C & F FINANCIAL CORP
Form 10-K
March 07, 2014

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

(Mark One)

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

For the fiscal year ended December 31, 2013

or

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

For the transition period from to _________

Commission file number 000-23423

C&F FINANCIAL CORPORATION

(Exact name of registrant as specified in its charter)

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

802 Main Street

West Point, VA 23181

(Address of principal executive offices) (Zip Code)

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

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

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

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

NONE

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

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

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

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

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

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

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

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

The aggregate market value of voting and non-voting common stock held by non-affiliates of the registrant as of June 30, 2013 was $172,111,461.

There were 3,403,859 shares of common stock outstanding as of February 27, 2014.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the definitive Proxy Statement to be delivered to shareholders in connection with the Annual Meeting of Shareholders to be held April 15, 2014 are incorporated by reference in Part III of this report.

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PART I

ITEM 1. BUSINESS

General

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

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

On October 1, 2013, the Corporation acquired all of the outstanding common stock of Central Virginia Bankshares, Inc. (CVBK) in an all-cash transaction in which CVBK shareholders received $0.32 for each share of CVBK common stock they owned, or approximately $846,000 in the aggregate. In addition, the Corporation purchased from the U.S. Treasury for $3.4 million all of CVBK's preferred stock and warrants issued to the U.S. Treasury under the Capital Purchase Program (CPP). CVBK is a one-bank holding company incorporated under the laws of the Commonwealth of Virginia. CVBK owns all of the stock of Central Virginia Bank (CVB), which is an independent commercial bank chartered under the laws of the Commonwealth of Virginia. CVB's sole subsidiary, CVB Title Services, Inc., was incorporated under the laws of the Commonwealth of Virginia for the primary purpose of owning membership interests in two insurance-related limited liability companies. The Corporation is in the process of obtaining regulatory approval to merge CVBK into the Corporation and CVB into C&F Bank. Management anticipates that these mergers will take place late in the first quarter of 2014.

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

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

The Corporation also owns three non-operating subsidiaries, C&F Financial Statutory Trust II (Trust II) formed in December 2007, C&F Financial Statutory Trust I (Trust I) formed in July 2005, and, by virtue of the Corporation's acquisition of CVBK, Central Virginia Bankshares Statutory Trust I (CVBK Trust I) formed in December 2003. These trusts were formed for the purpose of issuing $10.0 million each for Trust II and Trust I of the Corporation's junior subordinated debt securities, and $5.0 million for CVBK Trust I of CVBK's junior subordinated debt securities in private placements to institutional investors. Trust II and Trust I are unconsolidated subsidiaries of the Corporation and CVBK Trust I is an unconsolidated subsidiary of CVBK. The principal assets of these trusts are $10.3 million each for Trust II and Trust I of the Corporation's junior subordinated debt securities and $5.2 million for CVBK Trust I of CVBK's junior subordinated debt securities (such securities of the Corporation and of CVBK referred to herein as “trust preferred capital notes”) that are reported as liabilities of the consolidated Corporation.

Retail Banking

We provide retail banking services through C&F Bank and CVB (collectively, the Banks). C&F Bank provides retail banking services at its main office in West Point, Virginia, and 17 Virginia branches located one each in Chester, Hampton, Mechanicsville, Midlothian, Newport News, Norge, Providence Forge, Quinton, Saluda, Sandston, Varina, West Point and Yorktown, and two each in Williamsburg and Richmond. CVB provides retail banking services at its main office in Powhatan, Virginia, and six Virginia branches located one each in Cartersville, Cumberland and Richmond, and three in Midlothian. These branches provide a wide range of banking services to individuals and businesses. These services include various types of checking and savings deposit accounts, as well as business, real estate, development, mortgage, home equity and installment loans. The Banks also offer ATMs, internet banking and debit and credit cards, as well as travelers' checks, safe deposit box rentals, collection, notary public, wire service and other customary bank services to its customers. Revenues from retail banking operations consist primarily of interest earned on loans and investment securities and fees related to deposit services. At December 31, 2013, assets of the Retail Banking segment totaled $1.16 billion. For the year ended December 31, 2013, the net income for this segment totaled $3.3 million. The Retail Banking segment's total assets and net income as of and for the year ended December 31, 2013 include CVB's total assets as of December 31, 2013 and CVB's results of operations from October 1, 2013, the date of acquisition.

Mortgage Banking

We conduct mortgage banking activities through C&F Mortgage, which was organized in September 1995. C&F Mortgage provides mortgage loan origination services through 13 locations in Virginia, two in Maryland and one in Gastonia, North Carolina. The Virginia offices are located one each in Charlottesville, Fishersville, Fredericksburg, Glen Allen, Hanover, Harrisonburg, Lynchburg, Newport News, Roanoke, Virginia Beach and Williamsburg, and two in Midlothian. The Maryland offices are located in Annapolis and Waldorf. C&F Mortgage offers a wide variety of residential mortgage loans, which are originated for sale generally to the following investors: Wells Fargo Home Mortgage; Franklin American Mortgage Company; Penny Mac Corporation; and the Virginia Housing Development Authority (VHDA). C&F Mortgage does not securitize loans. C&F Bank may also purchase permanent loans from C&F Mortgage. C&F Mortgage originates conventional mortgage loans, mortgage loans insured by the Federal Housing Administration (the FHA), mortgage loans guaranteed by the United States Department of Agriculture (the USDA) and the Veterans Administration (the VA), and home equity loans. A majority of the conventional loans are conforming loans that qualify for purchase by the Federal National Mortgage Association (Fannie Mae) or the Federal Home Loan Mortgage Corporation (Freddie Mac). The remainder of the conventional loans is non-conforming in that they do not meet Fannie Mae or Freddie Mac guidelines, but are eligible for sale to various other investors. Through its subsidiaries, C&F Mortgage also provides ancillary mortgage loan origination services for loan settlement and residential appraisals. Revenues from mortgage banking operations consist principally of gains on sales of loans to investors in the secondary mortgage market, loan origination fee income and interest earned on mortgage loans held for sale. At December 31, 2013, assets of the Mortgage Banking segment totaled $50.8 million. For the year ended December 31, 2013, net income for this segment totaled $2.0 million.

Consumer Finance

We conduct consumer finance activities through C&F Finance. C&F Finance is a regional finance company providing automobile loans throughout Virginia and in portions of Alabama, Florida, Georgia, Illinois, Indiana, Kentucky, Maryland, Missouri, North Carolina, Ohio, Tennessee, Texas and West Virginia through its offices in Richmond and Hampton, Virginia, in Nashville, Tennessee and in Hunt Valley, Maryland. C&F Finance is an indirect lender that provides automobile financing through lending programs that are designed to serve customers in the “non-prime” market who have limited access to traditional automobile financing. C&F Finance generally purchases automobile retail installment sales contracts from manufacturer-franchised dealerships with used-car operations and through selected independent dealerships. C&F Finance selects these dealers based on the types of vehicles sold. Specifically, C&F Finance prefers to finance later model, low mileage used vehicles because the initial depreciation on new vehicles is extremely high. The typical borrowers on the retail installment sales contracts purchased have experienced prior credit difficulties. Because C&F Finance serves customers who are unable to meet the credit standards imposed by most traditional automobile financing sources, C&F Finance typically charges interest at higher rates than those charged by traditional financing sources. As C&F Finance provides financing in a relatively high-risk market, it expects to experience a higher level of credit losses than traditional automobile financing sources. Revenues from consumer finance operations consist principally of interest earned on automobile loans. At December 31, 2013, assets of the Consumer Finance segment totaled $278.9 million. For the year ended December 31, 2013, net income for this segment totaled $10.5 million.

Employees

At December 31, 2013, we employed 643 full-time equivalent employees. We consider relations with our employees to be excellent.

Competition

Retail Banking

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

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

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

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

Mortgage Banking

C&F Mortgage competes with large national and regional banks, credit unions, smaller regional mortgage lenders and small local broker operations. Due to the increased regulatory and compliance burden, the industry has seen a consolidation in the number of competitors in the marketplace. The guidelines surrounding agency business (i.e., loans sold to Fannie Mae and Freddie Mac) continue to be stringent and the associated mortgage insurance for loans above 80 percent loan-to-value has continued to tighten. The housing markets in which C&F Mortgage competes have continued to be less than robust. More recently, increases in the 10-year treasury rate have caused mortgage rates to increase, which in turn caused a significant decline in refinance activity. These conditions have a dramatic effect on mortgage banking.

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

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

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

Consumer Finance

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

During 2008 and 2009, there was a significant contraction in the number of institutions providing automobile financing for the non-prime market. This contraction accompanied the economic downturn and the tightening of credit, which contributed to increasing defaults, a decline in collateral values and higher charge-offs. As these issues have abated, institutions with access to capital have begun to re-enter the market, resulting in intensified competition for loans and qualified personnel and, to a lesser extent thus far, credit easing. To continue to operate profitably, lenders must have a high level of operational and risk management skills and access to competitive costs of funds.

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

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

Regulation and Supervision

General

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

As previously disclosed, the Corporation plans to merge CVBK with and into the Corporation, with the Corporation surviving, and merge CVB with and into C&F Bank, with C&F Bank surviving. The Corporation expects that these mergers will be effective during the later part of the first quarter of 2014. The following discussion focuses on regulation and supervision of the Corporation and C&F Bank. As a bank holding company, CVBK is subject to substantially similar regulations as the Corporation. Because CVB is a Virginia chartered banking corporation and is a member of the Federal Reserve System, CVB is subject to substantially similar regulations as C&F Bank and is also subject to additional regulations applicable to bank members of the Federal Reserve System.

Regulatory Reform

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

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

Regulation of the Corporation

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

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

Each of the Banks' depository accounts is insured by the Federal Deposit Insurance Corporation (the FDIC) against loss to the depositor to the maximum extent permitted by applicable law, and federal law and regulatory policy impose a number of obligations and restrictions on the Corporation and C&F Bank to reduce potential loss exposure to depositors and to the FDIC insurance funds. For example, pursuant to the Dodd-Frank Act and Federal Reserve policy, a bank holding company must commit resources to support its subsidiary depository institutions, which is referred to as serving as a "source of strength." In addition, insured depository institutions under common control must reimburse the FDIC for any loss suffered or reasonably anticipated by the Deposit Insurance Fund (DIF) as a result of the default of a commonly controlled insured depository institution. The FDIC may decline to enforce the provisions if it determines that a waiver is in the best interest of the DIF. An FDIC claim for damage is superior to claims of stockholders of an insured depository institution or its holding company but is subordinate to claims of depositors, secured creditors and holders of subordinated debt, other than affiliates, of the commonly controlled insured depository institution.

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

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

Capital Requirements

The Federal Reserve Board and the FDIC have issued substantially similar risk-based and leverage capital guidelines that currently apply to banking organizations they supervise. Under the currently applicable risk-based capital requirements, the Corporation and the Banks are required to maintain a minimum ratio of total capital to risk-weighted assets of at least 8.0 percent and a minimum ratio of Tier 1 capital to risk-weighted assets of at least 4.0 percent. At least half of the total capital must be Tier 1 capital, which includes common equity, retained earnings and qualifying perpetual preferred stock, less certain intangibles and other adjustments. The remainder may consist of Tier 2 capital, such as a limited amount of subordinated and other qualifying debt (including certain hybrid capital instruments), other qualifying preferred stock and a limited amount of the general loan loss allowance. As long as the Corporation has total consolidated assets of less than $15 billion, under currently applicable capital standards the Corporation may include in Tier 1 and total capital the Corporation’s trust preferred securities that were issued before May 19, 2010. The currently applicable capital guidelines also provide that banking organizations experiencing internal growth or making acquisitions must maintain capital positions substantially above the minimum supervisory levels, without significant reliance on intangible assets.

