



You belong here.

COLONY

BANKCORP, INC.

2016 ANNUAL REPORT

A photograph of a woman with voluminous, curly, light-brown hair. She is smiling warmly and looking down at a light-colored smartphone held in both hands. She is wearing a dark purple top under a grey button-down shirt. The background is a bright, out-of-focus outdoor setting. The image is framed by a dark red diagonal border.

Vision

Colony Bank strives to be a high performance community bank, providing shareholders with a fair return on their investment while improving the quality of life in the communities we serve.

Mission

Our mission can best be accomplished by applying sound banking principles in corporate decision-making and by providing our customers a degree of highly personalized, professional service that is unmatched in the market.

SERVICE | STABILITY | SUCCESS



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Dear Shareholders,

2016 was a year of significant accomplishment for Colony Bankcorp, Inc. Improvement in profitability, reduction in non-performing assets, repayment of TARP preferred securities, and an upgrade in facilities were the highlights of the year. Details of these highlights are summarized below:

Profitability:

- Consolidated income of \$8,673,210 compared to \$8,372,697 in 2015, a 3.59% increase.
- Income available to shareholders of \$7,179,900 compared to \$5,997,687 in 2015, a 19.71% increase.

Non-Performing Assets:

- Non-Performing assets decreased from \$23.3 million on 12/31/15 to \$18.8 million, a 19.2% reduction.
- Foreclosed real estate (OREO) decreased from \$8.8 million on 12/31/15 to \$6.4 million, a 27.3% reduction.
- Net charge offs were \$742,612 or .10% of total loans compared to \$1,063,911 or .14% of total loans in 2015.
- Loss on sale of foreclosed real estate (OREO) was \$648,138 compared to \$1,044,219 in 2015, a reduction of 37.93%.
- Past due loans of 30 days or more were 1.59% of total loans compared to 2.62% on 12/31/15.
- Criticized assets to capital and reserves was 25.67%, down from 31.36% at year end 2015.

TARP Preferred Securities:

- Outstanding TARP preferred securities were reduced from \$18,021,000 to \$9,360,000 during 2016.
- TARP preferred dividend expense declined from \$2,375,010 in 2015 to \$1,493,310 in 2016, a 37.12% reduction.

Facilities:

- A loan production office was opened on the town square in Statesboro.
- A full service office was opened on Drayton Street in historic downtown Savannah.
- A full service office was opened in historic downtown Tifton.
- Two Tifton offices and offices in Chester and Pitts were closed during the year to achieve strategic efficiency.

Continuing these trends into 2017 and beyond is our strategic plan. As we look forward to the next year, we anticipate challenges and uncertainty. The election results of November, 2016 have created the potential for significant changes in the economy. Healthcare, immigration, interest rates, inflation, regulation, tax reform and trade policy are all in line for change, and no one is certain of the direction or outcome. Any one of these

hot button issues can have a significant impact on our marketplace and/or our industry. We are confident that Colony is prepared for whatever changes occur, and that regardless, we can achieve our strategic objectives.

Confidence can be a marvelous motivator and is an indicator of what people expect, without any guarantee of certainty. Fortunately, as we enter 2017, both the University of Georgia Selig Center for Economic Growth (SCEG) and the Bureau of Business Research and Economic Development (BBRED) at Georgia Southern University indicate that confidence is surging. The SCEG states "Many of the same forces that contributed specifically to Georgia's growth in the past two years will be even stronger in 2017." Ayers said. "First, Georgia has even more projects in its economic development pipeline. Second, Georgia's economy will get more leverage from the housing recovery than the national economy. Third, Georgia's manufacturers will continue to do better than U.S. manufacturers. Fourth, Georgia will see faster population growth."

The BBRED reports "In the fourth quarter of 2016, participants were feeling positive about current business conditions in Georgia. Looking forward to the first quarter of 2017, participants are very optimistic that future business conditions will improve in Georgia. This is a major shift from the previous survey where the respondents felt only slightly positive about business conditions." "Many participants have an optimistic view going into 2017. Generally, participants are hoping that certainty is returning to the business world," said Ben McKay, research specialist at BBRED.

Confidence is a wonderful feeling to have! Hopefully we will look back on 2017 and see that the current level of confidence was well founded.

We want to thank B. Gene Waldron for serving as the Chairman of the Board of Colony Bankcorp, Inc. from 2012 until 2016. Mr. Waldron led the company during a very difficult period and we thank him for his service. Mark H. Masee became Chairman of the Board at the annual Shareholders meeting in May, 2016. Mr. Masee has been a Board member of Colony Bankcorp, Inc. for many years, most recently serving as Vice Chairman.

