31, 2015		
(Amounts in thousands)	Nonaccrual [1]	Accruing	Total	Nonaccrual [1]	Accruing	Total
Commercial loans						
Single family non-owner occupied	$ 38	$ 892	$ 930	$ 130	$ 820	$ 950
Non-farm, non-residential		4,160	4,160		4,600	4,600
Consumer real estate loans						
Home equity lines		158	158	127	43	170
Single family owner occupied	905	7,503	8,408	733	8,256	8,989
Owner occupied construction	341	239	580	349	243	592
Total TDRs	$ 1,284	$ 12,952	$ 14,236	$ 1,339	$ 13,962	$ 15,301
Allowance for loan losses related to TDRs			$ 670			$ 590

(1) Nonaccrual TDRs are included in total nonaccrual loans disclosed in the nonaccrual table above.

The following table presents interest income recognized on TDRs for the periods indicated:

	Year Ended December 31,		
(Amounts in thousands)	2016	2015	2014
Interest income recognized	$ 424	$ 608	$ 597

37

Table of Contents

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following table presents loans modified as TDRs, by type of concession made and loan class, that were restructured during the periods indicated. The post-modification recorded investment represents the loan balance immediately following modification.

	Year Ended December 31,					
	2016			2015		
(Amounts in thousands)	Total Contracts	Pre-Modification Recorded Investment	Post-Modification Recorded Investment	Total Contracts	Pre-Modification Recorded Investment	Post-Modification Recorded Investment
Below market interest rate and extended payment term Single family owner occupied	1	$ 115	$ 115	5	$ 342	$ 342
Total	1	$ 115	$ 115	5	$ 342	$ 342

There were no payment defaults on loans modified as TDRs that were restructured within the previous 12 months as of December 31, 2016 and 2015.

The following table provides information about OREO, which consists of properties acquired through foreclosure, as of the dates indicated:

	December 31,	
(Amounts in thousands)	2016	2015
Non-covered OREO	$ 5,109	$ 4,873
Covered OREO	276	4,034
Total OREO	$ 5,385	$ 8,907
Non-covered OREO secured by residential real estate	$ 1,746	$ 2,677
Residential real estate loans in the foreclosure process [1]	2,539	2,727

(1) The recorded investment in consumer mortgage loans collateralized by residential real estate that are in the process of foreclosure according to local requirements of the applicable jurisdiction.

Table of Contents

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Note 6. Allowance for Loan Losses

The following tables present the changes in the allowance for loan losses, by loan segment, during the periods indicated:

	Year Ended December 31, 2016			
(Amounts in thousands)	**Commercial**	**Consumer Real Estate**	**Consumer and Other**	**Total Allowance**
Allowance, excluding PCI				
Beginning balance	$ 13,133	$ 6,356	$ 690	$ 20,179
Provision for loan losses charged to operations	30	385	881	1,296
Charge-offs	(2,392)	(1,612)	(1,172)	(5,176)
Recoveries	919	358	360	1,637
Net charge-offs	(1,473)	(1,254)	(812)	(3,539)
Ending balance	$ 11,690	$ 5,487	$ 759	$ 17,936
PCI allowance				
Beginning balance	$	$ 54	$	$ 54
Recovery of loan losses		(42)		(42)
Benefit attributable to the FDIC indemnification asset		1		1
Recovery of loan losses charged to operations		(41)		(41)
Recovery of loan losses recorded through the FDIC indemnification asset		(1)		(1)
Ending balance	$	$ 12	$	$ 12
Total allowance				
Beginning balance	$ 13,133	$ 6,410	$ 690	$ 20,233
Provision for loan losses	30	343	881	1,254
Benefit attributable to the FDIC indemnification asset		1		1
Provision for loan losses charged to operations	30	344	881	1,255
Recovery of loan losses recorded through the FDIC indemnification asset		(1)		(1)
Charge-offs	(2,392)	(1,612)	(1,172)	(5,176)
Recoveries	919	358	360	1,637
Net charge-offs	(1,473)	(1,254)	(812)	(3,539)
Ending balance	$ 11,690	$ 5,499	$ 759	$ 17,948

Table of Contents

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	Year Ended December 31, 2015			
(Amounts in thousands)	**Commercial**	**Consumer Real Estate**	**Consumer and Other**	**Total Allowance**
Allowance, excluding PCI				
Beginning balance	$ 13,010	$ 6,489	$ 670	$ 20,169
Provision for loan losses charged to operations	931	95	1,140	2,166
Charge-offs	(1,282)	(906)	(1,557)	(3,745)
Recoveries	474	678	437	1,589
Net charge-offs	(808)	(228)	(1,120)	(2,156)
Ending balance	$ 13,133	$ 6,356	$ 690	$ 20,179
PCI allowance				
Beginning balance	$ 37	$ 21	$	$ 58
(Recovery of) provision for loan losses	(37)	33		(4)
Benefit attributable to the FDIC indemnification asset	29			29
(Recovery of) provision for loan losses charged to operations	(8)	33		25
Recovery of loan losses recorded through the FDIC indemnification asset	(29)			(29)
Ending balance	$	$ 54	$	$ 54
Total allowance				
Beginning balance	$ 13,047	$ 6,510	$ 670	$ 20,227
Provision for loan losses	894	128	1,140	2,162
Benefit attributable to the FDIC indemnification asset	29			29
Provision for loan losses charged to operations	923	128	1,140	2,191
Recovery of loan losses recorded through the FDIC indemnification asset	(29)			(29)
Charge-offs	(1,282)	(906)	(1,557)	(3,745)
Recoveries	474	678	437	1,589
Net charge-offs	(808)	(228)	(1,120)	(2,156)
Ending balance	$ 13,133	$ 6,410	$ 690	$ 20,233

Table of Contents

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following tables present the allowance for loan losses and recorded investment in loans evaluated for impairment, excluding PCI loans, by loan class, as of the dates indicated:

