



*2018 Annual
Financial Report*

PIONEER BANKSHARES, INC. AND SUBSIDIARY

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PIONEER BANKSHARES, INC. AND SUBSIDIARY

Market Data

The Common Stock of the Company trades on the OTC Bulletin Board under the symbol “PNBI” and transactions generally involve a small number of shares. The Company’s transfer agent is Computershare, Inc. located at 480 Washington Boulevard, 29th Floor, in Jersey City, New Jersey, 07013. The following table shows actual trade prices during the year. Other transactions may have occurred which were not included in the table.

COMMON STOCK TRADE PRICES

<u>2017</u>	<u>High</u>	<u>Low</u>
First Quarter	\$ 24.00	\$ 22.10
Second Quarter	24.20	22.75
Third Quarter	24.20	23.00
Fourth Quarter	24.00	21.75
<u>2018</u>	<u>High</u>	<u>Low</u>
First Quarter	\$ 30.75	\$ 27.00
Second Quarter	32.00	30.00
Third Quarter	32.00	31.40
Fourth Quarter	32.98	29.15

The Company has declared dividends on its Common Stock as follows:

<u>Declared Date</u>	<u>Record Date</u>	<u>Payment Date</u>	<u>Per Share Amount</u>
3/09/17	3/23/17	3/31/17	\$.20
6/08/17	6/22/17	6/30/17	.20
8/10/17	9/14/17	9/29/17	.20
11/09/17	12/14/17	12/29/17	.20
Total for 2017			<u>\$.80</u>
2/08/18	3/20/18	3/30/18	\$.21
5/17/18	6/19/18	6/29/18	.21
8/16/18	9/18/18	9/28/18	.21
12/20/18	12/21/18	12/31/18	.21
Total for 2018			<u>\$.84</u>

The Company’s ability to pay dividends is subject to certain restrictions imposed by the Federal Reserve and capital requirements of Federal and Virginia banking statutes and regulations. Additionally, the Company intends to follow a policy of retaining sufficient earnings in order to maintain the net worth and reserves of the Bank at adequate levels and to provide for the Company’s growth and ability to compete in its market area.

PIONEER BANKSHARES, INC. AND SUBSIDIARY

FINANCIAL HIGHLIGHTS (In thousands, except for per share information)

	<u>2018</u>	<u>2017</u>
Results of Operations		
Interest and dividend income	\$ 10,137	\$ 9,625
Interest expense	1,032	834
Net interest income	<u>9,105</u>	<u>8,791</u>
Provision for loan losses	354	384
Net interest income after provision for loan losses	<u>8,751</u>	<u>8,407</u>
Noninterest income	1,157	1,749
Noninterest expense	7,477	7,121
Income before income taxes	<u>2,431</u>	<u>3,035</u>
Income tax expense	202	994
Net Income	<u>\$ 2,229</u>	<u>\$ 2,041</u>
Financial Condition, At Year End		
Assets	\$ 213,514	\$ 203,452
Deposits	177,491	166,933
Loans, net of allowance	167,201	160,959
Stockholders' Equity	28,862	27,414
Per Share Data		
Net income per share, basic and diluted	\$ 2.29	\$ 2.10
Dividends per share	.84	.80
Book value per share	29.53	28.13
Performance Ratios		
Return on average assets ¹	1.08%	1.02%
Return on average equity ¹	7.93%	7.58%
Dividend payout ratio	36.78%	38.10%
Average equity to average assets ¹	13.62%	13.40%

¹Ratios are based primarily on daily average balances

PIONEER BANKSHARES, INC. AND SUBSIDIARY

General Business Description

Pioneer Bankshares, Inc. (the “Company”), a Virginia one bank holding company headquartered in Stanley, Virginia, was incorporated under the laws of the Commonwealth of Virginia on November 4, 1983. The Company’s wholly-owned subsidiary, Pioneer Bank, Inc. (the “Bank”) was established as a national bank in 1909. The Bank converted from a national bank to a state chartered bank, effective April 1994, and changed its name to Pioneer Bank, effective April 1999.

Pioneer Bank’s main branch and corporate office are located in Stanley, Virginia, with other branch locations in Shenandoah, Luray, Harrisonburg, Stanardsville, Ruckersville, and Charlottesville, Virginia. The Bank also operates a small finance company known as Valley Finance Services, a Division of Pioneer Bank, which specializes in consumer and auto lending.

Pioneer Bank also owns and operates two subsidiaries, one of which is Pioneer Financial Services, LLC. Income received from insurance services and non-banking investment services is handled through Pioneer Financial Services, LLC. The second subsidiary owned by Pioneer Bank is Pioneer Special Assets, LLC, which is generally used in conjunction with foreclosed properties, as a means of minimizing the risk of liability to the Bank.

The assets of the Company consist primarily of all of the stock of the Bank, real estate holdings leased to the Bank, a portfolio of equity investment securities, and minimal cash accounts.

The Bank is engaged in the general commercial banking business, primarily serving the counties of Page, Greene, Rockingham, and Albemarle, Virginia. In addition, the close proximity and mobile nature of individuals and businesses in adjoining Virginia counties and nearby cities places these markets within the Bank’s targeted trade area. The Bank also anticipates serving some individuals and businesses from other areas, including, but not limited to, the counties surrounding Page County.

The Bank offers a full range of banking and related financial services focused primarily towards serving individual consumers, small to medium size commercial businesses, and the professional community. The Bank strives to serve the banking needs of its customers while developing personal, hometown relationships. The Bank’s Board of Directors and management believe that the marketing of customized banking services will enable the Bank to continue its position in the financial services marketplace.

The Bank provides individual consumers, professionals and small and medium size commercial businesses in its market area with responsive and technologically advanced banking services. These services include competitively priced loans that are based on deposit relationships, easy access to the Bank’s decision-makers, and quick and innovative action necessary to meet a customer’s banking needs. The Bank’s capitalization and lending limit enables it to satisfy the credit needs of a large portion of the targeted market segment. In the event there are customers whose loan requirements exceed the Bank’s lending limit, the Bank will seek to arrange such loans on a participation basis with other financial institutions or private investors. The Board of Directors and management believe the Bank’s present capitalization will support substantial growth in deposits and loans.



Independent Auditor's Report

To the Board of Directors and Stockholders
Pioneer Bancshares, Inc. and Subsidiary
Stanley, Virginia

Report on the Financial Statements

We have audited the accompanying consolidated financial statements of Pioneer Bankshares, Inc. and its Subsidiary, which comprise the consolidated balance sheets as of December 31, 2018 and 2017, the related consolidated statements of income, comprehensive income, changes in stockholders' equity and cash flows for the years then ended, and the related notes to the consolidated financial statements (collectively, the financial statements).

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Pioneer Bankshares, Inc. and its Subsidiary as of December 31, 2018 and 2017, and the results of their operations and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Yount, Hyde & Barbour, P.C.

Winchester, Virginia
April 9, 2019

PIONEER BANKSHARES, INC. AND SUBSIDIARY

CONSOLIDATED BALANCE SHEETS DECEMBER 31, 2018 AND 2017

(In Thousands, except share and per share data)

	<u>2018</u>	<u>2017</u>
ASSETS		
Cash and due from banks	\$ 8,035	\$ 3,630
Interest-bearing deposits in other banks	10,429	8,634
Federal funds sold	2,369	2,876
Securities available for sale, at fair value	13,974	16,296
Equity securities, at fair value	357	---
Restricted securities, at cost	553	705
Loans receivable, net of allowance of \$2,148 in 2018 and \$2,005 in 2017	167,201	160,959
Bank premises and equipment, net	4,831	4,631
Accrued interest receivable	1,093	1,076
Other real estate owned, net of valuation allowance	487	335
Other assets	4,185	4,310
Total Assets	<u>\$ 213,514</u>	<u>\$ 203,452</u>
LIABILITIES		
Deposits		
Noninterest bearing:	\$ 54,747	\$ 51,443
Interest bearing:		
Demand	34,253	45,321
Savings	41,515	25,483
Time deposits	46,976	44,686
Total Deposits	177,491	166,933
Accrued expenses and other liabilities	1,286	1,580
Borrowings	5,875	7,525
Total Liabilities	<u>184,652</u>	<u>176,038</u>
STOCKHOLDERS' EQUITY		
Common stock; \$.50 par value, authorized 5,000,000 shares; outstanding – 977,419 and 974,563 shares in 2018 and 2017, respectively	489	487
Retained earnings	28,498	26,812
Accumulated other comprehensive income (loss)	(125)	115
Total Stockholders' Equity	<u>28,862</u>	<u>27,414</u>
Total Liabilities and Stockholders' Equity	<u>\$ 213,514</u>	<u>\$ 203,452</u>

See Notes to Consolidated Financial Statements.

PIONEER BANKSHARES, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF INCOME YEARS ENDED DECEMBER 31, 2018 AND 2017

(In Thousands, except per share data)

	<u>2018</u>	<u>2017</u>
INTEREST AND DIVIDEND INCOME:		
Loans including fees	\$ 9,511	\$ 9,207
Interest on securities – taxable	255	141
Interest on securities – nontaxable	29	36
Deposits and federal funds sold	209	109
Dividends	133	132
Total Interest and Dividend Income	<u>10,137</u>	<u>9,625</u>
INTEREST EXPENSE:		
Deposits	960	723
Borrowings	72	111
Total Interest Expense	<u>1,032</u>	<u>834</u>
NET INTEREST INCOME	9,105	8,791
PROVISION FOR LOAN LOSSES	354	384
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	<u>8,751</u>	<u>8,407</u>
NONINTEREST INCOME:		
Service charges on deposit accounts	1,183	1,141
Commission income	82	83
Other income	83	85
Gains on sales of securities available for sale, net	---	440
Change in fair value of equity securities	(191)	---
Total Noninterest Income	<u>1,157</u>	<u>1,749</u>
NONINTEREST EXPENSES:		
Salaries and employee benefits	3,485	3,140
Occupancy expenses	560	487
Equipment expenses	368	304
ATM expenses	337	298
Contributions	23	154
Sales and franchise tax	172	117
Director compensation and fees	154	137
(Gain) Loss on other real estate owned	(59)	156
Liability bond insurance	115	105
Professional and audit fees	362	343
Data processing fees	503	484
Telephone	211	193
Amortization expenses	210	210
Other expenses	1,036	993
Total Noninterest Expenses	<u>7,477</u>	<u>7,121</u>
INCOME BEFORE INCOME TAXES	2,431	3,035
INCOME TAX EXPENSE	202	994
NET INCOME	<u>\$ 2,229</u>	<u>\$ 2,041</u>
PER SHARE DATA:		
Net income, basic and diluted	\$ 2.29	\$ 2.10
Dividends	<u>\$ 0.84</u>	<u>\$ 0.80</u>

See Notes to Consolidated Financial Statements.

PIONEER BANKSHARES, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME YEARS ENDED DECEMBER 31, 2018 AND 2017

(In Thousands of Dollars)

	<u>2018</u>	<u>2017</u>
Net Income	\$2,229	\$2,041
Other comprehensive (loss) income, net of tax:		
Unrealized (losses) gains on securities available for sale:		
Unrealized holding (losses) gains arising during period, (net of tax of \$13 and \$156 for 2018 and 2017, respectively)	(49)	303
Reclassification adjustment for (gains) included in net income (net of tax of \$150 for 2017)	---	<u>(290)</u>
Other comprehensive (loss) income	<u>(49)</u>	<u>13</u>
Comprehensive income	<u>\$ 2,180</u>	<u>\$ 2,054</u>

See Notes to Consolidated Financial Statements.

PIONEER BANKSHARES, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY YEARS ENDED DECEMBER 31, 2018 AND 2017

(In Thousands of Dollars)

	<u>Common Stock</u>	<u>Retained Earnings</u>	<u>Accumulated Other Comprehensive Income (Loss)</u>	<u>Total</u>
BALANCE DECEMBER 31, 2016	\$ 485	\$ 25,451	\$ 83	\$ 26,019
Net Income		2,041		2,041
Other Comprehensive Income			13	13
Cash Dividends		(778)		(778)
Stock issued for compensation	2	117		119
Reclassification of stranded tax effects from change in tax rate		(19)	19	---
	<u>2</u>	<u>(19)</u>	<u>19</u>	<u>---</u>
BALANCE DECEMBER 31, 2017	\$ <u>487</u>	\$ <u>26,812</u>	\$ <u>115</u>	\$ <u>27,414</u>
Cumulative effect adjustment – ASU 2016-01		191	(191)	---
Net Income		2,229		2,229
Other Comprehensive Loss			(49)	(49)
Cash Dividends		(820)		(820)
Stock issued for compensation	<u>2</u>	<u>86</u>		<u>88</u>
BALANCE DECEMBER 31, 2018	\$ <u>489</u>	\$ <u>28,498</u>	\$ <u>(125)</u>	\$ <u>28,862</u>

See Notes to Consolidated Financial Statements.