In July 2013, the federal bank regulatory agencies adopted final rules (i) to implement the Basel III capital framework as outlined by the Basel Committee on Banking Supervision and (ii) for calculating risk-weighted assets (collectively, the Basel III Final Rules). These final rules establish a new comprehensive capital framework for U.S. banking organizations, require bank holding companies and their bank subsidiaries to maintain substantially more capital with a greater emphasis on common equity, and make selected changes to the calculation risk-weighted assets. The Basel III Final Rules, among other things, (i) introduce as a new capital measure “Common Equity Tier 1” (CET1), (ii) specify that Tier 1 capital consists of CET1 and “Additional Tier 1 capital” instruments meeting specified requirements, (iii) define CET1 narrowly by requiring that most adjustments to regulatory capital measures be made to CET1 and not to the other components of capital and (iv) expand the scope of the adjustments as compared to existing regulations. The Basel III Capital Rules implement the new minimum capital ratios and risk-weighting calculations on January 1, 2015, and Basel III's capital conservation buffer and regulatory capital adjustments and deductions will be phased in from 2015 to 2019.

When fully phased in, the Basel III Final Rules will require banks to maintain (i) a minimum ratio of CET1 to risk-weighted assets of at least 4.5%, plus a 2.5% “capital conservation buffer” (which is added to the 4.5% CET1 ratio as that buffer is phased in, effectively resulting in a minimum ratio of CET1 to risk-weighted assets of at least 7%), (ii) a minimum ratio of Tier 1 capital to risk-weighted assets of at least 6.0%, plus the capital conservation buffer (which is added to the 6.0% Tier 1 capital ratio as that buffer is phased in, effectively resulting in a minimum Tier 1 capital ratio of 8.5% upon full implementation), (iii) a minimum ratio of Total (that is, Tier 1 plus Tier 2) capital to risk-weighted assets of at least 8.0%, plus the capital conservation buffer (which is added to the 8.0% total capital ratio as that buffer is phased in, effectively resulting in a minimum total capital ratio of 10.5% upon full implementation) and (iv) a minimum leverage ratio of 3%, calculated as the ratio of Tier 1 capital to balance sheet exposures plus certain off-balance sheet exposures (computed as the average for each quarter of the month-end ratios for the quarter).

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

The Basel III Final Rules provide new deductions from and adjustments to CET1. These include, for example, the requirement that mortgage servicing rights, deferred tax assets dependent upon future taxable income and significant investments in non-consolidated financial entities be deducted from CET1 to the extent that any one such category exceeds 10% of CET1 or all such categories in the aggregate exceed 15% of CET1.

The Basel III Final Rules also revise the general rules for calculating a banking organization's total risk-weighted assets and the risk weightings that are applied to many classes of assets held by community banks, importantly including applying higher risk weightings to certain commercial real estate loans.

Limits on Dividends

The Corporation is a legal entity that is separate and distinct from C&F Bank. A significant portion of the revenues of the Corporation result from dividends paid to it by C&F Bank. Both the Corporation and C&F Bank are subject to laws and regulations that limit the payment of dividends, including limits on the sources of dividends and requirements to maintain capital at or above regulatory minimums. Banking regulators have indicated that Virginia banking organizations should generally pay dividends only (1) from net undivided profits of the bank, after providing for all expenses, losses, interest and taxes accrued or due by the bank and (2) if the prospective rate of earnings retention appears consistent with the organization’s capital needs, asset quality and overall financial condition. In addition, the FDIA prohibits insured depository institutions such as C&F Bank from making capital distributions, including paying dividends, if, after making such distribution, the institution would become undercapitalized as defined in the statute. We do not expect that any of these laws, regulations or policies will materially affect the ability of the Corporation or C&F Bank to pay dividends.

On June 30, 2010, CVBK and CVB entered into a written agreement with the Federal Reserve Bank of Richmond and the Virginia Bureau of Financial Institutions (VBFI). Among other things, the written agreement restricts CVBK and CVB from paying dividends and making other capital distributions without the written consent of the Federal Reserve Bank and the VBFI. Since acquiring CVBK and CVB on October 1, 2013, this restriction has not significantly affected the operations of the Corporation or C&F Bank. The Corporation anticipates merging CVBK with and into the Corporation and CVB with and into C&F Bank during the later part of the first quarter of 2014, and further anticipates that the written agreement will terminate upon completion of these mergers.

The Dodd-Frank Act

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

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

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

- Restrict the preemption of state law by federal law and disallow subsidiaries and affiliates of national banks from availing themselves of such preemption.
- Impose comprehensive regulation of the over-the-counter derivatives market, subject to significant rulemaking processes, which would include certain provisions that would effectively prohibit insured depository institutions from

conducting certain derivatives businesses in the institution itself.

- Require depository institutions with total consolidated assets of more than $10 billion to conduct regular stress tests and require large, publicly traded bank holding companies to create a risk committee responsible for the oversight of enterprise risk management.
- Require loan originators to retain 5 percent of any loan sold or securitized, unless it is a “qualified residential mortgage,” subject to certain exceptions.
- Prohibit banks and their affiliates from engaging in proprietary trading and investing in and sponsoring certain unregistered investment companies (the Volker Rule).
- Implement corporate governance revisions that apply to all public companies not just financial institutions.

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

Insurance of Accounts, Assessments and Regulation by the FDIC

The Banks' deposits are insured by the DIF of the FDIC up to the standard maximum insurance amount for each deposit insurance ownership category. As of January 1, 2014, the basic limit on FDIC deposit insurance coverage is $250,000 per depositor. Under the FDIA, the FDIC may terminate deposit insurance upon a finding that the institution has engaged in unsafe and unsound practices, is in an unsafe or unsound condition to continue operations, or has violated any applicable law, regulation, rule, order or condition imposed by the FDIC, subject to administrative and potential judicial hearing and review processes.

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

The Dodd-Frank Act transferred to the FDIC increased discretion with regard to managing the required amount of reserves for the DIF, or the “designated reserve ratio.” Among other changes, the Dodd-Frank Act (i) raised the minimum designated reserve ratio to 1.35 percent and removed the upper limit on the designated reserve ratio, (ii) requires that the designated reserve ratio reach 1.35 percent by September 2020, and (iii) requires the FDIC to offset the effect on institutions with total consolidated assets of less than $10 billion of raising the designated reserve ratio from 1.15 percent to 1.35 percent. The FDIA requires that the FDIC consider the appropriate level for the designated reserve ratio on at least an annual basis. On October 2010, the FDIC adopted a new DIF restoration plan to ensure that the fund reserve ratio reaches 1.35 percent by September 30, 2020, as required by the Dodd-Frank Act.

Regulation of the Banks and Other Subsidiaries

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

Community Reinvestment Act. The CRA imposes on financial institutions an affirmative and ongoing obligation to meet the credit needs of their local communities, including low and moderate-income neighborhoods, consistent with the safe and sound operation of those institutions. A financial institution's efforts in meeting community credit needs are assessed based on specified factors. These factors also are considered in evaluating mergers, acquisitions and applications to open a branch or facility. In 2012, C&F Bank and CVB each received a "Satisfactory" CRA rating.

Federal Home Loan Bank of Atlanta. C&F Bank and CVB are members of the Federal Home Loan Bank (FHLB) of Atlanta, which is one of 12 regional FHLBs that provide funding to their members for making housing loans as well as for affordable housing and community development loans. Each FHLB serves as a reserve, or central bank, for the members within its assigned region. Each FHLB makes loans to members in accordance with policies and procedures established by the Board of Directors of the FHLB. As members, the Banks must purchase and maintain stock in the FHLB. At December 31, 2013, C&F bank owned $3.5 million and CVB owned $464,000 of FHLB stock.

Federal Reserve Bank Stock. CVB is a member of the Federal Reserve System. As a member, CVB must purchase and maintain stock in the Federal Reserve Bank. The stock may not be sold, traded, or pledged as security for a loan; dividends are, by law, six percent per year. At December 31, 2013, CVB owned $347,000 of Federal Reserve Bank stock.

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

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

Mortgage Banking Regulation. In connection with making mortgage loans, the Banks are subject to rules and regulations that, among other things, establish standards for loan origination, prohibit discrimination, provide for inspections and appraisals of property, require credit reports on prospective borrowers, in some cases, restrict certain loan features and fix maximum interest rates and fees, require the disclosure of certain basic information to mortgagors concerning credit and settlement costs, limit payment for settlement services to the reasonable value of the services rendered and require the maintenance and disclosure of information regarding the disposition of mortgage applications based on race, gender, geographical distribution and income level. The Banks' mortgage origination activities are subject to the Equal Credit Opportunity Act (ECOA), Truth-in-Lending Act (TILA), Home Mortgage Disclosure Act, Real Estate Settlement Procedures Act, and Home Ownership Equity Protection Act, and the regulations promulgated under these acts, among other additional state and federal laws, regulations and rules.

The Banks' mortgage origination activities are also subject to Regulation Z, which implements TILA. As recently amended and effective January 10, 2014, certain provisions of Regulation Z require mortgage lenders to make a reasonable and good faith determination, based on verified and documented information, that a consumer applying for a mortgage loan has a reasonable ability to repay the loan according to its terms. Alternatively, a mortgage lender can originate "qualified mortgages", which are generally defined as mortgage loans without negative amortization, interest-only payments, balloon payments, terms exceeding 30 years, and points and fees paid by a consumer equal to or less than 3% of the total loan amount. Higher-priced qualified mortgages (e.g., subprime loans) receive a rebuttable presumption of compliance with ability-to-repay rules, and other qualified mortgages (e.g., prime loans) are deemed to comply with the ability-to-repay rules. The Corporation's Mortgage Banking segment predominately originates mortgage loans that comply with Regulation Z's "qualified mortgage" rules.

In addition to certain regulations applicable to the Banks, the Corporation's Mortgage Banking segment is subject to the rules and regulations of, and examination by, the Department of Housing and Urban Development (HUD), the FHA, the USDA, the VA and state regulatory authorities with respect to originating, processing and selling mortgage loans. Those rules and regulations, among other things, establish standards for loan origination, prohibit discrimination, provide for inspections and appraisals of property, require credit reports on prospective borrowers and, in some cases, restrict certain loan features and fix maximum interest rates and fees.

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

Certain federal regulatory agencies, and in particular, the CFPB, the Federal Trade Commission, and the Federal Reserve, have recently become more active in investigating the products, services and operations of banks and other finance companies engaged in auto finance activities. These investigations have extended to banks that engage in indirect automobile lending, and the CFPB has released regulatory guidance that deems automobile lenders within the CFPB’s jurisdiction responsible for ECOA noncompliance even if such noncompliance is a result of dealer lending practices. As of January 1, 2014, the Corporation and C&F Finance are not subject to supervision by the CFPB.

Other Regulations

Prompt Correction Action. The federal banking agencies have broad powers under current federal law to take prompt corrective action to resolve problems of insured depository institutions. The extent of these powers depends upon whether the institution in question is “well capitalized,” “adequately capitalized,” “undercapitalized,” “significantly undercapitalized” or “critically undercapitalized.” These terms are defined under uniform regulations issued by each of the federal banking agencies regulating these institutions. An insured depository institution which is less than adequately capitalized must adopt an acceptable capital restoration plan, is subject to increased regulatory oversight and is increasingly restricted in the scope of its permissible activities. As of December 31, 2013, the Banks were each considered “well capitalized.”