	December 31, 2016			
(Amounts in thousands)	Loans Individually Evaluated for Impairment	Allowance for Loans Individually Evaluated	Loans Collectively Evaluated for Impairment	Allowance for Loans Collectively Evaluated
Commercial loans				
Construction, development, and other land	$	$	$ 60,281	$ 889
Commercial and industrial			93,099	495
Multi-family residential	281		133,947	1,157
Single family non-owner occupied	1,910	31	139,711	2,721
Non-farm, non-residential	1,454		600,915	6,185
Agricultural			6,028	43
Farmland	981	18	31,145	151
Total commercial loans	4,626	49	1,065,126	11,641
Consumer real estate loans				
Home equity lines			122,000	895
Single family owner occupied	5,120	770	501,617	3,594
Owner occupied construction	336		44,199	228
Total consumer real estate loans	5,456	770	667,816	4,717
Consumer and other loans				
Consumer loans			77,524	759
Other			3,971	
Total consumer and other loans			81,495	759
Total loans, excluding PCI loans	$ 10,082	$ 819	$ 1,814,437	$ 17,117

	December 31, 2015			
(Amounts in thousands)	Loans Individually Evaluated for Impairment	Allowance for Loans Individually Evaluated	Loans Collectively Evaluated for Impairment	Allowance for Loans Collectively Evaluated
Commercial loans				
Construction, development, and other land	$	$	$ 53,437	$ 1,119
Commercial and industrial			89,885	504
Multi-family residential			95,486	1,535
Single family non-owner occupied	1,401	124	147,209	3,245
Non-farm, non-residential	14,094	1,568	478,839	4,825

Agricultural			2,945	22
Farmland			28,183	190
Total commercial loans	15,495	1,692	895,984	11,440
Consumer real estate loans				
Home equity lines			126,691	1,091
Single family owner occupied	6,874	672	495,761	4,297
Owner occupied construction	349	7	43,323	290
Total consumer real estate loans	7,223	679	665,775	5,678
Consumer and other loans				
Consumer loans			72,084	690
Other			7,338	
Total consumer and other loans			79,422	690
Total loans, excluding PCI loans	$ 22,718	$ 2,371	$ 1,641,181	$ 17,808

Table of Contents

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following table presents the allowance for loan losses on PCI loans and recorded investment in PCI loans, by loan pool, as of the dates indicated:

	December 31, 2016		December 31, 2015	
(Amounts in thousands)	Recorded Investment	Allowance for Loan Pools With Impairment	Recorded Investment	Allowance for Loan Pools With Impairment
Commercial loans				
Waccamaw commercial	$ 260	$	$ 3,788	$
Peoples commercial	4,491		5,525	
Other	1,095		1,254	
Total commercial loans	5,846		10,567	
Consumer real estate loans				
Waccamaw serviced home equity lines	20,178		29,241	
Waccamaw residential	1,320		1,678	1
Peoples residential	1,085	12	1,156	53
Total consumer real estate loans	22,583	12	32,075	54
Total PCI loans	$ 28,429	$ 12	$ 42,642	$ 54

Management believed the allowance was adequate to absorb probable loan losses inherent in the loan portfolio as of December 31, 2016.

Note 7. FDIC Indemnification Asset

In connection with the FDIC-assisted acquisition of Waccamaw in 2012, the Company entered into loss share agreements with the FDIC that covered $56.99 million of loans and $276 thousand of OREO as of December 31, 2016, compared to $83.04 million of loans and $4.03 million of OREO as of December 31, 2015. Under the loss share agreements, the FDIC agrees to cover 80% of most loan and foreclosed real estate losses and reimburse certain expenses incurred in relation to these covered assets. Loss share coverage will expire June 30, 2017, for commercial loans, with recoveries continuing until June 30, 2019. Loss share coverage will expire June 30, 2022, for single family loans. The Company s consolidated statements of income include the expense on covered assets net of estimated reimbursements. The following table presents the changes in the FDIC indemnification asset during the periods indicated:

	Year Ended December 31,	
(Amounts in thousands)	2016	2015
Beginning balance	$ 20,844	$ 27,900
Decrease in estimated losses on covered loans	(1)	(28)
Increase in estimated losses on covered OREO	1,045	1,489
Reimbursable expenses from the FDIC	162	545
Net amortization	(5,474)	(6,379)
Reimbursements from the FDIC	(4,403)	(2,683)

Ending balance	$ 12,173	$ 20,844

Table of Contents

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Note 8. Premises, Equipment, and Leases

Premises and Equipment

The following table presents the components of premises and equipment as of the dates indicated:

(Amounts in thousands)	December 31, 2016	2015
Land	$ 18,987	$ 19,155
Buildings and leasehold improvements	46,740	50,776
Equipment	32,519	36,709
Total premises and equipment	98,246	106,640
Accumulated depreciation and amortization	(48,161)	(53,884)
Total premises and equipment, net	$ 50,085	$ 52,756

Impairment charges related to certain long-term investments in land and buildings totaled $364 thousand in 2016, $259 thousand in 2015, and $935 thousand in 2014. Depreciation and amortization expense for premises and equipment was $3.56 million in 2016, $4.14 million in 2015, and $4.41 million in 2014.

Leases

The Company enters into various noncancelable operating leases. The following schedule presents the future minimum lease payments required under noncancelable operating leases, with initial or remaining terms in excess of one year, by year, as of December 31, 2016:

(Amounts in thousands)	
2017	$ 341
2018	199
2019	110
2020	97
2021	97
2022 and thereafter	791
	$ 1,635

Lease expense was $784 thousand in 2016, $862 thousand in 2015, and $1.06 million in 2014. Certain portions of the Company s leases have been sublet to third parties for properties not currently being used by the Company. Future minimum lease payments to be received under noncancelable subleases totaled $1 thousand as of December 31, 2016.

Note 9. Goodwill and Other Intangible Assets

Goodwill

The company has one reporting unit for goodwill impairment testing purposes Community Banking. Prior to October 2016, the Company maintained two reporting units Community Banking and Insurance Services. The Insurance Services reporting unit consisted of the Company s wholly owned subsidiary Greenpoint, which was sold in October 2016. The Company performed its annual qualitative assessment of goodwill as of October 31, 2016, and concluded that no impairment charge was necessary. No events have occurred after the 2016 analysis to indicate potential impairment.

