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FRB RICHMOND

Board of Governors of the Federal Reserve System

Annual Report of Holding Companies—FR Y-6

Report at the close of business as of the end of fiscal year

This Report is required by law: Section 5(c)(1)(A) of the Bank Holding Company Act (12 U.S.C. § 1844(c)(1)(A)); sections 8(a) and 13(a) of the International Banking Act (12 U.S.C. §§ 3106(a) and 3108(a)); sections 11(a)(1), 25, and 25A of the Federal Reserve Act (12 U.S.C. §§ 248(a)(1), 602, and 611a); and sections 113, 165, 312, 618, and 809 of the Dodd-Frank Act (12 U.S.C. §§ 5361, 5365, 5412, 1850a(c)(1), and 5468(b)(1)). Return to the appropriate Federal Reserve Bank the original and the number of copies specified.

This report form is to be filed by all top-tier bank holding companies, top-tier savings and loan holding companies, and U.S. intermediate holding companies organized under U.S. law, and by any foreign banking organization that does not meet the requirements of and is not treated as a qualifying foreign banking organization under Section 211.23 of Regulation K (12 C.F.R. § 211.23). (See page one of the general instructions for more detail of who must file.) The Federal Reserve may not conduct or sponsor, and an organization (or a person) is not required to respond to, an information collection unless it displays a currently valid OMB control number.

NOTE: The *Annual Report of Holding Companies* must be signed by one director of the top-tier holding company. This individual should also be a senior official of the top-tier holding company. In the event that the top-tier holding company does not have an individual who is a senior official and is also a director, the chairman of the board must sign the report. If the holding company is an ESOP/ESOT formed as a corporation or is an LLC, see the General Instructions for the authorized individual who must sign the report.

I, James H. Sills, III
Name of the Holding Company Director and Official

President and CEO
Title of the Holding Company Director and Official

attest that the *Annual Report of Holding Companies* (including the supporting attachments) for this report date has been prepared in conformance with the instructions issued by the Federal Reserve System and are true and correct to the best of my knowledge and belief.

With respect to information regarding individuals contained in this report, the Reporter certifies that it has the authority to provide this information to the Federal Reserve. The Reporter also certifies that it has the authority, on behalf of each individual, to consent or object to public release of information regarding that individual. The Federal Reserve may assume, in the absence of a request for confidential treatment submitted in accordance with the Board's "Rules Regarding Availability of Information," 12 C.F.R. Part 261, that the Reporter and individual consent to public release of all details in the report concerning that individual.

James H. Sills, III
Signature of Holding Company Director and Official

March 26, 2018
Date of Signature

For holding companies not registered with the SEC–
Indicate status of Annual Report to Shareholders:

- [x] is included with the FR Y-6 report
- [ ] will be sent under separate cover
- [ ] is not prepared

For Federal Reserve Bank Use Only

RSSD ID 2807810
C.I. ______

Date of Report (top-tier holding company's fiscal year-end):

December 31, 2017
Month / Day / Year

No LEI
Reporter's Legal Entity Identifier (LEI) (20-Character LEI Code)

Reporter's Name, Street, and Mailing Address

M&F Bancorp, Inc.
Legal Title of Holding Company

2634 Durham Chapel Hill Blvd
(Mailing Address of the Holding Company) Street / P.O. Box

Durham	NC	27707
City	State	Zip Code

Physical Location (if different from mailing address)

Person to whom questions about this report should be directed:

Kathy E. Fox	VP/Controller
Name	Title

919-536-7547
Area Code / Phone Number / Extension

919-687-7807
Area Code / FAX Number

kathy.fox@mfbonline.com
E-mail Address

www.mfbonline.com
Address (URL) for the Holding Company's web page

Is confidential treatment requested for any portion of this report submission? .... 0=No 1=Yes **0**

In accordance with the General Instructions for this report (check only one),

1. a letter justifying this request is being provided along with the report .... [ ]
2. a letter justifying this request has been provided separately ... [ ]

NOTE: Information for which confidential treatment is being requested must be provided separately and labeled as "confidential."

Public reporting burden for this information collection is estimated to vary from 1.3 to 101 hours per response, with an average of 5.50 hours per response, including time to gather and maintain data in the required form and to review instructions and complete the information collection. Send comments regarding this burden estimate or any other aspect of this collection of information, including suggestions for reducing this burden to: Secretary, Board of Governors of the Federal Reserve System, 20th and C Streets, NW, Washington, DC 20551, and to the Office of Management and Budget, Paperwork Reduction Project (7100-0297), Washington, DC 20503.

For Use By Tiered Holding Companies

Top-tiered holding companies must list the names, mailing address, and physical locations of each of their subsidiary holding companies below.

Legal Title of Subsidiary Holding Company

(Mailing Address of the Subsidiary Holding Company) Street / P.O. Box

City State Zip Code

Physical Location (if different from mailing address)

Legal Title of Subsidiary Holding Company

(Mailing Address of the Subsidiary Holding Company) Street / P.O. Box

City State Zip Code

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City State Zip Code

Physical Location (if different from mailing address)

FORM FR Y-6
M&F BANCORP, INC
FISCAL YEAR ENDING DECEMBER 31, 2017

REPORT ITEM

1 The bank holding company prepares an annual report for its securities holders and is not registered with the SEC. The bank holding company deregisered from the SEC on 9/13/16. As specified by Federal Reserve Bank of Richmond, 2 copies are enclosed.

2A Organizational Chart

M&F BANCORP, INC
NO LEI
DURHAM, NC
INCORPORATED IN NORTH CAROLINA

100%
MECHANICS & FARMERS BANK
NO LEI
DURHAM, NC
INCORPORATED IN NORTH CAROLINA

2.B. Domestic branch listing submitted via email on March 5, 2018 to the Federal Reserve Bank.

Results: A list of branches for your depository institution: MECHANICS & FARMERS BANK (ID_RSSD: 332224).
This depository institution is held by M&F BANCORP, INC. (2807810) of DURHAM, NC.
The data are as of 12/31/2017. Data reflects information that was received and processed through 01/04/2018.

Reconciliation and Verification Steps
1. In the **Data Action** column of each branch row, enter one or more of the actions specified below
2. If required, enter the date in the **Effective Date** column

Actions
OK: If the branch information is correct, enter 'OK' in the **Data Action** column.
Change: If the branch information is incorrect or incomplete, revise the data, enter 'Change' in the **Data Action** column and the date when this information first became valid in the **Effective Date** column.
Close: If a branch listed was sold or closed, enter 'Close' in the **Data Action** column and the sale or closure date in the **Effective Date** column.
Delete: If a branch listed was never owned by this depository institution, enter 'Delete' in the **Data Action** column.
Add: If a reportable branch is missing, insert a row, add the branch data, and enter 'Add' in the **Data Action** column and the opening or acquisition date in the **Effective Date** column.

If printing this list, you may need to adjust your page setup in MS Excel. Try using landscape orientation, page scaling, and/or legal sized paper.

Submission Procedure
When you are finished, send a saved copy to your FRB contact. See the detailed instructions on this site for more information.
If you are e-mailing this to your FRB contact, put your institution name, city and state in the subject line of the e-mail.

Note:
To satisfy the **FR Y-10 reporting requirements**, you must also submit FR Y-10 Domestic Branch Schedules for each branch with a **Data Action** of Change, Close, Delete, or Add.
The FR Y-10 report may be submitted in a hardcopy format or via the FR Y-10 Online application - https://y10online.federalreserve.gov.

* FDIC UNINUM, Office Number, and ID_RSSD columns are for reference only. Verification of these values is not required.

Data Action	Effective Date	Branch Service Type	Branch ID_RSSD*	Popular Name	Street Address	City	State	Zip Code	County	Country	FDIC UNINUM*	Office Number*	Head Office	Head Office ID_RSSD*	Comments
OK		Full Service (Head Office)	332224	MECHANICS & FARMERS BANK	116 WEST PARRISH STREET	DURHAM	NC	27701	DURHAM	UNITED STATES	Not Required	Not Required	MECHANICS & FARMERS BANK	332224	
OK		Full Service	278425	CHARLOTTE BRANCH	101 BEATTIES FORD RD	CHARLOTTE	NC	28216	MECKLENBURG	UNITED STATES	Not Required	Not Required	MECHANICS & FARMERS BANK	332224	
OK		Full Service	577324	CHAPEL HILL BOULEVARD BRANCH	2705 CHAPEL HILL BLVD	DURHAM	NC	27707	DURHAM	UNITED STATES	Not Required	Not Required	MECHANICS & FARMERS BANK	332224	
OK		Full Service	474928	GREENSBORO BRANCH	100 SOUTH MURROW BOULEVARD	GREENSBORO	NC	27401	GUILFORD	UNITED STATES	Not Required	Not Required	MECHANICS & FARMERS BANK	332224	
OK		Full Service	394428	RALEIGH BRANCH	13 EAST HARGETT ST	RALEIGH	NC	27601	WAKE	UNITED STATES	Not Required	Not Required	MECHANICS & FARMERS BANK	332224	
OK		Full Service	455020	ROCK QUARRY ROAD BRANCH	1824 ROCK QUARRY RD	RALEIGH	NC	27610	WAKE	UNITED STATES	Not Required	Not Required	MECHANICS & FARMERS BANK	332224	
OK		Full Service	174424	WINSTON-SALEM BRANCH	770 MARTIN LUTHER KING JR DRIVE	WINSTON SALEM	NC	27101	FORSYTH	UNITED STATES	Not Required	Not Required	MECHANICS & FARMERS BANK	332224	