PIONEER BANKSHARES, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF CASH FLOWS YEARS ENDED DECEMBER 31, 2018 AND 2017

	<u>2018</u>	<u>2017</u>
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	\$ 2,229	\$ 2,041
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	354	384
(Gain) on sales of securities available for sale, net	---	(440)
Net amortization on securities	20	20
Fair Value adjustment on equity securities	191	---
Purchases of equity securities	(7,156)	---
Proceeds from sales of equity securities	11,592	---
Deferred income tax (benefit) expense	(18)	262
Depreciation	333	327
Amortization	210	210
Stock based compensation	88	102
(Gain) Loss on other real estate owned	(59)	156
Loss (Gain) on sales and disposals equipment, net	29	(14)
Loss on charitable contribution of other real estate owned	3	13
Net change in:		
Accrued interest receivable	(17)	(151)
Other assets	(54)	(15)
Accrued expenses and other liabilities	(294)	(153)
	<u>7,451</u>	<u>2,742</u>
Net Cash Provided by Operating Activities		
	<u>7,451</u>	<u>2,742</u>
CASH FLOWS FROM INVESTING ACTIVITIES:		
Net change in interest-bearing deposits in other banks	(1,795)	(2,004)
Net change in federal funds sold	507	(1,066)
Net change in restricted securities	152	(11)
Proceeds from calls, maturities, sales, and principal payments of securities available for sale	1,737	9,403
Purchase of securities available for sale	(4,481)	(16,982)
Net (increase) in loans	(7,024)	(3,101)
Proceeds on sale of other real estate	332	1,409
Purchase of bank premises and equipment	(571)	(209)
Proceeds from sales of equipment	9	21
	<u>(11,134)</u>	<u>(12,540)</u>
Net Cash (Used in) Investing Activities		
	<u>(11,134)</u>	<u>(12,540)</u>
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net change in:		
Demand and savings deposits	8,268	10,162
Time deposits	2,290	(2,111)
Proceeds from borrowings	2,501	3,000
Curtailements of borrowings	(4,151)	(3,750)
Exercise of stock options	---	17
Dividends paid	(820)	(778)
	<u>8,088</u>	<u>6,540</u>
Net Cash Provided by Financing Activities		
	<u>8,088</u>	<u>6,540</u>
CASH AND CASH EQUIVALENTS		
Net increase (decrease) in cash and cash equivalents	4,405	(3,258)
Cash and cash equivalents, beginning of year	<u>3,630</u>	<u>6,888</u>
Cash and cash equivalents, end of year	<u>\$ 8,035</u>	<u>\$ 3,630</u>
Supplemental Disclosure of Cash Paid During the Year for:		
Interest	\$ 953	\$ 809
Income taxes	281	830
Supplemental Disclosure of non-cash activity:		
Unrealized (loss) gain on securities available for sale	(62)	19
Other real estate acquired in settlement of loans	428	494

See Notes to Consolidated Financial Statements.

PIONEER BANKSHARES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

The accounting and reporting policies of Pioneer Bankshares, Inc. ("Company"), and its subsidiary Pioneer Bank ("Bank"), conform to accounting principles generally accepted in the United States of America and to accepted practice within the banking industry. A summary of significant accounting policies is as follows:

Consolidation Policy - The consolidated financial statements of the Company include the Bank and Pioneer Financial Services, LLC, and Pioneer Special Assets, LLC which are wholly-owned subsidiaries of the Bank. All significant inter-company balances and transactions have been eliminated.

Use of Estimates - In preparing consolidated financial statements in conformity with accounting principles generally accepted in the United States of America, management is required 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 revenue and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses and the valuation of other real estate owned.

Reclassifications - Certain reclassifications have been made to prior period balances to conform to the current year presentation. None were of a material nature and had no effect on prior year net income or stockholders equity.

Subsequent Events - In preparing these financial statements, the Company has evaluated events and transactions for potential recognition or disclosure through April 9, 2019, which is the date the financial statements were available to be issued. In the opinion of management, all subsequent events requiring recognition or disclosure have been included in the consolidated financial statements.

Securities - Debt securities are classified as held to maturity and carried at amortized cost when management has the positive intent and ability to hold them to maturity. Debit securities which the Company intends to hold for indefinite periods of time, including securities used as part of the Company's asset/liability management strategy are classified as available for sale. Securities available for sale are carried at fair value, with unrealized holding gains and losses reported in other comprehensive income, net of tax. At December 31, 2018 and 2017, all debt securities were classified as available for sale.

Interest income includes amortization of purchase premium or discount. Premiums and discounts on debt securities are amortized on the level-yield method without anticipating prepayments, except for mortgage backed securities where prepayments are anticipated.

Impairment of securities occurs when the fair value of a security is less than its amortized cost. For debt securities, impairment is considered other-than-temporary and recognized in its entirety in net income if either (1) the Company intends to sell the security or (2) it is more likely than not that the Company will be required to sell the security before recovery of its amortized cost basis. If, however, the Company does not intend to sell the security and it is not more-than-likely that the Company will be required to sell the security before recovery, management must determine what portion of the impairment is attributable to a credit loss, which occurs when the amortized cost of the security exceeds the present value of the cash flows expected to be collected from the security. If there is no credit loss, there is no other-than-temporary impairment. If there is a credit loss, other-than-temporary impairment exists, and the credit loss must be recognized in net income and the remaining portion of impairment must be recognized in other comprehensive income.

The Company regularly reviews each debit security for other-than-temporary impairment based on criteria that include the extent to which cost exceeds market price, the duration of that market decline, the financial health of and specific prospects for the issuer, a best estimate of the present value of cash flows expected to be collected from debt securities, the institution's intention with regard to holding the security and the likelihood that the Company would be required to sell the security before recovery.

Equity securities with readily determinable fair values are carried at fair value, with changes in fair value reported in net income. Restricted equity securities are carried at cost and are periodically evaluated for impairment based on the ultimate recovery of par value. The entirety of any impairment on equity securities is recognized in earnings.

PIONEER BANKSHARES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued):

On January 1, 2018, the Company adopted ASU 2016-01, which requires equity investments (except those accounted for under the equity method of accounting or those that result in consolidation of the investee) to be measured at fair value with changes in fair value recognized in net income. The adoption of this standard resulted in a \$191,000 increase to beginning retained earnings and a \$191,000 decrease to beginning other comprehensive income. Changes in fair value subsequent to the date of adoption are recorded in noninterest income.

Gains and losses on sales of securities are recorded on the trade date and determined using the specific identification method.

Loans Receivable - Loans receivable are intended to be held until maturity and are reported at their outstanding principal balance less any adjustments for charge-offs, net of unearned interest, the allowance for loan losses, and deferred loan fees and costs. Interest is computed by methods which generally result in level rates of return on principal. Interest income is generally not recognized on nonaccrual loans and payments received on such loans are applied as a reduction of the loan principal balance. Loan origination fees, net of certain direct origination costs, are deferred and recognized as an adjustment of the related loan yield using the interest method.

The Company classifies all loans as past due when the payment of principal and interest based upon contractual terms is 30 or more days delinquent.

The accrual of interest on loans is generally discontinued at the time the loan is 90 days delinquent unless the credit is well-secured and in process of collection for all loan classes. Commercial non-real estate classes are placed on nonaccrual status when it is probable that principal or interest is not fully collectible, or generally when principal or interest becomes 90 days past due, whichever occurs first. Real estate loans, which includes the residential, commercial, construction and land categories, are generally placed on nonaccrual status when principal and interest becomes 90 days past due. Consumer non-real estate loans, including personal automobile loans and all other individual loans are placed on nonaccrual status at varying intervals, based on the type of product, generally when principal and interest becomes between 90 days and 120 days past due. Revolving consumer credit card loans are not placed on nonaccrual but are generally charged-off if they reach 120 days past due, with unpaid fees and finance charges reversed against interest income. Consumer non-real estate loans are typically charged off between 90 and 120 days past due unless the loan is well secured and in the process of collection and are subject to mandatory charge-off at a specified delinquency date consistent with regulatory guidelines. In most cases, loans are placed on non-accrual or charged off at an earlier date if collection of principal or interest is considered doubtful. All other loan classes are generally charged off within the range of 90 to 180 days, unless there are specific or extenuating circumstances that warrant further collection or legal actions.

Interest accrued but not collected for loans that are placed on nonaccrual or charged off is reversed against interest income. The interest on these loans is accounted for on the cash-basis or cost-recovery method, until qualifying for return to accrual. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured. Payments received on nonaccrual loans are applied as a reduction to the remaining principal balance as long as concern exists as to the ultimate collection of the principal. Loans are generally removed from nonaccrual status when the concern no longer exists as to the collectability of principal and interest and the borrower has been able to demonstrate a specific period of payment performance.

Allowance for Loan Losses – The provision for loan losses charged to operations is an amount sufficient to bring the allowance for loan losses to an estimated balance that management considers adequate to absorb probable losses inherent in the portfolio. This evaluation process is inherently subjective, as it requires estimates that are susceptible to significant revision as more information becomes available. The allowance evaluation process also gives consideration to risk characteristics associated with each segment of the loan portfolio, which are further defined in Note 6 of this report.

Loans are generally charged against the allowance when management believes the collectability of the principal is unlikely. Recoveries of amounts previously charged-off are credited to the allowance. Management's determination of the adequacy of the allowance is based on the evaluation of the composition of the loan portfolio, the value and adequacy of collateral, current economic conditions, historical loan loss experience, concentrations of credit within the portfolio, loan growth trends, levels of adversely classified loans, past due trends, as well as other factors related to the knowledge and experience of lending personnel and legal, regulatory, or compliance issues related to lending practices. While management uses

PIONEER BANKSHARES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 *SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued):*

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

The allowance consists of specific and various general components. The specific component relates to loans classified as impaired. Specific allowances on an impaired loan is established when the discounted cash flows (or collateral value or observable market price) of the impaired loan is lower than the carrying value of that loan. The general component covers non-impaired loans and is based on historical loss experience adjusted for qualitative factors.

A loan is considered impaired when, based on current information and events, it is probable that the Company will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired.

Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed.

Impairment is measured on a loan by loan basis for commercial and construction loans by either the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's obtainable market price, or the fair value of the collateral if the loan is collateral dependent. Large commercial real estate loans and construction land loans are reviewed and evaluated on an annual basis or as they become delinquent so as to determine any possible impairment. Residential real estate loans are specifically evaluated for possible impairment on a case by case basis as they become delinquent or are identified as a potential problem credit. Large groups of smaller balance homogeneous loans are collectively evaluated for impairment. Accordingly, the Company does not generally separately identify individual consumer loans for impairment disclosures.

Troubled Debt Restructurings - In situations where, for economic or legal reasons related to a borrower's financial condition, management may grant a concession to the borrower that it would not otherwise consider, the related loan is classified as a troubled debt restructure (TDR). Management strives to identify borrowers in financial difficulty early and work with them to modify their loan to more affordable terms before their loan reaches nonaccrual status. These modified terms may include rate reductions, principal forgiveness, payment forbearance and other actions intended to minimize the economic loss and to avoid foreclosure or repossession of the collateral. In cases where borrowers are granted new terms that provide for a reduction of either interest or principal, management measures any impairment on the restructuring as noted above for impaired loans.

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

Bank Premises and Equipment – Land values are carried at cost. Bank premises and equipment are stated at cost less accumulated depreciation. Depreciation is charged to income over estimated useful lives ranging from 3 to 40 years, on a straight-line method.

PIONEER BANKSHARES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued):

Other Real Estate Owned- Assets acquired through, or in lieu of, loan foreclosure are held for sale and are initially recorded at fair value less cost to sell at the date of foreclosure, establishing a new cost basis. Subsequent to foreclosure, valuations are periodically performed by management and the assets are carried at the lower of carrying amount or fair value less cost to sell. Revenue and expenses from operations and changes in the valuation allowance are included in net expenses from other real estate owned. At December 31, 2018, the balance of other real estate owned consisted of a commercial real estate property with an approximate value of \$381,000 and a consumer real estate property with an approximate value of \$106,000. These were recorded as a result of obtaining physical possession of the property. At December 31, 2018, there were no formal foreclosure proceedings in process. At December 31, 2017, the balance of other real estate owned included commercial real estate properties with approximate values of \$335,000. These were recorded as a result of obtaining physical possession of the property. At December 31, 2017, there were no formal foreclosure proceedings in process.