Incentive Compensation. The Federal Reserve, the Office of the Comptroller of the Currency (OCC) and the FDIC have issued regulatory guidance (the Incentive Compensation Guidance) intended to ensure that the incentive compensation policies of banking organizations do not undermine the safety and soundness of such organizations by encouraging excessive risk-taking. The Federal Reserve will review, as part of the regular, risk-focused examination process, the incentive compensation arrangements of banking organizations, such as the Corporation, that are not "large, complex banking organizations." The findings will be included in reports of examination, and deficiencies will be incorporated into the organization's supervisory ratings. Enforcement actions may be taken against a banking organization if its incentive compensation arrangements, or related risk-management control or governance processes, pose a risk to the organization's safety and soundness and the organization is not taking prompt and effective measures to correct the deficiencies.

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

Financial Holding Company Status. As provided by the Gramm-Leach-Bliley Act of 1999 (GLBA), a bank holding company may become eligible to engage in activities that are financial in nature or incident or complimentary to financial activities by qualifying as a financial holding company. To qualify as a financial holding company, each insured depository institution controlled by the bank holding company must be well-capitalized, well-managed and have at least a satisfactory rating under the CRA. In addition, the bank holding company must file with the Federal Reserve Board a declaration of its intention to become a financial holding company. To date, the Corporation has not filed a declaration to become a financial holding company, and qualification as such by other bank holding companies has not had a material effect on the Corporation's or the Banks' business.

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

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

Although these laws and programs impose compliance costs and create privacy obligations and, in some cases, reporting obligations, these laws and programs do not materially affect the Banks' products, services or other business activities.

Stress Testing. As required by the Dodd-Frank Act, the federal banking agencies have implemented stress testing requirements for certain financial institutions, including bank holding companies and state chartered banks, with more than $10 billion in total consolidated assets. Although these requirements do not apply to institutions with less than $10 billion in total consolidated assets, the federal banking agencies emphasize that all banking organizations, regardless of size, should have the capacity to analyze the potential effect of adverse market conditions or outcomes on the organization's financial condition. Based on existing regulatory guidance, the Corporation and the Banks will be expected to consider the institution's interest rate risk management, commercial real estate loan concentrations and other credit-related information, and funding and liquidity management during this analysis of adverse outcomes.

Volcker Rule. The Dodd-Frank Act prohibits bank holding companies and their subsidiary banks from engaging in proprietary trading except in limited circumstances, and places limits on ownership of equity investments in private equity and hedge funds (the Volcker Rule). On December 10, 2013, the U.S. financial regulatory agencies (including the Federal Reserve, the FDIC and the SEC) adopted final rules to implement the Volcker Rule. In relevant part, these final rules would have prohibited banking entities from owning collateralized debt obligations (CDOs) backed by trust preferred securities (TruPS), effective July 21, 2015. However, subsequent to these final rules the U.S. financial regulatory agencies issued an interim rule effective April 1, 2014 to exempt CDOs backed by TruPS from the Volker Rule and the final rule, provided that (a) the CDO was established prior to May 19, 2010, (b) the banking entity reasonably believes that the CDO’s offering proceeds were used to invest primarily in TruPS issued by banks with less than $15 billion in assets, and (iii) the banking entity acquired the CDO investment on or before December 10, 2013. Neither the Corporation nor the Banks currently have any CDO investments, and the Corporation believes that its financial condition will not be significantly affected by the Volcker Rule, the final rule or the interim rule.

Written Agreement of CVBK and CVB, and Acquisition of CVBK by the Corporation

On June 30, 2010, CVBK and CVB entered into a written agreement with the Federal Reserve Bank of Richmond and the VBFI (the Written Agreement). The written agreement required CVBK and CVB to submit plans to the Federal Reserve Bank and the VBFI to improve the financial condition, operational condition, management and oversight of CVBK and CVB, respectively. The Written Agreement also restricts CVBK and CVB from paying dividends and making other capital distributions without the written consent of the Federal Reserve Bank and the VBFI. Since acquiring CVBK and CVB on October 1, 2013, the Written Agreement has not significantly affected the operations of the Corporation or C&F Bank. Additionally, in connection with the acquisition of CVBK, the Corporation committed to its federal and state banking regulators that the Corporation would commit management and financial resources to solidify the operational and financial condition of CVBK and CVB.

The Corporation believes that CVBK and CVB are in substantial compliance with the Written Agreement, and that the Corporation has provided sufficient management and financial resources to solidify the condition of CVBK and CVB. The Corporation anticipates completing the mergers of CVBK with and into the Corporation and CVB with and into the C&F Bank during the later part of the first quarter of 2014, and further anticipates that the Written Agreement will terminate upon completion of these mergers.

Future Regulation

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

Available Information

The Corporation's SEC filings are filed electronically and are available to the public over the Internet at the SEC's web site at http://www.sec.gov. In addition, any document filed by the Corporation with the SEC can be read and copied at the SEC's public reference facilities at 100 F Street, N.E., Room 1580, Washington, D.C. 20549. Copies of documents can be obtained at prescribed rates by writing to the Public Reference Section of the SEC at 100 F Street, N.E., Washington, D.C. 20549. The public may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. The Corporation's SEC filings also are available through our web site at http://www.cffc.com under "Investor Relations/SEC Filings" as of the day they are filed with the SEC. Copies of documents also can be obtained free of charge by writing to the Corporation's secretary at P.O. Box 391, West Point, VA 23181 or by calling 804-843-2360.

ITEM 1A. RISK FACTORS

A continuation or deterioration of the current economic environment could adversely affect our financial condition and results of operations.

A continuation or deterioration of the current economic environment could adversely affect the Corporation's performance, both directly by affecting our revenues and the value of our assets and liabilities, and indirectly by affecting our counterparties and the economy generally. Overall, during 2013 the economic environment has been adverse for many households and businesses in our markets, the Commonwealth of Virginia and the United States. Dramatic declines in the housing market that began during the recession have resulted in significant write-downs of asset values by financial institutions. The Corporation has recognized elevated loan loss provisions and write-downs and other expenses associated with foreclosed properties beginning in 2008 as the level of nonperforming assets increased throughout the period. The economic recovery has been less than robust and there can be no assurance that the measured economic recovery will continue. The continued high levels of unemployment coupled with the continued stagnation in the housing market has and may continue to have an adverse effect on the Corporation's results of operations.

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

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

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

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

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

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

A wide range of regulatory initiatives directed at the financial services industry have been proposed in recent years. One of those initiatives, the Dodd-Frank Act, was signed into law on July 21, 2010. The Dodd-Frank Act represents a sweeping overhaul of the financial services industry regulatory environment within the United States and mandates significant changes in the financial regulatory landscape that will affect all financial institutions, including the Corporation. The Dodd-Frank Act will likely increase our regulatory compliance burden and may have a material adverse effect on us, by increasing the costs associated with our regulatory examinations and compliance measures. The federal regulatory agencies, and particularly bank regulatory agencies, have been given significant discretion in drafting the Dodd-Frank Act’s implementing rules and regulations, many of which have not been finalized. Consequently, many of the details and much of the impact of the Dodd-Frank Act will depend on the final implementing rules and regulations, and it remains too early to fully assess the complete effect of the Dodd-Frank Act and related regulatory rulemaking processes on our business, financial condition or results of operations.

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

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

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

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

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

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

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

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

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

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

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

Our profitability depends in substantial part on our net interest margin, which is the difference between the interest earned on loans, securities and other interest-earning assets, and interest paid on deposits and borrowings divided by total interest-earning assets. Changes in interest rates will affect our net interest margin in diverse ways, including the pricing of loans and deposits, the levels of prepayments and asset quality. We are unable to predict actual fluctuations of market interest rates because many factors influencing interest rates are beyond our control. We attempt to minimize our exposure to interest rate risk, but we are unable to eliminate it. We believe that our current interest rate exposure is manageable and does not indicate any significant exposure to interest rate changes. Since the interest rate cuts made by the Federal Reserve Bank in September 2007, our net interest margin has recovered gradually over the past several years because we have been able to reprice fixed-rate deposits at lower rates, as well as implement policies that established floors on certain variable rate loans. The Federal Reserve's Federal Open Market Committee has stated it will keep the federal funds target rate at 0%-0.25% until economic and labor conditions (as indicated by the unemployment rate) improve, which is currently expected to be until 2015. While such a continuance of accommodative monetary policy could allow us to continue to reprice a portion of our fixed-rate deposits at lower rates, sustained low interest rates could put further pressure on the yields generated by our loan portfolio and on our net interest margin. There is no guarantee we will continue to be able to reprice deposits at favorable rates as competition for deposits from both local and national financial institutions is intense, and continued pressure on our asset yields and net interest margin could adversely affect our results of operations.

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

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

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

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

At December 31, 2013, 23 percent of our loan portfolio consisted of commercial, financial and agricultural loans, which include loans secured by real estate for builder lines, acquisition and development and commercial development, as well as commercial loans secured by personal property. These loans generally carry larger loan balances and involve a greater degree of financial and credit risk than home equity and residential loans. The increased financial and credit risk associated with these types of loans is a result of several factors, including the concentration of principal in a limited number of loans and to borrowers in similar lines of business, the size of loan balances, the effects of general economic conditions on income-producing properties and the increased difficulty of evaluating and monitoring these types of loans.

At December 31, 2013, 34 percent of our loan portfolio consisted of consumer finance loans that provide automobile financing for customers in the non-prime market. During periods of economic slowdown or recession, delinquencies, defaults, repossessions and losses may increase in this portfolio. Significant increases in the inventory of used automobiles during periods of economic recession may also depress the prices at which we may sell repossessed automobiles or delay the timing of these sales. Because we focus on non-prime borrowers, the actual rates of delinquencies, defaults, repossessions and losses on these loans are higher than those experienced in the general automobile finance industry and could be dramatically affected by a general economic downturn. In addition, our servicing costs may increase without a corresponding increase in our finance charge income. While we manage the higher risk inherent in loans made to non-prime borrowers through our underwriting criteria for installment sales contracts we purchase and collection methods, we cannot guarantee that these criteria or methods will ultimately provide adequate protection against these risks.

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

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

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

One of the components of our strategic plan is to generate significant noninterest income from C&F Mortgage, which originates a variety of residential loan products for sale into the secondary market to investors. Increases in the 10-year treasury rate that occurred during 2013 caused mortgage rates to increase, which in turn caused a dramatic decline in refinance activity, dampened demand for residential mortgage loans, and resulted in pressure on loan origination volume at C&F Mortgage.

In addition, credit markets have continued to experience difficult conditions and volatility. While payment defaults by borrowers and mortgage loan foreclosures may have abated, investors continue to submit claims in an attempt to minimize their losses. This may result in potential repurchase or indemnification liability to C&F Mortgage on residential mortgage loans originated and sold into the secondary market in the event of claims by investors of borrower misrepresentation, fraud, early-payment default, or underwriting error, as investors attempt to minimize their losses. While we entered into an agreement with our then largest purchaser of loans that resolved all known and unknown indemnification obligations related to loans sold to this investor through 2010, and while we mitigate the risk of repurchase liability by underwriting to the purchasers’ guidelines, we cannot be assured that a prolonged period of payment defaults and foreclosures will not result in an increase in requests for repurchases or indemnifications, or that established reserves will be adequate, which could adversely affect the Corporation’s net income.

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

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

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

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

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

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

Because we originate loans secured by real estate, we may have to foreclose on the collateral property to protect our investment and may thereafter own and operate such property, in which case we are exposed to the risks inherent in the ownership of real estate. The amount that we, as a mortgagee, may realize after a default is dependent upon factors outside of our control, included, but not limited to general or local economic conditions, environmental cleanup liability, neighborhood values, interest rates, real estate tax rates, operating expenses of the mortgaged properties, and supply of and demand for properties. Certain expenditures associated with the ownership of income-producing real estate, principally real estate taxes and maintenance costs, may adversely affect the net cash flows generated by the real estate. Therefore, the cost of operating income-producing real property may exceed the rental income earned from such property, and we may have to advance funds in order to protect our investment or we may be required to dispose of the real property at a loss.