Table of Contents

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following table presents the changes in goodwill, by reporting unit, during the periods indicated:

(Amounts in thousands)	Community Banking	Insurance Services	Total
Balance January 1, 2014	$ 96,541	$ 8,914	$ 105,455
Acquisitions and dispositions, net	(6,454)		(6,454)
Cash consideration paid	1,368	353	1,721
Balance December 31, 2014	$ 91,455	$ 9,267	$ 100,722
Balance January 1, 2015	$ 91,455	$ 9,267	$ 100,722
Acquisitions and dispositions, net		(324)	(324)
Cash consideration paid		88	88
Balance December 31, 2015	$ 91,455	$ 9,031	$ 100,486
Balance January 1, 2016	$ 91,455	$ 9,031	$ 100,486
Acquisitions and dispositions, net	1,290	(5,997)	(4,707)
Other [(1)]	3,034	(3,034)	
Balance December 31, 2016	$ 95,779	$	$ 95,779

(1) Represents the transfer of goodwill after the sale of Greenpoint to one reporting unit

Other Intangible Assets

The Company s other intangible assets include core deposit and other identifiable intangibles. As of December 31, 2016, the remaining lives of core deposit intangibles ranged from 6 years to 9 years and the weighted average remaining life was 7 years. Other identifiable intangibles consist primarily of the value assigned to contractual rights arising from insurance agency acquisitions. The following table presents the components of other intangible assets, by reporting unit, as of the dates indicated:

	December 31,			
	2016	2015		
(Amounts in thousands)	Total	Community Banking	Insurance Services	Total
Core deposit intangibles	$ 11,536	$ 12,282	$	$ 12,282
Accumulated amortization	(4,515)	(7,958)		(7,958)
Core deposit intangibles, net	7,021	4,324		4,324
Other identifiable intangibles	3,508	535	3,711	4,246
Accumulated amortization	(3,322)	(464)	(2,863)	(3,327)
Other identifiable intangibles, net	186	71	848	919

Total other intangible assets, net	$ 7,207	$ 4,395	$ 848	$ 5,243

Table of Contents

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Amortization expense for other intangible assets was $1.14 million in 2016, $1.12 million in 2015, and $787 thousand in 2014. The following schedule presents the estimated amortization expense for intangible assets, by year, as of December 31, 2016:

(Amounts in thousands)	
2017	$ 1,029
2018	1,029
2019	1,029
2020	1,029
2021	1,015
2022 and thereafter	2,034
	$ 7,165

Note 10. Deposits

The following table presents the components of deposits as of the dates indicated:

	December 31,	
(Amounts in thousands)	**2016**	**2015**
Noninterest-bearing demand deposits	$ 427,705	$ 451,511
Interest-bearing deposits:		
Interest-bearing demand deposits	378,339	347,705
Money market accounts	196,997	213,982
Savings deposits	326,263	316,603
Certificates of deposit	382,503	408,519
Individual retirement accounts	129,531	134,939
Total interest-bearing deposits	1,413,633	1,421,748
Total deposits	$ 1,841,338	$ 1,873,259

The following schedule presents the contractual maturities of time deposits, by year, as of December 31, 2016:

(Amounts in thousands)	
2017	$ 254,738
2018	88,596
2019	53,400
2020	68,644
2021	44,968
2022 and thereafter	1,688

	$ 512,034

Table of Contents

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Time deposits of $250 thousand or more totaled $41.55 million as of December 31, 2016, and $41.35 million as of December 31, 2015. The following schedule presents the contractual maturities of time deposits of $250 thousand or more as of December 31, 2016:

(Amounts in thousands)	
Three months or less	$ 6,274
Over three through six months	2,687
Over six through twelve months	10,890
Over twelve months	21,698
	$ 41,549

Note 11. Borrowings

The following table presents the components of borrowings as of the dates indicated:

	December 31,			
	2016		2015	
(Amounts in thousands)	**Balance**	**Weighted Average Rate**	**Balance**	**Weighted Average Rate**
Short-term borrowings				
Retail repurchase agreements	$ 73,005	0.07%	$ 88,614	0.10%
Long-term borrowings				
Wholesale repurchase agreements	25,000	3.18%	50,000	3.71%
Long-term FHLB advances	65,000	4.04%	65,000	4.04%
Other borrowings				
Subordinated debt	15,464	3.65%	15,464	3.23%
Other debt	244		292	
Total borrowings	$ 178,713		$ 219,370	

The following schedule presents the contractual and weighted average maturities of long-term borrowings, by year, as of December 31, 2016:

(Amounts in thousands)	**Wholesale Repurchase Agreements**	**FHLB Borrowings**	**Total**
2017	$	$ 15,000	$ 15,000
2018			
2019	25,000		25,000
2020			
2021		50,000	50,000
2022 and thereafter			
	$ 25,000	$ 65,000	$ 90,000

Weighted average maturity (in years)	2.15	3.17	2.89

The FHLB may redeem callable advances at quarterly intervals, which could substantially shorten the advances lives. If called, the advance may be paid in full or converted into another FHLB credit product. Prepayment of an advance may result in substantial penalties based on the differential between the contractual note and current advance rate for similar maturities. The Company pledged certain loans to secure FHLB advances and letters of

46

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

credit totaling $1.03 billion as of December 31, 2016. Unused borrowing capacity with the FHLB totaled $558.75 million, net of FHLB letters of credit $75.72 million, as of December 31, 2016. The FHLB letters of credit provide an attractive alternative to pledging securities for public unit deposits.

Investment securities pledged to secure repurchase agreements remain under the Company s control during the agreements terms. The counterparties may redeem callable repurchase agreements, which could substantially shorten the borrowings lives. The prepayment or unwind of a repurchase agreement may result in substantial penalties based on market conditions.