Income Taxes – Amounts provided for income tax expense are based on income reported for financial statement purposes rather than amounts currently payable under income tax laws. Deferred income tax assets and liabilities are determined using the balance sheet method. Under this method, the net deferred tax asset or liability is determined based on the tax effects of the temporary differences between the book and tax basis of the various balance sheet assets and liabilities and gives current recognition to changes in tax rates and laws.

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

Tax positions that meet the more-likely-than-not recognition threshold are measured as the largest amount of tax benefit that is more than 50 percent likely of being realized upon settlement with the applicable taxing authority. The portion of the benefits associated with tax positions taken that exceeds the amount measured as described above is reflected as a liability for unrecognized tax benefits in the accompanying balance sheets along with any associated interest and penalties that would be payable to the taxing authorities upon examination. There were no such liabilities recorded as of December 31, 2018 or December 31, 2017.

Interest and penalties associated with unrecognized tax benefits are classified as additional income taxes in the Company's consolidated statements of income.

Financial Instruments - In the ordinary course of business, the Bank has entered into off-balance-sheet financial instruments consisting of commitments to extend credit, commitments under credit-card arrangements, commercial letters of credit, and standby letters of credit. Such financial instruments are recorded in the financial statements when they are funded.

The Bank's exposure to credit loss is represented by the contractual amount of these commitments. The Bank uses the same credit policies in making commitments as it does for other loans. Commitments to extend credit are generally made for a period of one year or less and interest rates are determined when funds are disbursed. Collateral and other security for the loans are determined on a case-by-case basis. Since some of the commitments are expected to expire without being drawn upon, the contract or notional amounts do not necessarily represent future cash requirements.

Cash and Cash Equivalents – For purposes of reporting cash flows, cash and cash equivalents include cash on hand and amounts due from banks.

Advertising Costs - The Company follows the policy of charging the production costs of advertising to expense as incurred. Advertising expense amounted to \$59,000 and \$31,000, for the years ended December 31, 2018 and 2017, respectively.

Earnings Per Share – Basic earnings per share represents income available to common shareholders divided by the weighted-average number of common shares outstanding during the period. Diluted earnings per share reflect additional

PIONEER BANKSHARES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued):

common shares that would have been outstanding if dilutive potential common shares had been issued, as well as any adjustment to income that would result from the assumed issuance. Potential common shares that may be issued by the Company are determined using the treasury stock method.

Stock Compensation – On an annual basis, the company pays two-thirds of its board of director fees and retainer fees in the form of stock compensation. Additionally, a portion of certain officers' bonuses are periodically paid with stock compensation. The fair market value of the Company's stock at the time of the stock issuance is used as the pricing factor to arrive at the appropriate number of shares issued.

There were no stock options or other stock awards outstanding at December 31, 2018 and 2017 that were issued under the Company's 1998 Stock Incentive Plan which expired in 2008.

Comprehensive Income – Comprehensive income consists of net income and other comprehensive income. Other comprehensive income includes unrealized gains and losses on securities available for sale.

Recently Adopted Standards – On January 1, 2018, the Company adopted ASU No. 2014-09, "Revenue from Contracts with Customers: Topic 606." This ASU revised guidance for the recognition, measurement, and disclosure of revenue from contracts with customers. The original guidance was amended through subsequent accounting standard updates that resulted in technical corrections, improvements, and a one-year deferral of the effective date to January 1, 2018. The guidance, as amended, is applicable to all entities and replaces significant portions of existing industry and transaction-specific revenue recognition rules with a more principles-based recognition model. Most revenue associated with financial instruments, including interest income, loan origination fees, and credit card fees, is outside the scope of the guidance, as are other items such as gains and losses on securities transactions. The guidance is primarily applicable to noninterest revenue streams such as deposit related charges and fees and certain other sources of the company's noninterest income.

As the guidance does not apply to revenue associated with financial instruments, including loans and securities that are accounted for under other GAAP, the new guidance did not have a material impact on revenue most closely associated with financial instruments, interest income. The Company completed its overall assessment of the revenue streams and review of related contracts potentially effected by the ASU and concluded that ASU 2014-09 did not materially change the method in which the Company currently recognizes revenue for its in-scope revenue streams. The Company adopted ASC 606 using the modified retrospective method applied to all contracts not completed as of January 1, 2018. The implementation of the new standard did not have a material impact on the measurement or recognition of revenue and as such, a cumulative effect adjustment to opening retained earnings was not deemed necessary.

Recent Accounting Pronouncements – In February 2016, the FASB issued ASU No. 2016-02, "Leases (Topic 842)." Among other things, in the amendments in ASU 2016-02, lessees will be required to recognize the following for all leases (with the exception of short-term leases) at the commencement date: (1) A lease liability, which is a lessee's obligation to make lease payments arising from a lease, measured on a discounted basis; and (2) A right-of-use asset, which is an asset that represents the lessee's right to use, or control the use of, a specified asset for the lease term. Under the new guidance, lessor accounting is largely unchanged. Certain targeted improvements were made to align, where necessary, lessor accounting with the lessee accounting model and Topic 606, Revenue from Contracts with Customers. The amendments in this ASU are effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. Early application is permitted upon issuance. Lessees (for capital and operating leases) and lessors (for sales-type, direct financing, and operating leases) must apply a modified retrospective transition approach for leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements. The modified retrospective approach would not require any transition accounting for leases that expired before the earliest comparative period presented. Lessees and lessors may not apply a full retrospective transition approach. The FASB made subsequent amendments to Topic 842 in July 2018 through ASU 2018-10 ("Codification Improvements to Topic 842, Leases.") and ASU 2018-11 ("Leases (Topic 842): Targeted Improvements.") Among these amendments is the provision in ASU 2018-11 that provides entities with an additional (and optional) transition method to adopt the new leases standard. Under this new transition method, an entity initially applies the new leases standard at the adoption date and recognizes a cumulative-effect adjustment to the opening balance of retained earnings in the period of adoption. Consequently, an entity's reporting for the comparative periods presented in the financial statements in which it adopts the new leases standard will continue to be in accordance with current GAAP (Topic 840, Leases). The effect of adopting this standard on January 1, 2019 was an approximate \$290,000 increase in assets and liabilities on our consolidated balance sheet.

PIONEER BANKSHARES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 *SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued):*

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

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

In March 2017, the FASB issued ASU 2017-08, “Receivables—Nonrefundable Fees and Other Costs (Subtopic 310-20), Premium Amortization on Purchased Callable Debt Securities.” The amendments in this ASU shorten the amortization period for certain callable debt securities purchased at a premium. Upon adoption of the standard, premiums on these qualifying callable debt securities will be amortized to the earliest call date. Discounts on purchased debt securities will continue to be accreted to maturity. The amendments are effective for fiscal years beginning after December 15, 2018, and interim periods within those fiscal years. Early adoption is permitted, including adoption in an interim period. Upon transition, entities should apply the guidance on a modified retrospective basis, with a cumulative-effect adjustment to retained earnings as of the beginning of the period of adoption and provide the disclosures required for a change in accounting principle. The Company does not expect the adoption of ASU 2017-08 to have a material impact on its consolidated financial statements.

In June 2018, the FASB issued ASU 2018-07, “Compensation- Stock Compensation (Topic 718): Improvements to Nonemployee Share-Based Payment Accounting.” The amendments expand the scope of Topic 718 to include share-based payments issued to non-employees for goods or services, which were previously excluded. The amendments will align the accounting for share-based payments to nonemployees and employees more similarly. The amendments are effective for fiscal years beginning after December 15, 2018, and interim periods within those fiscal years. Early adoption is permitted. The Company does not expect the adoption of ASU 2018-07 to have a material impact on its consolidated financial statements.

In August 2018, the FASB issued ASU 2018-13, “Fair Value Measurement (Topic 820): Disclosure Framework—Changes to the Disclosure Requirements for Fair Value Measurement.” The amendments modify the disclosure requirements in Topic 820 to add disclosures regarding changes in unrealized gains and losses, the range and weighted average of significant unobservable inputs used to develop Level 3 fair value measurements and the narrative description of measurement uncertainty. Certain disclosure requirements in Topic 820 are also removed or modified. The amendments are effective for fiscal years beginning after December 15, 2019, and interim periods within those fiscal years. Certain of the amendments are to be applied prospectively while others are to be applied retrospectively. Early adoption is permitted. The Company does not expect the adoption of ASU 2018-13 to have a material impact on its consolidated financial statements.

PIONEER BANKSHARES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 2 NATURE OF OPERATIONS:

The Company operates under a charter issued by the Commonwealth of Virginia and provides commercial banking services to its customers through its subsidiary bank. As a state chartered member bank, the Bank is subject to regulation by the Virginia Bureau of Financial Institutions and the Board of Governors of the Federal Reserve Banking System. As of December 31, 2018, the Bank had seven physical locations available to customers with 3 branches being located in Page County, 2 in Greene County, 1 in Rockingham County, and 1 in Albemarle County. The Bank also operates two separate subsidiaries, one being known as Pioneer Financial Services, LLC, which offers a variety of consumer investment and insurance services. The second subsidiary owned by Pioneer Bank is Pioneer Special Assets, LLC, which is generally used in conjunction with certain foreclosed properties. The Bank also operates a small consumer loan finance company known as Valley Finance Services, a Division of Pioneer Bank, which specializes in consumer and auto lending.

NOTE 3 CASH AND DUE FROM BANKS:

The Bank is required to maintain average reserve balances based on a percentage of deposits. The average balance of cash, which the Federal Reserve Bank required to be on reserve, was \$1.7 million and \$2.0 million at December 31, 2018 and December 31, 2017, respectively. These reserve requirements were satisfied by available vault cash and/or funds on deposit with the Federal Reserve Bank at December 31, 2018 and 2017. The Bank also maintains required deposit relationships with 3 separate correspondent banks in accordance with their separate and individual Fed Funds Credit Line Agreements. The amount on deposit with these correspondent banks was \$791,000 and \$200,000, as of December 31, 2018 and 2017, respectively.

NOTE 4 DEPOSITS IN AND FEDERAL FUNDS SOLD TO BANKS:

The Bank had cash deposited in and federal funds sold to other banks, most of which exceed federally insured limits, totaling approximately \$9.9 million and \$4.7 million at December 31, 2018 and 2017, respectively. Management has established acceptable risk tolerances relating to uninsured deposits in other banks and diversifies these funds in accordance with policy guidelines.

NOTE 5 INVESTMENT SECURITIES:

The amortized cost and fair value of securities available for sale at December 31, 2018 and 2017 were as follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(In Thousands)			
<u>December 31, 2018</u>				
Available for Sale				
U.S. treasury securities	\$ 3,581	\$ ---	\$ (56)	\$ 3,525
Mortgage-backed securities	4,387	5	(33)	4,359
Agency securities	4,000	---	(71)	3,929
State and municipals	2,164	7	(10)	2,161
	<u>\$ 14,132</u>	<u>\$ 12</u>	<u>\$ (170)</u>	<u>\$ 13,974</u>
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(In Thousands)			
<u>December 31, 2017</u>				
Available for Sale				
U.S. treasury securities	\$ 4,073	\$ ---	\$ (43)	\$ 4,030
Mortgage-backed securities	1,481	1	(22)	1,460
Agency securities	3,523	2	(25)	3,500
State and municipals	2,331	7	(16)	2,322
Equity securities	4,742	245	(3)	4,984
	<u>\$ 16,150</u>	<u>\$ 255</u>	<u>\$ (109)</u>	<u>\$ 16,296</u>

PIONEER BANKSHARES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 5 INVESTMENT SECURITIES: (continued)

There were no sales of securities available for sale during the year ended December 31, 2018. Proceeds from sales of securities available for sale during 2017 totaled \$6.2 million. Gross gains and gross losses realized on these sales were \$444,000 and \$(4,000), respectively. The net gain realized on these sales of \$440,000 was reclassified from accumulated other comprehensive income to income and included in “gains on sales of securities available for sale, net” in the consolidated statements of income. The income tax related to the reclassification resulted in \$150,000 of income tax expense, which was included in the “income tax expense” line item on the consolidated statements of income.