FORM FR Y-6
M&F BANCORP, INC
FISCAL YEAR ENDING DECEMBER 31, 2017

REPORT ITEM 3: SHAREHOLDERS
1.A.B.C. AND 2.A.B.C

CURRENT SHAREHOLDERS WITH OWNERSHIP, CONTROL OR HOLDING OF %5 OR MORE WITH POWER TO VOTE AS FISCAL YEAR ENDING 12/31/2017			SHAREHOLDER NOT LISTED IN 3.1.A THROUGH 3.1.C THAT HAD OWNERSHIP, CONTROL OR HOLDINGS OF %5 OR MORE WITH POWER TO VOTE DURING FISCAL YEAR ENDING 12/31/2017		
1.A NAMES & ADDRESSES CITY, STATE, COUNTRY	1.B COUNTRY OF CITIZENSHIP OR INCORPORATION	1.C NUMBER AND PERCENTAGE OF EACH CLASS OF VOTING SECURITIES	2.A NAMES & ADDRESSES CITY, STATE, COUNTRY	2.B COUNTRY OF CITIZENSHIP OR INCORPORATION	2.C NUMBER AND PERCENTAGE OF EACH CLASS OF VOTING SECURITIES
*JAMES E SANSOM CHAPEL HILL, NC, USA	USA	60,266 2.96%	N/A	N/A	N/A
*BERYL VIVIAN GILMORE BETHESDA, MD, USA	USA	60,266 2.96%			
*SARAH GENEVIEVE SANSOM STEWART NEW YORK, NY, USA	USA	60,266 2.96%			
NORTH CAROLINA MUTUAL LIFE INSURANCE COMPANY DURHAM, NC 27701	USA	186,040 9.16%			
JULIA W TAYLOR TRUST** PITTSBORO, NC, USA	USA	159,614 7.86%			

*The M&F Bancorp, Inc. stock pertaining to the Estate of the late Dr. Vivian M. Sansom which included 180,798 shares of common stock was settled in 2017. The new owners who are siblings, own 60,266 individually and 180,798 collectively.

**Common stock owned by the Julia W. Taylor Trust for which Ms. Taylor also serves as trustee and as such, has voting and investment power over these shares.

FORM FR Y-6
M&F BANCORP, INC
FISCAL YEAR ENDING DECEMBER 31, 2017

REPORT ITEM 4: INSIDERS
1,2,3 A.B.C. AND 4 A.B.C.

1 NAME &ADDRESS CITY, STATE, COUNTRY	2 PRINCIPAL OCCUPATION IF OTHER THAN WITH BANK HOLDING COMPANY	3.A. TITLE & POSITION WITH BANK HOLDING COMPANY	3.B TITLE & POSITION WITH SUBSIDIARIES (INCLUDE NAMES OF OTHER BUSINESSES	3.C TITLE & POSITION WITH OTHER BUSINESSES (INCLUDE NAMES OF OTHER BUSINESSES	4.A. PERCENTAGE OF VOTING SHARES IN BANK HOLDING COMPANY	4.B PERCENTAGE OF VOTING SHARES IN SUBSIDIARIES(INCLUDE NAMES)	4.C (INCLUDES PARTNERSHIPS) IF %25 OR MORE OF VOTING SECURITIES ARE HELD (LIST NAMES OF COMPANIES AND PERCENTAGE OF VOTING)
MICHAEL L LAWRENCE DURHAM, NC, USA	PRESIDENT/CEO, NORTH CAROLINA MUTUAL LIFE INS COMPANY	DIRECTOR	DIRECTOR	PRESIDENT/CEO, N C MUTUAL LIFE INS CO DIRECTOR NC STATE INVESTMENT FUND BOARD	Less than 1% of Company's o/s stock	NONE	LAWRENCE PROPERTIES LLC 100% ALSET LLC 100%
WILLIE T CLOSS, JR DURHAM, NC, USA	FINANCIAL CONSULTANT	DIRECTOR	DIRECTOR	DIRECTOR NORTH CAROLINA MUTUAL LIFE INS COMPANY	Less than 1% of Company's o/s stock	NONE	NONE
PATRICIA R HEALY RALEIGH, NC, USA	HYDE STREET HOLDINGS LLC	DIRECTOR	DIRECTOR	RREEF AMERICA III, DIRECTOR ULI AMERICAS, TRUSTEE/GOVERNOR, MIP, LLC, MEMBER MANAGER OCI, LLC MEMBER MANAGER HARGETT PLACE INC, PRINCIPAL	Less than 1% of Company's o/s stock	NONE	MIP, LLC, MEMBER MANAGER 90% OCI, LLC MEMBER MANAGER 50% HARGETT PLACE INC 100% PRINCIPAL HYDE STREET HOLDINGS, LLC 100% PRINCIPAL
JAMES H SPEED, JR DURHAM, NC, USA	RETIRED PRESIDENT/CEO NORTH CAROLINA MUTUAL LIFE INS COMPANY	DIRECTOR	DIRECTOR	BROWN CAPITAL MGT MUTUAL FUNDS HILLMAN CAPITAL MANAGEMENT INVESTMENT TRUST STARBOARD INVESTMENT TRUST INVESTORS TITLE COMPANY CAROLINA MOTOR CLUB, INC CENTAUR MUTUAL FUNDS WST INVESTMENT TRUST CHESAPEAKE INVESTMENT TRUST	Less than 1% of Company's o/s stock	NONE	SPEED FINANCIAL GROUP, INC 60% PRIDE INVESTMENTS LLC 5%
RAYMOND C. PIERCE DURHAM, NC, USA	PRESIDENT/CEO SOUTHERN EDUCATION FOUNDATION	DIRECTOR	DIRECTOR	PRESIDENT, R2P INNOVATIONS	Less than 1% of Company's o/s stock	NONE	R2P INNOVATIONS 10%
JAMES A STEWART DURHAM, NC, USA	BROKER/ CONSULTANT STEWART INVESTMENT PROPERTIES, INC	CHAIRMAN/ DIRECTOR	CHAIRMAN/ DIRECTOR	BROKER/ CONSULTANT STEWART INVESTMENT PROPERTIES, INC MAJAJA, INC PRESIDENT CLEARVIEW HOUSING CORP, PRESIDENT CLEARVIEW COMMERCIAL PROP, LLC, MANAGER CAMELLIA ASSOCIATES, LLC, MANAGER STEWART, MARTIN & MCCOY, LLC, MEMBER MANAGER	2.10%	NONE	STEWART INVESTMENT PROPERTIES, INC 100% MAJAJA, INC PRESIDENT 50% CLEARVIEW HOUSING CORP, PRESIDENT 45.07% CLEARVIEW COMMERCIAL PROPERTIES LLC, MEMBER/MANAGER 45.07% CAMELLIA ASSOCIATES, LLC, MEMBER/MANAGER 51% MATHISON ASSOCIATES, LP 25% STEWART MARTIN MCKOY LLC 33.33% MAJAJA SILER CITY LLC MANAGER 50%
CONNIE J. WHITE DURHAM, NC, USA	RETIRED MANAGEMENT CONSULTANT	DIRECTOR	VICE CHAIR/DIRECTOR	NONE	Less than 1% of Company's o/s stock	NONE	NONE
JAMES H. SILLS, III DURHAM, NC, USA	N/A	PRESIDENT/CEO/DIRECTOR	PRESIDENT/CEO/DIRECTOR M&F BANK	DIRECTOR, HS VERIFICATION, LLC	0	NONE	HOMELAND SECURITY VERIFICATION, LLC 100% HSP ASSOCIATES, LLC 100%
RANDALL C. HALL DURHAM, NC, USA	N/A	SVP/CFO	SVP/CFO/HR	N/A	Less than 1% of Company's o/s stock	NONE	NONE
VALERIE M. QUIETT DURHAM, NC, USA	N/A	SVP/ CHIEF LEGAL OFFICER/ CORP SEC/COMPLIANCE OFFICER	SVP/ CHIEF LEGAL OFFICER/ SECRETARY/COMPLIANCE OFFICER	N/A	0	NONE	NONE

M&F Bancorp, Inc.

2 0 1 7
ANNUAL REPORT

M&F Bancorp, Inc.

Chairman and President's Letter

In 2017, the Board of Directors and management team continued to improve all the operational areas of M&F Bancorp, Inc. (the "Company") and M&F Bank (the "Bank"). During the majority of the year, we experienced improvements in loan growth, fee income and controlling non-interest expenses. During the fourth quarter of 2017, the Memoranda of Understanding with our regulators, which had been in place since 2010, were removed – a sign of improved and stable financial performance. However, for the second time in our 110 year history, the Company realized a year-end loss. For 2017, the loss totaled $2.6 million. During the second half of 2017, we had two events that impacted our profitability. First, we had a large shared national credit, which declared bankruptcy and resulted in a charge-off in the amount of $1.5 million and largely resulted in the provision for loan losses of $1.2 million. Second, the enactment of the new federal tax law, signed in late December 2017, negatively affected the net loss for the Company for the fourth quarter and year by $2.1 million. Many banks large and small were hit with this one-time charge that comes from revaluing net deferred tax assets as a result of a decrease in federal tax rate to 21%. Beginning in 2018, income tax expense will be positively affected by the substantial reduction in the corporate tax rate. The law provides for the corporate tax rate to be reduced from 35% to 21%.

As noted above, two major events changed our balance sheet in 2017. We continued to achieved our major goal of maintaining a clean balance sheet to improve our overall asset quality ratios which are now more in-line with peer banks. We continued to maintain a reduced delinquency percentage below 2.0% for the entire year. Total loans were $153.6 million as of December 2017 versus $150.3 million in 2016. Total assets as of December 2017 were $255.1 million versus $256.4 million in 2016. We finished the year with $20.2 million in capital versus $22.3 million in 2016. During the third quarter, we received our fifth Bank Enterprise Award from the U.S. Treasury in the amount of $227 thousand, which is a testament to our commitment to serve low/moderate income communities within our footprint. We believe that the Bank is sound, healthy and continues to be well-capitalized.

During 2017, one of the Bank's major goals was to continue to diversify our loan portfolio. Our Sales Team made significant strides in making loans to small and medium sized businesses of all types. This helps the Bank spread the risk and better align with the growth in the markets served. As you may be aware, the banking industry is now more technology focused than ever before. In response to this technology focus, we launched a totally new website, mobile app and tablet platform in 2017. Additionally, in an effort to connect with the communities that the Bank serves, we hired new associates in various sales roles, engaged all of our City Advisory Boards and started a statewide Millennial Advisory Board to help us improve our connection with the millennial population. Going forward, we intend to offer new loan and deposit products that leverage our technology capabilities and attract new customers to the Bank.