The following schedule presents the contractual maturities of repurchase agreements, by type of collateral pledged, as of December 31, 2016:

(Amounts in thousands)	U.S. Agency Securities	Municipal Securities	Mortgage-backed Agency Securities	Total
Overnight and continuous	$ 18,680	$ 44,414	$ 7,821	$ 70,915
Up to 30 days				
30 90 days				
Greater than 90 days		1,204	25,886	27,090
	$ 18,680	$ 45,618	$ 33,707	$ 98,005

Subordinated debt consists of $15.46 million of junior subordinated debentures (Debentures) the Company issued to the Trust in October 2003 with an interest rate of three-month London InterBank Offered Rate (LIBOR) plus 2.95%. The Debentures mature on October 8, 2033, and are callable quarterly. The Trust purchased the Debentures through the issuance of trust preferred securities, which had substantially identical terms as the Debentures. Net proceeds from the offering were contributed as capital to the Bank to support further growth. The Company s obligations under the Debentures and other relevant Trust agreements, in aggregate, constitute a full and unconditional guarantee of the Trust s obligations. The preferred securities issued by the Trust are not included in the consolidated balance sheets; however, these securities qualify as Tier 1 capital for regulatory purposes, subject to guidelines issued by the Board of Governors of the Federal Reserve System (Federal Reserve). The Federal Reserve s quantitative limits did not prevent the Company from including all $15.46 million in trust preferred securities outstanding in Tier 1 capital as of December 31, 2016 and 2015. On January 9, 2017, the Company redeemed all of its trust preferred securities.

In addition, the Company maintains a $15.00 million unsecured, committed line of credit with an unrelated financial institution with an interest rate of one-month LIBOR plus 2.00% and an April 2017 maturity. There was no outstanding balance on the line as of December 31, 2016, or December 31, 2015.

Note 12. Derivative Instruments and Hedging Activities

As of December 31, 2016, the Company s derivative instruments consisted of interest rate swaps. Generally, derivative instruments help the Company manage exposure to market risk and meet customer financing needs. Market risk represents the possibility that fluctuations in external factors such as interest rates, market-driven loan rates, prices, or other economic factors will adversely affect economic value or net interest income.

The Company uses interest rate swap contracts to modify its exposure to interest rate risk caused by changes in the LIBOR curve in relation to certain designated fixed rate loans. These instruments are used to convert these fixed rate loans to an effective floating rate. If the LIBOR rate falls below the loan s stated fixed rate for a given period, the Company will owe the floating rate payer the notional amount times the difference between LIBOR

Table of Contents

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

and the stated fixed rate. If LIBOR is above the stated rate for a given period, the Company will receive payments based on the notional amount times the difference between LIBOR and the stated fixed rate. The Company s interest rate swaps qualify as fair value hedging instruments; therefore, fair value changes in the derivative and hedged item attributable to the hedged risk are recognized in earnings in the same period.

The Company s interest rate swaps include a fourteen-year, $1.20 million notional interest rate swap agreement entered into in March 2015 and a fifteen-year, $4.37 million notional interest rate swap agreement entered into in February 2014. The swap agreements, which are accounted for as fair value hedges, and the loans hedged by the agreements are recorded at fair value. The fair value hedges were effective as of December 31, 2016. The following table presents the notional, or contractual, amounts and fair values of derivative instruments as of the dates indicated:

	December 31,					
	2016			2015		
(Amounts in thousands)	**Notional or Contractual Amount**	**Derivative Assets**	**Derivative Liabilities**	**Notional or Contractual Amount**	**Derivative Assets**	**Derivative Liabilities**
Derivatives designated as hedges						
Interest rate swaps	$ 4,835	$	$ 167	$ 5,151	$	$ 251
Total derivatives	$ 4,835	$	$ 167	$ 5,151	$	$ 251

The following table presents the effect of derivative and hedging activity, if applicable, on the consolidated statements of income for the periods indicated:

	Year Ended December 31,			
(Amounts in thousands)	**2016**	**2015**	**2014**	**Income Statement Location**
Derivatives designated as hedges				
Interest rate swaps	$ 116	$ 122	$ 162	Interest and fees on loans
Total derivatives	$ 116	$ 122	$ 162	

Table of Contents

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Note 13. Employee Benefit Plans
Defined Benefit Plans

The Company maintains two nonqualified domestic, noncontributory defined benefit plans (the Benefit Plans) for key members of senior management and non-management directors. The Company s unfunded Benefit Plans include the Supplemental Executive Retention Plan (SERP) and the Directors Supplemental Retirement Plan (Directors Plan). The SERP provides for a defined benefit, at normal retirement age, targeted at 35% of the participant s projected final average compensation, subject to a defined maximum annual benefit. Benefits under the SERP generally become payable at age 62. The Directors Plan provides for a defined benefit, at normal retirement age, up to 100% of the participant s highest consecutive three-year average compensation. Benefits under the Directors Plan generally become payable at age 70. The following table presents the changes in the aggregate actuarial benefit obligation during the periods indicated:

	December 31,	
(Amounts in thousands)	**2016**	**2015**
Beginning balance	$ 8,390	$ 7,631
Plan change	69	
Service cost	184	180
Interest cost	382	334
Actuarial loss	367	363
Benefits paid	(211)	(118)
Ending balance	$ 9,181	$ 8,390

The following table presents the components of net periodic pension cost and the assumed discount rate for the periods indicated:

	Year Ended December 31,		
(Amounts in thousands, except discount rate)	**2016**	**2015**	**2014**
Service cost	$ 184	$ 180	$ 128
Interest cost	382	334	336
Amortization of prior service cost	226	260	260
Amortization of losses	47	66	
Net periodic cost	$ 839	$ 840	$ 724
Assumed discount rate	4.22%	4.62%	4.41%

The following schedule presents the projected benefit payments to be paid under the Benefit Plans, by year, as of December 31, 2016:

(Amounts in thousands)	
2017	$ 465
2018	462
2019	458
2020	529
2021	587
2022 through 2026	2,937

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Employee Welfare Plan

The Company provides various medical, dental, vision, life, accidental death and dismemberment, and long-term disability insurance benefits to all full-time employees who elect coverage under this program. A third-party administrator manages the health plan. Monthly employer and employee contributions are made to a tax-exempt employee benefits trust where the third-party administrator processes and pays claims. As of December 31, 2016, stop-loss insurance coverage generally limits the Company s risk of loss to $125 thousand for individual claims and $3.92 million for aggregate claims. Expenses related to the health plan totaled $3.48 million in 2016, $3.06 million in 2015, and $2.88 million in 2014.

Deferred Compensation Plan

The Company maintains deferred compensation agreements with certain current and former officers that provide benefit payments, over various periods, commencing at retirement or death. Accrued benefits are based on the present values of expected payments and estimated life expectancies and totaled $458 thousand as of December 31, 2016 and 2015. Expenses related to the deferred compensation plan totaled $60 thousand in each of the three years ended December 31, 2016.