During January, 2017, the Board of Directors declared a cash dividend to shareholders of \$.025 per share payable March 31, 2017 to shareholders of record March 1, 2017. This dividend is the first paid by Colony Bankcorp, Inc. to its common shareholders since 2009 and is indicative of the confidence of the Board that we have survived the great recession and are poised for better days.

As always the board, management, and employees of Colony appreciate your support during 2016 and look forward to serving you during the coming year.



Edward P. Loomis, Jr.
President and
Chief Executive Officer



Mark H. Masee
Chairman of the Board



2016 KEY PERFORMANCE INDICATORS

Years Ended December 31, 2016 and 2015

Dollar amounts in thousands except per share data	2016	2015	Percent Change
Total Assets	\$1,210,442	\$1,174,149	3.09%
Total Deposits	\$1,044,357	\$1,011,554	3.24%
Loans (Net of Unearned Income)	\$753,922	\$758,279	(0.57)%
Net Income	\$7,180	\$5,998	19.71%
Per Share Data:			
Basic Earnings	\$0.85	\$0.71	19.72%
Common Book Value/Share	\$9.96	\$9.18	8.50%

KEY TRENDS

A Historical Comparative

Years Ending	2016	2015	2014	2013	2012
Net Income (in thousands)	\$7,180	\$5,998	\$4,843	\$3,120	\$1,206
Return on Average Shareholders' Equity	7.17%	5.90%	5.11%	3.34%	1.25%
Diluted Earnings Per Share	\$0.84	\$0.71	\$0.57	\$0.37	\$0.14

RETURN ON AVERAGE ASSETS	
2016	2015
0.62%	0.52%

NET INTEREST MARGIN	
2016	2015
3.51%	3.52%

Financial

SUMMARY

BOARD OF *directors*

Edward P. Loomis, Jr.

President/CEO
Colony Bankcorp, Inc.
Fitzgerald, Georgia

Mark H. Massee

Chairman
Colony Bankcorp, Inc.
President
Massee Builders, Inc.
Mayor of City of Fitzgerald
Fitzgerald, Georgia

B. Gene Waldron

Vice Chairman
Colony Bankcorp, Inc.
President/CEO
Waldron Enterprises, Inc.
Douglas, Georgia

Terry L. Hester

EVP/Chief Financial Officer
Colony Bankcorp, Inc.
Fitzgerald, Georgia

Jonathan W.R. Ross

President
Ross Construction Co., Inc.
Tifton, Georgia

Scott L. Downing

President
SDI Investments
Fitzgerald, Georgia

**Michael Frederick
(Freddie) Dwozan, Jr.**

President/CEO/Owner
Medical Center
Prescription Shop
Eastman, Georgia



Executive OFFICERS

Edward P. Loomis, Jr
President/CEO

Terry L. Hester
EVP/Chief Financial Officer

J. Stan Cook
EVP/Chief Operations Officer

Edward L. Bagwell, III
SVP/Chief Credit Officer

Lee A. Northcutt
EVP/Regional Executive Officer

M. Edward Hoyle, Jr.
EVP/Regional Executive Officer

MARKET presidents

Jeffery Alton
Market President
Thomaston

Bill Marsh
Market President
Tifton

Jon Butler
Market President
Eastman/Soperton

Scott Miller
Market President
Douglas/Broxton

Chip Carroll
Market President
Quitman

Walter Patten
Market President
Sylvester

Bob Evans
Market President
Cordele

John Roberts
Market President
Columbus

Phil Franklin
Market President
Albany/Leesburg/Chehaw

Kirk Scott
Market President
Warner Robins/Centerville

John Gandy
Market President
Moultrie

Eddie Smith
Market President
Valdosta

Drew Hulsey
Market President
Savannah/Statesboro

Mark Turner
Market President
Fitzgerald

Andy Johnson
Market President
Ashburn

Nic Worthy
Market President
Rochelle



McNAIR, McLEMORE, MIDDLEBROOKS & Co., LLC

CERTIFIED PUBLIC ACCOUNTANTS

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March 10, 2017

**REPORT OF INDEPENDENT
REGISTERED PUBLIC ACCOUNTING FIRM**

The Board of Directors and Stockholders
Colony Bankcorp, Inc.

We have audited the accompanying consolidated balance sheets of **Colony Bankcorp, Inc. and Subsidiary** as of December 31, 2016 and 2015 and the related consolidated statements of operations, comprehensive income (loss), changes in stockholders' equity and cash flows for each of the years in the three-year period ended December 31, 2016. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Colony Bankcorp, Inc. and Subsidiary as of December 31, 2016 and 2015, and the results of its operations and cash flows for each of the years in the three-year period ended December 31, 2016 in conformity with accounting principles generally accepted in the United States of America.