It may be difficult to integrate the business of CVB and we may fail to realize all of the anticipated benefits of the acquisition of CVB.

If our costs to integrate the business of CVB into our existing operations are greater than anticipated or we are not able to achieve the anticipated benefits of the merger, including cost savings and other synergies, our business could be negatively affected. In addition, it is possible that the ongoing integration processes could result in the loss of key employees, loss of customers, error or delays in systems implementation, the disruption of our ongoing businesses or inconsistencies in standards, controls, procedures and policies that adversely affect our ability to maintain relationships with customers and employees or to achieve the anticipated benefits of the merger. Integration efforts also may divert management attention and resources, which could adversely affect our ability to service our existing business and generate new business, which in turn could adversely affect our business and financial results.

We may incur losses on loans, securities and other acquired assets of CVB that are materially greater than reflected in our preliminary fair value adjustments.

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

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

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

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

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

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

While most of our core data processing is conducted internally, certain key applications are outsourced to third party providers. If our third party providers encounter difficulties or if we have difficulty in communicating with such third parties, it will significantly affect our ability to adequately process and account for customer transactions, which would significantly affect our business operations.

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

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

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

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

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

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

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

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

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

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

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

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

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

Although our common stock is listed for trading on NASDAQ Global Select Market, the trading volume in our common stock may be lower than that of other larger financial institutions. A public trading market having the desired characteristics of depth, liquidity and orderliness depends on the presence in the marketplace of willing buyers and sellers of the common stock at any given time. This presence depends on the individual decisions of investors and general economic and market conditions over which we have no control. Given the potential for lower relative trading volume in our common stock, significant sales of the common stock in the public market, or the perception that those sales may occur, could cause the trading price of our common stock to decline or to be lower than it otherwise might be in the absence of these sales or perceptions.

ITEM 1B. UNRESOLVED STAFF COMMENTS

The Corporation has no unresolved comments from the SEC staff.

ITEM 2. PROPERTIES

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

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

C&F Bank owns a building located at 3600 LaGrange Parkway in Toano, Virginia. The building was acquired in 2004 and has 85,000 square feet. Approximately 30,000 square feet were renovated in 2005 in order to house the C&F Bank's operations center, which consists of C&F Bank’s loan, deposit and administrative functions and staff.

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

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

C&F Bank owns 15 other retail banking branch locations and leases one retail banking branch location and one regional commercial lending office in Virginia. Rental expense for leased locations totaled $117,000 for the year ended December 31, 2013.

CVB owns a building located at 2351 Anderson Highway in Powhatan, Virginia. The building, originally constructed in 2005, has two floors totaling 16,000 square feet. This building houses CVB's Main Office and corporate and administrative functions and staff. CVB owns a building located at 2036 New Dorset Road in Powhatan, Virginia. The building was built in 1996 and has three floors totaling 14,000 square feet housing CVB's operations center. CVB owns six other retail banking branch locations.

C&F Mortgage's Newport News loan production office is located on the second floor of C&F Bank's Newport News branch building and its Williamsburg loan production office is located on the second floor of C&F Bank's Jamestown Road branch location. In addition, C&F Mortgage has 14 loan production offices leased from nonaffiliates including 11 in Virginia, two in Maryland, and one in North Carolina. Rental expense for leased locations totaled $916,000 for the year ended December 31, 2013.

The Hampton office of C&F Finance is located on the second floor of C&F Bank's Hampton branch building. In January 2011, C&F Finance entered into a five-year lease agreement with an unrelated third party for approximately 17,000 square feet of office space in Richmond, Virginia, which is being used for C&F Finance's headquarters and its loan and administrative functions and staff. C&F Finance has two leased offices, one each in Maryland and Tennessee. Rental expense for leased locations totaled $341,000 for the year ended December 31, 2013.

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

ITEM 3. LEGAL PROCEEDINGS

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

ITEM 4. MINE SAFETY DISCLOSURES

None.

EXECUTIVE OFFICERS OF THE REGISTRANT

Name (Age) **Present Position**	**Business Experience** **During Past Five Years**
Larry G. Dillon (61) Chairman, President and Chief Executive Officer	Chairman, President and Chief Executive Officer of the Corporation and C&F Bank since 1989; Chairman, President and Chief Executive Officer of CVBK and CVB since 2013
Thomas F. Cherry (45) Executive Vice President Chief Financial Officer and Secretary	Secretary of the Corporation and C&F Bank since 2002; Executive Vice President and Chief Financial Officer of the Corporation and C&F Bank since December 2004; Executive Vice President and Chief Financial Officer of CVBK and CVB since 2013
Bryan E. McKernon (57) President and Chief Executive Officer, C&F Mortgage	President and Chief Executive Officer of C&F Mortgage since 1995
S. Dustin Crone (45) President, C&F Finance	President of C&F Finance since 2010; Executive Vice President of C&F Finance from 2006 through 2009
John A. Seaman, III (56) Senior Vice President and Chief Credit Officer, C&F Bank and CVB	Senior Vice President and Chief Credit Officer of C&F Bank since October 2011 and of CVB since 2013; Director of Homebuilder Banking-Special Situations Group, Mid-Atlantic Region, Wells Fargo Bank, N.A., with particular responsibility for residential loan resolution and workouts from 2008 through September 2011

PART II

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

The Corporation's common stock is listed for trading on the NASDAQ Global Select Market of the NASDAQ Stock Market under the symbol "CFFI." As of February 27, 2014, there were approximately 2,200 shareholders of record. As of that date, the closing price of our common stock on the NASDAQ Global Select Stock Market was $36.87. Following are the high and low sales prices as reported by the NASDAQ Stock Market, along with the dividends that were declared quarterly in 2013 and 2012.

	2013			**2012**		
Quarter	**High**	**Low**	**Dividends**	**High**	**Low**	**Dividends**
First	**$42.00**	**$36.80**	**$ 0.29**	**$31.53**	**$26.40**	**$ 0.26**
Second	**55.99**	**38.35**	**0.29**	**41.95**	**28.25**	**0.26**
Third	**59.59**	**48.06**	**0.29**	**43.42**	**38.51**	**0.27**
Fourth	**56.68**	**43.17**	**0.29**	**40.00**	**33.06**	**0.29**

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

Issuer Purchases of Equity Securities

The following table summarizes repurchases of the Corporation's common stock that occurred during the three months ended December 31, 2013.

(Dollars in thousands, except for per share amounts)	**Total Number of Shares Purchased** [1]	**Average Price Paid per Share**	**Total Number of Shares Purchased as Part of Publicly**	**Maximum Number (or Approximate Dollar Value)**

			Announced Plans or Programs	of Shares that May Yet Be Purchased Under the Plans or Programs
October 1, 2013 - October 31, 2013	**—**	**$ —**	**—**	**$ —**
November 1, 2013 - November 30, 2013	**—**	**—**	**—**	**—**
December 1, 2013 - December 31, 2013	**1,090**	**45.07**	**—**	**—**
Total	**1,090**	**$ 45.07**	**—**	**$ —**

[1] These shares were withheld from employees to satisfy tax withholding obligations arising upon the vesting of restricted shares.

ITEM 6. SELECTED FINANCIAL DATA

Five Year Financial Summary

(Dollars in thousands, except share and per share amounts)	**2013**		**2012**		**2011**		**2010**		**2009**	
Selected Year-End Balances:										
Total assets	**$1,312,297**		$977,018		$928,124		$904,137		$888,430	
Total shareholders' equity	**112,941**		102,197		96,090		92,777		88,876	
Total loans (net)	**785,532**		640,283		616,984		606,744		613,004	
Total deposits	**1,008,292**		686,184		646,416		625,134		606,630	
Summary of Operations:										
Interest income	**$80,212**		$76,964		$73,790		$69,848		$64,971	
Interest expense	**8,623**		10,111		11,881		13,235		15,459	
Net interest income	**71,589**		66,853		61,909		56,613		49,512	
Provision for loan losses	**15,085**		12,405		14,160		14,959		18,563	
Net interest income after provision for loan losses	**56,504**		54,448		47,749		41,654		30,949	
Noninterest income	**22,220**		20,622		17,171		17,935		19,824	
Noninterest expenses	**57,612**		51,042		46,209		48,530		43,302	
Income before taxes	**21,112**		24,028		18,711		11,059		7,471	
Income tax expense	**6,710**		7,646		5,735		2,949		1,945	
Net income	**14,402**		16,382		12,976		8,110		5,526	
Effective dividends on preferred stock	**—**		311		1,183		1,149		1,130	
Net income available to common shareholders	**$14,402**		$16,071		$11,793		$6,961		$4,396	
Per share:										
Earnings per common share—basic	**$4.36**		$5.00		$3.76		$2.26		$1.44	
Earnings per common share—assuming dilution	**4.18**		4.86		3.72		2.24		1.44	
Dividends	**1.16**		1.08		1.01		1.00		1.06	
Weighted average number of shares—assuming dilution	**3,443,982**		3,305,902		3,172,277		3,103,469		3,048,491	
Significant Ratios:										
Return on average assets	**1.35**	**%**	1.71	%	1.30	%	0.78	%	0.50	%
Return on average common equity	**13.39**		17.05		14.86		9.74		6.60	
Dividend payout ratio – common shares	**26.61**		21.60		26.86		44.25		73.48	
Average common equity to average assets	**10.07**		10.03		8.75		8.01		7.61	

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

Cautionary Statement Regarding Forward-Looking Statements

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

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

- the value of securities held in the Corporation’s investment portfolios
- demand for loan products
- the quality or composition of the loan portfolios and the value of the collateral securing those loans
- the commercial and residential real estate markets
- the inventory level and pricing of used automobiles, including sales prices of repossessed vehicles
- the level of net charge-offs on loans and the adequacy of our allowance for loan losses
- deposit flows
- demand in the secondary residential mortgage loan markets
- the level of indemnification losses related to mortgage loans sold
- the strength of the Corporation’s counterparties
- competition from both banks and non-banks
- demand for financial services in the Corporation’s market area
- the Corporation's expansion and technology initiatives
- reliance on third parties for key services
- accounting principles, policies and guideline and elections by the Corporation thereunder

These risks are exacerbated by the turbulence over the past several years in the global and United States financial markets. Sustained weakness in the global and United States financial markets could further affect the Corporation’s performance, both directly by affecting the Corporation’s revenues and the value of its assets and liabilities, and indirectly by affecting the Corporation’s counterparties and the economy in general. While there are some signs of improvement in the economic environment, there was a prolonged period of volatility and disruption in the markets, and unemployment has risen to, and remains at, high levels. There can be no assurance that these unprecedented developments will not continue to materially and adversely affect our business, financial condition and results of operations, as well as our ability to raise capital for liquidity and business purposes.

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

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

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

The following discussion supplements and provides information about the major components of the results of operations, financial condition, liquidity and capital resources of the Corporation. This discussion and analysis should be read in conjunction with the accompanying consolidated financial statements.