Employee Stock Ownership and Savings Plan

The Company maintains the Employee Stock Ownership and Savings Plan (KSOP) that consists of a 401(k) savings feature that covers all employees that meet minimum eligibility requirements. The Company matches employee contributions at levels determined by the Board of Directors annually. These contributions are made in the first quarter following each plan year and employees must be employed on the last day of the plan year to be eligible. Matching contributions to qualified deferrals under the 401(k) savings component of the KSOP totaled $1.50 million in 2016, $1.53 million in 2015, and $1.58 million in 2014. The KSOP held 410,384 shares of the Company s common stock as of December 31, 2016, 428,785 shares as of December 31, 2015, and 457,765 shares as of December 31, 2014. Substantially all plan assets are invested in the Company s common stock.

Equity-Based Compensation Plans

The Company maintains equity-based compensation plans to promote the long-term success of the Company by encouraging officers, employees, directors, and other individuals performing services for the Company to focus on critical long-range objectives. The Company s equity-based compensation plans include the 2012 Omnibus Equity Compensation Plan (2012 Plan), 2004 Omnibus Stock Option Plan, 2001 Director s Option Plan, 1999 Stock Option Plan, and various other plans obtained through acquisitions. As of December 31, 2016, the 2012 Plan was the only plan available for the issuance of future grants. All plans issued or obtained before the 2012 Plan are frozen and no new grants may be issued; however, any options or awards unexercised and outstanding under those plans remain in effect per their respective terms. The 2012 Plan authorized 600,000 shares available for potential grants of incentive stock options, nonqualified stock options, performance awards, restricted stock, restricted stock units, stock appreciation rights, bonus stock, and stock awards. Grants issued under the 2012 Plan state the period of time the grant may be exercised, not to exceed more than ten years from the date granted. The Company s Compensation and Retirement Committee determines the vesting period for each grant; however, if no vesting period is specified the vesting occurs in 25% increments on the first four anniversaries of the grant date.

Table of Contents

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following table presents the pre-tax compensation expense and excess tax benefit recognized in earnings for all equity-based compensation plans for the periods indicated:

	Year Ended December 31,		
(Amounts in thousands)	**2016**	**2015**	**2014**
Pre-tax compensation expense	$ 209	$ 110	$ 332
Excess tax benefit	174	8	5

Stock Options

The following table presents stock option activity and related information for the year ended December 31, 2016:

(Amounts in thousands, except share and per share data)	**Option Shares**	**Weighted Average Exercise Price Per Share**	**Weighted Average Remaining Contractual Term (Years)**	**Aggregate Intrinsic Value**
Outstanding, January 1, 2016	236,404	$ 20.17		
Granted	32,768	20.15		
Exercised	(43,463)	17.26		
Canceled	(25,313)	28.56		
Outstanding, December 31, 2016	200,396	$ 19.73	6.1	$ 2,123
Exercisable, December 31, 2016	167,628	$ 19.65	5.5	$ 1,790

The following table presents the total options granted and the weighted average assumptions used to estimate the fair value of those options during the periods indicated:

	Year Ended December 31,		
	2016	**2015**	**2014**
Stock options granted	$ 32,768	$	$
Grant-date fair value per share	10.16		
Volatility	25.04%		
Risk-free rate	1.56%		
Expected dividend yield	3.09%		
Expected term (in years)	6.50		

The intrinsic value of options exercised totaled $434 thousand in 2016, $20 thousand in 2015, and $13 thousand in 2014. As of December 31, 2016, unrecognized compensation cost related to nonvested stock options was $101 thousand with an expected weighted average recognition period of 1.11 years. The actual compensation cost recognized might differ from this estimate due to various items, including new grants and changes in estimated forfeitures.

Table of Contents

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Restricted Stock Awards

The following table presents restricted stock activity and related information for the year ended December 31, 2016:

	Shares	Weighted Average Grant-Date Fair Value
Nonvested, January 1, 2016	5,327	$ 16.85
Granted	46,033	19.97
Vested	(21,533)	17.90
Canceled	(2,024)	19.27
Nonvested, December 31, 2016	27,803	$ 20.59

As of December 31, 2016, unrecognized compensation cost related to nonvested restricted stock awards was $447 thousand with an expected weighted average recognition period of 2.03 years. The actual compensation cost recognized might differ from this estimate due to various items, including new awards granted and changes in estimated forfeitures.

Performance Stock Awards

Performance stock awards represent restricted stock that may be issuable in the future if specific performance criteria are met. The following table presents performance stock activity and related information for the year ended December 31, 2016:

	Shares	Weighted Average Grant-Date Fair Value
Nonvested, January 1, 2016	9,848	$ 15.83
Granted		
Vested	(9,848)	15.83
Canceled		
Nonvested, December 31, 2016		$

As of December 31, 2016, there was no unrecognized compensation cost related to nonvested performance stock awards. The actual compensation cost recognized might differ from this estimate due to various items, including new awards granted, changes in estimated forfeitures, and resolution of performance contingencies.

Table of Contents

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Note 14. Other Operating Income and Expense

The following table presents the components of other operating income and expense for the periods indicated:

(Amounts in thousands)	Year Ended December 31, 2016	2015	2014
Other operating income			
Bank owned life insurance	$ 955	$ 1,971	$ 1,587
Other [(1)]	2,254	2,158	2,768
Total other operating income	$ 3,209	$ 4,129	$ 4,355
Other operating expense			
Service fees	$ 3,641	$ 3,401	$ 3,856
ATM processing expenses	2,024	2,407	2,102
Telephone and data communications	1,598	1,595	1,715
Advertising and public relations	1,532	1,309	1,001
Professional fees	1,501	1,272	1,436
OREO expense and net loss	1,420	2,438	2,094
Office supplies	1,220	1,228	1,514
Other [(1)]	7,011	7,461	8,524
Total other operating expense	$ 19,947	$ 21,111	$ 22,242

(1) Other components of other operating income or expense that do not exceed 1% of total income.