We were not engaged to examine management's assessment of the effectiveness of Colony Bankcorp, Inc.'s internal control over financial reporting as of December 31, 2016 included under Item 9A, *Controls and Procedures*, in Colony Bankcorp, Inc.'s Annual Report on Form 10-K and, accordingly, we do not express an opinion thereon.

McNair, McLemore, Middlebrooks & Co., LLC
McNAIR, McLEMORE, MIDDLEBROOKS & CO., LLC

COLONY BANKCORP, INC. AND SUBSIDIARY
CONSOLIDATED BALANCE SHEETS
DECEMBER 31

ASSETS

	2016	2015
Cash and Cash Equivalents		
Cash and Due from Banks	28,822,104	\$ 22,256,646
Interest-Bearing Deposits	46,344,859	38,615,299
Investment Securities		
Available for Sale, at Fair Value	323,657,870	296,149,299
Federal Home Loan Bank Stock, at Cost	3,010,000	2,730,500
Loans	754,283,563	758,635,595
Allowance for Loan Losses	(8,923,293)	(8,603,905)
Unearned Interest and Fees	(361,042)	(356,798)
	744,999,228	749,674,892
Premises and Equipment	27,969,260	26,453,530
Other Real Estate (Net of Allowance of \$1,878,127 and \$1,582,101 in 2016 and 2015, Respectively)	6,439,226	8,839,103
Other Intangible Assets	80,515	116,264
Other Assets	29,118,555	29,313,894
Total Assets	1,210,441,617	\$1,174,149,427

See accompanying notes which are an integral part of these financial statements.

**COLONY BANKCORP, INC. AND SUBSIDIARY
CONSOLIDATED BALANCE SHEETS
DECEMBER 31**

LIABILITIES AND STOCKHOLDERS' EQUITY

	2016	2015
Deposits		
Noninterest-Bearing	\$ 159,058,633	\$ 133,886,271
Interest-Bearing	885,297,895	877,667,965
	1,044,356,528	1,011,554,236
Borrowed Money		
Subordinated Debentures	24,229,000	24,229,000
Other Borrowed Money	46,000,000	40,000,000
	70,229,000	64,229,000
Other Liabilities	2,468,356	2,909,569
 Commitments and Contingencies		
 Stockholders' Equity		
Preferred Stock, Stated Value \$1,000; 10,000,000 Shares Authorized, 9,360 and 18,021 Shares Issued and Outstanding as of December 31, 2016 and 2015	9,360,000	18,021,000
Common Stock, Par Value \$1; 20,000,000 Shares Authorized, 8,439,258 Shares Issued and Outstanding as of December 31, 2016 and 2015	8,439,258	8,439,258
Paid-In Capital	29,145,094	29,145,094
Retained Earnings	51,465,521	44,285,621
Accumulated Other Comprehensive Loss, Net of Tax	(5,022,140)	(4,434,351)
	93,387,733	95,456,622
 Total Liabilities and Stockholders' Equity	\$1,210,441,617	\$1,174,149,427

See accompanying notes which are an integral part of these financial statements.