M&F Bank remains committed to our mission as a true community bank, which includes providing high quality banking services to the entire community and reinvesting into our local economies. As always, we thank you for your trust and confidence, and we hope we can count on your continued support as we move into the promising year ahead.

In closing, we appreciate all shareholder referrals for commercial loans, mortgage loans, wealth management and deposit accounts. Thank you for your continued support.

Sincerely,

James A. Stewart	James H. Sills, III
Chairman of the Board	President and Chief Executive Officer

M&F BANCORP, INC. AND SUBSIDIARY

CONSOLIDATED BALANCE SHEETS

(Dollars in thousands except for share data)		December 31, 2017		December 31, 2016
ASSETS				
Cash and cash equivalents:				
Cash and due from banks	$	2,255	$	2,053
Interest-bearing cash		21,762		17,619
Total cash and cash equivalents		24,017		19,672
Interest-bearing time deposits		3,210		1,235
Investment securities available-for-sale, at fair value		57,488		65,004
Other invested assets		256		298
Loans held for sale		-		975
Loans, net of unearned income and deferred fees		153,565		149,339
Allowance for loan losses ("ALLL")		(1,885)		(2,417)
Loans, net		151,680		146,922
Interest receivable		651		629
Bank premises and equipment, net		2,437		5,060
Cash surrender value of bank-owned life insurance		8,733		8,480
OREO		104		367
Deferred tax assets and taxes receivable, net		4,875		6,756
Other assets		1,623		997
TOTAL ASSETS	$	255,074	$	256,395
LIABILITIES AND STOCKHOLDERS' EQUITY				
Deposits:				
Interest-bearing deposits	$	183,128	$	181,830
Noninterest-bearing deposits		47,315		47,586
Total deposits		230,443		229,416
Other borrowings		769		862
Other liabilities		3,681		3,794
Total liabilities		234,893		234,072
COMMITMENTS AND CONTINGENCIES (Notes 9, 10, 11, 15 and 17)				
Stockholders' equity:				
Series C Junior Participating Preferred Stock- $0.01 par value, 21,000 shares authorized, no shares issued or outstanding		-		-
Common stock, no par value, 10,000,000 shares authorized; 2,031,337 shares issued and outstanding		8,732		8,732
Retained earnings		13,894		16,072
Accumulated other comprehensive loss		(2,445)		(2,481)
Total stockholders' equity		20,181		22,323
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$	255,074	$	256,395

See notes to consolidated financial statements.

M&F BANCORP, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS

(Dollars in thousands)	For the Years Ended December 31, 2017	2016
Net loss	$ (2,591)	$ (3,938)
Other comprehensive income (loss):		
Investment securities:		
Unrealized holding gains (losses) on investment securities available-for-sale	329	(890)
Tax effect	(118)	318
Reclassification of accumulated comprehensive loss due to tax rate change	(176)	-
Reclassification adjustments for net realized gains	-	(241)
Tax effect	-	86
Net of tax amount	35	(727)
Defined benefit pension plans:		
Net actuarial gains	373	623
Tax effect	(135)	(243)
Reclassification of accumulated comprehensive loss due to tax rate change	(237)	-
Prior service cost	-	-
Tax effect	-	-
Net of tax amount	1	380
Other comprehensive income (loss), net of tax	36	(347)
Comprehensive loss	$ (2,555)	$ (4,285)

See notes to consolidated financial statements

M&F BANCORP, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Dollars in thousands)	For the Years Ended December 31, 2017	2016
Cash flows from operating activities:		
Net loss	$ (2,591)	$ (3,938)
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	1,171	5,181
Depreciation and amortization	405	429
Amortization of discounts/premiums on investment securities available-for-sale, net	381	490
Net gains on sales of investment securities available-for-sale	-	(241)
Net loss on sales of interest-bearing time deposits	-	6
Increase in cash surrender value of bank-owned life insurance	(253)	(252)
Loss on disposal of fixed assets	6	-
Net losses on sales of OREO	15	328
Contribution of OREO	-	10
Proceeds from sales of loans held for sale	1,005	5,797
Net gain on loan held for sale	(30)	-
Writedowns of OREO	100	645
Write-off prepaid rent	46	-
Write-off prepaid lease commissions	78	-
Net changes in:		
Accrued interest receivable and other assets	1,256	(1,966)
Other liabilities	(207)	(1,971)
Net cash provided by operating activities	1,382	4,518
Cash flows from investing activities:		
Activity in available for sale securities:		
Sales	-	27,901
Maturities and calls	1,000	36,960
Principal collections	6,464	9,131
Purchases	-	(60,435)
Proceeds from sales of interest-bearing time deposits	-	5,424
Purchases of interest bearing time deposits	(1,975)	-
FHLB stock purchases	(591)	-
FHLB stock redemptions	633	-
Net (increase) decrease in loans	(6,133)	2,352
Purchases of bank premises and equipment	(906)	(1,077)
Proceeds from sale of bank premises and equipment	3,185	-
Proceeds from sales of OREO	352	1,601
Net cash provided by investing activities	2,029	21,857
Cash flows from financing activities:		
Net increase (decrease) in deposits	1,027	(25,284)
Proceeds from other borrowings	9,097	144
Repayments of other borrowings	(9,190)	(220)
Redemption of Series A preferred stock, net of issuance costs	-	(9,388)
Cash dividends	-	(228)
Net cash provided by (used in) financing activities	934	(34,976)
Net increase (decrease) in cash and cash equivalents	4,345	(8,601)
Cash and cash equivalents as of the beginning of the period	19,672	28,273
Cash and cash equivalents as of the end of the period	$ 24,017	$ 19,672

See notes to consolidated financial statements.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of Operations - M&F Bancorp, Inc. (the "Company") is a bank holding company, and the parent company of Mechanics and Farmers Bank (the "Bank"), a state chartered commercial bank incorporated in North Carolina ("NC") in 1907, which began operations in 1908. The Bank has seven branches in NC: two in Durham, two in Raleigh, and one each in Charlotte, Greensboro and Winston-Salem. The Company, headquartered in Durham, operates as a single business segment and offers a wide variety of consumer and commercial banking services and products almost exclusively in NC.

Basis of Presentation - The Consolidated Financial Statements include the accounts and transactions of the Company and the Bank, the wholly owned subsidiary. All significant inter-company accounts and transactions have been eliminated in consolidation.

Cash and Cash Equivalents - The cash and cash equivalents are comprised of highly liquid short-term investments that are carried at cost, which approximates market value, and cash held at the Federal Reserve Bank of Richmond ("FRB"). The Board of Governors of the Federal Reserve (the "Federal Reserve") and banking laws in NC require banks to maintain average balances in relation to specific percentages of their customers' deposits as a reserve. As of December 31, 2017 and 2016, the Bank, held deposits as shown:

(Dollars in thousands)	Federal Reserve Required Average	Excess	Bank Federal Funds Sold	Core Deposits	Total
December 31, 2017	$ 1,864	$ 19,347	$ -	$ 2,806	$ 24,017
December 31, 2016	$ 1,848	$ 15,218	$ -	$ 2,606	$ 19,672

As of December 31, 2017 and 2016, the Bank did not hold any deposits at other financial institutions in excess of the federally insured balances.

Interest-bearing Time Deposits in Banks – Interest-bearing time deposits in banks mature within five years and are carried at cost.

Investment Securities - Debt securities that the Company has the positive intent and ability to hold to maturity are classified as "held to maturity securities" and reported at amortized cost. Debt and equity securities that are bought and held principally for the purpose of selling in the near term are classified as "trading securities" and reported at fair value, with unrealized gains and losses included in consolidated earnings. Debt securities not classified as either held to maturity securities or trading securities, and equity securities not classified as trading securities, are classified as "available-for-sale securities" and reported at fair value, with unrealized gains and losses excluded from consolidated earnings and reported as a separate component of consolidated stockholders' equity and as an item of other comprehensive income. The unrealized gain or loss of a security is identified and removed from other comprehensive income when a security is sold, matured, or called. The initial classification of securities is determined at the date of purchase. Gains and losses on sales of investment securities, computed based on specific identification of the adjusted cost of each security, are included in noninterest income at the time of sale. Premiums and discounts on debt securities are recognized in interest income using the interest method over the period to maturity, or when the debt securities are called.

Declines in the fair value of individual held to maturity and available-for-sale securities below their costs that are other-than-temporary result in write-downs of the individual securities to their respective fair value. There were no credit write-downs in consolidated earnings as realized losses. Transfers of securities between classifications, of which there were none in 2017 or 2016, are accounted for at fair value. No securities were classified as trading or held to maturity as of December 31, 2017 and 2016.

Other Invested Assets - Other invested assets are investments in Federal Home Loan Bank of Atlanta (the "FHLB") stock carried at historical cost, as adjusted for any other-than-temporary impairment loss. As of December 31, 2017 and 2016, the Company's investments in FHLB stock were $0.3 million.

Loans - Loans are stated at the amount of unpaid principal, net of deferred loan origination fees and costs. Loans (net) are reduced by the ALLL. Nonrefundable loan fees associated with the origination or acquisition of loans are deferred and recognized as an adjustment of the loan yield over the life of the loan using the effective interest method. Interest on loans is accrued on the daily balances of unpaid principal outstanding. Interest income is accrued and credited to income only if deemed collectible. Other loan fees and charges, representing service costs for the prepayment of loans, for delinquent payments, or for miscellaneous loan services, are recorded in income when collected.

Non-Performing Loans and Leases - Generally, all classes of loans and leases are placed on non-accrual status upon becoming contractually past due 90 days or more as to principal or interest (unless loans are adequately secured by collateral, are in the process of collection, and are reasonably expected to result in repayment), or where substantial doubt about full repayment of principal or interest is evident.