CRITICAL ACCOUNTING POLICIES

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

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

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

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

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

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

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

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

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

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

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

Goodwill: The Corporation's goodwill was recognized in connection with the Corporation's acquisition of CVBK in October 2013 and C&F Bank's acquisition of C&F Finance Company in September 2002. With the adoption of Accounting Standards Update (ASU) 2011-08, *Intangible-Goodwill and Other-Testing Goodwill for Impairment*, in 2012, the Corporation is no longer required to perform a test for impairment unless, based on an assessment of qualitative factors related to goodwill, we determine that it is more likely than not that the fair value of goodwill is less than its carrying amount. If the likelihood of impairment is more than 50 percent, the Corporation must perform a test for impairment and we may be required to record impairment charges. In assessing the recoverability of the Corporation's goodwill, major assumptions used in determining impairment are increases in future income, sales multiples in determining terminal value and the discount rate applied to future cash flows. If an impairment test is performed, we will prepare a sensitivity analysis by increasing the discount rate, lowering sales multiples and reducing increases in future income.

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

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

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

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

OVERVIEW

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

On October 1, 2013, the Corporation acquired all of the outstanding common stock of CVBK. The Corporation's financial position and results of operations as of and for the year ended December 31, 2013 include CVBK's financial position as of December 31, 2013 and CVBK's results of operations from October 1, 2013. Since the acquisition the Corporation has separately tracked the performance, financial condition and capital levels of CVBK and CVB.

Financial Performance Measures

Net income for the Corporation was $14.4 million in 2013, compared with net income of $16.4 million in 2012. Net income available to common shareholders for 2013 was $14.4 million, or $4.18 per common share assuming dilution, compared with $16.1 million, or $4.86 per common share assuming dilution for 2012. The difference between reported net income and net income available to common shareholders is a result of the Series A Preferred Stock dividends and accretion of the discount related to the Corporation’s participation in the Capital Purchase Program (CPP). The change in financial results for 2013, as compared to 2012, was principally attributable to (1) the first-time inclusion of CVBK's earnings, which included the net accretion of purchase accounting adjustments that were recognized when CVBK's assets and liabilities were marked to fair value as of the acquisition date, (2) improved earnings at C&F Bank resulting from a lower level of nonperforming assets during 2013, (3) an earnings decline in the Consumer Finance segment as an increasing volume of loan defaults and lower sale prices on repossessed vehicles sold resulted in an increase in its provision for loan losses, (4) an earnings decline in the Mortgage Banking segment resulting from lower loan production and expansion costs, and (5) expenses associated with the Corporation's acquisition of CVBK. See “Principal Business Activities” below for additional discussion.

The Corporation’s ROE and ROA were 13.39 percent and 1.35 percent, respectively, for the year ended December 31, 2013, compared to 17.05 percent and 1.71 percent for the year ended December 31, 2012. The decrease in these ratios during 2013 resulted from capital and asset growth, including growth due to the acquisition of CVBK, coupled with lower earnings during 2013.

2014 Outlook

Management believes the Corporation's financial performance in 2014 will be tempered by (i) costs associated with the integration of CVB into C&F Bank and strategic expansion efforts to grow its brand recognition, (ii) continued sluggish mortgage loan demand that may continue to depress loan production levels in the Mortgage Banking segment and that would be exacerbated by further increases in interest rates, and (iii) elevated charge-off levels in the Consumer Finance segment. The following factors could influence the Corporation’s financial performance in 2014:

- Retail Banking: The Retail Banking segment includes C&F Bank and CVB (collectively, the Banks). Our ability to achieve loan growth will be a significant influence on the Banks' performance during 2014. General economic trends in the Banks' markets have contributed to lackluster demand for new loans and increased competition to satisfy the limited loan demand that exists. It will be challenging to maintain the Retail Banking segment's net interest margin at its current level if funds obtained from loan repayments and from deposit growth cannot be fully used to originate new loans and instead are reinvested in lower-yielding assets. As part of our strategy to access loan demand and build our brand, C&F Bank has strengthened its commercial lending presence in Richmond, Virginia, improved its small business loan platform, and by virtue of the acquisition of CVBK, expanded its branch network from 18 branch locations to 25. While we will incur additional costs to fully integrate CVB's operations into C&F Bank, once successfully completed, we will be able to leverage the substantial cost of our technology investments over the past several years in systems and products that enhance fraud prevention and deliver state-of-the-art banking products to our customers.

- Mortgage Banking: C&F Mortgage generates significant noninterest income from the sale of residential loan products into the secondary market to investors. Our ability to maintain a level of loan production in 2014 sufficient to sustain profitability will be dependent on inter-related factors beyond our control, such as changes in interest rates, housing starts and loan demand. If mortgage interest rates rise during 2014, C&F Mortgage may experience a continuation of lower loan demand, particularly for mortgage refinancings, which could negatively affect earnings of the Mortgage Banking segment in 2014. In addition, during 2014 C&F Mortgage will continue to (i) incur fixed costs associated with its expansion into the Virginia Beach, Virginia area, (ii) compete to retain and attract qualified loan officers, especially given the heightened federal regulation of lending practices and loan terms and (iii) incur higher costs related to compliance with new residential mortgage regulations.

- Consumer Finance: C&F Finance provides automobile financing through lending programs that are designed to serve customers in the non-prime market. Loan performance within this market segment is particularly vulnerable to a protracted period of unemployment because unemployment benefits expire for those who have not been able to find employment and households may be underemployed. C&F Finance began experiencing higher delinquency levels and charge-offs during the second half of 2013, and if raised unemployment rates persist and if resale values on repossessed vehicles continue to decline, the elevated levels of charge-offs may continue in 2014, which will negatively affect the Consumer Finance segment's earnings in 2014. In addition, loan yields have been negatively affected by aggressive loan pricing strategies used by competitors attempting to grow market share in automobile financing. The combination of these factors may result in slower loan growth in the Consumer Finance segment during 2014. We also expect continued strong competition for qualified personnel in 2014, which may affect personnel costs at C&F Finance during 2014.

Principal Business Activities

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

Retail Banking: The Retail Banking segment reported net income of $3.3 million for the year ended December 31, 2013, compared to $2.2 million for the year ended December 31, 2012. The improvement in financial results for 2013, as compared to 2012, resulted from (1) CVB's net income of $651,000 since its acquisition on October 1, 2013, which includes $549,000 ($844,000 before income taxes) of net accretion of purchase accounting adjustments that were recognized when CVB's assets and liabilities were marked to fair value as of the acquisition date, (2) the effects of the continued low interest rate environment on C&F Bank's cost of deposits, coupled with the continued shift in its deposit mix to lower rate non-term deposit accounts, (3) improved loan credit quality at C&F Bank resulting in a decrease in the provision for loan losses, (4) a significant decline in C&F Bank's foreclosed properties resulting in lower holding costs and loss provisions and (5) higher service charges on C&F Bank's deposit accounts resulting from increased customer activity. Partially offsetting these positive factors at C&F Bank were (1) higher personnel costs associated with the addition of commercial loan personnel focused on growing the segment's commercial and small business loan portfolios, (2) higher occupancy expenses associated with depreciation and maintenance of technology investments related to expanding the banking products we offer to our customers and to improving our operational efficiency and security and (3) higher data processing expenses related to check card processing and mobile banking products and services.

C&F Bank's nonperforming assets were $6.0 million at December 31, 2013, compared to $17.7 million at December 31, 2012. Nonperforming assets at December 31, 2013 included $3.7 million in nonaccrual loans, compared to $11.5 million at December 31, 2012, and $2.2 million in foreclosed properties, compared to $6.2 million at December 31, 2012. Troubled debt restructured (TDR) loans were $5.2 million at December 31, 2013, of which $2.6 million were included in nonaccrual loans, as compared to $16.5 million of TDR loans at December 31, 2012, of which $9.8 million were included in nonaccrual loans. The decreases in nonaccrual and TDR loans were primarily a result of (1) the sale of $10.9 million of TDR loans during the first quarter of 2013 related to one commercial relationship, $5.2 million of which was on nonaccrual status at December 31, 2012 and (2) the pay-off of $2.0 million of nonaccrual TDR loans related to one commercial relationship. The sale of notes referred to above resulted in a $2.1 million charge-off, which was previously included in the allowance for loan losses and contributed to the decline in C&F Bank's allowance for loan losses as a percentage of total loans to 2.82 percent at December 31, 2013 from 3.38 percent at December 31, 2012. Other real estate owned at December 31, 2013 primarily consists of residential lots. These properties are evaluated regularly and have been written down to their estimated fair values less selling costs.

Loans acquired from CVB were adjusted to fair market value upon acquisition, thus eliminating CVB's allowance for losses on October 1, 2013. The fair market valuation includes adjustments for interest rates and credit quality. The loans acquired from CVB are segregated between purchased performing and purchased credit impaired (PCI) loans. The fair market value interest adjustments for the purchased performing and PCI loans were reductions of $1.3 million and $5.2 million, respectively. The fair market value credit adjustments for the purchased performing and PCI loans were reductions of $5.7 million and $11.7 million, respectively. PCI loans that were classified as nonperforming loans by CVBK are no longer classified as nonperforming. Management believes it has appropriately provided for potential credit losses inherent in the acquired loan portfolio at the date of acquisition in its fair market value adjustments.

Mortgage Banking: C&F Mortgage reported net income of $2.0 million for the year ended December 31, 2013, compared to $2.2 million for the year ended December 31, 2012. Net income at the Mortgage Banking segment was negatively affected by (1) higher mortgage interest rates primarily occurring during the third and fourth quarters of 2013 that caused lower loan application volume and correspondingly lower loan production for the three and twelve months ended December 31, 2013, (2) lower net interest income and gains on sales of loans resulting from lower loan production and (3) higher non-production based personnel costs associated with expansion into Virginia Beach, Virginia and with regulatory compliance.

During the second quarter of 2013, C&F Mortgage elected to begin using fair value accounting for loans held for sale and interest rate lock commitments, as well as for forward loan sales commitments and hedging instruments that are used to reduce the effect of changes in interest rates on loans that are to be sold in the secondary market. Under fair value accounting, gains on loans to be sold in the secondary market are recognized as loan applications progress through the origination pipeline, as opposed to recognizing gains when the loans are sold, as was done in the past. C&F Mortgage's pre-tax income for 2013 included gains of $333,000 attributable to fair value adjustments.

Loan origination volume for the year ended December 31, 2013 declined to $721.3 million from $840.1 million for the year ended December 31, 2012. During 2013, the amount of loan originations for refinancings and new and resale home purchases were $223.6 million and $497.7 million, respectively, compared to $344.4 million and $495.7 million, respectively, during 2012. The decrease in origination volume is largely a result of higher mortgage interest rates primarily occurring during the third and fourth quarters of 2013. The lower volume of loan originations in 2013 resulted in a decrease in gains on sales of loans, which were $7.5 million (including the positive effect of $333,000 of fair market value adjustments) for the year ended December 31, 2013, compared to $7.7 million for the year ended December 31, 2012.

Consumer Finance: C&F Finance reported net income of $10.5 million for the year ended December 31, 2013, compared to $12.6 million for the year ended December 31, 2012. While C&F Finance's net income for 2013 continued to benefit from the low funding costs on its variable-rate borrowings, these benefits were more than offset by (1) increases in the segment's provision for loan losses resulting from higher loan charge-offs due to persistently raised unemployment rates and lower resale values on repossessed vehicles and (2) a decline in average loan yields as a result of aggressive loan pricing strategies used by competitors attempting to grow market share in automobile financing.

C&F Finance's allowance for loan losses as a percentage of loans at December 31, 2013 was 8.32 percent, as compared with 7.96 percent at December 31, 2012. The increase in loan charge-offs during 2013 and the increase in the allowance for loan losses as a percentage of loans are a result of the current economic environment. Management believes that the current allowance for loan losses is adequate to absorb probable losses in the loan portfolio. However, if the current economic environment continues and credit easing by new entrants and competitors in the automobile financing sector intensifies, the Consumer Finance segment could continue to experience an elevated level of charge-offs during 2014, which may result in higher provisions for loan losses and limit loan portfolio growth.