Note 15. Income Taxes

Income tax expense is comprised of current and deferred, federal and state income taxes on the Company s pre-tax earnings. The following table presents the components of the income tax provision for the periods indicated:

(Amounts in thousands)	Year Ended December 31, 2016	2015	2014
Current tax expense (benefit):			
Federal	$ 13,634	$ (254)	$ 7,234
State	675	581	1,325
Total current tax expense	14,309	327	8,559
Deferred tax expense (benefit):			
Federal	(1,480)	10,034	2,971
State	(10)	1,020	794
Total deferred tax expense (benefit)	(1,490)	11,054	3,765

Total income tax expense	$ 12,819	$ 11,381	$ 12,324

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The Company s effective tax rate, income tax as a percent of pre-tax income, may vary significantly from the statutory rate due to permanent differences and available tax credits. Permanent differences are income and expense items excluded by law in the calculation of taxable income. The Company s most significant permanent differences generally include interest income on municipal securities and increases in the cash surrender value of life insurance policies. The following table reconciles the Company s income tax expense to the amount computed by applying the federal statutory tax rate to pre-tax income for the periods indicated:

	Year Ended December 31,					
	2016		2015		2014	
(Amounts in thousands)	**Amount**	**Percent**	**Amount**	**Percent**	**Amount**	**Percent**
Income tax at the federal statutory rate	$ 13,281	35.00%	$ 12,572	35.00%	$ 13,235	35.00%
State income taxes, net of federal benefit	598	1.58%	639	1.78%	1,006	2.66%
	13,878	36.58%	13,212	36.78%	14,241	37.66%
Increase (decrease) resulting from:						
Tax-exempt interest income	(1,336)	-3.52%	(1,463)	-4.07%	(1,645)	-4.35%
Nondeductible goodwill	340	0.89%				
Bank owned life insurance	(335)	-0.88%	(690)	-1.92%	(555)	-1.47%
Other items, net	271	0.71%	322	0.89%	283	0.75%
Income tax at the effective tax rate	$ 12,819	33.78%	$ 11,381	31.68%	$ 12,324	32.59%

Deferred taxes derived from continuing operations reflect the net effect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and amounts used for tax purposes. The following table presents the significant components of the net deferred tax asset as of the dates indicated:

	December 31,	
(Amounts in thousands)	**2016**	**2015**
Deferred tax assets		
Allowance for loan losses	$ 6,644	$ 7,741
Unrealized losses on available-for-sale securities	326	2,331
Unrealized asset losses	913	1,506
Purchase accounting	5,384	5,014
FDIC assisted transactions	6,540	6,551
Intangible assets	4,062	4,082
Deferred compensation assets	4,669	4,529
Deferred loan fees	1,979	1,402
Other deferred tax assets	825	1,181
Total deferred tax assets	31,342	34,337
Deferred tax liabilities		
FDIC indemnification asset	11,927	13,162
Fixed assets	2,042	2,658
Odd days interest deferral	1,283	1,975
Other	347	347

Total deferred tax liabilities	15,599	18,142
Net deferred tax asset	$ 15,743	$ 16,195

The Company had no unrecognized tax benefits or accrued interest and penalties as of December 31, 2016 or 2015.

Table of Contents

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Note 16. Accumulated Other Comprehensive Income

The following table presents the changes in AOCI, net of tax and by component, during the periods indicated:

(Amounts in thousands)	Unrealized Gains (Losses) on Available-for-Sale Securities	Employee Benefit Plans	Total
Balance January 1, 2014	$ (13,640)	$ (1,100)	$ (14,740)
Other comprehensive income (loss) before reclassifications	8,051	(401)	7,650
Reclassified from AOCI	1,323	162	1,485
Other comprehensive income (loss), net	9,374	(239)	9,135
Balance December 31, 2014	$ (4,266)	$ (1,339)	$ (5,605)
Balance January 1, 2015	$ (4,266)	$ (1,339)	$ (5,605)
Other comprehensive income (loss) before reclassifications	471	(226)	245
Reclassified from AOCI	(90)	203	113
Other comprehensive income (loss), net	381	(23)	358
Balance December 31, 2015	$ (3,885)	$ (1,362)	$ (5,247)
Balance January 1, 2016	$ (3,885)	$ (1,362)	$ (5,247)
Other comprehensive income (loss) before reclassifications	647	(276)	371
Reclassified from AOCI	2,694	171	2,865
Other comprehensive income (loss), net	3,341	(105)	3,236
Balance December 31, 2016	$ (544)	$ (1,467)	$ (2,011)

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following table presents reclassifications out of AOCI, by component, during the periods indicated:

(Amounts in thousands)	**Year Ended December 31, 2016**	**2015**	**2014**	**Income Statement Line Item Affected**
Available-for-sale securities				
(Gains) losses recognized	(335)	(144)	1,385	Net gain (loss) on sale of securities
OTTI recognized	4,646		737	Net impairment losses recognized in earnings
Reclassified out of AOCI, before tax	4,311	(144)	2,122	Income before income taxes
Income tax (expense) benefit	(1,617)	54	(799)	Income tax expense
Reclassified out of AOCI, net of tax	2,694	(90)	1,323	Net income
Employee benefit plans				
Amortization of prior service cost	226	260	260	(1)
Amortization of net actuarial loss	47	66		(1)
Reclassified out of AOCI, before tax	273	326	260	Income before income taxes
Income tax expense	(102)	(123)	(98)	Income tax expense
Reclassified out of AOCI, net of tax	171	203	162	Net income
Total reclassified out of AOCI, net of tax	$ 2,865	$ 113	$ 1,485	Net income

(1) Amortization is included in net periodic pension cost. See Note 13, Employee Benefit Plans

Note 17. Fair Value
Financial Instruments Measured at Fair Value

The following discussion describes the valuation methodologies used for instruments measured at fair value, as well as the general classification of such instruments under the valuation hierarchy.