Equity securities consisted of investments in mutual funds and the common stock of certain community banking institutions at December 31, 2018 and 2017. Prior to January 1, 2018 equity securities were classified as available for sale with changes in fair value reported in accumulated other comprehensive income. As described in Note 1, the Company adopted ASU 2016-01 effective January 1, 2018 and as of that date equity securities are no longer classified as available for sale and changes in fair value are recorded through earnings. The following table presents information on the change in the fair value of equity securities that was recognized in earnings during the year ended December 31, 2018, as well as the portion of that balance which relates to equity securities still held at December 31, 2018:

	For the Year Ended December 31, 2018 (In thousands)
Net losses recognized during the year on equity securities	\$ (191)
Less: Net losses recognized on equity securities sold	<u>(193)</u>
Net unrealized gains recognized on equity securities still held at the balance sheet date	<u>\$ 2</u>

The amortized cost and fair value of securities available for sale at December 31, 2018, by contractual maturity, are shown in the following schedule. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	<u>Securities Available for Sale</u>	
	<u>Amortized</u> <u>Cost</u>	<u>Fair</u> <u>Value</u>
	(In Thousands)	
Due within one year	\$ 1,410	\$ 1,405
Due after one year through five years	7,789	7,694
Due five years through ten years	1,741	1,681
Due after ten years	<u>3,192</u>	<u>3,194</u>
	<u>\$ 14,132</u>	<u>\$ 13,974</u>

PIONEER BANKSHARES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 5 INVESTMENT SECURITIES: (Continued):

Securities available for sale with an amortized cost of \$45,000 and \$74,000 and fair value of \$45,000 and \$74,000 at December 31, 2018 and 2017, respectfully, were pledged to secure public deposits and for other purposes required by law.

Management recognizes that current economic conditions and market trends may result in other than temporary impairment on securities in the Company's portfolio. Management's evaluation of the individual securities within the investment portfolio is performed on a quarterly basis and assesses the unrealized loss positions that exist to determine whether there is potential other than temporary impairment. The key factors considered during this evaluation process are the amount of unrealized loss, percentage decline in value, length of time in loss position, near-term prospects of the issuer, current market activity, financial strength ratings from industry reports, credit quality, credit ratings, as well as management's intent and ability to hold securities until such time that they can recover in value and further assessment and determination that the institution will not be required to sell such investments to meet operational cash flow needs in the near future. In analyzing an issuer's financial condition, management also 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. As of December 31, 2018 and 2017, the Company's evaluation concluded there was no other-than-temporary impairment present.

As of December 31, 2018, there were 21 securities available for sale that had unrealized losses, which were considered to be temporary. The schedule of unrealized losses on these securities by category and length of time that individual securities have been in a continuous loss position was as follows (in thousands):

		<u>Mortgaged Backed Securities</u>	<u>Agency Securities</u>	<u>State and Municipal Securities</u>	<u>US Treasury Securities</u>	<u>Total</u>
Less than 12 Months	Fair Value	\$ 1,371	\$---	\$ 161	\$ ---	\$1,532
	Unrealized Losses	(2)	---	(1)	---	(3)
More than 12 Months	Fair Value	1,141	2,929	1,103	3,525	8,698
	Unrealized Losses	(31)	(71)	(9)	(56)	(167)
Total	Fair Value	2,512	2,929	1,264	3,525	10,230
	Unrealized Losses	(33)	(71)	(10)	(56)	(170)

PIONEER BANKSHARES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 5 INVESTMENT SECURITIES: (Continued):

As of December 31, 2017, there were 22 securities available for sale that had unrealized losses, which were considered to be temporary. The schedule of unrealized losses on these securities by category and length of time that individual securities have been in a continuous loss position was as follows (in thousands):

		<u>Mortgaged Backed Securities</u>	<u>Agency Securities</u>	<u>State and Municipal Securities</u>	<u>US Treasury Securities</u>	<u>Equity Securities</u>	<u>Total</u>
Less than 12 Months	Fair Value	\$ 887	\$ 3,008	\$ 1,797	\$ 3,947	\$ 819	\$10,458
	Unrealized Losses	(4)	(25)	(16)	(27)	(3)	(75)
More than 12 Months	Fair Value	548	---	---	83	---	631
	Unrealized Losses	(18)	---	---	(16)	---	(34)
Total	Fair Value	1,435	3,008	1,797	4,030	819	11,089
	Unrealized Losses	(22)	(25)	(16)	(43)	(3)	(109)

The Bank also holds additional investments in the Federal Home Loan Bank of Atlanta (“FHLB”) in the form of FHLB stock, which is a membership requirement. Loan advances from FHLB are subject to additional stock purchase requirements, which are generally redeemed as outstanding loan balances are repaid, subject to FHLB’s quarterly excess capital evaluation process. FHLB evaluates the excess capital stock of its members on a quarterly basis to determine stock repurchase activities. Additionally, the FHLB generally pays quarterly dividends on the outstanding stock investment of each of its members.

FHLB stock is generally viewed as a long term investment and is considered to be a restricted security, which is carried at cost, because there is no market for the stock other than FHLB or other member institutions. As of December 31, 2018 and 2017 the Bank’s investment in FHLB stock totaled approximately \$428,000 and \$580,000, respectively, and was included in restricted securities on the consolidated balance sheets.

Management’s evaluation of FHLB stock for possible impairment is based on the ultimate recoverability of par value rather than recognizing temporary declines in value. Management’s evaluation of FHLB stock as of December 31, 2018 and 2017 did not consider this investment to be other than temporarily impaired, and therefore, no impairment has been recognized.

PIONEER BANKSHARES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 6 LOANS:

Loans are stated at their face amount, net of deferred loan fees, and are classified as follows:

	December 31, 2018	December 31, 2017
	(In Thousands)	
Real estate loans		
Construction & land loans	\$ 6,440	\$ 5,459
Residential equity lines of credit	1,343	1,486
Residential 1-4 family	61,236	64,333
Residential second mortgages 1 - 4 family	2,600	1,575
Residential multifamily	5,350	5,420
Commercial agricultural loans	4,179	4,153
Commercial municipal loans	228	160
Commercial owner & non-owner occupied	53,879	51,389
Total real estate loans	<u>135,255</u>	<u>133,975</u>
Commercial non real estate loans	10,192	9,241
Consumer non real estate loans		
Personal installments	23,251	19,027
Credit cards	<u>651</u>	<u>721</u>
Total consumer installment loans	23,902	19,748
Gross loans ⁽¹⁾	<u>169,349</u>	<u>162,964</u>
Less allowance for loan losses	<u>(2,148)</u>	<u>(2,005)</u>
Net loans receivable	<u>\$ 167,201</u>	<u>\$ 160,959</u>

(1)Gross loans are presented net of deferred loan fees and discounts of \$392,000 and \$222,000 respectively for December 31, 2018 and 2017.

The Bank grants commercial, real estate and consumer installment loans to its customers. Collateral requirements for loans are determined on a case by case basis depending upon the purpose of the loan and the financial condition of the borrower. The ultimate collectability of the Bank's loan portfolio and the ability to realize the value of any underlying collateral, if needed, are influenced by the economic conditions of its market service area.

The Bank's loan portfolio is concentrated in real estate loans, including those secured by residential consumer properties and small business commercial properties. The residential real estate loans, including equity lines of credit, residential 1 – 4 family first and second mortgages, and multifamily loans totaled \$70.5 million as of December 31, 2018 as compared to \$72.8 million at December 31, 2017. The small business commercial real estate loans, including commercial construction and land loans, agricultural/farm loans, and other business properties totaled \$62.9 million as of December 31, 2018 as compared to \$60.2 million at December 31, 2017. Management has established specific lending criteria relating to real estate loans as a means of assessing the risk inherent in the portfolio.

Deposit account overdrafts are also classified as loans and totaled \$48,000 and \$45,000 as of December 31, 2018 and 2017, respectively.

PIONEER BANKSHARES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 6 LOANS: (continued)

The following table reflects the detailed breakdown of impaired loans with and without a recorded allowance by loan class for the year ended December 31, 2018 (in thousands):

Impaired Loans with a Recorded Allowance <u>December 31, 2018</u>	<u>Recorded Investment</u>	<u>Unpaid Principal</u>	<u>Related Allowance</u>	<u>Average Recorded Investment</u>	<u>Interest Income Recognized</u>
Residential Real Estate 1-4 Family Residences	\$ 183	\$ 183	\$ 32	\$ 192	\$ ---
Commercial Real Estate Owner Occupied	932	932	195	446	46
Commercial – Non Real Estate Industrial loans	---	---	---	22	---
Totals	<u>\$ 1,115</u>	<u>\$ 1,115</u>	<u>\$ 227</u>	<u>\$ 660</u>	<u>\$ 46</u>

Impaired Loans without a Recorded Allowance <u>December 31, 2018</u>	<u>Recorded Investment</u>	<u>Unpaid Principal</u>	<u>Average Recorded Investment</u>	<u>Interest Income Recognized</u>
Construction & Land Loans Commercial	\$ ---	\$ ---	\$ 195	\$ ---
Other – land only	---	---	8	---
Residential Real Estate 1-4 Family Residences	2,061	2,061	2,098	68
Commercial Real Estate Owner Occupied	3,169	3,169	3,855	167
Non-owner Occupied	250	250	254	15
Agricultural Loans	229	229	230	--
Commercial – Non Real Estate Industrial loans	237	237	216	5
Totals	<u>\$ 5,946</u>	<u>\$ 5,946</u>	<u>\$6,856</u>	<u>\$ 255</u>

PIONEER BANKSHARES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 6 LOANS: (continued)

The following table reflects the detailed breakdown of impaired loans with and without a recorded allowance by loan class for the year ended December 31, 2017 (in thousands):

Impaired Loans with a Recorded Allowance <u>December 31, 2017</u>	<u>Recorded Investment</u>	<u>Unpaid Principal</u>	<u>Related Allowance</u>	<u>Average Recorded Investment</u>	<u>Interest Income Recognized</u>
Residential Real Estate					
1-4 Family Residences	\$ 201	\$ 201	\$ 38	\$ 236	\$ ---
Commercial Real Estate					
Owner Occupied	---	---	---	252	--
Commercial – Non Real Estate					
Industrial loans	<u>43</u>	<u>43</u>	<u>21</u>	<u>116</u>	<u>---</u>
Totals	<u>\$ 244</u>	<u>\$ 244</u>	<u>\$ 59</u>	<u>\$ 604</u>	<u>\$ ---</u>
Impaired Loans without a Recorded Allowance <u>December 31, 2017</u>	<u>Recorded Investment</u>	<u>Unpaid Principal</u>	<u>Average Recorded Investment</u>	<u>Interest Income Recognized</u>	
Construction & Land Loans					
Commercial	\$ 389	\$ 389	\$ 437	\$ ---	
Other – land only	16	16	17	2	
Residential Real Estate					
1-4 Family Residences	2,134	2,134	2,360	66	
Commercial Real Estate					
Owner Occupied	4,541	4,541	3,959	181	
Non-owner Occupied	258	258	262	15	
Agricultural Loans	230	230	251	--	
Commercial – Non Real Estate					
Industrial loans	<u>194</u>	<u>194</u>	<u>198</u>	<u>4</u>	
Totals	<u>\$ 7,762</u>	<u>\$ 7,762</u>	<u>\$7,484</u>	<u>\$ 268</u>	

PIONEER BANKSHARES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 6 LOANS: (continued)

The following table reflects the amounts of outstanding delinquencies by loan class as of December 31, 2018 (in thousands):

<u>Past Due Loans by Class</u>	<u>30-59 Days</u>	<u>60-89 Days</u>	<u>90 Days or More</u>	<u>Total Past Due</u>	<u>Total Current</u>	<u>Total Loans</u>
Construction & Land Loans						
Residential	\$ ---	\$ ---	\$ ---	\$ ---	\$ 1,787	\$ 1,787
Commercial	---	---	---	---	423	423
Other – Land only	---	---	---	---	4,230	4,230
Residential Real Estate						
Equity Lines of Credit	---	---	62	62	1,281	1,343
1-4 Family Residences	2,759	674	86	3,519	60,317	63,836
Multifamily Dwellings	---	---	---	---	5,350	5,350
Commercial Real Estate						
Owner occupied	379	---	431	810	39,811	40,621
Non-owner occupied	---	---	---	---	13,258	13,258
Agricultural / Farm loans	---	---	---	---	4,179	4,179
Municipals	---	---	---	---	228	228
Commercial – Non Real Estate						
Agricultural	5	---	---	5	215	220
Industrial	78	---	---	78	9,377	9,455
Municipals	---	---	---	---	517	517
Consumer – Non Real Estate						
Credit Cards	6	1	1	8	643	651
Automobile loans	758	272	185	1,215	15,413	16,628
Other personal loans	<u>78</u>	<u>7</u>	<u>54</u>	<u>139</u>	<u>6,484</u>	<u>6,623</u>
Totals Gross Loans	<u>\$ 4,063</u>	<u>\$ 954</u>	<u>\$ 819</u>	<u>\$ 5,836</u>	<u>\$ 163,513</u>	<u>\$ 169,349</u>