Other and Eliminations: The net loss for this combined segment was $1.4 million for the year ended December 31, 2013, compared to a net loss of $607,000 for the year ended December 31, 2012. The "other segment" includes the Corporation's holding company, which recognized $1.0 million in transaction costs, net of taxes ($1.2 million before taxes) during the year ended December 31, 2013 associated with the Corporation's acquisition of CVBK.

Capital Management

Total shareholders’ equity was $112.9 million at December 31, 2013, compared to $102.2 million at December 31, 2012. Capital growth resulted from earnings for the year ended December 31, 2013 and from employees' stock option exercises, offset in part by the payment of dividends on common stock. Capital also included a $5.0 million net decrease in other comprehensive income due to the decline in the unrealized gain in the securities portfolio during 2013 due to rising interest rates. For the years ended December 31, 2013, 2012 and 2011, the Corporation's average common equity to average assets ratio was 10.07%, 10.03% and 8.75%, respectively. The Corporation's capital ratios exceed current regulatory capital standards for being well-capitalized.

The Corporation's board of directors continued its policy of paying dividends in 2013 and declared a quarterly cash dividend of 29 cents per common share for the fourth quarter of 2013. The dividend payout ratio was 26.6 percent of basic earnings per share for the year ended December 31, 2013. The board of directors continues to evaluate our dividend payout in light of changes in economic conditions, our capital levels and our expected future levels of earnings, and the changes to the regulatory capital framework implemented by the Basel III Final Rules that were approved during 2013 by the federal banking agencies and will be effective (subject to certain limited phase-in schedules) on January 1, 2015.

RESULTS OF OPERATIONS

NET INTEREST INCOME

The following table shows the average balance sheets for each of the years ended December 31, 2013, 2012 and 2011 and includes the average balances of CVBK since October 1, 2013, the date the Corporation acquired CVBK. The table also shows the amounts of interest earned on earning assets, with related yields, and interest expense on interest-bearing liabilities, with related rates. Net interest income also includes the net interest income of CVBK since October 1, 2013, which includes accretion and amortization associated with the fair value adjustments recognized in connection with the Corporation's purchase of CVBK. Loans include loans held for sale. Loans placed on a nonaccrual status are included in the balances and are included in the computation of yields, but had no material effect. Interest on tax-exempt loans and securities is presented on a taxable-equivalent basis (which converts the income on loans and investments for which no income taxes are paid to the equivalent yield as if income taxes were paid using the federal corporate income tax rate of 34 percent in all three years presented).

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

(Dollars in thousands)	**2013 Average Balance**	**Income/ Expense**	**Yield/ Rate**	**2012 Average Balance**	**Income/ Expense**	**Yield/ Rate**	**2011 Average Balance**	**Income/ Expense**	**Yield/ Rate**
Assets									
Securities:									
Taxable	**$47,886**	**$1,065**	**2.22 %**	$20,376	$336	1.65 %	$19,366	$314	1.62 %
Tax-exempt	**116,846**	**6,928**	**5.93**	117,612	7,059	6.00	118,984	7,362	6.19
Total securities	**164,732**	**7,993**	**4.85**	137,988	7,395	5.36	138,350	7,676	5.55
Loans, net	**761,751**	**74,456**	**9.77**	732,972	71,998	9.82	683,648	68,630	10.04
Interest-bearing deposits in other banks and Fed funds sold	**68,093**	**159**	**0.23**	11,695	22	0.19	19,863	46	0.23
Total earning assets	**994,576**	**82,608**	**8.31**	882,655	79,415	9.00	841,861	76,352	9.07
Allowance for loan losses	**(34,880)**			(35,126)			(30,652)		
Total non-earning assets	**108,088**			92,821			95,048		
Total assets	**$1,067,784**			$940,350			$906,257		
Liabilities and Shareholders' Equity									
Time and savings deposits:									
Interest-bearing deposits	**$137,615**	**$412**	**0.30 %**	$110,237	$410	0.37 %	$109,314	$552	0.51 %
Money market deposit accounts	**132,449**	**382**	**0.29**	98,045	369	0.38	77,882	507	0.65
Savings accounts	**61,237**	**73**	**0.12**	45,645	45	0.10	42,083	43	0.10
Certificates of deposit, $100 thousand or more	**133,363**	**1,464**	**1.10**	134,668	2,047	1.52	135,307	2,684	1.98
Other certificates of deposit	**179,387**	**1,920**	**1.07**	163,921	2,454	1.50	172,675	3,217	1.86
Total time and savings deposits	**644,051**	**4,251**	**0.66**	552,516	5,325	0.96	537,261	7,003	1.30
Borrowings	**167,003**	**4,372**	**2.62**	162,312	4,786	2.95	159,710	4,878	3.05
	811,054	**8,623**	**1.06**	714,828	10,111	1.41	696,971	11,881	1.70

Total interest-bearing liabilities								
Demand deposits	**123,859**			104,737			93,912		
Other liabilities	**25,348**			23,749			20,410		
Total liabilities	**960,261**			843,314			811,293		
Shareholders' equity	**107,523**			97,036			94,964		
Total liabilities and shareholders' equity	**$1,067,784**			$940,350			$906,257		
Net interest income		**$73,985**			$69,304			$64,471	
Interest rate spread			**7.25 %**			7.59 %			7.37 %
Interest expense to average earning assets			**0.87 %**			1.15 %			1.41 %
Net interest margin			**7.44 %**			7.85 %			7.66 %

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

TABLE 2: Rate-Volume Recap

	2013 from 2012 Increase (Decrease)		**Total**	**2012 from 2011 Increase (Decrease)**		**Total**
(Dollars in thousands)	**Due to Rate**	**Volume**	**Increase (Decrease)**	**Due to Rate**	**Volume**	**Increase (Decrease)**
Interest income:						
Loans	**$(357)**	**$2,815**	**$2,458**	$(1,501)	$4,869	$3,368
Securities:						
Taxable	**150**	**579**	**729**	5	17	22
Tax-exempt	**(85)**	**(46)**	**(131)**	(219)	(84)	(303)
Interest-bearing deposits in other banks and Fed funds sold	**7**	**130**	**137**	(8)	(16)	(24)
Total interest income	**(285)**	**3,478**	**3,193**	(1,723)	4,786	3,063
Interest expense:						
Time and savings deposits:						
Interest-bearing deposits	**(89)**	**91**	**2**	(147)	5	(142)
Money market deposit accounts	**(98)**	**111**	**13**	(248)	110	(138)
Savings accounts	**11**	**17**	**28**	(2)	4	2
Certificates of deposit, $100 thousand or more	**(563)**	**(20)**	**(583)**	(624)	(13)	(637)
Other certificates of deposit	**(749)**	**215**	**(534)**	(606)	(157)	(763)
Total time and savings deposits	**(1,488)**	**414**	**(1,074)**	(1,627)	(51)	(1,678)
Borrowings	**(549)**	**135**	**(414)**	(171)	79	(92)
Total interest expense	**(2,037)**	**549**	**(1,488)**	(1,798)	28	(1,770)
Change in net interest income	**$1,752**	**$2,929**	**$4,681**	$75	$4,758	$4,833

2013 Compared to 2012

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

Average loans, which includes both loans held for investment and loans held for sale, increased $28.8 million to $761.8 million for the year ended December 31, 2013, compared to the same period of 2012. In total, average loans held for investment increased $45.2 million from the year ended December 31, 2012 to the same period in 2013, which included increases of $36.1 million attributable to the acquisition of CVBK on October 1, 2013 and $20.7 million attributable to growth in the Consumer Finance segment's average loan portfolio. These increases were offset in part by a $12.0 million decline in C&F Bank's portfolio of average loans held for investment, where loan production has been negatively affected by weak demand for new loans in the current economic environment and intense competition for loans in our markets. The Mortgage Banking segment's average portfolio of loans held for sale decreased $16.4 million during 2013, compared to 2012. The decline in demand for mortgage loans and refinancing activity during 2013 resulted in a $118.8 million decrease in loan originations during 2013 compared to 2012.

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

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

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

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

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

It will be challenging to maintain the Retail Banking segment's net interest margin at its current level if funds obtained from loan repayments and from deposit growth cannot be fully used to originate new loans and instead are reinvested in lower-yielding earning assets, and if the reduction in earning asset yields exceeds interest rate declines in interest-bearing liabilities, which are approaching their interest rate floors. However, the Retail Banking segment's net interest margin in future periods will include accretion associated with the fair value adjustments to the loans purchased in the CVBK acquisition. If the current volatility in the ten-year treasury yield and in mortgage interest rates continues, the Mortgage Banking segment may continue to experience lower loan demand, particularly for refinancings, which could reduce interest income on loans originated for sale, further contributing to a deterioration in net interest margin. The net interest margin at the Consumer Finance segment will be most affected by increasing competition and loan pricing strategies that competitors may use to grow market share in automobile financing. This increased competition may result in lower yields as the Consumer Finance segment responds to competitive pricing pressures and fewer purchases of automobile retail installment sales contracts.

2012 Compared to 2011

Net interest income, on a taxable-equivalent basis, was $69.3 million for the year ended December 31, 2012, compared to $64.5 million for the year ended December 31, 2011. The higher net interest income during 2012, as compared to the same period of 2011, resulted from a 19 basis point increase in net interest margin to 7.85 percent, coupled with a 4.8 percent increase in average earning assets. The increase in net interest margin was principally a result of growth in the Consumer Finance segment's loan portfolio (which generates higher yields than the Retail Banking segment's loan portfolio) and decreases in the rates paid by the Retail Banking segment on savings and time deposits, partially offset by lower yields on the aggregate loan portfolio and municipal securities. The decreases in rates paid on time and savings deposits were primarily a result of the sustained low interest rate environment and the repricing of higher rate certificates of deposit as they matured to lower rates. In addition, the mix in interest-bearing deposits has shifted to shorter-term deposit accounts, including demand deposits and money market deposit accounts. The decreases in the yields on loans resulted primarily from higher average loans held for sale at the Mortgage Banking segment, which typically are lower yielding than loans held for investment. The increase in average loans held for sale offset the favorable effects of a change in the mix of loans held for investment, specifically an increase in higher yielding average loans at the Consumer Finance segment and a decline in lower yielding average loans at the Retail Banking segment, which resulted in higher yields on loans held for investment. The decline in the yield on securities resulted from calls and maturities of higher-yielding securities and purchases of municipal securities with lower yields in the current low interest rate environment.

Average loans, which includes both loans held for investment and loans held for sale, increased to $733.0 million for the year ended December 31, 2012 from $683.6 million for the year ended December 31, 2011. A portion of the increase occurred in the Mortgage Banking segment’s portfolio of loans held for sale, the average balance of which increased $28.2 million during 2012 compared to 2011. This increase is indicative of higher mortgage loan production due to the continued low interest rate environment that has led to increased mortgage borrowing and refinancing activity during 2012. In total, average loans to non-affiliates held for investment increased $21.2 million during 2012. The Consumer Finance segment's average loan portfolio increased $24.3 million during 2012 as a result of robust demand in existing and new markets. The increase in average loans at the Consumer Finance segment was offset in part by a $3.1 million decrease in the Retail Banking and Mortgage Banking segments' portfolios of average loans held for investment. Of this $3.1 million decrease, $2.9 million occurred in the Retail Banking loan portfolio, where loan production has been negatively affected by weak demand for new loans in the current economic environment and intensified competition for loans in our markets.

The overall yield on average loans decreased 22 basis points to 9.82 percent for the year ended December 31, 2012, when compared to 2011, principally as a result of the higher level of lower-yielding Mortgage Banking segment loans held for sale as a percentage of total loans, as well as a slight decrease in the yield on the Consumer Finance segment loans as a result of increased competition for automobile financing loans in the segment's markets.