When a loan or lease is placed on non-accrual status, regardless of class, the accrued and unpaid interest receivable is reversed and the loan or lease is accounted for on the cash or cost recovery method until qualifying for return to accrual status. All payments received on non-accrual loans and leases are applied against the principal balance of the loan or lease. Loans may be returned to accrual status when all principal and interest amounts contractually due (including any arrearages) are reasonably assured of repayment within a reasonable period, the borrower has demonstrated payment performance for a minimum of six months in accordance with the original or revised contractual terms of the loan, and when doubt about repayment is resolved.

assessments. The methodologies for measuring the appropriate level of the ALLL include the combination of a quantitative historical loss history by loan type and a qualitative analysis for loans not classified as impaired or TDRs, and a specific allowance method for impaired and TDR loans. The qualitative analysis is patterned after the guidelines provided under the Securities Exchange Commission ("SEC") Staff Accounting Bulletin 102 and the Federal Financial Institutions Examination Council ("FFIEC") Interagency Policy Statement on the Allowance for Loan and Lease Losses and include the following:

- Changes in lending policies and procedures, including underwriting standards and collection, charge-off, and recovery practices;
- Changes in national economic and business conditions and developments and the effect of unemployment on African Americans, who are the majority of our customers;
- Changes in the nature and volume of the loan portfolio;
- Changes in the experience, ability, and depth of lending management and staff;
- Changes in trends of the volume and severity of past due and classified loans; and changes in trends in the volume of non-accrual loans, troubled debt restructurings and classified loans;
- Changes in the quality of the loan review system and the degree of oversight by the Bank's Board of Directors;
- The existence and effect of any concentrations of credit, and changes in the level of such concentrations; and
- The effect of external factors such as competition and legal and regulatory requirements.

Management has developed, from historical loan and economic information, quantitative drivers for certain qualitative factors. Management has identified which factors, by nature, are subjective, such as lending policies, competition, and regulatory requirements. The quantitative drivers, to which different weights are assigned based on management's judgment, are reviewed and updated quarterly. The quantitative loss history was based on a five-year rolling look back period at December 31, 2017 and 2016.

A specific ALLL is established for loans identified as impaired or TDRs, based on significant conditions or circumstances related to the specific credits. The specific allowance amounts are determined by a method prescribed by Accounting Standards Codification ("ASC") 310, *Receivables.* Loans identified as impaired are accounted for in accordance with one of three valuations: (i) the present value of future cash flows discounted at the loan's effective interest rate; (ii) the loan's observable market price, or (iii) the fair value of the collateral, if the loan is collateral dependent, less estimated liquidation costs. A loan is considered impaired when it is probable that not all amounts due (principal and interest) will be collectible according to the original contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. The significance of payment delays and payment shortfalls are considered on a loan-by-loan basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed.

For commercial business, faith-based non-profit, real estate and certain consumer loans, the measurement of loan impairment is based on the present value of the expected future cash flows, discounted at the loan's effective interest rate, or on the fair value of the loan's collateral if the loan is collateral dependent. Most consumer loans are smaller balance and homogeneous, and are evaluated for impairment on a collective basis, applying the quantitative loss history and the qualitative factors. Impairment losses are included in the ALLL through a charge to the provision for loan losses.

The Company uses several credit quality indicators to manage credit risk in an ongoing manner. The Company's risk rating system was developed to aid in the risk management process by grouping credits with similar risk profiles into pass, special mention, substandard or doubtful categories. Credit risk ratings are applied individually to all classes of loans and leases. Internal credit reviews and external contracted credit review examinations are used to determine and validate loan risk grades. The credit review system takes into consideration factors such as: borrower's background and experience; historical and current financial condition; credit history and payment performance; economic conditions and their impact on various industries; type, market value and volatility of the market value of collateral; lien position; and the financial strength of guarantors.

The process of assessing the adequacy of the ALLL is necessarily subjective. Further, and particularly in periods of economic downturns, it is reasonably possible that future credit losses may exceed historical loss levels and may also exceed management's current estimates of incurred credit losses inherent within the loan portfolio. As such, there can be no assurance that future loan charge-offs will not exceed management's current estimate of what constitutes a reasonable ALLL.

The Company and the Bank are subject to periodic examination by their federal and state regulators, and may be required by such regulators to recognize additions to the allowance for loan losses based on their assessment of credit information available to them at the time of their examinations.

Reserve for Unfunded Commitments - The Unfunded Reserve is a component of other liabilities and represents the estimate for probable credit losses inherent in unfunded commitments to extend credit. Unfunded commitments to extend credit include unfunded loans with available balances, new commitments to lend that are not yet funded, and standby and commercial letters of credit. The process used to determine the Unfunded Reserve is consistent with the process for determining the ALLL, as adjusted for estimated funding probabilities and historical five-year rolling look back quantitative loan loss factor at December 31, 2017 and 2016. The level of the Unfunded Reserve is adjusted by recording an expense or recovery in other noninterest expense. The balances of $48 thousand and $23 thousand for December 31, 2017 and 2016, respectively, were reflected in other liabilities on the Consolidated Balance Sheet.

Bank Premises and Equipment, Net - Premises and equipment are stated at cost less accumulated depreciation and amortization. For financial reporting purposes, depreciation and amortization are computed by the straight-line method and are charged to operations over the between market participants on the measurement date. GAAP establishes a fair value hierarchy that prioritizes the information used to develop those assumptions. The fair value hierarchy gives the highest priority to quoted prices in active markets (observable inputs) and the lowest priority to the Company's assumptions (unobservable inputs). GAAP requires fair value measurements to be separately disclosed by level within the fair value hierarchy. For assets and liabilities recorded at fair value, the Company maximizes the use of observable inputs and minimizes the use of unobservable inputs when developing fair value measurements.

The Company utilizes fair value measurements to record fair value adjustments to certain assets and liabilities and to determine fair value disclosures. Available-for-sale investment securities are recorded at fair value on a recurring basis. Additionally, the Company may be required to record at fair value other assets on a nonrecurring basis, such as loans held for sale, loans held for investment and certain other assets.

Under GAAP, the Company groups assets and liabilities at fair value in three levels, based on the markets in which the assets and liabilities are traded and the reliability of the assumptions used to determine fair value. The Company did not have any changes in leveling inputs in 2017.

These levels are:

Level 1 — Valuations for assets and liabilities traded in active exchange markets, such as the New York Stock Exchange.

Level 2 — Valuations are obtained from readily available pricing sources via independent providers for market transactions involving similar assets or liabilities. The Company's principal market for these securities is the secondary institutional markets and valuations are based on observable market data in those markets. Level 2 securities include U.S. Government agency securities ("U.S. Agencies"), U.S. Government sponsored residential mortgage backed securities ("MSB") and State and Municipal Bonds ("Municipals").

Level 3 — Valuations for assets and liabilities that are derived from other valuation methodologies, including option pricing models, discounted cash flow models and similar techniques, and not based on market exchange, dealer, or broker traded transactions. Level 3 valuations incorporate certain assumptions and projections in determining the fair value assigned to such assets.

Use of Estimates - The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Material estimates that are susceptible to change in the near term relate to the determination of the ALLL and the provision for loan losses, the evaluation of other-than-temporary impairment of investment securities, accounting for deferred tax assets and related valuation allowances, the determination of the fair values of investment securities and other accounting for incentive compensation, and post-retirement benefits. Actual results could differ from those estimates.

Significant Group Concentrations - Most of the Bank's activities are with customers located within the state of NC. The Bank does have concentrations with respect to loans to and deposits from faith-based non-profit organizations as outlined in Note 6 to the Consolidated Financial Statements.

New Accounting Pronouncements –

In May 2014, the FASB issued guidance to change the recognition of revenue from contracts with customers. The core principle of the new guidance is that an entity should recognize revenue to reflect the transfer of goods and services to customers in an amount equal to the consideration the entity receives or expects to receive. The guidance will be effective for the Company for reporting periods beginning after December 15, 2017.

The Company will apply the guidance using a modified retrospective approach. The Company's revenue is comprised of net interest income and noninterest income. The scope of the guidance explicitly excludes net interest income as well as many other revenues for financial assets and liabilities including loans, leases, securities, and derivatives. Accordingly, the majority of our revenues will not be affected. The Company has performed an assessment of its revenue contracts related to revenue streams that are within the scope of the standard. Our accounting policies will not change materially since the principles of revenue recognition from the ASU are largely consistent with existing guidance and current practices applied by our businesses. We have not identified material changes to the timing or amount of revenue recognition. Based on the updated guidance, we do anticipate changes in our disclosures associated with our revenues. We will provide qualitative disclosures of our performance obligations related to our revenue recognition, and we continue to evaluate disaggregation for significant categories of revenue in the scope of the guidance.

In August 2014, the FASB issued guidance that is intended to define management's responsibility to evaluate whether there is substantial doubt about an organization's ability to continue as a going concern and to provide related footnote disclosures. In connection with preparing financial statements, management evaluates whether there are conditions or events, considered in the aggregate, that raise substantial doubt about the organization's ability to continue as a going concern within one year after the date that the financial statements are issued. The amendments were effective for the Company for annual period ending after December 15, 2016, and for annual periods and interim periods thereafter. These amendments did not have a material effect on the Company's financial statements.

In August 2015, the FASB deferred the effective date of ASU 2014-09, "Revenue from Contracts with Customers". As a result of the deferral, the guidance in ASU 2014-09 will be effective for the Company for reporting periods beginning after December 15, 2017. The Company will apply the guidance using a modified retrospective approach. The Company does not expect these amendments to have a material effect on its financial statements.

In January 2016, the FASB amended the "Financial Instruments" topic of the ASC to address certain aspects of recognition, measurement, In March 2017, the FASB amended the requirements in the Compensation—Retirement Benefits Topic of the ASC related to the income statement presentation of the components of net periodic benefit cost for an entity's sponsored defined benefit pension and other postretirement plans. The amendments will be effective for the Company for interim and annual periods beginning after December 15, 2017. Early adoption is permitted. The Company does not expect these amendments to have a material effect on its financial statements.