PIONEER BANKSHARES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 6 LOANS: (continued)

The following table reflects the amounts of outstanding delinquencies by loan class as of December 31, 2017 (in thousands):

<u>Past Due Loans by Class</u>	<u>30-59 Days</u>	<u>60-89 Days</u>	<u>90 Days or More</u>	<u>Total Past Due</u>	<u>Total Current</u>	<u>Total Loans</u>
Construction & Land Loans						
Residential	\$ ---	\$ ---	\$ ---	\$ ---	\$ 926	\$ 926
Commercial	---	---	---	---	1,154	1,154
Other – Land only	55	---	---	55	3,324	3,379
Residential Real Estate						
Equity Lines of Credit	---	40	---	40	1,446	1,486
1-4 Family Residences	2,895	909	198	4,002	61,906	65,908
Multifamily Dwellings	---	---	---	---	5,420	5,420
Commercial Real Estate						
Owner occupied	40	---	---	40	36,373	36,413
Non-owner occupied	---	---	---	---	14,976	14,976
Agricultural / Farm loans	---	---	---	---	4,153	4,153
Municipals	---	---	---	---	160	160
Commercial – Non Real Estate						
Agricultural	---	---	---	---	169	169
Industrial	85	21	6	112	8,884	8,996
Municipals	---	---	---	---	76	76
Consumer – Non Real Estate						
Credit Cards	12	5	13	30	691	721
Automobile loans	647	132	140	919	12,561	13,480
Other personal loans	<u>119</u>	<u>18</u>	<u>16</u>	<u>153</u>	<u>5,394</u>	<u>5,547</u>
Totals Gross Loans	<u>\$ 3,853</u>	<u>\$ 1,125</u>	<u>\$ 373</u>	<u>\$ 5,351</u>	<u>\$ 157,613</u>	<u>\$ 162,964</u>

PIONEER BANKSHARES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 6 LOANS: (continued)

The following table represents loans 90 days delinquent and still accruing interest and loans in a nonaccrual status as of December 31, 2018 by loan class (in thousands):

	<u>90 days past due & still accruing interest</u>	<u>Nonaccrual Loans</u>
Construction & Land Loans		
Other- Land Only	\$ ---	\$ 13
Residential Real Estate		
Equity Lines of Credit	61	---
1-4 Family Residences	86	1,174
Commercial Real Estate		
Owner occupied	---	1,092
Agricultural / Farm loans	---	229
Commercial Non-Real Estate		
Industrial	---	67
Consumer – Non Real Estate		
Automobile loans	186	---
Other personal loans	<u>44</u>	<u>10</u>
Totals Gross Loans	<u>\$ 377</u>	<u>\$ 2,585</u>

The following table represents loans 90 days delinquent and still accruing interest and loans in a nonaccrual status as of December 31, 2017 by loan class (in thousands):

	<u>90 days past due & still accruing interest</u>	<u>Nonaccrual Loans</u>
Construction & Land Loans		
Commercial	\$ ---	\$ 389
Other- Land Only	---	18
Residential Real Estate		
1-4 Family Residences	198	1,254
Commercial Real Estate		
Owner occupied	---	644
Agricultural / Farm loans	---	230
Commercial Non-Real Estate		
Industrial	6	134
Consumer – Non Real Estate		
Automobile loans	140	---
Other personal loans	<u>16</u>	<u>---</u>
Totals Gross Loans	<u>\$ 360</u>	<u>\$ 2,669</u>

PIONEER BANKSHARES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 6 LOANS: (continued)

Loans past due greater than 90 days and still accruing interest at December 31, 2018 and 2017 totaled \$377,000 and \$360,000, respectively. Management continually monitors past due accounts and places these accounts in nonaccrual status if the payment plans are not adhered to. Nonaccrual loans excluded from impaired loan disclosure amounted to \$219,000 and \$241,000, at December 31, 2018 and 2017, respectively. The nonaccrual loans excluded from impaired loan disclosure at December 31, 2018 and 2017 consisted of several real estate and consumer loans which were in the process of collection.

The loan portfolio is comprised of various categories or segments, each of which have certain risk characteristics that are evaluated at the time of loan origination and periodically thereafter. Construction loans carry risks associated with whether or not the project will be completed according to schedule and within its original budget, as well as valuation risk associated with the overall value of the collateral upon completion. Residential real estate loans carry risks associated with continued credit-worthiness and financial stability of the borrower, as well as potential valuation changes relating to collateral. Commercial real estate loans carry risks associated with the continued operations of the business, as well as sufficient cash flow and profitability to service the debt. Additionally, commercial real estate loans are subject to risks associated with potential collateral valuation changes.

Commercial non-real estate loans, including those in the industrial and agricultural categories, carry similar risks to the commercial real estate loans, as they are dependent upon the continued successful business operations and cash flow. Commercial non-real estate loans also carry a risk associated with collateral being more difficult to assess. Consumer loans carry risks associated with the continued credit-worthiness and financial stability of the borrower, as well as potential for rapid depreciation or reduced value of the collateral, especially in automobile lending.

Management has developed an internal loan risk rating system as part of its credit analysis process which serves as the credit quality indicator for loans in the portfolio. Non-retail loans (i.e. all loans, excluding loans to consumers for home mortgages or other consumer purposes) are assigned an appropriate risk rating at the time of origination based on specific assessment factors relating to the borrower's ability to meet contractual obligations under the loan agreement. This process includes reviewing borrowers' financial information, historical payment experience, credit documentation, public information, and other information specific to each borrower. Loan rating assessments also include consideration of business cash flow and debt obligations. Risk ratings are generally reviewed on an annual basis for credit relationships with total credit exposure of \$500,000 or more, or at any point management becomes aware of information affecting the borrower's ability to fulfill their obligations. Management utilizes both internal and external loan review processes as a means of monitoring the appropriateness of risk ratings across the loan portfolio. Retail credits are assigned a pass rating at the time of their origination. Updates to risk ratings assigned to retail credits are made primarily on the basis of the payment activity.

The Bank's internal rating system includes multiple ratings considered to be indicative of pass rated credits, as well as several non-pass or classified ratings consisting of special mention, substandard, doubtful, and loss. Pass credits generally consist of loans secured by cash or cash equivalents and loans to borrowers with a strong cash flow ratio, stable financial net worth and above average sources of liquidity to meet financial obligations and may also include loans to borrowers that may have minor, yet manageable, weaknesses related to the stability of cash flow and repayment sources and may require periodic monitoring. Special mention credits are loans that have identified weaknesses or adverse trends in the borrower's financial position that could potentially impact the Bank's credit position at some future date if not monitored closely. Substandard credits are those loans that have been identified as having a well-defined, specific, or major weakness in the primary cash flow sources or upon which significant reliance is being placed on secondary sources of repayment due to the borrower's financial difficulties. Potential for losses related to substandard credits is evaluated on a regular basis with specific allocations being made as needed, as well as other corrective actions necessary to protect the institution. Loans categorized as doubtful also have well defined weaknesses with the added characteristic of the likelihood that collection of payment in full is highly questionable or perhaps improbable. Loans classified as loss are considered to be totally uncollectible or of such little value that their continuance on the Bank's books as an asset is not warranted. Retail credits 60-89 days past due and those 90 or more days past due are disclosed as special mention and substandard, respectively.

PIONEER BANKSHARES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 6 LOANS: (continued)

The following tables represent summaries of the Bank's loan portfolio by class and credit quality indicator as of December 31, 2018 (in thousands):

	<u>Pass</u>	<u>Special Mention</u>	<u>Substandard</u>	<u>Doubtful</u>	<u>Loss</u>	<u>Total Loans</u>
Construction & Land Loans						
Residential	\$ 1,787	\$ ---	\$ ---	\$ ---	\$ ---	\$ 1,787
Commercial	423	---	---	---	---	423
Other – Land only	4,230	---	---	---	---	4,230
Residential Real Estate						
Equity Lines of Credit	1,281	---	62	---	---	1,343
1-4 Family Residences	62,232	786	818	---	---	63,836
Multifamily Dwellings	5,350	---	---	---	---	5,350
Commercial Real Estate						
Owner occupied	32,699	3,923	3,999	---	---	40,621
Non-owner occupied	10,276	2,732	250	---	---	13,258
Agricultural / Farm loans	2,895	1,055	229	---	---	4,179
Municipals	228	---	---	---	---	228
Commercial – Non Real Estate						
Agricultural	220	---	---	---	---	220
Industrial	9,201	16	238	---	---	9,455
Municipals	517	---	---	---	---	517
Consumer – Non Real Estate						
Credit Cards	649	1	1	---	---	651
Automobile loans	16,171	272	185	---	---	16,628
Other personal loans	<u>6,562</u>	<u>7</u>	<u>54</u>	<u>---</u>	<u>---</u>	<u>6,623</u>
Totals Gross Loans	<u>\$154,721</u>	<u>\$8,792</u>	<u>\$ 5,836</u>	<u>\$ ---</u>	<u>\$ ---</u>	<u>\$ 169,349</u>

PIONEER BANKSHARES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 6 LOANS: (continued)

The following tables represent summaries of the Bank's loan portfolio by class and credit quality indicator as of December 31, 2017 (in thousands):

	<u>Pass</u>	<u>Special Mention</u>	<u>Substandard</u>	<u>Doubtful</u>	<u>Loss</u>	<u>Total Loans</u>
Construction & Land Loans						
Residential	\$ 926	\$ ---	\$ ---	\$ ---	\$ ---	\$ 926
Commercial	765	---	389	---	---	1,154
Other – Land only	3,360	19	---	---	---	3,379
Residential Real Estate						
Equity Lines of Credit	1,446	40	---	---	---	1,486
1-4 Family Residences	64,054	909	945	---	---	65,908
Multifamily Dwellings	5,420	---	---	---	---	5,420
Commercial Real Estate						
Owner occupied	28,030	4,526	3,857	---	---	36,413
Non-owner occupied	14,718	---	258	---	---	14,976
Agricultural / Farm loans	2,824	1,099	230	---	---	4,153
Municipals	160	---	---	---	---	160
Commercial – Non Real Estate						
Agricultural	169	---	---	---	---	169
Industrial	8,749	75	172	---	---	8,996
Municipals	76	---	---	---	---	76
Consumer – Non Real Estate						
Credit Cards	703	5	13	---	---	721
Automobile loans	13,208	132	140	---	---	13,480
Other personal loans	<u>5,513</u>	<u>18</u>	<u>16</u>	---	---	<u>5,547</u>
Totals Gross Loans	<u>\$150,121</u>	<u>\$6,823</u>	<u>\$ 6,020</u>	<u>\$ ---</u>	<u>\$ ---</u>	<u>\$ 162,964</u>

PIONEER BANKSHARES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 6 LOANS: (continued)

Loans classified as troubled debt restructurings are monitored for payment default on an on-going basis. There were 3 accounts that defaulted within 12 months of the original modification date during the year ended December 31, 2018. Those accounts consisted of one commercial real estate loan in the amount of \$309,000 and two commercial non-real estate accounts totaling \$56,000. There were no accounts that defaulted within 12 months of the original modification date during the year ended December 31, 2017. The Bank defines default as those accounts having payments 90 days or more past due as of December 31, 2018 and December 31, 2017.

At December 31, 2018, there were a total of \$3.4 million in loans classified as troubled debt restructurings. There were no accounts added to the troubled debt restructuring category during 2018. There were approximately \$1.6 million in restructured loan balances classified as performing and in compliance with their modified terms at December 31, 2018. Restructured loans classified as nonperforming based on their past due or nonaccrual status at December 31, 2018 totaled \$1.8 million. There were unfunded commitments in the amount of \$40,000 for loans classified as troubled debt restructures as of December 31, 2018.