Assets and Liabilities Reported at Fair Value on a Recurring Basis

Available-for-Sale Securities. Securities available for sale are reported at fair value on a recurring basis. The fair value of Level 1 securities is based on quoted market prices in active markets, if available. The Company also uses Level 1 inputs to value equity securities that are traded in active markets. If quoted market prices are not available, fair values are measured utilizing independent valuation techniques of identical or similar securities for which significant assumptions are primarily derived from or corroborated by observable market data. Level 2 securities use fair value measurements from independent pricing services obtained by the Company. These fair value measurements consider observable data that may include dealer quotes, market spreads, cash flows, the Treasury yield curve, live trading levels, trade execution data, market consensus prepayment speeds, credit information, and bond terms and conditions. The Company s Level 2 securities include Treasury securities, single issue trust preferred securities, corporate securities, mortgage-backed securities, and certain equity securities that are not actively traded. Securities are based on Level 3 inputs when there is limited activity or less transparency to the valuation inputs. In the absence of observable or corroborated market data, internally developed estimates that incorporate market-based assumptions are used when such information is available.

Fair value models may be required when trading activity has declined significantly or does not exist, prices are not current, or pricing variations are significant. For Level 3 securities, the Company obtains the cash flow of

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

specific securities from third parties that use modeling software to determine cash flows based on market participant data and knowledge of the structures of each individual security. The fair values of Level 3 securities are determined by applying proper market observable discount rates to the cash flow derived from third-party models. Discount rates are developed by determining credit spreads above a benchmark rate, such as LIBOR, and adding premiums for illiquidity, which are based on a comparison of initial issuance spread to LIBOR versus a financial sector curve for recently issued debt to LIBOR. Securities with increased uncertainty about the receipt of cash flows are discounted at higher rates due to the addition of a deal specific credit premium based on assumptions about the performance of the underlying collateral. Finally, internal fair value model pricing and external pricing observations are combined by assigning weights to each pricing observation. Pricing is reviewed for reasonableness based on the direction of specific markets and the general economic indicators.

Loans Held for Investment. Loans held for investment are reported at fair value using discounted future cash flows that apply current interest rates for loans with similar terms and borrower credit quality. Loans related to fair value hedges are recorded at fair value on a recurring basis.

Deferred Compensation Assets and Liabilities. Securities held for trading purposes are recorded at fair value on a recurring basis and included in other assets in the consolidated balance sheets. These securities include assets related to employee deferred compensation plans, which are generally invested in Level 1 equity securities. The liability associated with these deferred compensation plans is carried at the fair value of the obligation to the employee, which corresponds to the fair value of the invested assets.

Derivative Assets and Liabilities. Derivatives are recorded at fair value on a recurring basis. The Company obtains dealer quotes, Level 2 inputs, based on observable data to value derivatives.

The following tables summarize financial assets and liabilities recorded at fair value on a recurring basis, by the level of valuation inputs in the fair value hierarchy, as of the dates indicated:

	December 31, 2016			
	Total Fair Value	Fair Value Measurements Using		
(Amounts in thousands)		Level 1	Level 2	Level 3
Available-for-sale securities				
U.S. Agency securities	$ 1,345	$	$ 1,345	$
Municipal securities	113,331		113,331	
Single issue trust preferred securities	19,939		19,939	
Mortgage-backed Agency securities	30,891		30,891	
Equity securities	73	55	18	
Total available-for-sale securities	165,579	55	165,524	
Fair value loans	4,701		4,701	
Deferred compensation assets	3,224	3,224		
Deferred compensation liabilities	3,224	3,224		
Derivative liabilities	167		167	

Table of Contents

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

		December 31, 2015 Fair Value Measurements Using		
(Amounts in thousands)	**Total Fair Value**	**Level 1**	**Level 2**	**Level 3**
Available-for-sale securities				
U.S. Agency securities	$ 30,702	$	$ 30,702	$
Municipal securities	128,678		128,678	
Single issue trust preferred securities	47,832		47,832	
Corporate securities	70,333		70,333	
Certificates of deposit	5,000		5,000	
Mortgage-backed Agency securities	83,556		83,556	
Equity securities	72	54	18	
Total available-for-sale securities	366,173	54	366,119	
Fair value loans	4,886		4,886	
Deferred compensation assets	3,464	3,464		
Deferred compensation liabilities	3,464	3,464		
Derivative liabilities	251		251	

No changes in valuation techniques or transfers into or out of Level 3 of the fair value hierarchy occurred during the years ended December 31, 2016 or 2015.

Assets Measured at Fair Value on a Nonrecurring Basis

Impaired Loans. Impaired loans are recorded at fair value on a nonrecurring basis when repayment is expected solely from the sale of the loan s collateral. Fair value is based on appraised value adjusted for customized discounting criteria, Level 3 inputs.

The Company maintains an active and robust problem credit identification system. The impairment review includes obtaining third-party collateral valuations to help management identify potential credit impairment and determine the amount of impairment to record. The Company s Special Assets staff manages and monitors all impaired loans. Internal collateral valuations are generally performed within two to four weeks of identifying the initial potential impairment. The internal valuation compares the original appraisal to current local real estate market conditions and considers experience and expected liquidation costs. The Company typically receives a third-party valuation within thirty to forty-five days of completing the internal valuation. When a third-party valuation is received, it is reviewed for reasonableness. Once the valuation is reviewed and accepted, discounts are applied to fair market value, based on, but not limited to, our historical liquidation experience for like collateral, resulting in an estimated net realizable value. The estimated net realizable value is compared to the outstanding loan balance to determine the appropriate amount of specific impairment reserve.

Specific reserves are generally recorded for impaired loans while third-party valuations are in process and for impaired loans that continue to make some form of payment. While waiting to receive the third-party appraisal, the Company regularly reviews the relationship to identify any potential adverse developments and begins the tasks necessary to gain control of the collateral and prepare it for liquidation, including, but not limited to, engagement of counsel, inspection of collateral, and continued communication with the borrower. Generally, the only difference between the current appraised value, less liquidation costs, and the carrying amount of the loan, less the specific reserve, is any downward adjustment to the appraised value that the Company deems appropriate, such as the costs to sell the property. Impaired loans that do not meet certain criteria and do not have a specific reserve have typically been written down through partial charge-offs to net realizable value. Based on prior experience, the Company rarely returns loans to performing status after they have been partially charged off. Credits identified as impaired move quickly through the process towards ultimate resolution, except in cases involving bankruptcy and various state judicial processes that may extend the time for ultimate resolution.