In March 2017, the FASB amended the requirements in the Receivables—Nonrefundable Fees and Other Costs Topic of the ASC related to the amortization period for certain purchased callable debt securities held at a premium. The amendments shorten the amortization period for the premium to the earliest call date. The amendments will be effective for the Company for interim and annual periods beginning after December 15, 2018. Early adoption is permitted. The Company does not expect these amendments to have a material effect on its financial statements.

In February 2018, the FASB Issued (ASU 2018-02), Income Statement (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income, which requires Companies to reclassify the stranded effects in other comprehensive income to retained earnings as a result of the change in the tax rates under the Tax Cuts and Jobs Act. The Company has opted to early adopt this pronouncement by retrospective application to each period (or periods) in which the effect of the change in the tax rate under the Tax Cuts and Jobs Act is recognized. The impact of the reclassification from other comprehensive income to retained earnings is $0.4 million.

Other accounting standards that have been issued or proposed by the FASB or other standards-setting bodies are not expected to have a material impact on the Company's financial position, results of operations or cash flows.

2. INVESTMENT SECURITIES

The main objectives of the Company's investment strategy are to provide a source of liquidity while managing our interest rate risk, and to generate an adequate level of interest income without taking undue risks. The Company's investment policy permits investments in various types of securities, certificates of deposit and federal funds sold in compliance with various restrictions in the policy. As of December 31, 2017 and 2016, all investment securities were classified as available-for-sale.

The Company's available-for-sale securities totaled $57.5 million and $65.0 million as of December 31, 2017 and 2016, respectively. In the normal course of business, the Company pledges securities to the FRB and to public housing authorities in NC and the NC Department of State Treasurer ("State Treasurer") as collateral for public deposits. The following table shows the amounts pledged:

(Dollars in thousands)	December 31, 2017	December 31, 2016
Pledged to FRB	$ 1,288	$ 1,298
Pledged to public housing authorities	2,010	4,163
Pledged to the State Treasurer	18,380	19,494

The Company's investment portfolio consists of the following securities:

- U.S. Government agency securities ("U.S. Agencies")
- U.S. Government sponsored residential mortgage backed securities ("MBS"), and
- Municipal securities ("Municipals")

The amortized cost, gross unrealized gains and losses and fair values of investment securities at December 31, 2017 and 2016 were:

(Dollars in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
December 31, 2017				
U.S. Agencies	$ 18,313	$ -	$ (480)	$ 17,833
MBS				
Residential	38,708	-	(830)	37,878
Municipals	1,821	-	(44)	1,777
Total	$ 58,842	$ -	$ (1,354)	$ 57,488
December 31, 2016				
U.S. Agencies	$ 19,309	$ -	$ (540)	$ 18,769
MBS				
Residential	45,525	-	(1,083)	44,442
Municipals	1,853	-	(60)	1,793
Total	$ 66,687	$ -	$ (1,683)	$ 65,004

Sales of securities available-for-sale for the year ended December 31, 2017 and 2016 resulted in aggregate gross realized gains of $0 and $0.4

As of December 31, 2017 and 2016, the fair value of securities with gross unrealized losses by length of time that the individual securities have been in an unrealized loss position is as follows:

(Dollars in thousands)	Less Than 12 Months		12 Months or Greater		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
December 31, 2017						
U.S. Agencies	$ 17,833	$ (480)	$ -	$ -	$ 17,833	$ (480)
MBS						
Residential	1,330	(12)	36,548	(818)	37,878	(830)
Municipals	1,217	(44)	-	-	1,217	(44)
Total	$ 20,380	$ (536)	$ 36,548	$ (818)	$ 56,928	$ (1,354)

(Dollars in thousands)	Less Than 12 Months		12 Months or Greater		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
December 31, 2016						
U.S. Agencies	$ 18,769	$ (540)	$ -	$ -	$ 18,769	$ (540)
MBS						
Residential	38,971	(941)	5,471	(142)	44,442	(1,083)
Municipals	1,793	(60)	-	-	1,793	(60)
Total	$ 59,533	$ (1,541)	$ 5,471	$ (142)	$ 65,004	$ (1,683)

All securities owned as of December 31, 2017 and 2016 were investment grade. The Company evaluates securities for other-than-temporary impairment, at least on a quarterly basis. Consideration is given to the financial condition and near-term prospects of the issuer, the length of time and extent to which the fair value has been less than cost, and our intent and ability to retain our investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value. As of December 31, 2017 and 2016, the Company held 53 and 55 investment positions, respectively, with unrealized losses of $1.4 million and $1.7 million, respectively. These investments were in U.S. Agencies, MBS and municipals. In analyzing an issuer's financial condition, management considers whether the securities are issued by the federal government or its agencies, whether downgrades by bond rating agencies have occurred, and industry analysts' reports. Management has determined that all declines in the market value of available-for-sale securities are not other-than-temporary, and will not be likely required to sell.

3. FHLB STOCK

To be a member of the FHLB System, the Bank is required to maintain an investment in capital stock of the FHLB in an amount equal to 0.09% of the Bank's total assets of the prior year (up to a maximum of $15.0 million), plus 4.25% of its outstanding FHLB advances at December 31, 2017 and 2016. The carrying value of FHLB stock, which is included in other invested assets, as of December 31, 2017 and 2016 was $0.3 million. No ready market exists for the FHLB stock, and it has no quoted market value, however, management believes that the cost approximates the market value as of December 31, 2017 and 2016. Management has reviewed its investment in FHLB stock for impairment and does not believe it is impaired as of December 31, 2017 or 2016. The FHLB of Atlanta in which the Company owns stock has been profitable in each of the years ended December 31, 2017 and 2016.

4. RECONCILIATIONS OF BASIC AND DILUTED EARNINGS PER SHARE ("EPS")

Basic EPS is computed by dividing net income after preferred stock dividends by the weighted average number shares of common stock outstanding for the period. Basic EPS excludes the dilutive effect that could occur if any options or warrants to purchase shares of common stock were exercised. Diluted EPS is computed by dividing net income by the sum of the weighted average number of shares of common stock outstanding for the period plus the number of additional shares of common stock that would have been outstanding if the potentially dilutive common shares had been issued. There are no stock options or warrants outstanding for any of the periods being reported.

5. ACCUMULATED OTHER COMPREHENSIVE LOSS

Comprehensive loss includes net income (loss) and all other changes to the Company's equity, with the exception of transactions with stockholders. The Company's other comprehensive loss and accumulated other comprehensive loss are comprised of unrealized gains and losses on certain

For all classes of commercial loans, a quarterly evaluation of specific individual borrowers is performed to identify impaired loans. The identification of specific borrowers for review is based on a review of non-accrual loans as well as those loans specifically identified by management as exhibiting above average levels of risk through the loan classification process. The ALLL attributed to impaired loans and TDRs considers all available evidence based on significant conditions or circumstances related to the specific credits. The specific allowance amounts are determined by a method prescribed by ASC 310. The loans identified as impaired and TDRs are accounted for in accordance with one of three valuations: (i) the present value of future cash flows discounted at the loan's effective interest rate; (ii) the loan's observable market price, or (iii) the fair value of the collateral, if the loan is collateral dependent, less estimated liquidation costs. Factors considered by management in determining impairment include payment status, collateral value, alternate use of special purpose real estate which could adversely impact resale, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. The significance of payment delays and payment shortfalls are considered on a loan-by-loan basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed. Interest payments made on impaired loans are typically applied to principal unless collectability of the principal amount is reasonably assured, in which case interest income may be accrued or recognized on a cash basis.

Most consumer loans are evaluated for impairment on a collective basis, because these loans are for smaller balances and are homogeneous. Any loans, including commercial loans, not specifically identified as impaired or TDRs, are collectively evaluated and segmented by loan type, applying two factors: the quantitative loss history by loan type for the previous five year periods at December 31, 2017 and 2016 compared to average loans outstanding for the same period (the "quantitative factor"), and a qualitative factor that is comprised of quantitatively-driven calculations based on historical data, and subjective factors (the "qualitative factors"). The quantitative portion of the ALLL is adjusted for qualitative factors to account for model imprecision and to incorporate the range of probable outcomes inherent in the estimates used for the allowance.

The quantitative factor by loan type is applied against the unimpaired loan balances and smaller-balance homogenous impaired loans not in the process of foreclosure for which there is no specific reserve to determine the quantitative reserve. The qualitative factors, including (i) policy underwriting, charge-off and collection, (ii) national and local economic conditions, (iii) nature and volume of the portfolio, (iv) experience, ability, and depth of lending team, (v) trends of past due, classified loans, and restructurings, (vi) quality of loan review and board oversight, (vii) existence, levels, and effect of loan concentrations and (viii) effects of external factors such as competition and regulatory oversight, are adjusted quarterly based on historical information for any quantifiable factors and qualitative judgments for subjective factors (those considered subjective are policy, underwriting, experience, ability and depth of lending team, quality of loan review and board oversight, and effects of external factors), and applied in total to each loan balance by loan type. The Company continues to enhance its modeling of the portfolio and underlying risk factors through quarterly analytical reviews with the goal of ensuring it captures all pertinent factors contributing to risk of loss inherent in the loan portfolio. Under ASC 310, the non-homogenous impaired loans, homogenous small balance real estate secured loans in process of foreclosure for which the value is less than the loan principal balance, and TDRs, are reviewed individually for impairment.

The process of assessing the adequacy of the ALLL is inherently subjective. Further, and particularly in terms of economic downturns, it is reasonably possible that future credit losses may exceed historical loss levels and may also exceed management's current estimates of incurred credit losses inherent within the loan portfolio. As such, there can be no assurance that future loan charge-offs will not exceed management's current estimate of what constitutes a reasonable allowance for loan losses.

The Company and the Bank are subject to periodic examination by their federal and state banking regulators, and may be required by their regulators to recognize additions to the allowance for loan losses based on their assessment of credit information available to them at the time of their examinations.

Loans are generally placed on non-accrual status when the scheduled payments reach 90 days past due. Loans are charged-off, with Board of Directors' approval, when the Chief Credit Officer and his staff determine that all reasonable means of collection of the outstanding balances, except foreclosure, have been exhausted. The Company continues its collection efforts subsequent to charge-off, which historically has resulted in some recoveries each year.