At December 31, 2017, there were a total of \$5.0 million in loans classified as troubled debt restructurings, with approximately \$781,000 being loans that were modified during 2017. There were approximately \$3.0 million in restructured loan balances classified as performing and in compliance with their modified terms at December 31, 2017. Restructured loans classified as nonperforming based on their past due or nonaccrual status at December 31, 2017 totaled \$2.0 million. Loans modified and classified as troubled debt restructurings during the reporting period ending December 31, 2017 are reported in the table below. These loans are also included in the impaired loan disclosures previously presented within this report.

(Dollars in thousands)

	Number of TDR modifications	Pre- modification outstanding recorded investment	Post- modification outstanding recorded investment
Commercial non real estate – industrial	2	\$56	\$56
Commercial real estate – owner occupied	2	\$639	\$726
Total	<u>4</u>	<u>\$ 695</u>	<u>\$782</u>

PIONEER BANKSHARES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 7 ALLOWANCE FOR LOAN LOSSES (ALLL):

The summary table below includes the allowance allocations and total loans evaluated both individually and collectively for impairment, as well as a roll-forward representation of the activity that has occurred in the allowance account during the period ending December 31, 2018 (in thousands):

	Construction & Land Loans	Residential Real Estate	Commercial Real Estate	Commercial Non-Real Estate	Consumer Non-Real Estate	Total
ALLL ending balance 12/31/2017	<u>\$ 31</u>	<u>\$ 700</u>	<u>\$ 589</u>	<u>\$ 97</u>	<u>\$ 588</u>	<u>\$ 2,005</u>
Charge-offs	---	---	(13)	---	(439)	(452)
Recoveries	---	5	17	4	215	241
Provision	<u>8</u>	<u>(57)</u>	<u>159</u>	<u>(27)</u>	<u>271</u>	<u>354</u>
ALLL ending Balance 12/31/2018	<u>\$ 39</u>	<u>\$ 648</u>	<u>\$ 752</u>	<u>\$ 74</u>	<u>\$ 635</u>	<u>\$ 2,148</u>
Evaluated individually for impairment	--	32	195	---	---	227
Evaluated collectively for impairment	39	616	557	74	635	1,921
Total Gross Loans 12/31/2018	<u>\$ 6,440</u>	<u>\$ 70,529</u>	<u>\$ 58,286</u>	<u>\$ 10,192</u>	<u>\$ 23,902</u>	<u>\$ 169,349</u>
Evaluated individually for impairment	---	2,244	4,580	237	---	7,061
Evaluated collectively for impairment	6,440	68,285	53,706	9,955	23,902	162,288

PIONEER BANKSHARES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 7 ALLOWANCE FOR LOAN LOSSES (ALLL): (continued)

The summary table below includes the allowance allocations and total loans evaluated both individually and collectively for impairment, as well as a roll-forward representation of the activity that has occurred in the allowance account during the period ending December 31, 2017 (in thousands):

	Construction & Land Loans	Residential Real Estate	Commercial Real Estate	Commercial Non-Real Estate	Consumer Non-Real Estate	Total
ALLL ending balance 12/31/2016	<u>\$ 31</u>	<u>\$ 660</u>	<u>\$ 598</u>	<u>\$ 179</u>	<u>\$ 554</u>	<u>\$ 2,022</u>
Charge-offs	---	(100)	---	(5)	(530)	(635)
Recoveries	---	60	---	18	156	234
Provision	---	<u>80</u>	<u>(9)</u>	<u>(95)</u>	<u>408</u>	<u>384</u>
ALLL ending Balance 12/31/2017	<u>\$ 31</u>	<u>\$ 700</u>	<u>\$ 589</u>	<u>\$ 97</u>	<u>\$ 588</u>	<u>\$ 2,005</u>
Evaluated individually for impairment	--	38	--	21	---	59
Evaluated collectively for impairment	31	662	589	76	588	1,946
Total Gross Loans 12/31/2017	<u>\$ 5,459</u>	<u>\$ 72,814</u>	<u>\$ 55,702</u>	<u>\$ 9,241</u>	<u>\$ 19,748</u>	<u>\$ 162,964</u>
Evaluated individually for impairment	405	2,335	5,029	237	---	8,006
Evaluated collectively for impairment	5,054	70,479	50,673	9,004	19,748	154,958

PIONEER BANKSHARES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 8 **BANK PREMISES and EQUIPMENT:**

Bank premises, equipment and computer software included in the financial statements at December 31, 2018 and 2017 are as follows:

	<u>2018</u>	<u>2017</u>
	(In Thousands)	
Land	\$ 1,627	\$ 1,627
Land improvements and buildings	6,017	5,856
Furniture and equipment	5,789	5,604
Computer software	<u>1,777</u>	<u>1,667</u>
	15,210	14,754
Less accumulated depreciation	<u>10,379</u>	<u>10,123</u>
Net	<u>\$ 4,831</u>	<u>\$ 4,631</u>

Depreciation and amortization related to bank premises, equipment and software included in operating expense was \$333,000 and \$327,000 for December 31, 2018 and 2017, respectively.

NOTE 9 **LEASE COMMITMENTS:**

The Company has a lease commitment relating to its Charlottesville branch location. The lease agreement term for this branch has an expiration date of May 31, 2023. The Company's future minimum rental payments as required under the remaining non-cancelable lease terms as of December 31, 2018, were as follows:

	(In Thousands)
2019	\$ 67
2020	69
2021	70
2022	72
2023	<u>30</u>
TOTAL:	<u>\$ 308</u>

Lease expense, included in occupancy expense, was \$53,000 and \$44,000 for the years ending in December 31, 2018 and 2017, respectively.

PIONEER BANKSHARES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 10 DEPOSITS:

The Bank's total deposit portfolio consists primarily of demand checking accounts, savings accounts and time deposit accounts. Total deposits were \$177.5 million and \$166.9 million as of December 31, 2018 and 2017, respectively. CDARs deposits included in this total were \$3.3 million and \$10.2 million as of December 31, 2018 and 2017, respectively. Customer time deposit balances that met or exceeded the \$250,000 FDIC insurance limit totaled \$4.5 million and \$3.9 million as of December 31, 2018 and 2017, respectively. At December 31, 2018, time deposit scheduled maturities (in thousands) are as follows:

2019	\$	23,400
2020		10,295
2021		6,306
2022		6,282
2023		627
Thereafter		<u>66</u>
Total	\$	<u>46,976</u>

The Bank has one customer with large deposit balances exceeding 5% of total deposits as of December 31, 2018. The total deposit balances for this customer as of December 31, 2018 were \$18.0 million or 10.16% of total deposits.

NOTE 11 BORROWINGS:

The Bank has a line of credit with the Federal Home Loan Bank of Atlanta upon which credit advances can be made up to 40% of total Bank assets, subject to certain eligibility requirements. This represents a total credit line of approximately \$83.6 million and \$79.2 million as of December 31, 2018 and 2017, respectively. FHLB advances bear interest at a fixed or floating rate depending on the terms and maturity of each advance and numerous renewal options are available. These advances are secured by first lien 1-4 family residential mortgages totaling \$61.2 million at December 31, 2018. On certain fixed rate advances, the FHLB may convert the advance to an indexed floating rate at some set point in time for the remainder of the term. If the advance converts to a floating rate, the Bank may repay all or part of the advance without a prepayment penalty. At December 31, 2018 and December 31, 2017, total outstanding borrowings with FHLB were \$5.9 million and \$7.5 million, respectively. Outstanding FHLB advances at December 31, 2018 consisted of two fixed rate advances of \$3.4 million and \$2.5 million carrying interest rates of 1.36% and 3.37%, respectively. The \$2.5 million advance requires quarterly interest payments with the full amount of principal due at maturity in December 2028. The \$3.4 million advance matures in January 2021 and requires monthly interest payments with quarterly principal payments. The remaining scheduled principal repayments on this advance at December 31, 2018 were as follows:

(In thousands)	
Due in 2019	\$ 1,500
Due in 2020	1,500
Due in 2021	<u>375</u>
Total	<u>\$ 3,375</u>

The Bank also has available credit lines with other correspondent banks totaling \$14.0 million, which can be used for short-term liquidity purposes, if necessary. Any funds borrowed on these credit lines are required to be repaid within 7 to 30 consecutive business days. The interest rate on such borrowings is set in accordance with the then current daily market rate. As of December 31, 2018, there were no outstanding borrowings against these credit facilities.

PIONEER BANKSHARES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 12 DIVIDEND LIMITATION ON SUBSIDIARY BANK:

A principal source of funds of the Company is dividend transfers paid by the Bank. The amount of dividends the Bank may pay to the Company is regulated by the Federal Reserve. As of December 31, 2018, the maximum amount of dividends the Bank could pay to the Company was \$4.3 million or 14.86% of the consolidated net assets, without requesting permission from the Federal Reserve Bank. There are additional regulatory guidelines, which establishes further limitations for banks based on quarterly earnings.

NOTE 13 INCOME TAXES:

The Company files income tax returns in the U.S. federal jurisdiction and the state of Virginia. The Company is no longer subject to U.S. federal, state and local income tax examinations by tax authorities for years prior to 2015. The components of income tax expense are as follows:

	<u>2018</u>	<u>2017</u>
	(In Thousands)	
Current income tax expense	\$ 220	\$ 732
Deferred income tax (benefit) expense	(18)	40
Deferred tax asset adjustment for enacted change in tax rate	---	<u>222</u>
	<u>\$ 202</u>	<u>\$ 994</u>

The results for the year ended December 31, 2017 include the effect of the Tax Cuts and Jobs Act (the Act), which was signed into law on December 22, 2017. Among other things, the Act permanently lowered the federal corporate income tax rate to 21% from the maximum rate prior to the passage of the Act of 35%, effective January 1, 2018. As a result of the reduction of the federal corporate income tax rate, U.S. GAAP required companies to re-measure their deferred tax assets and deferred tax liabilities, including those accounted for in accumulated other comprehensive income, as of the date of the Act's enactment and record the corresponding effects in income tax expense. As a result of the permanent reduction in the corporate income tax rate, the Company recognized a \$222,000 reduction in the value of its net deferred tax asset and recorded a corresponding incremental income tax expense of \$222,000 in the Company's consolidated results of operations for the fourth quarter of 2017. The Company's evaluation of the effect of the Act was subject to refinement for up to one year after enactment.

The reasons for the differences between income tax expense and the amount computed by applying the statutory federal income tax rate are as follows:

	<u>2018</u>	<u>2017</u>
	(In Thousands)	
Income taxes computed at the applicable federal income tax rate	\$ 510	\$ 1,032
Increase (decrease) resulting from:		
Tax-exempt income and dividends	(18)	(38)
Low income housing investments	(315)	(267)
Impact of enacted change in tax rate	---	222
Other	<u>25</u>	<u>45</u>
Income Tax Expense	<u>\$ 202</u>	<u>\$ 994</u>

PIONEER BANKSHARES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 13 INCOME TAXES: (continued)

At December 31, the net deferred tax asset was made up of the following:

	<u>2018</u>	<u>2017</u>
	(In Thousands)	
Deferred Tax Assets:		
Allowance for loan losses	\$ 347	\$ 309
Other real estate owned	11	60
Nonaccrual interest	172	202
Securities available for sale	33	---
Deferred loan fees	70	26
Other	<u>3</u>	<u>3</u>
Total	\$ <u>636</u>	\$ <u>600</u>
Deferred Tax Liabilities:		
Depreciation	\$ 121	\$ 91
Cash surrender value of life insurance	44	42
Securities available for sale	---	30
Goodwill	76	76
Other	<u>7</u>	<u>3</u>
Total	\$ <u>248</u>	\$ <u>242</u>
Net Deferred Tax Assets	\$ <u><u>388</u></u>	\$ <u><u>358</u></u>

NOTE 14 REGULATORY MATTERS:

The Bank is subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory, and possibly additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Bank must meet specific capital guidelines that involve quantitative measures of assets, liabilities, and certain off-balance sheet items as calculated under regulatory accounting practices. The Bank's capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

The regulatory capital requirements under Basel III became effective January 1, 2015, with full compliance with all of the requirements to be phased in over a multi-year schedule, and fully phased in by January 1, 2019. As part of the requirements, the Common Equity Tier I Capital ratio is calculated and utilized in the assessment of capital for all institutions. In addition, a capital conservation buffer must be maintained in excess of the minimum capital requirements to allow an institution to avoid restrictions on dividend payments, share repurchase transactions, and discretionary bonus payments. The capital conservation buffer requirement began its phase-in on January 1, 2016, at 0.625% of risk-weighted assets, and increased by the same percentage in each successive year until fully implemented at 2.5% on January 1, 2019. The capital conservation buffer is applicable to all ratios with the exception of the leverage ratio, which is noted below as Tier I Capital to Average Assets.