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

OREO. OREO is recorded at fair value on a nonrecurring basis using Level 3 inputs. The Company calculates the fair value of OREO from current or prior appraisals that have been adjusted for valuation declines, estimated selling costs, and other proprietary qualitative adjustments that are deemed necessary.

The following tables present assets measured at fair value on a nonrecurring basis, by the level of valuation inputs in the fair value hierarchy, as of the dates indicated:

		December 31, 2016 Fair Value Measurements Using		
(Amounts in thousands)	Total Fair Value	Level 1	Level 2	Level 3
Impaired loans, non-covered	$ 4,078	$	$	$ 4,078
OREO, non-covered	5,109			5,109
OREO, covered	265			265

		December 31, 2015 Fair Value Measurements Using		
(Amounts in thousands)	Total Fair Value	Level 1	Level 2	Level 3
Impaired loans, non-covered	$ 9,164	$	$	$ 9,164
OREO, non-covered	4,819			4,819
OREO, covered	4,034			4,034

Quantitative Information about Level 3 Fair Value Measurements

The following table provides quantitative information for assets measured at fair value on a nonrecurring basis using Level 3 valuation inputs as of the dates indicated:

	Valuation	Unobservable	Discount Range (Weighted Average)	
	Technique	Input	December 31, 2016	December 31, 2015
Impaired loans, non-covered	Discounted appraisals (1)	Appraisal adjustments (2)	3% to 39% (17%)	1% to 39% (21%)
OREO, non-covered	Discounted appraisals (1)	Appraisal adjustments (2)	0% to 88% (30%)	1% to 100% (33%)
OREO, covered	Discounted appraisals (1)	Appraisal adjustments (2)	0% to 44% (40%)	21% to 65% (46%)

(1) Fair value is generally based on appraisals of the underlying collateral.
(2) Appraisals may be adjusted by management for customized discounting criteria, estimated sales costs, and proprietary qualitative adjustments.

Fair Value of Financial Instruments

The Company uses various methodologies and assumptions to estimate the fair value of certain financial instruments. A description of valuation methodologies used for instruments not previously discussed is as follows:

Cash and Cash Equivalents. Cash and cash equivalents are reported at their carrying amount, which is considered a reasonable estimate due to the short-term nature of these instruments.

Held-to-Maturity Securities. Securities held to maturity are reported at fair value using quoted market prices or dealer quotes.

Table of Contents

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

FDIC Indemnification Asset. The FDIC indemnification asset is reported at fair value using discounted future cash flows that apply current discount rates.

Accrued Interest Receivable/Payable. Accrued interest receivable/payable is reported at their carrying amount, which is considered a reasonable estimate due to the short-term nature of these instruments.

Deposits and Securities Sold Under Agreements to Repurchase. Deposits without a stated maturity, such as demand, interest-bearing demand, and savings, are reported at their carrying amount, the amount payable on demand as of the reporting date, which is considered a reasonable estimate of fair value. Deposits and repurchase agreements with fixed maturities and rates are reported at fair value using discounted future cash flows that apply interest rates available in the market for instruments with similar characteristics and maturities.

FHLB and Other Borrowings. FHLB and other borrowings are reported at fair value using discounted future cash flows that apply interest rates available to the Company for borrowings with similar characteristics and maturities. Trust preferred obligations are reported at fair value using current credit spreads in the market for similar issues.

Off-Balance Sheet Instruments. The Company believes that fair values of unfunded commitments to extend credit, standby letters of credit, and financial guarantees are not meaningful; therefore, off-balance sheet instruments are not addressed in the fair value disclosures. The Company believes it is not feasible or practical to accurately disclose the fair values of off-balance sheet instruments due to the uncertainty and difficulty in assessing the likelihood and timing of advancing available proceeds, the lack of an established market for these instruments, and the diversity in fee structures. For additional information about the unfunded, contractual value of off-balance sheet financial instruments, see Note 20, Litigation, Commitments, and Contingencies, to the Consolidated Financial Statements of this report.

The following tables present the carrying amounts and fair values of financial instruments, by the level of valuation inputs in the fair value hierarchy, as of the dates indicated:

	December 31, 2016				
			Fair Value Measurements Using		
(Amounts in thousands)	**Carrying Amount**	**Fair Value**	**Level 1**	**Level 2**	**Level 3**
Assets					
Cash and cash equivalents	$ 76,307	$ 76,307	$ 76,307	$	$
Securities available for sale	165,579	165,579	55	165,524	
Securities held to maturity	47,133	47,266		47,266	
Loans held for investment, net of allowance	1,835,000	1,805,999		4,701	1,801,298
FDIC indemnification asset	12,173	8,112			8,112
Interest receivable	5,553	5,553		5,553	
Deferred compensation assets	3,224	3,224	3,224		
Liabilities					
Demand deposits	427,705	427,705		427,705	
Interest-bearing demand deposits	378,339	378,339		378,339	
Savings deposits	523,260	523,260		523,260	
Time deposits	512,034	507,917		507,917	
Securities sold under agreements to repurchase	98,005	98,879		98,879	
Interest payable	1,280	1,280		1,280	
FHLB and other borrowings	80,708	83,551		83,551	
Derivative financial liabilities	167	167		167	
Deferred compensation liabilities	3,224	3,224	3,224		

Table of Contents

FIRST COMMUNITY BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	December 31, 2015				
	Carrying		Fair Value Measurements Using		
(Amounts in thousands)	Amount	Fair Value	Level 1	Level 2	Level 3
Assets					
Cash and cash equivalents	$ 51,787	$ 51,787	$ 51,787	$	$
Securities available for sale	366,173	366,173	54	366,119	
Securities held to maturity	72,541	72,490		72,490	
Loans held for investment, net of allowance	1,686,308	1,685,061		4,886	1,680,175
FDIC indemnification asset	20,844	10,753			10,753
Interest receivable	6,007	6,007		6,007	
Deferred compensation assets	3,464	3,464	3,464		
Liabilities					
Demand deposits	451,511	451,511		451,511	
Interest-bearing demand deposits	347,705	347,705		347,705	
Savings deposits	530,585	530,585		530,585	
Time deposits	543,458	541,059		541,059	
Securities sold under agreements to repurchase	138,614	&n			