	December 31, 2017						
(Dollars in thousands)	**Commercial**	**Commercial Real Estate**	**Faith Based Non-Profit**	**Residential Real Estate**	**Consumer**	**Other Loans**	**Total**
ALLL:							
Ending ALLL balance attributable to loans:							
Individually evaluated for impairment	$ -	$ 66	$ 153	$ 12	$ -	$ -	$ 231
Collectively evaluated for impairment	28	845	628	115	30	8	1,654
Total ending ALLL balance	$ 28	$ 911	$ 781	$ 127	$ 30	$ 8	$ 1,885
Loans:							
Loans individually evaluated for impairment	$ 1,024	$ 4,495	$ 8,776	$ 480	$ -	$ -	$ 14,775
Loans collectively evaluated for impairment	11,104	51,832	64,229	10,515	1,057	53	138,790
Total ending loans balance	$ 12,128	$ 56,327	$ 73,005	$ 10,995	$ 1,057	$ 53	$ 153,565

	December 31, 2016						
(Dollars in thousands)	**Commercial**	**Commercial Real Estate**	**Faith Based Non-Profit**	**Residential Real Estate**	**Consumer**	**Other Loans**	**Total**
ALLL:							
Ending ALLL balance attributable to loans:							
Individually evaluated for impairment	$ -	$ 178	$ 312	$ 2	$ -	$ -	$ 492
Collectively evaluated for impairment	92	798	849	139	34	13	1,925
Total ending ALLL balance	$ 92	$ 976	$ 1,161	$ 141	$ 34	$ 13	$ 2,417
Loans:							
Loans individually evaluated for impairment	$ -	$ 4,868	$ 10,305	$ 462	$ -	$ -	$ 15,635
Loans collectively evaluated for impairment	13,087	42,378	67,634	9,536	1,017	52	133,704
Total ending loans balance	$ 13,087	$ 47,246	$ 77,939	$ 9,998	$ 1,017	$ 52	$ 149,339

The following tables show impaired loans with and without valuation allowances as of December 31, 2017 and 2016:

	December 31, 2017				
(Dollars in thousands)	Unpaid Principal Balance	Recorded Investment	ALLL Allocated	Interest Earned For the Year	Average Recorded Investment
With no related allowance recorded:					
Commercial	$ 1,024	$ 1,024	$ -	$ 20	$ 128
Commercial real estate:					
Other	-	-	-	15	190
Faith based non-profit:					
Owner occupied	2,391	2,394	-	138	1,691
Residential real estate:					
First mortgage	114	115	-	16	130
Multifamily	-	-	-	12	56
Home equity	229	233	-	11	204
Impaired loans with no allowance recorded	$ 3,758	$ 3,766	$ -	$ 212	$ 2,399
With an allowance recorded:					
Commercial	$ -	$ -	$ -	$ 109	$ 646
Commercial real estate:					
Owner occupied	4,495	4,502	66	183	4,540
Other	-	-	-	-	27
Faith based non-profit:					
Owner occupied	6,386	6,404	153	282	7,558
Residential real estate:					
First mortgage	-	-	-	3	53
Home equity	138	138	12	-	86
Impaired loans with allowance recorded	$ 11,019	$ 11,044	$ 231	$ 577	$ 12,910
Total impaired loans	$ 14,777	$ 14,810	$ 231	$ 789	$ 15,309

The following table presents details of TDR a loan that was restructured during the year ended December 31, 2016:

(Dollars in thousands)	Number of loans	TDR Modifications For the Year Ended December 31, 2016 Pre-modification Outstanding Recorded Investment	Post-modification Outstanding Recorded Investment
Below market interest rates:			
Residential real estate:			
Home equity	1	$ 182	$ 176
Total	1	$ 182	$ 176

The were no loans modified as a TDR with a payment default occurring within 12 months of the restructure date, during the years ended December 31, 2017 or 2016.

The following tables present the recorded investment in non-accrual and loans past due over 90 days still on accrual by class of loans as of December 31, 2017 and 2016:

December 31, 2017 *(Dollars in thousands)*	Non-accrual	Number	90 Days or More Past Due Still Accruing	Number
Commercial	$ 1,024	1	$ -	-
Commercial real estate:				
Other	-	1	-	-
Faith-based non-profit:				
Owner occupied	1,099	1	-	-
Residential real estate:				
First mortgage	13	1	-	-
Home equity	367	3	-	-
Total	$ 2,503	7	$ -	-

December 31, 2016 *(Dollars in thousands)*	Non-accrual	Number	90 Days or More Past Due Still Accruing	Number
Commercial real estate:				
Other	$ 77	2	$ -	-
Faith-based non-profit:				
Owner occupied	1,578	3	129	2
Residential real estate:				
First mortgage	19	1	-	-
Multifamily	-	-	-	-
Home equity	174	2	-	-
Total	$ 1,848	8	$ 129	2

Non-accrual loans and loans past due over 90 days still on accrual include both smaller balance homogenous loans that are collectively evaluated for impairment and individually classified impaired loans. Loans from which principal or interest is in default for 90 days or more are classified as a non-accrual unless they are well secured and in process of collection. Loans past due over 90 days still accruing were matured loans that were well secured and in process of collection. Borrowers have continued to make payments on these loans while

The following table displays all non-accrual loans and loans 90 or more days past due and still on accrual for the period ended December 31, 2017.

(Dollars in thousands)	Amount	Number
Loans past due over 90 days still on accrual	$ -	-
Non-accrual loans past due		
Less than 30 days	$ 2,503	7
30-59 days	-	-
60-89 days	-	-
90+ days	-	-
Non-accrual loans	$ 2,503	7

The following table displays all non-accrual loans and loans 90 or more days past due and still on accrual for the period ended December 31, 2016.

(Dollars in thousands)	Amount	Number
Loans past due over 90 days still on accrual	$ 129	2
Non-accrual loans past due		
Less than 30 days	$ 210	5
30-59 days	-	-
60-89 days	-	-
90+ days	1,638	4
Non-accrual loans	$ 1,848	9

The Company categorizes loans into risk categories based on relevant information about the ability of borrowers to service their debt such as current financial information, historical payment experience, credit documentation, public information, and current economic trends, among other factors. The Company analyzes loans for reserves according to the loan's classification as to credit risk.This analysis includes homogenous loans, such as commercial, commercial real estate and faith based non–profit entities, and mortgage loans in process of foreclosure for which the loan to value does not support repayment in full. This analysis is performed on at least a quarterly basis.The Company uses the following definitions for risk ratings:

- Special Mention. Loans classified as special mention have a potential weakness that deserves management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan or of the institution's credit position at some future date. These loans exhibit a moderate likelihood of some loss related to those loans and leases that are considered special mention.

- Substandard. Loans classified as substandard are inadequately protected by the current sound financial repayment capacity and service coverage of the debtor or of the collateral pledged, if any. Loans so classified have a well-defined weakness or weaknesses that may jeopardize the liquidation of or repayment according to the original terms of the debt. In addition to commercial and faith-based non-profit loans with identified weaknesses, substandard loans include loans within the mortgage and consumer portfolio segments that are past due 90 days or more as to principal or interest if the loan to value does not support full repayment. Substandard loans are evaluated for impairment on an individual loan basis unless the substandard loan is a smaller balance homogenous loan that is not a TDR and is not in the process of foreclosure. These loan exhibits a distinct possibility that the company will sustain some loss if the deficiencies related to the loans is not corrected in a timely manner.

- Doubtful. Loans classified as doubtful have all the weaknesses inherent in those classified as substandard, with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions, and values, highly questionable and improbable.

- Pass. Loans are classified as pass in all classes within the commercial, faith-based non-profit, mortgage, consumer, and other portfolio segments that are not identified as special mention, substandard, or doubtful, are contractually current as to principal and interest, and are otherwise in compliance with the contractual terms of the loan agreement. These loans exhibit a low likelihood of loss related to loans that are considered pass.

7. BANK PREMISES AND EQUIPMENT

The following is a summary of bank premises and equipment, net as of December 31, 2017 and 2016:

(Dollars in thousands)	December 31, 2017	December 31, 2016
Land	$ 281	$ 747
Buildings and leasehold improvements	4,236	8,061
Furniture and equipment	2,485	2,778
Capital lease	344	655
Construction in progress	249	236
Bank premises and equipment	7,595	12,477
Less: accumulated depreciation and amortization	(5,158)	(7,417)
Bank premises and equipment, net	$ 2,437	$ 5,060

Total depreciation expense was $0.4 million for the years ended December 31, 2017 and 2016.

8. DEPOSITS

Deposits are the Bank's primary source of funds for making loans and purchasing investments. The Bank offers a variety of deposit account products to commercial and consumer customers. The total deposits that were re-classified to loans due to overdrafts were $27 thousand and $26 thousand at December 31, 2017 and 2016, respectively.

The following shows the maturity schedule of all time deposits:

(Dollars in thousands)	Amount
2018	$ 87,847
2019	4,717
2020	3,093
2021	53
2022	103
Total	$ 95,813

Principal maturities of time deposits of $250,000 or more as of December 31, 2017 and 2016 were as follows:

	December 31, 2017		December 31, 2016	
(Dollars in thousands)	Amount	Average Rate	Amount	Average Rate
Three months or less	$ 770	0.55 %	$ 1,247	0.26 %
Over three months to six months	2,534	0.66	806	0.37
Over six months to twelve months	14,137	0.91	6,310	0.50
Over one year to five years	1,283	0.38	9,019	0.99
Total	$ 18,724	0.83 %	$ 17,382	0.73 %

For the years ended December 31, 2017 and 2016, the Bank had $0.1 million in interest expense for time deposits greater than $250,000.

In the normal course of business, certain directors and executives of the Company and the Bank, including their immediate families and companies in which they have an interest, are deposit customers. These relationships had aggregate deposits of $0.9 million and $1.1 million as of December 31, 2017 and 2016, respectively.