The quantitative measures established by regulation ensure capital adequacy and require the Bank to maintain minimum amounts and ratios as set forth in the table below. Management believes, as of December 31, 2018 and 2017, the Bank met all capital adequacy requirements to which it was subject. As of December 31, 2018, the most recent notification from the Bank's primary federal regulator categorized the Bank as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized the Bank must maintain minimum total risk-based, Tier I risk-based, Common Equity Tier I, and Tier I leverage ratios as set forth in the table. The Bank's actual capital amounts and ratios are also presented below:

PIONEER BANKSHARES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 14 REGULATORY MATTERS: (continued)

	<u>Actual</u>		<u>For Capital Adequacy Purposes</u>		<u>Minimum To Be Well Capitalized</u>	
	<u>Amount</u>	<u>Ratio</u>	<u>Amount</u>	<u>Ratio</u>	<u>Amount</u>	<u>Ratio</u>
As of December 31, 2018:						
Total Capital to Risk Weighted Assets:						
Pioneer Bank	\$ 25,924	16.3%	\$ 12,713	≥ 8.0%	\$ 15,891	≥10.0%
Tier I Capital to Risk Weighted Assets:						
Pioneer Bank	\$ 23,936	15.1%	\$ 9,535	≥ 6.0%	\$ 12,713	≥ 8.0%
Common Equity Tier I Capital to Risk Weighted Assets:						
Pioneer Bank	\$ 23,936	15.1%	\$ 7,151	≥ 4.5%	\$ 10,329	≥ 6.5%
Tier I Capital to Average Assets:						
Pioneer Bank	\$ 23,936	11.7%	\$ 8,214	≥ 4.0%	\$ 10,267	≥ 5.0%
As of December 31, 2017:						
Total Capital to Risk Weighted Assets:						
Pioneer Bank	\$ 23,427	15.8%	\$ 11,882	≥ 8.0%	\$ 14,853	≥10.0%
Tier I Capital to Risk Weighted Assets:						
Pioneer Bank	\$ 21,569	14.5%	\$ 8,912	≥ 6.0%	\$ 11,882	≥ 8.0%
Common Equity Tier I Capital to Risk Weighted Assets:						
Pioneer Bank	\$ 21,569	14.5%	\$ 6,684	≥ 4.5%	\$ 9,654	≥ 6.5%
Tier I Capital to Average Assets:						
Pioneer Bank	\$ 21,569	10.9%	\$ 7,914	≥ 4.0%	\$ 9,893	≥ 5.0%

NOTE 15 EARNINGS PER SHARE:

The following shows the weighted average number of shares used in computing earnings per share and the dilutive effect of potential common stock. Potential dilutive common stock had no effect on income available to common shareholders.

	<u>2018</u>		<u>2017</u>	
	<u>Weighted Average Shares</u>	<u>Per Share Amount</u>	<u>Weighted Average Shares</u>	<u>Per Share Amount</u>
Basic earnings per share	975,427	<u>\$2.29</u>	971,408	<u>\$ 2.10</u>
Effect of dilutive securities:				
Stock options	----		----	
Diluted earnings per share	<u>975,427</u>	<u>\$ 2.29</u>	<u>971,408</u>	<u>\$ 2.10</u>

There were no potentially dilutive securities outstanding during the year ended December 31, 2018. For 2017, all average outstanding option shares were excluded from the computation of diluted earnings per share because their effects were anti-dilutive.

PIONEER BANKSHARES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 16 OFF-BALANCE SHEET COMMITMENTS:

The contract or notional amount of financial instruments with off-balance sheet risks are as follows:

	December 31,	
	2018	2017
	(In Thousands)	
Unfunded lines of credit (commercial and personal)	\$ 7,718	\$ 5,058
Loan commitments and letters of credit (commercial and personal)	5,799	6,299
Credit card unused credit limits	1,606	1,448

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Bank evaluates each customer's credit worthiness on a case-by-case basis. The amount of collateral obtained, if it is deemed necessary by the Bank, is based on management's credit evaluation of the counter-party.

Unfunded commitments under commercial lines of credit, revolving credit lines and overdraft protection agreements are commitments for possible future extensions of credit to existing customers. These lines of credit generally are un-collateralized and usually do not contain a specified maturity date and may not be drawn upon to the total extent to which the Bank is committed.

Commercial and standby letters of credit are conditional commitments issued by the Bank to guarantee the performance of a customer to a third party. Those letters of credit are primarily issued to support public and private borrowing arrangements. Essentially all letters of credit issued have expiration dates within one year. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. The Bank generally holds collateral supporting those commitments for which collateral is deemed necessary.

NOTE 17 TRANSACTIONS WITH RELATED PARTIES:

During the year, executive officers and directors (and companies controlled by them) were customers of and had transactions with the Company in the normal course of business. These transactions were made on substantially the same terms as those prevailing for other customers and did not involve any abnormal risk. Deposit account balances of executive officers and directors totaled \$23.7 million as of December 31, 2018 and \$20.8 million for the year ended December 31, 2017. Loan transactions, including all extensions of credit to such related parties are shown in the following schedule:

	2018	2017
	(In Thousands)	
Total loans, beginning of year	\$ 2,228	\$ 801
New loans	---	2,012
Payments	(89)	(585)
Total loans, end of year	\$ 2,139	\$ 2,228

PIONEER BANKSHARES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 18 **FAIR VALUE MEASUREMENTS:**

The Company uses fair value measurements to record fair value adjustments to certain assets and liabilities and to determine fair value disclosures. In accordance with the Fair Value Measurements and Disclosures topic of FASB ASC, the fair value of a financial instrument is the price (exit price) that would be received to sell an asset or paid to transfer the liability in the principal or most advantageous market for the asset or the liability in an orderly transaction between market participants at the measurement date. Fair value is best determined based upon quoted market prices. However, in many instances, there are no quoted market prices for the Company's various financial instruments. In cases where quoted market prices are not available, fair values are based on estimates using present value or other valuation techniques. Those techniques are significantly affected by the assumptions used, including the discount rate and estimates of future cash flows. Accordingly, the fair value estimates may not be realized in an immediate settlement of the instrument.

The fair value guidance provides a consistent definition of fair value, which focuses on exit price in the principal or most advantageous market for the asset or the liability and in an orderly transaction (that is, not a forced liquidation or distressed sale) between market participants at the measurement date under current market conditions. If there has been a significant decrease in the volume and level of activity for the asset or liability, a change in valuation technique or the use of multiple valuation techniques may be appropriate. In such instances, determining the price at which willing market participants would transact at the measurement date under current market conditions depends on the facts and circumstances and requires the use of significant judgment. The fair value is a reasonable point within the range that is most representative of fair value under current market conditions. U.S. GAAP requires that valuation techniques maximize the use of observable inputs and minimize the use of unobservable inputs.

In accordance with this guidance, the Company groups financial assets and financial liabilities generally measured at fair value into three levels, based on the markets in which the assets and liabilities are traded and the reliability of the assumptions used to determine the fair value.

Level 1 – Valuation is based on quoted prices in active markets for identical assets and liabilities.

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

Level 3 – Valuation is based on model-based techniques that use one or more significant inputs or assumptions that are unobservable in the market.

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

Securities available for sale: Securities available for sale are recorded at fair value on a recurring basis. Fair value measurement is based upon quoted market prices in active markets, when available (Level 1). 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 derived primarily from or corroborated by observable market data. Third party vendors compile prices from various sources and may determine the fair value of identical or similar securities by using pricing models that considers observable market data (Level 2).

Equity securities: Equity securities are recorded at fair value on a recurring basis. Fair values for equity securities are based upon quoted market prices for identical securities in active markets (Level 1) or quoted prices for identical securities in markets not deemed to be active due to the volume of shares transferred and frequency of trades (Level 2).

PIONEER BANKSHARES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 18 FAIR VALUE MEASUREMENTS (continued):

The following table presents the balances of financial assets measured at fair value on a recurring basis as of December 31, 2018 and December 31, 2017:

Description	Balances Outstanding (In Thousands)	Fair Value Measurements Using:		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
<u>As of December 31, 2018</u>				
U.S. treasury securities	\$ 3,525	\$ ---	\$ 3,525	\$ ---
Mortgage-backed Securities	4,359	---	4,359	---
Agency securities	3,929	---	3,929	---
State & Municipals	<u>2,161</u>	---	<u>2,161</u>	---
Total Available –for-sale securities	<u>\$ 13,974</u>	<u>\$ ---</u>	<u>\$ 13,974</u>	<u>\$ ---</u>
Equity Securities	\$ 357	\$ 352	\$ 5	\$ ---
<u>As of December 31, 2017</u>				
U.S. treasury securities	\$ 4,030	\$ ---	\$ 4,030	\$ ---
Mortgage-backed Securities	1,460	---	1,460	---
Agency securities	3,500	---	3,500	---
State & Municipals	2,322	---	2,322	---
Equity Securities	<u>4,984</u>	<u>4,984</u>	---	---
Total Available –for-sale securities	<u>\$ 16,296</u>	<u>\$ 4,984</u>	<u>\$ 11,312</u>	<u>\$ ---</u>

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

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

Impaired Loans: The Fair Value Measurement accounting standard also applies to loans measured for impairment including impaired loans measured at an observable market price (if available), or at the fair value of the loan’s collateral (if the loan is collateral dependent). Fair value of the loan’s collateral, when the loan is dependent on collateral, is determined by appraisals or independent valuation which is then adjusted for the cost related to liquidation of the collateral.

Loans are designated as impaired when, in the judgment of management based on current information and events, it is probable that all amounts according to the contractual terms of the loan agreement will not be collected when due. The measurement of loss associated with impaired loans can be based on either the observable market price of the loan or the fair value of the collateral. Fair value is measured based on the value of the collateral securing the loans. Collateral may be in the form of real estate or business assets including equipment, inventory, and accounts receivable. The vast majority of the collateral is real estate. The value of real estate collateral is determined utilizing a market valuation approach based on an appraisal, of one year or less, conducted by an independent, licensed appraiser using observable market data (Level 2). However, if the collateral is a house or building in the

PIONEER BANKSHARES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 18 FAIR VALUE MEASUREMENTS (continued):

process of construction or if an appraisal of the property is more than one year old, not solely based on observable market comparables or management determines the fair value of the collateral is further impaired below the appraised value, then a Level 3 valuation is considered to measure the fair value. The value of business equipment is based upon an outside appraisal if deemed significant, or the net book value on the applicable business financial statement if not considered significant using observable market data. Internal collateral evaluations relating to commercial loans secured by business assets such as inventory and equipment are generally performed on an annual basis. However, since this is not a formalized or certified valuation, these evaluations are considered to be level 3 for fair value disclosure and reporting purposes. Likewise, values for inventory and accounts receivables collateral are based on financial statement balances or aging reports (Level 3). Impaired loans allocated to the Allowance for Loan Losses are measured at fair value on a nonrecurring basis. Any fair value adjustments are recorded in the period incurred as provision for loan losses on the Consolidated Statements of Income.

For residential and commercial real estate loans considered to be collateral dependent, appraisals or updated collateral evaluations are generally obtained in conjunction with specific allowance allocations and/or anticipated foreclosure proceedings, on a case by case basis, depending upon the strength of additional mitigating arrangements with individual borrowers. The outstanding principal balance of impaired loans net of specific reserves considered to be collateral dependent in the level 3 category as of December 31, 2018 totaled approximately \$888,000 compared to \$185,000 at December 31, 2017. These loans primarily consisted of business asset loans and certain real estate properties with appraisal valuations that were in the process of being updated. As a general rule, management utilizes a significant discount factor for outdated appraisals when calculating its allowance allocation estimates and making specific reserves. Local professional realtors are also contacted regarding potential fair market values in an effort to ensure that the discounted values are within reasonable ranges on individual properties. Additionally, updated tax assessed values are also considered in this evaluation process on a case by case basis.

Other Real Estate Owned: Certain assets such as other real estate owned (OREO) are measured at fair market value less selling expenses. Fair value of OREO properties held are generally based on current appraisal values, as previously defined above.