Average securities available for sale decreased $362,000 for the year ended December 31, 2012, when compared to 2011. The decrease resulted from the effect of the lower interest rate environment on call activity, coupled with limited availability of reinvestment opportunities that satisfy the investment portfolio's role in managing interest rate sensitivity, providing liquidity and serving as an additional source of interest income. The lower yield on the available-for-sale securities portfolio during 2012 resulted from the calls and maturities of higher-yielding securities and purchases of lower yielding securities in the current low interest rate environment, as well as purchases of shorter term securities with lower yields throughout 2012 and 2011.

Average interest-bearing deposits in other banks and Federal funds sold decreased $8.2 million for the year ended December 31, 2012, when compared to 2011, as a result of deploying excess liquidity to partially fund loan demand at the Mortgage Banking and Consumer Finance segments. The average yield on these overnight funds declined four basis points during 2012 as a result of the continuing low interest rate environment.

Average interest-bearing time and savings deposits increased $15.3 million for the year ended December 31, 2012, compared to 2011, mainly due to a shift to shorter-term money market deposit accounts, which provide depositors greater flexibility for funds management and investing decisions in this low interest rate environment. The average cost of deposits declined 34 basis points during 2012 because time deposits that matured throughout 2012 and 2011 repriced at lower interest rates or were not renewed, interest rates paid on interest-bearing demand and money market deposits accounts decreased as a result of the sustained low interest rate environment and the balances of short-term savings and money market deposits, which pay a lower interest rate, increased.

Average borrowings increased $2.6 million for the year ended December 31, 2012, compared to 2011. This increase occurred in short-term fed funds purchased in order to fund the Mortgage Banking segment's portfolio of loans held for sale. The average cost of borrowings declined 10 basis points during 2012 because of the higher average balance of fed funds purchased in relation to total borrowings, as well as the maturity of $10.0 million of FHLB advances during the third quarter of 2012, which were replaced by advances carrying lower interest rates.

NONINTEREST INCOME

TABLE 3: Noninterest Income

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

(Dollars in thousands)	Year Ended December 31, 2012 Retail Banking	Mortgage Banking	Consumer Finance	Other and Eliminations	Total
Gains on sales of loans*	$—	$ 7,692	$ —	$ —	$7,692
Service charges on deposit accounts	3,326	—	—	—	3,326
Other service charges and fees	2,431	3,669	11	199	6,310
Gains on calls of available for sale securities	11	—	—	—	11
Other income	356	646	1,138	1,143	3,283
Total noninterest income	$6,124	$ 12,007	$ 1,149	$ 1,342	$20,622

(Dollars in thousands)	Year Ended December 31, 2011 Retail Banking	Mortgage Banking	Consumer Finance	Other and Eliminations	Total
Gains on sales of loans*	$—	$ 6,219	$ —	$ —	$6,219
Service charges on deposit accounts	3,509	—	—	—	3,509

Other service charges and fees	2,245	2,876	10	159	5,290
Gains on calls of available for sale securities	13	—	—	—	13
Other income	190	55	845	1,050	2,140
Total noninterest income	$5,957	$ 9,150	$ 855	$ 1,209	$17,171

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

2013 Compared to 2012

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

2012 Compared to 2011

Total noninterest income increased $3.5 million, or 20.1 percent, for the year ended December 31, 2012, compared to the same period in 2011. This increase resulted from higher gains on sales of loans and ancillary loan production fees at the Mortgage Banking segment due to the increase in loan originations and sales, coupled with increases in other income from higher activity-based debit card interchange fees at the Retail Banking segment and higher loan servicing fees at the Consumer Finance segment. In addition, there was $827,000 of unrealized appreciation in the Corporation's nonqualified defined contribution plan, as described in Item 8, "Financial Statements and Supplementary Data," under the heading "Note 12: Employee Benefit Plans." Partially offsetting these increases was a decline in the Retail Banking segment's service charges on deposit accounts, which resulted from lower overdraft fees during 2012.

NONINTEREST EXPENSE

TABLE 4: Noninterest Expense

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

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

Total noninterest expense	$27,947	$ 10,060	$ 11,691	$ 1,344	$51,042

(Dollars in thousands)	Year Ended December 31, 2011 Retail Banking	Mortgage Banking	Consumer Finance	Other and Eliminations	Total
Salaries and employee benefits*	$14,722	$ 2,169	$ 6,712	$ 839	$24,442
Occupancy expense	3,886	1,901	677	27	6,491
Other expenses:					
OREO expenses	1,416	11	—	—	1,427
Provision for indemnification losses	—	807	—	—	807
Other expenses	6,724	3,028	2,883	407	13,042
Total other expenses	8,140	3,846	2,883	407	15,276
Total noninterest expense	$26,748	$ 7,916	$ 10,272	$ 1,273	$46,209

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

2013 Compared to 2012

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

2012 Compared to 2011

Total noninterest expenses increased $4.8 million, or 10.5 percent, for the year ended December 31, 2012, compared to the same period in 2011. This increase occurred primarily from higher personnel costs at (1) the Mortgage Banking segment due to higher production and income-based compensation, which resulted from the increase in loan production and sales during 2012, as well as higher non-production compensation in order to manage the increasingly complex regulatory environment in which the Mortgage Banking segment operates, (2) the Retail Banking segment due to increased staffing in the branch network to support customer service initiatives, and (3) the Consumer Finance segment due to an increase in the number of personnel to support expansion into new markets and loan growth. In addition, there were increases in occupancy expense during 2012 at the Retail Banking segment due to depreciation and maintenance of technology investments related to expanding the banking products we offer to our customers and to improving our operational efficiency and security and at the Consumer Finance segment due to the relocation in April 2011 to a larger leased headquarters building and depreciation and maintenance of technology to support growth. The Mortgage Banking segment recognized a higher provision for indemnification losses during 2012 in connection with loans sold to investors.

INCOME TAXES

Applicable income taxes on 2013 earnings amounted to $6.7 million, resulting in an effective tax rate of 31.8 percent, compared with $7.6 million, or 31.8 percent, in 2012 and $5.7 million, or 30.7 percent, in 2011. While earnings of the Retail Banking segment, which are exempt from state income taxes and include tax-exempt income on securities issued by states and political subdivisions, increased in 2013, the effective rate remained the same for 2013 in relation to 2012 because the Corporation's earnings included $707,000 of non-deductible expenses associated with the acquisition of CVBK on October 1, 2013. The increase in the effective rate in 2012 in relation to 2011 resulted from higher pre-tax earnings at the non-bank business segments, which are not exempt from state income taxes and do not generate tax-exempt income. In addition, during 2012 there was a decrease at the Retail Banking segment in tax-exempt income generated by tax-exempt securities issued by states and political subdivisions.

ASSET QUALITY

Allowance and Provision for Loan Losses

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

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

- Real estate residential mortgage loans carry risks associated with the continued credit-worthiness of the borrower and changes in the value of the collateral.

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

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

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

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

Allowance for Loan Losses Methodology – Consumer Finance. The Consumer Finance segment's loans consist of non-prime automobile loans. These loans carry risks associated with (1) the continued credit-worthiness of borrowers who may be unable to meet the credit standards imposed by most traditional automobile financing sources and (2) the value of rapidly-depreciating collateral. These loans do not lend themselves to a classification process because of the short duration of time between delinquency and repossession. Therefore, the loan loss allowance review process generally focuses on the rates of delinquencies, deferrals, defaults, repossessions and losses. Allowance factors also include an analysis of charge-off history for relevant periods of time which can vary depending on economic conditions, and our judgment based on the overall analysis of the lending environment. Loans are segregated between performing and nonperforming loans. Performing loans are those that have made timely payments in accordance with the terms of the loan agreement and are not past due 90 days or more. Nonperforming loans are those that do not accrue interest and are greater than 90 days past due.

In accordance with its policies and guidelines and consistent with industry practices, C&F Finance, at times, offers payment deferrals to borrowers, whereby the borrower is allowed to move up to two payments within a twelve-month rolling period to the end of the loan. A fee will be collected for extensions only in states that permit it. An account for which all delinquent payments are deferred is classified as current at the time the deferment is granted and therefore is not included as a delinquent account. Thereafter, such an account is aged based on the timely payment of future installments in the same manner as any other account. We evaluate the results of this deferment strategy based upon the amount of cash installments that are collected on accounts after they have been deferred versus the extent to which the collateral underlying the deferred accounts has depreciated over the same period of time. Based on this evaluation, we believe that payment deferrals granted according to our policies and guidelines are an effective portfolio management technique and result in higher ultimate cash collections. Payment deferrals may affect the ultimate timing of when an account is charged off. Increased use of deferrals may result in a lengthening of the loss confirmation period, which would increase expectations of credit losses inherent in the portfolio and therefore increase the allowance for loan losses and related provision for loan losses. The average amounts deferred, as a percentage of loans outstanding, was 1.32 percent in 2013, 0.73 percent in 2012 and 0.69 percent in 2011.

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

TABLE 5: Allowance for Loan Losses

	Year Ended December 31,				
(Dollars in thousands)	**2013**	2012	2011	2010	2009
Allowance, beginning of period	**$35,907**	$33,677	$28,840	$24,027	$19,806
Provision for loan losses:					
Retail Banking segment	**1,030**	2,400	6,000	6,500	6,400
Mortgage Banking segment	**90**	165	360	34	563
Consumer Finance segment	**13,965**	9,840	7,800	8,425	11,600
Total provision for loan losses	**15,085**	12,405	14,160	14,959	18,563
Loans charged off:					
Real estate—residential mortgage	**849**	793	1,096	334	1,655
Real estate—construction[1]	—	—	—	—	2,234
Commercial, financial and agricultural[2]	**2,298**	2,074	2,566	3,787	1,110
Equity lines	**126**	159	52	44	—
Consumer	**399**	337	319	189	190
Consumer finance	**16,398**	10,134	8,144	7,976	10,988
Total loans charged off	**20,070**	13,497	12,177	12,330	16,177
Recoveries of loans previously charged off:					
Real estate—residential mortgage	**106**	35	98	6	3
Real estate—construction[1]	3	—	—	—	11
Commercial, financial and agricultural[2]	**227**	121	173	21	27
Equity lines	**28**	79	12	32	—
Consumer	**173**	207	122	83	63
Consumer finance	**3,393**	2,880	2,449	2,042	1,731
Total recoveries	**3,930**	3,322	2,854	2,184	1,835
Net loans charged off	**16,140**	10,175	9,323	10,146	14,342
Allowance, end of period	**$34,852**	$35,907	$33,677	$28,840	$24,027
Ratio of net charge-offs to average total loans outstanding during period for Retail Banking and Mortgage Banking	**0.73 %**	0.72 %	0.89 %	0.97 %	1.09 %
Ratio of net charge-offs to average total loans outstanding during period for Consumer Finance	**4.59 %**	2.76 %	2.39 %	2.89 %	5.18 %

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

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

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

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

TABLE 6: Allocation of Allowance for Loan Losses

	December 31,				
(Dollars in thousands)	**2013**	2012	2011	2010	2009
Allocation of allowance for loan losses, end of year:					
Real estate—residential mortgage	**$2,355**	$2,358	$2,379	$1,442	$1,295
Real estate—construction[1]	**434**	424	480	581	281
Commercial, financial and agricultural [2]	**7,805**	9,824	10,040	8,688	7,022
Equity lines	**892**	885	912	380	211
Consumer	**273**	283	319	307	267
Consumer finance	**23,093**	22,133	19,547	17,442	14,951
Unallocated	**—**	—	—	—	—
Balance, December 31	**$34,852**	$35,907	$33,677	$28,840	$24,027
Ratio of loans to total year-end loans:					
Real estate—residential mortgage	**23 %**	22 %	22 %	23 %	23 %
Real estate—construction[1]	**1**	1	1	2	2
Commercial, financial and agricultural [2]	**35**	30	33	34	39
Equity lines	**6**	5	5	5	5
Consumer	**1**	1	1	1	1
Consumer finance	**34**	41	38	35	30
	100 %	100 %	100 %	100 %	100 %

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

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

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

TABLE 7A: Credit Quality Indicators *

(Dollars in thousands)	**Pass**	**Special Mention**	**Substandard**	**Substandard Nonaccrual**	**Total[1]**
Real estate – residential mortgage	**$180,670**	**$2,209**	**$ 3,580**	**$ 1,996**	**$188,455**
Real estate – construction[2]	**2,899**	**116**	**2,795**	**—**	**5,810**

Commercial, financial and agricultural [3]	**243,576**	**8,571**	**34,573**	**1,873**	**288,593**
Equity lines	**48,603**	**1,003**	**898**	**291**	**50,795**
Consumer	**8,616**	**2**	**158**	**231**	**9,007**
	$484,364	**$11,901**	**$ 42,004**	**$ 4,391**	**$542,660**

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

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

[1] At December 31, 2013, the Corporation did not have any loans classified as Doubtful or Loss.
[2] Includes the Corporation's real estate construction lending and consumer real estate lot lending.
[3] Includes the Corporation's commercial real estate lending, land acquisition and development lending, builder line lending and commercial business lending.