The Bank had two and three deposit relationships for the year ended December 31, 2017 and 2016 with balances in excess of five percent of total deposits totaling $35.0 million and $50.0 million, respectively.

The following is the outstanding principal maturities and interest rate of the Company's FHLB advances as of December 31, 2017:

December 31, 2017

Maturity Date		Amount	Rate
(Dollars in thousands)			
2018	$	26	0.50%
2019		27	0.50%
2020		532	0.50%
2021		-	-
Thereafter		-	-
	$	585	0.50%

12. INCOME TAXES

On December 22, 2017, the President of the United States signed into law the Tax Cuts and Jobs Act (the "2017 Tax Act"). The 2017 Tax Act includes a number of changes to existing US. Tax laws that impact the Company, most notable a reduction of the U.S. corporate income tax rate from 34% to 21% for tax years beginning after December 31, 2017.

The Company recognized the income effects of the 2017 Tax Act in its 2017 consolidated financial statements in Staff Accounting Bulletin No. 118, which provides guidance for the application of ASC Topic 740,"Income Taxes," in the reporting period in which the 2017 Tax Act was signed into law. As such the Company's consolidated financial results reflect the income tax effects of the 2017 Tax Act for which the accounting under ASC Topic 740 is complete and provision amounts for those specific income tax effects of the 2017 Tax Act for which the accounting under ASC Topic 740 is incomplete buy a reasonable estimate could be determined. The Company did not identify items for which the income tax effects of the 2017 Tax Act have not been completed and a reasonable estimate could not be determined as of December 31, 2017.

The components of the income tax expense (benefit) for the years ended December 31, 2017 and 2016 were as follows:

(Dollars in thousands)		2017		2016
Income tax expense (benefit)				
Current	$	156	$	(20)
Deferred		1,465		(2,313)
Total	$	1,621	$	(2,333)

A reconciliation of reported income tax expense for the years ended December 31, 2017 and 2016 to the amount of tax expense computed by multiplying income before income taxes by the statutory federal income tax rate follows:

(Dollars in thousands)		2017		2016
Statutory federal income tax rate		34%		34%
Tax provision at statutory rate	$	(330)	$	(2,132)
Increase (decrease) in income taxes resulting from:				
State income taxes net of federal benefit		35		(53)
Tax exempt interest income		-		(28)
Decrease in deferred tax valuation allowance		(34)		(28)
Cash surrender value of life insurance		(86)		(86)
Revalution of deferred tax assets and liabilities due to Tax Cuts and Jobs Act		2,088		-
Other		(52)		(6)
Total	$	1,621	$	(2,333)

It is expected that the Bank will contribute $0.2 million to the Cash Balance Plan during 2018.

The following table shows the type of assets held in the Cash Balance Plan:

	As of December 31,	
Asset Category	**2017**	**2016**
Equity securities	67.8%	65.9%
Debt securities	29.7%	31.8%
Real estate	0.0%	0.1%
All other assets	2.5%	2.2%
Total	100.0%	100.0%

The Bank sponsors a nonqualified Supplemental Executive Retirement Plan ("SERP"). The SERP, which is unfunded, provides certain individuals with pension benefits, outside the Bank's noncontributory defined-benefit Cash Balance Plan, based on average earnings, years of service and age at retirement. Participation in the SERP is at the discretion of the Bank's Board of Directors. The Company and Bank purchased bank owned life insurance ("BOLI") in 2002 in the aggregate amount of approximately $12.9 million face value covering all the participants in the SERP. Increases in the cash surrender value of BOLI policies totaled $0.3 million for the years ended December 31, 2017 and 2016. The cash surrender value of the BOLI owned by the Bank was $8.7 million and $8.5 million as of December 31, 2017 and 2016, respectively. The Bank has the ability and the intent to keep this life insurance in force indefinitely. The insurance proceeds may be used, at the sole discretion of the Bank, to fund the benefits payable under the SERP.

Since there are no assets in the plan, contributions are equal to the benefits paid. It is expected that $0.2 million will be paid in benefits during 2018.

The SERP and the Cash Balance Plan components of the net periodic benefit cost reflected in salaries and employee benefits expense for the years ended December 31, 2017 and December 31, 2016 were:

	Cash Balance Plan		SERP		Total	
(Dollars in thousands)	2017	2016	2017	2016	2017	2016
Service costs	$ 146	$ 163	$ -	$ -	$ 146	$ 163
Interest cost	203	217	73	77	276	294
Expected return on Plan assets	(381)	(344)	-	-	(381)	(344)
Amortization of prior service cost and recognized net actuarial gain	120	175	25	25	145	200
Net periodic pension cost	$ 88	$ 211	$ 98	$ 102	$ 186	$ 313

The following table shows the change in the projected benefit obligations and plan assets for the years ended December 31, 2017 and 2016:

	Cash Balance Plan		SERP		Total	
(Dollars in thousands)	2017	2016	2017	2016	2017	2016
Change in projected benefit obligations:						
Benefit obligation at beginning of year	$ 5,663	$ 6,142	$ 2,034	$ 2,129	$ 7,697	$ 8,271
Service cost	146	163	-	-	146	163
Interest cost	202	217	73	77	275	294
Actuarial gain (loss)	130	(394)	53	(18)	183	(412)
Benefits and expenses paid	(275)	(465)	(154)	(154)	(429)	(619)
Benefit obligation at end of year	5,866	5,663	2,006	2,034	7,872	7,697
Change in plan assets:						
Fair value of plan assets at beginning of year	5,534	5,094	-	-	5,534	5,094
Actual return on plan assets	790	355	-	-	790	355
Employer contributions	550	550	154	154	704	704
Benefits and expenses paid	(275)	(465)	(154)	(154)	(429)	(619)
Fair value of plan assets at year end	6,599	5,534	-	-	6,599	5,534
Funded status	$ 733	$ (129)	$ (2,006)	$ (2,034)	$ (1,273)	$ (2,163)

Asset Category	Target Weight	Minimum Weight	Maximum Weight
Cash	0%	0%	10%
Equities:			
US	66%	56%	76%
Non-US	7%	0%	14%
Fixed Income	27%	20%	37%

Equity investments must be listed on the New York, American, NASDAQ, or other similar stock exchanges traded in the over-the-counter market with the requirement that such stocks have adequate liquidity relative to the size of the investment.

Fixed income investments must have a credit rating of B or better from Standard and Poor's or Moody's. The fixed income portfolio should be constructed so as to have an average maturity not exceeding 10 years. No more than 5% of the fixed income portfolio should be invested in any one issuer. U.S. Treasury and Agency securities are exempt from this restriction.

Cash and equivalent instruments that are acceptable are repurchase agreements, bankers' acceptances, U.S. treasury bills, money market funds, and certificates of deposit.

The portfolio shall be structured to meet financial objectives over a period of 11 or more years. Over that time horizon, the total rate of return should equal at least 103% of the applicable blended benchmark returns and place in the top half of group performance. Benchmarks which may be used for portfolio performance comparison are as follows:

- U.S. Large Cap Equities: S&P 500, Russell 1000, Russell 1000 Value, and Russell 1000 Growth
- U.S. Mid Cap Equities: S&P 400 Mid Cap, Russell Mid Cap Value, and Russell Mid Cap Growth
- U.S. Small Cap Equities: S&P 600 Small Cap, Russell 2000 Value, and Russell 2000 Growth
- Non-U.S. Equities: MSCI EAFE IL
- Fixed Income: Lehman Brothers Intermediate Government/Corporate
- Cash: U.S. 3-Month Treasury Bill

The Company groups assets and liabilities at fair value in three levels, based on the markets in which the assets and liabilities are traded and the reliability of the assumptions used to determine fair value. These levels were:

(Dollars in thousands)	December 31, 2017	December 31, 2016
Beginning Balance	$ 2,070	$ 1,864
Draws/Advances	5,995	777
Repayments	(6,780)	(571)
Removal of loan due to director retirement	(86)	-
Ending Balance	$ 1,199	$ 2,070

The Bank leases certain real estate from a shareholder, who owns 5% or more of the Company's stock. The arm's length transaction consists of a lease with nine years remaining on its term, with three five-year renewal options, and calls for an annual 2% increase in rents. The lease does not present any unfavorable features.

15. REGULATORY MATTERS AND RESTRICTIONS

On August 7, 2015, the Bank entered into a memorandum of understanding with the Federal Deposit Insurance Corporation ("FDIC") and the Office of the North Carolina Commissioner of Banks ("NCCOB"). The informal agreement required the Bank take certain actions to enhance its management of adversely classified assets, remain well-capitalized and improve earnings. It also restricted that dividends could not be paid to the holding company without prior approval and required reporting of progress of implementing additional management improvement plans. On August 19, 2010, the Company entered into a memorandum of understanding with the FRB. The informal agreement required the Company to receive prior approval for payment of any dividends, to repurchase stock, or to receive any dividends from the Bank. On October 24, 2017, the FRB terminated its memorandum of understanding with the Company, and subsequently on November 6, 2017, the FDIC and NCCOB terminated their memorandum of understanding with the Bank.

On August 20, 2010, the Company issued 11,735 shares of $1,000 liquidation value, Series B Fixed Rate Cumulative Perpetual Preferred Stock, ("Series B Preferred Stock"), under the Community Development Capital Initiative ("CDCI"), part of the United States Department of the Treasury (the "Treasury") Troubled Asset Relief Program ("TARP"). Participation in the CDCI placed restrictions on the Company's ability to declare or pay dividends or distributions on, or purchase, redeem or otherwise acquire for consideration, shares of its capital stock, including restrictions against the Company (i) increasing dividends payable on its common stock from the last quarterly cash dividend per share declared on the common stock prior to November 17, 2008; (ii) increasing its aggregate per share dividends and distributions above the aggregate dividends and distributions paid for the immediately prior fiscal year; and (iii) declaring or paying dividends or distributions on, or repurchasing, redeeming or otherwise acquiring for consideration, shares of its capital stock in the event that the Company fails to declare and pay full dividends (or declare and set aside a sum sufficient for payment thereof) on the Series B Preferred Stock. During 2015, the Company did not declare any dividends to its common stockholders. As a consequence of these restrictions, the Company was not able pay further dividends to its common stockholders. These restrictions remained until all of the Series B Preferred Stock had been redeemed in full. On December 20, 2016, the Company redeemed all outstanding TARP in consideration of $9.4 million, a discount of 20%, which resulted in a gain of $2.3 million.