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

Description of Assets:	Balances Outstanding (In Thousands)	Carrying values		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
As of December 31, 2018				
Impaired Loans, net of allowance	\$ 888	\$---	\$---	\$ 888
Other Real Estate Owned	\$ 487	\$---	\$---	\$ 487
As of December 31, 2017				
Impaired Loans, net of allowance	\$ 185	\$---	\$---	\$ 185
Other Real Estate Owned	\$ 335	\$---	\$---	\$ 335

PIONEER BANKSHARES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 18 FAIR VALUE MEASUREMENTS (continued):

The following table displays quantitative information about Level 3 Fair Value Measurements for December 31, 2018 (dollars in thousands):

	Quantitative information about Level 3 Fair Value Measurements			
	Fair Value	Valuation Technique(s)	Unobservable Input	Range (Weighted Average)
Assets				
Impaired loans	\$ 888	Discounted appraised value or recent tax assessment values	Selling cost	0% - 10% (7%)
OREO properties	\$ 487		Discount for lack of marketability, Age of appraisal, or Condition of property	10% - 25% (15%)

The following table displays quantitative information about Level 3 Fair Value Measurements for December 31, 2017 (dollars in thousands):

	Quantitative information about Level 3 Fair Value Measurements			
	Fair Value	Valuation Technique(s)	Unobservable Input	Range (Weighted Average)
Assets				
Impaired loans	\$ 185	Discounted appraised value or recent tax assessment values	Selling cost	0% - 10% (7%)
OREO properties	\$ 335		Discount for lack of marketability, Age of appraisal, or Condition of property	10% - 30% (20%)

PIONEER BANKSHARES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 18 FAIR VALUE MEASUREMENTS (continued):

FASB ASC 825, Financial Instruments, requires disclosure about fair value of financial statements, including those financial assets and financial liabilities that are not required to be measured at fair value on a recurring or nonrecurring basis. ASC 825 excludes certain financial instruments and all nonfinancial instruments from its disclosure requirements. Accordingly, the aggregate fair value amounts are presented in the following tables whether or not recognized on the Consolidated Balance Sheets at fair value. Fair values for December 31, 2018 were estimated using an exit price notion in accordance with the prospective adoption of ASU 2106-01, "Recognition and Measurement of Financial Assets and Financial Liabilities." Fair values for December 31, 2017 were estimated using the guidance in effect for that period, which permitted the use of an entry price notion in the compilation of this disclosure.

The carrying values and estimated fair values of the Company's financial instruments as of December 31, 2018 are as follows:

	Carrying Value	Fair Value Measurements at December 31, 2018 using			Total Fair Value Balance
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
Assets					
(In thousands)					
Cash and cash equivalents	\$8,035	\$ 8,035	\$ ---	\$ ---	\$8,035
Interest bearing deposits in other banks	10,429	10,029	387	---	10,416
Federal funds sold	2,369	2,369	---	---	2,369
Securities available for sale	13,974	---	13,974	---	13,974
Equity securities	357	352	5	---	357
Loans, net	167,201	---	---	165,806	165,806
Bank owned life insurance	406	---	406	---	406
Accrued interest receivable	1,093	---	1,093	---	1,093
Liabilities					
Non-interest bearing deposits	54,747	---	54,747	---	54,747
Interest bearing deposits	34,253	---	34,253	---	34,253
Savings deposits	41,515	---	41,515	---	41,515
Time deposits	46,976	---	---	47,269	47,269
Borrowings	5,875	---	5,963	---	5,963
Accrued interest payable	188	---	188	---	188

PIONEER BANKSHARES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 18 FAIR VALUE MEASUREMENTS (continued):

Estimated fair value and the carrying value of financial instruments as of December 31, 2017 are as follows:

	Carrying Value	Fair Value Measurements at December 31, 2017 using			Total Fair Value Balance
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
<u>(In thousands)</u>					
Assets					
Cash and cash equivalents	\$3,630	\$ 3,630	\$ ---	\$ ---	\$ 3,630
Interest bearing deposits in other banks	8,634	8,284	339	---	8,623
Federal funds sold	2,876	2,876	---	---	2,876
Securities available for sale	16,296	4,984	11,312	---	16,296
Loans, net	160,959	---	---	164,867	164,867
Bank owned life insurance	388	---	388	---	388
Accrued interest receivable	1,076	---	1,076	---	1,076
Liabilities					
Non-interest bearing deposits	51,443	---	51,443	---	51,443
Interest bearing deposits	45,321	---	45,321	---	45,321
Savings deposits	25,483	---	25,483	---	25,483
Time deposits	44,686	---	---	45,082	45,082
Borrowings	7,525	---	7,599	---	7,599
Accrued interest payable	109	---	109	---	109

NOTE 19 BENEFIT PLANS:

The Bank has a 401(k) Profit Sharing Plan covering employees who have completed six months of service and are at least 21 years of age. Employees may contribute compensation subject to certain limits based on federal tax laws. The Bank makes matching contributions up to 3 percent of an employee's eligible annual compensation contributed to the Profit Sharing Plan. Additional amounts may be contributed, at the option of the Bank's Board of Directors. Employer contributions vest to the employee at 100% after six years of service. A year of vesting service is a plan year during which an employee is credited with at least 1,000 hours of service. Total expense attributable to this 401(k) plan amounted to approximately \$55,000 for both years ended in December 31, 2018 and 2017.

The Bank also provides a cafeteria insurance plan including medical, life, and long-term disability coverage for eligible employees. The net expense attributable to this insurance plan was approximately \$320,000 and \$289,000, for the years ending December 31, 2018 and 2017, respectively.

PIONEER BANKSHARES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 20 **LOW INCOME HOUSING TAX CREDIT INVESTMENTS:**

The Bank has invested in seven separate housing equity funds at December 31, 2018. The general purpose of these funds is to encourage and assist participants in investing in low-income residential rental properties located in the Commonwealth of Virginia, develop and implement strategies to maintain projects as low-income housing, deliver Federal Low Income Housing Credits to investors, allocate tax losses and other possible tax benefits to investors, and to preserve and protect project assets. The investments in these funds were recorded as other assets on the consolidated balance sheets and were \$2.3 million and \$2.5 million at December 31, 2018 and 2017, respectively. The expected terms of these investments and the related tax benefits run through 2033. Tax credits and other tax benefits recognized as a component of income tax expense during the years ended December 31, 2018 and 2017 were \$315,000 and \$267,000 respectively, related to these investments. Additional capital calls expected for the funds totaled \$472,000 thousand and \$1.0 million at December 31, 2018 and 2017, respectively, and are included in other liabilities on the consolidated balance sheets.

NOTE 21 **REVENUE RECOGNITION:**

On January 1, 2018, the company adopted ASU No. 2014-09, "Revenue from Contracts with Customers: Topic 606", and all subsequent amendments to the ASU No. 2014-09. Using Topic 606 guidelines, the company concluded that Topic 606 primarily applies to the Company's noninterest income excluding certain out-of-scope revenue streams (e.g. gains on sales of securities available for sale, change in fair value of equity securities, etc.).

Service Charges on Deposit Accounts

The majority of the company's noninterest income is derived from short term contracts associated with services provided for deposit account holders. These revenue streams are principally comprised of overdrawn account charges, account maintenance charges, ATM and interchange fees, and fees for various services such as stop payments, wire transfers, and cashiers checks. The Company's performance obligations on revenue generated from deposit accounts and other related services are generally satisfied immediately, when the transaction occurs, or by month-end. Typically, the duration of a contract does not extend beyond the services performed. Due to the short duration of most customer contracts which generate these sources of noninterest income, no significant judgments must be made in the determination of the amount and timing of revenue recognized. The company earns interchange fees from debit and credit cardholder transactions conducted through the Visa and MasterCard payment networks. Interchange fees from cardholder transactions represent a percentage of the underlying transaction value and are generally recognized daily, concurrently with the transaction processing services provided to the cardholder.

Commission Income

Commissions are primarily received on the brokerage of investment and insurance services to customers. Brokerage fee commissions are earned when a financial instrument trade is completed or an insurance contract is signed. Revenue from these services is recognized monthly.

PIONEER BANKSHARES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 21 REVENUE RECOGNITION (continued):

Noninterest income disaggregated by major source, for the years ended December 31, 2018 and 2017, consisted of the following:

Noninterest income (in thousands):	Years Ended December 31,	
	2018	2017
Service charges on deposit accounts [1]:		
Overdrawn account and nonsufficient funds charges	\$ 512	\$ 496
ATM and interchange fees	557	532
Monthly service charges	97	87
Other service charges	17	26
Commission income [1]	82	83
Gains on sales of available for sale securities, net	-	440
Change in fair value of equity securities	(191)	-
Other income [2]	83	85
Total noninterest income	<u>\$ 1,157</u>	<u>\$ 1,749</u>

[1] Income within the scope of Topic 606.

[2] For the years ended December 31, 2018 and 2017, includes other income within the scope of Topic 606 amounting to \$66 thousand and \$68 thousand, respectively.

PIONEER BANKSHARES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 22 PARENT CORPORATION ONLY FINANCIAL STATEMENTS:

BALANCE SHEETS

	December 31,	
	2018	2017
	(In Thousands)	
ASSETS		
Cash and cash equivalents	\$ 3,830	\$ 240
Investment in subsidiary	24,182	21,865
Equity securities, at fair value	357	---
Securities available for sale	---	4,984
Bank premises and equipment, net	416	441
Other assets	85	2
Total Assets	<u>\$ 28,870</u>	<u>\$ 27,532</u>
LIABILITIES		
Accrued expenses and other liabilities	\$ 8	\$ 118
Total Liabilities	<u>8</u>	<u>118</u>
STOCKHOLDERS' EQUITY		
Common stock	489	487
Retained earnings	28,498	26,812
Accumulated other comprehensive (loss) income	(125)	115
Total Stockholders' Equity	<u>28,862</u>	<u>27,414</u>
Total Liabilities and Stockholders' Equity	<u>\$ 28,870</u>	<u>\$ 27,532</u>

PIONEER BANKSHARES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 22 PARENT CORPORATION ONLY FINANCIAL STATEMENTS: (continued)

STATEMENTS OF INCOME

	December 31,	
	2018	2017
	(In Thousands)	
INCOME		
Dividends from subsidiary	\$ ---	\$ 325
Interest income	7	1
Dividend income	92	100
Gains on sales of securities available for sale, net	--	440
Change in fair value of equity securities	(191)	---
Rent income	82	82
Other income	---	1
Total (Loss) Income	<u>(10)</u>	<u>949</u>
EXPENSES		
Interest expense on borrowings	---	9
Compensation expense	66	60
Occupancy expenses	34	43
Other operating expenses	59	63
Total Expenses	<u>159</u>	<u>175</u>
Net (loss) income before income tax expense (benefit) and undistributed income of subsidiary	(169)	774
INCOME TAX EXPENSE (BENEFIT)	<u>(32)</u>	<u>118</u>
Net (loss) income before undistributed income of subsidiary	(137)	656
Undistributed income of subsidiary	<u>2,366</u>	<u>1,385</u>
NET INCOME	<u>\$ 2,229</u>	<u>\$ 2,041</u>

PIONEER BANKSHARES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 22 PARENT CORPORATION ONLY FINANCIAL STATEMENTS: (continued)

STATEMENTS OF CASH FLOWS

	<u>2018</u>	<u>December 31,</u> <u>2017</u>
		(In Thousands)
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	\$ 2,229	\$ 2,041
Adjustments to reconcile net income to net cash provided by operating activities:		
Undistributed subsidiary income	(2,366)	(1,385)
(Gain) Loss on securities transactions, net	---	(440)
Fair value adjustment on equity securities	191	---
Proceeds from sales of equity securities	11,592	---
Purchase of equity securities	(7,156)	---
Depreciation	25	27
Stock based compensation	88	102
Net change in:		
Other assets	(83)	130
Accrued expenses and other liabilities	(110)	85
Net Cash Provided by Operating Activities	<u>4,410</u>	<u>560</u>
CASH FLOWS FROM INVESTING ACTIVITIES:		
Proceeds from sales of securities available for sale	---	6,180
Purchase of securities available for sale	---	(9,384)
Net Cash Used In Investing Activities	<u>---</u>	<u>(3,204)</u>
CASH FLOWS FROM FINANCING ACTIVITIES:		
Curtailments of borrowings	---	(400)
Exercise of Stock Options	---	17
Dividends paid	(820)	(778)
Net Cash Used in Financing Activities	<u>(820)</u>	<u>(1,161)</u>
Net Increase (Decrease) in Cash and Cash Equivalents	3,590	(3,805)
Cash and Cash Equivalents, Beginning of Year	240	4,042
Cash and Cash Equivalents, End of Year	<u>\$ 3,830</u>	<u>\$ 240</u>
Supplemental Disclosure of non-cash activity:		
Unrealized gain on securities available for sale	---	89