Loans by credit quality indicators as of December 31, 2012 were as follows:

TABLE 7B: Credit Quality Indicators

(Dollars in thousands)	**Pass**	**Special Mention**	**Substandard**	**Substandard Nonaccrual**	**Total[1]**
Real estate – residential mortgage	$143,947	$ 1,374	$ 2,131	$ 1,805	$149,257
Real estate – construction[2]	2,133	—	2,929	—	5,062
Commercial, financial and agricultural [3]	167,693	6,678	21,247	9,434	205,052
Equity lines	31,199	1,327	767	31	33,324
Consumer	4,746	3	369	191	5,309
	$349,718	$ 9,382	$ 27,443	$ 11,461	$398,004

(Dollars in thousands)	**Performing**	**Non-performing**	**Total**
Consumer finance	$ 277,531	$ 655	$278,186

[1] At December 31, 2012, the Corporation did not have any loans classified as Doubtful or Loss.
[2] Includes the Corporation's real estate construction lending and consumer real estate lot lending.
[3] Includes the Corporation's commercial real estate lending, land acquisition and development lending, builder line lending and commercial business lending.

Because the Corporation acquired CVB's loan portfolio (including purchased performing loans and PCI loans) at fair value at October 1, 2013, the Corporation believes that the most relevant comparison of the Retail Banking segment's 2013 asset quality, as compared to 2012, is a discussion of C&F Bank's asset quality metrics.

C&F Bank's allowance for loan losses decreased $2.1 million since December 31, 2012, and the provision for loan losses decreased $1.4 million during 2013, as compared to 2012. The allowance for loan losses to total loans declined to 2.82 percent at December 31, 2013, compared to 3.38 percent at December 31, 2012. This decline resulted from improved credit quality in part due to the resolution of certain nonperforming notes, as discussed below. C&F Bank's substandard nonaccrual loans decreased to $3.7 million at December 31, 2013 from $11.5 million at December 31, 2012. This decline in substandard nonaccrual loans and the allowance ratio at C&F Bank occurred primarily as a result of (1) the sale of $10.9 million of TDRs related to one commercial relationship, $5.2 million of which was classified as nonaccruing at December 31, 2012 and (2) the pay-off of $2.0 million of TDRs related to one commercial relationship, which was classified as nonaccrual at December 31, 2012. The sale of notes referred to above resulted in a $2.1 million charge-off. Loss reserves that had previously been recorded for this relationship were adequate to cover the associated charge-off. C&F Bank's special mention and substandard loans also decreased to $8.6 million and $24.2 million, respectively, as a result of improved loan performance. We believe that the current level of the allowance for loan losses at C&F Bank is adequate to absorb any losses on existing loans that may become uncollectible. If current economic conditions continue or worsen, a higher level of nonperforming loans may be experienced in future periods, which may then require a higher provision for loan losses.

The Consumer Finance segment's allowance for loan losses increased to $23.1 million at December 31, 2013 from $22.1 million at December 31, 2012, and its provision for loan losses increased $4.1 million for the year ended December 31, 2013, as compared to 2012. The allowance for loan losses as a percentage of loans at December 31, 2013 was 8.32 percent, compared with 7.96 percent at December 31, 2012. The increase in the provision for loan losses during 2013 was primarily attributable to higher net charge-offs, which resulted from the uncertain economic conditions and lower resale prices of repossessed vehicles. We believe that the current level of the allowance for loan losses at the Consumer Finance segment is adequate to absorb any losses on existing loans that may become uncollectible. However, if unemployment levels remain elevated or increase in the future, or if the level of the inventory of repossessed vehicles increases or demand for used vehicles falls resulting in declining values of automobiles securing outstanding loans, or if credit easing by competitors in the automobile financing sector intensifies, a higher provision for loan losses may become necessary.

Nonperforming Assets

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

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

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

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

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

TABLE 8: Nonperforming Assets

Retail Banking Segment

(Dollars in thousands)	**2013**	2012	2011	2010	2009
C&F Bank					
Nonaccrual loans	**$3,740**	$11,461	$10,011	$7,765	$4,812
OREO*	**2,222**	6,236	6,059	10,295	12,360
Total nonperforming assets	**$5,962**	$17,697	$16,070	$18,060	$17,172
Accruing loans past due for 90 days or more	**$72**	$—	$68	$1,030	$451
Troubled debt restructurings	**$5,217**	$16,492	$17,094	$9,769	$3,111
Total loans	**$398,281**	$395,664	$401,745	$412,092	$445,093
Allowance for loan losses	**$11,231**	$13,381	$13,650	$11,228	$8,940
Nonperforming assets to total loans and OREO*	**1.49** %	4.40 %	3.94 %	4.28 %	3.75 %
Allowance for loan losses to total loans	**2.82**	3.38	3.40	2.72	2.01
Allowance for loan losses to nonaccrual loans	**300.29**	116.75	136.35	144.60	185.79
Central Virginia Bank (CVB)**					
Nonaccrual loans	**$651**	$—	$—	$—	$—
OREO*	**546**	—	—	—	—
Total nonperforming assets	**$1,197**	$—	$—	$—	$—
Accruing loans past due for 90 days or more	**$3**	$—	$—	$—	$—
Purchased performing troubled debt restructurings	**$403**	$—	$—	$—	$—

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

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

Mortgage Banking Segment

(Dollars in thousands)	**2013**	2012	2011	2010	2009
Nonaccrual loans	**$—**	$—	$621	$—	$204
OREO*	**—**	—	—	379	440

Total nonperforming assets	**$—**	$—	$621	$379	$644
Accruing loans past due for 90 days or more	**$—**	$—	$—	$—	$—
Troubled debt restructurings	**$—**	$—	$—	$—	$—
Total loans	**$2,914**	$2,340	$2,611	$2,739	$2,499
Allowance for loan losses	**$493**	$393	$480	$170	$136
Nonperforming assets to total loans and OREO*	**— %**	— %	23.78%	12.16%	21.91%
Allowance for loan losses to total loans	**16.92**	16.79	18.38	6.21	5.44
Allowance for loan losses to nonaccrual loans	**—**	—	77.29	—	66.67

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

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Consumer Finance Segment

(Dollars in thousands)	**2013**	2012	2011	2010	2009
Nonaccrual loans	**$1,187**	$655	$381	$151	$387
Accruing loans past due for 90 days or more	**$—**	$—	$—	$—	$—
Total loans	**$277,724**	$278,186	$246,305	$220,753	$189,439
Allowance for loan losses	**$23,093**	$22,133	$19,547	$17,442	$14,951
Nonaccrual consumer finance loans to total consumer finance loans	**0.43 %**	0.24 %	0.15 %	0.07 %	0.20 %
Allowance for loan losses to total consumer finance loans	**8.32**	7.96	7.94	7.90	7.89

Table 9 presents the changes in the OREO balance for 2013 and 2012:

TABLE 9: OREO Changes

	Year Ended December 31,	
(Dollars in thousands)	**2013**	**2012**
Balance at the beginning of year, gross	**$10,173**	$9,986
Transfers from loans	**588**	3,866
Acquired from CVBK	**395**	—
Capitalized costs	**—**	205
Charge-offs	**(261)**	(1,240)
Sales proceeds	**(4,209)**	(2,683)
Gain on disposition	**218**	39
Balance at the end of year, gross	**6,904**	10,173
Less allowance for losses	**(4,135)**	(3,937)
Balance at the end of year, net	**$2,769**	$6,236

Nonperforming assets of C&F Bank totaled $6.0 million at December 31, 2013, compared to $17.7 million at December 31, 2012, a 66 percent decrease during 2013. C&F Bank's nonperforming assets at December, 2013 included $3.7 million of nonaccrual loans, compared to $11.5 million at December 31, 2012, and $2.2 million of OREO compared to $6.2 million at December 31, 2012. The decrease in nonaccrual loans at C&F Bank since December 31, 2012 was primarily attributable to the sale of notes related to one commercial relationship, $5.2 million of which was on nonaccrual status at December 31, 2012, as well as the pay-off of notes related to another commercial relationship, $1.7 million of which was on nonaccrual status at December 31, 2012. The note sale resulted in a $2.1 million charge-off which reduced C&F Bank's ratio of the allowance for loan losses to total loans to 2.82 percent at December 31, 2013 from 3.38 percent at December 31, 2012. Despite the decline in this ratio, the ratio of the allowance for loan losses to nonaccrual loans increased to 300.29 percent at December 31, 2013 from 116.75 percent at December 31, 2012. Nonperforming assets of CVB totaled $1.2 million at December 31, 2013, and included $651,000 of nonaccrual purchased performing loans, which became nonaccrual in the fourth quarter of 2013, and $546,000 of OREO. Purchased credit impaired loans that were classified as nonperforming loans by CVB are no longer classified as nonperforming so long as, at acquisition and quarterly re-estimation periods, we believe we will fully collect the new carrying value of these loans.

We believe we have provided adequate loan loss reserves based on current appraisals or evaluations of the collateral. In some cases, appraisals have been adjusted to reflect current trends including sales prices, expenses, absorption periods and other current relevant factors.

The Corporation's aggregate OREO properties were $2.8 million at December 31, 2013, compared to $6.2 million at December 31, 2012, and primarily consisted of residential lots. These properties have been written down to their estimated fair values less cost to sell. The decline in OREO during 2013 resulted from sales, offset in part by $588,000 of loans transferred to OREO and $395,000 of OREO acquired from CVBK .

Nonaccrual loans at the Consumer Finance segment increased to $1.2 million at December 31, 2013 from $655,000 at December 31, 2012. As noted above, the allowance for loan losses at the Consumer Finance segment increased from $22.1 million at December 31, 2012 to $23.1 million at December 31, 2013, and the ratio of the allowance for loan losses to total consumer finance loans was 8.32 percent as of December 31, 2013, compared with 7.96 percent at December 31, 2012. Nonaccrual consumer finance loans remain relatively low compared to the allowance for loan losses and the total consumer finance loan portfolio because the Consumer Finance segment generally initiates repossession of loan collateral once a loan is 60 days or more past due but before the loan reaches 90 days or more past due and is evaluated for nonaccrual status.