The Company and the Bank are subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements may initiate certain mandatory and the possibility of additional discretionary, actions by regulators that, if undertaken, could have a direct material effect on the Company and the Bank's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Company and the Bank must meet specific capital guidelines that involve quantitative measures of their assets, liabilities and certain off-balance sheet items as calculated under regulatory accounting practices. The capital amounts and classification are subject to qualitative judgments by the regulators about components, risk weightings and other factors. Quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain minimum amounts and ratios (set forth in the table below) of total, Tier 1 and common equity Tier 1 capital (as defined in the regulations) to risk-weighted assets (as defined), and Tier 1 capital (as defined) to average assets (as defined). Management believes, as of December 31, 2017 and 2016, that the Company and the Bank met all capital adequacy requirements to which they are subject. To be categorized as well capitalized, the Bank must maintain minimum common equity Tier 1, total risk-based, Tier 1 risk-based and Tier 1 leveraged ratios as set forth in the table below.

16. HOLDING COMPANY CONDENSED FINANCIAL INFORMATION

The condensed financial data for the Company (holding company only) was:

Condensed Balance Sheets: *(Dollars in thousands)*	December 31, 2017	December 31, 2016
Assets:		
Cash and cash equivelents	$ 240	$ 229
Investment in subsidiary Bank	19,661	21,681
Other assets	489	425
Total Assets	$ 20,390	$ 22,335
Liabilities and Stockholders' Equity:		
Total liabilities	$ 209	$ 12
Stockholders' equity	20,181	22,323
Total Liabilities and Stockholders' Equity	$ 20,390	$ 22,335

Condensed Statements of Operations: *(Dollars in thousands)*	For the Years Ended December 31, 2017	For the Years Ended December 31, 2016
Undistributed net loss of subsidiary bank	$ (2,469)	$ (3,730)
Expenses, net	(122)	(208)
Net loss	$ (2,591)	$ (3,938)

Condensed Cash Flows: *(Dollars in thousands)*	For the Years Ended December 31, 2017	For the Years Ended December 31, 2016
Cash Flows from operating activities:		
Net loss	$ (2,591)	$ (3,938)
Adjustments to reconcile net income to net cash used in operating activities:		
Undistributed net loss of subsidiary	2,469	3,730
(Increase) decrease in other assets	(64)	10
Increase (decrease) in other liabilities	197	(26)
Net cash provided by (used in) operating activities	11	(224)
Investing Activities:		
Dividends from subsidiary	-	9,845
Net cash provided by investing activities	-	9,845
Financing activities:		
Dividends paid	-	(228)
Redemption of preferred stock	-	(9,388)
Net cash used in financing activities	-	(9,616)
Net increase in cash and cash equivalents	11	5
Cash and cash equivalents at beginning of year	229	224
Cash and cash equivalents at end of year	$ 240	$ 229

17. COMMITMENTS AND CONTINGENCIES

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

The Bank's exposure to credit losses in the event of non-performance by the other party to the financial instrument for commitments to extend credit and standby letters of credit is represented by the contractual amount of those instruments. The Bank utilizes the same credit policies and the reliability of the assumptions used to determine fair value. These levels are:

Level 1 — Valuations for assets and liabilities traded in active exchange markets, such as the New York Stock Exchange.

Level 2 — Valuations are obtained from readily available pricing sources via independent providers for market transactions involving similar assets or liabilities. The Company's principal market for these securities is the secondary institutional markets and valuations are based on observable market data in those markets. Level 2 securities include U. S. Agencies, state and municipal bonds and MBS.

Level 3 — Valuations for assets and liabilities that are derived from other valuation methodologies, including option pricing models, discounted cash flow models and similar techniques, and not based on market exchange, dealer, or broker traded transactions. Level 3 valuations incorporate certain assumptions and projections in determining the fair value assigned to such assets.

Assets and Liabilities Measured on a Recurring Basis:

Available-for-sale ("AFS") Investment Securities: Investment securities are recorded at fair value on a recurring basis. Fair value measurement is based upon quoted prices, if available. If quoted prices are not available, fair values are measured using matrix pricing, which is a mathematical technique used widely in the industry to value debt securities without relying exclusively on quoted prices for the specific securities but rather by relying on the securities' relationship to other benchmark quoted securities. Level 1 securities include those traded on nationally recognized securities exchanges, U.S. Treasury securities, and money market funds. Level 2 securities include U.S. Agencies, MBS issued by government sponsored entities, state and municipal bonds and corporate debt securities. Securities classified as Level 3 include asset-backed securities in less liquid markets. The Company did not hold any Level 1 or Level 3 AFS Investment Securities as of December 31, 2017 and 2016.

Assets measured at fair value on a recurring basis as of December 31, 2017 were as follows:

(Dollars in thousands)

Description	December 31, 2017	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Recurring				
U.S. Agencies	$ 17,833	$ -	$ 17,833	$ -
MBS				
Residential	37,878	-	37,878	-
Municipals	1,777	-	1,777	-
Total	$ 57,488	$ -	$ 57,488	$ -

Assets measured at fair value on a recurring basis as of December 31, 2016 were as follows:

(Dollars in thousands)

Description	December 31, 2016	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Recurring				
U.S. Agencies	$ 18,769	$ -	$ 18,769	$ -
MBS				
Residential	44,442	-	44,442	-
Municipals	1,793	-	1,793	-
Total	$ 65,004	$ -	$ 65,004	$ -

Assets and Liabilities Measured on a Nonrecurring Basis:

Held for Sale Loans: Loans held for sale are carried at the lower of aggregate cost, net of deferred fees, deferred origination costs or fair value. The fair value of loans the held for sale were determined by obtaining bids from potential acquirers for the loans. Held for sale loans are classified as Level 3 measurements due to the use of significant lack of liquidity for the loans.

Impaired loans: Impaired loans are evaluated and valued at the time the loan is identified as impaired, and are carried at the lower of cost or market value. Market value is measured based on the value of the collateral securing these loans or net present value of expected future cash flows discounted at the loan's effective interest rate. Collateral may be real estate and/or business assets including equipment, inventory, and/or accounts receivable. The value of business equipment, inventory, and accounts receivable collateral is based on net book value on the business' financial statements and, if necessary, discounted based on management's review and analysis. Appraised and reported

(Dollars in thousands)

Description		December 31, 2016	Valuation Technique	Significant Unobservable Inputs	Significant Unobservable Input Value
Nonrecurring:					
Held for sale loans	$	975	purchase agreement	purchase discount	-
OREO		367	discounted appraisals	collateral discounts	6-20%
Impaired loans		15,178	discounted appraisals	collateral discounts	6-20%
Total	$	16,520			

The Company discloses estimated fair values for its significant financial instruments. The methodologies for estimating the fair value of financial assets and liabilities that are measured at fair value on a recurring or non-recurring basis are discussed above. The methodologies for other financial assets and liabilities are discussed below.

The Company had no transfers between any of the three levels in 2017 or 2016.

Cash and Cash Equivalents: The carrying amount of cash, due from bank, and federal funds sold approximates fair value, and is therefore considered Level 1 input.

Loans (other than impaired), net of allowances for loan losses: Fair values are estimated for portfolios of loans with similar financial characteristics. The majority of the Company's loans and lending-related commitments are not carried at fair value on a recurring basis on the Consolidated Balance Sheets, nor are they actively traded.

The fair value of performing loans is calculated by discounting scheduled cash flows through their individual contractual maturity, using discount rates that reflect the credit risk, overhead expenses, interest rate earned and again, contractual maturity of each loan less credit component. The maturity is based on contractual maturities for each loan, modified as required by an estimate of the effect of historical prepayments and current economic conditions.

For all loans, assumptions regarding the characteristics and segregation of loans, maturities, credit risk, cash flows, and discount rates are judgmentally determined using specific borrower and other available information, and are therefore considered a Level 3 input.

Accrued Interest Receivable and Payable: The fair value of interest receivable and payable is estimated to approximate the carrying amounts and are therefore considered Level 1 input.

Deposits: The fair value of deposits with no stated maturity, such as demand deposits, checking accounts, savings and money market accounts, is equal to the carrying amount. The fair value of certificates of deposit is based on the discounted value of contractual cash flows, where the discount rate is estimated using the market rates currently offered for deposits of similar remaining maturities and are therefore considered Level 2 input.

Borrowings: The fair value of borrowings is based on the discounted value of estimated cash flows. The discounted rate is estimated using market rates currently offered for similar advances or borrowings and are therefore considered Level 3 input.

Off-Balance Sheet Instruments: Since the majority of the Company's off-balance sheet instruments consist of non- fee producing variable rate commitments, the Company has determined they do not have a distinguishable fair value.

20. SUBSEQUENT EVENTS

Subsequent events are events or transactions that occur after the balance sheet date, but before financial statements are issued. Recognized subsequent events are events or transactions that provide additional evidence about conditions that existed at the date of the balance sheet. Nonrecognized subsequent events are events that provide evidence about conditions that did not exist at the date of the balance sheet but arose after that date. Management has reviewed events occurring through March 14, 2018, the date the financial statements were available to be issued, and noted, no subsequent events requiring accrual or disclosure.

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President and CEO

Randall C. Hall, CPA, CRP, CGMA
Senior Vice President/Chief Financial Officer & Chief Operations Officer

Valerie M. Quiett, Esq.
Senior Vice President/Chief Legal Officer/Corporate Secretary

Bank Officers

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President and CEO

Randall C. Hall, CPA, CRP, CGMA
Senior Vice President/Chief Financial Officer & Chief Operations Officer

Percy W. "Pete" Williams
Senior Vice President/Chief Credit Officer

Travis C. Rouse
Senior Vice President/Chief Sales Officer

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