COLONY BANKCORP, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF OPERATIONS
FOR THE YEARS ENDED DECEMBER 31

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Interest Income			
Loans, Including Fees	\$38,942,503	\$39,716,269	\$39,735,615
Federal Funds Sold	-	14,561	32,100
Deposits with Other Banks	124,459	79,735	41,639
Investment Securities			
U.S. Government Agencies	5,263,741	4,235,207	4,737,878
State, County and Municipal	127,379	107,638	99,736
Dividends on Other Investments	131,007	122,070	115,134
	<u>44,589,089</u>	<u>44,275,480</u>	<u>44,762,102</u>
Interest Expense			
Deposits	4,781,228	4,856,673	5,113,024
Federal Funds Purchased	581	26	19
Borrowed Money	1,701,522	1,712,548	1,685,744
	<u>6,483,331</u>	<u>6,569,247</u>	<u>6,798,787</u>
Net Interest Income	<u>38,105,758</u>	<u>37,706,233</u>	<u>37,963,315</u>
Provision for Loan Losses	1,062,000	865,500	1,308,000
Net Interest Income After Provision for Loan Losses	<u>37,043,758</u>	<u>36,840,733</u>	<u>36,655,315</u>
Noninterest Income			
Service Charges on Deposits	4,307,214	4,268,438	4,649,008
Other Service Charges, Commissions and Fees	2,802,651	2,627,157	2,387,589
Mortgage Fee Income	681,806	527,187	419,963
Securities Gains (Losses)	385,223	(11,466)	23,735
Other	1,376,860	1,633,205	1,644,294
	<u>9,553,754</u>	<u>9,044,521</u>	<u>9,124,589</u>
Noninterest Expenses			
Salaries and Employee Benefits	18,482,693	17,589,631	17,507,926
Occupancy and Equipment	3,970,244	3,989,347	4,062,844
Directors' Fees	348,755	358,291	392,132
Legal and Professional Fees	791,563	737,731	785,683
Foreclosed Property	1,143,518	1,682,783	2,701,436
FDIC Assessment	603,654	899,302	965,898
Advertising	609,892	624,844	652,374
Software	1,112,065	992,593	925,489
Telephone	737,063	710,038	735,735
ATM/Card Processing	1,136,122	1,061,262	905,732
Other	5,137,400	5,078,932	5,344,743
	<u>34,072,969</u>	<u>33,724,754</u>	<u>34,979,992</u>
Income Before Income Taxes	<u>12,524,543</u>	<u>12,160,500</u>	<u>10,799,912</u>
Income Taxes	<u>3,851,333</u>	<u>3,787,803</u>	<u>3,268,287</u>
Net Income	<u>8,673,210</u>	<u>8,372,697</u>	<u>7,531,625</u>
Preferred Stock Dividends	1,493,310	2,375,010	2,688,604
Net Income Available to Common Stockholders	<u>\$ 7,179,900</u>	<u>\$ 5,997,687</u>	<u>\$ 4,843,021</u>
Net Income Per Share of Common Stock			
Basic	<u>\$ 0.85</u>	<u>\$ 0.71</u>	<u>\$ 0.57</u>
Diluted	<u>\$ 0.84</u>	<u>\$ 0.71</u>	<u>\$ 0.57</u>
Cash Dividends Declared Per Share of Common Stock	<u>\$ 0.00</u>	<u>\$ 0.00</u>	<u>\$ 0.00</u>
Weighted Average Shares Outstanding, Basic	<u>8,439,258</u>	<u>8,439,258</u>	<u>8,439,258</u>
Weighted Average Shares Outstanding, Diluted	<u>8,513,295</u>	<u>8,458,461</u>	<u>8,439,258</u>

See accompanying notes which are an integral part of these financial statements.

COLONY BANKCORP, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
FOR THE YEARS ENDED DECEMBER 31

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Net Income	<u>\$ 8,673,210</u>	<u>\$ 8,372,697</u>	<u>\$ 7,531,625</u>
Other Comprehensive Income (Loss)			
Gains (Losses) on Securities Arising During the Year	(505,367)	610,689	6,432,906
Tax Effect	171,825	(207,634)	(2,187,189)
Realized (Gains) Losses on Sale of AFS Securities	(385,223)	11,466	(23,735)
Tax Effect	130,976	(3,898)	8,070
Impairment Loss on Securities	-	-	-
Tax Effect	-	-	-
Change in Unrealized Gains (Losses) on Securities Available for Sale, Net of Reclassification Adjustment and Tax Effects	<u>(587,789)</u>	<u>410,623</u>	<u>4,230,052</u>
Comprehensive Income	<u><u>\$ 8,085,421</u></u>	<u><u>\$ 8,783,320</u></u>	<u><u>\$11,761,677</u></u>

See accompanying notes which are an integral part of these financial statements.

COLONY BANKCORP, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY
FOR THE YEARS ENDED DECEMBER 31, 2016, 2015 AND 2014

	Preferred Shares Issued	Preferred Stock	Common Shares Issued	Common Stock	Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total
Balance, December 31, 2013	28,000	28,000,000	8,439,258	8,439,258	29,145,094	33,444,913	(9,075,026)	89,954,239
Change in Net Unrealized Gains (Losses) on Securities Available for Sale, Net of Reclassification Adjustment and Tax Effects							4,230,052	4,230,052
Dividends on Preferred Shares						(2,688,604)		(2,688,604)
Net Income						7,531,625		7,531,625
Balance, December 31, 2014	28,000	28,000,000	8,439,258	8,439,258	29,145,094	38,287,934	(4,844,974)	99,027,312
Change in Net Unrealized Gains (Losses) on Securities Available for Sale, Net of Reclassification Adjustment and Tax Effects							410,623	410,623
Dividends on Preferred Shares	(9,979)	(9,979,000)				(2,375,010)		(2,375,010)
Redemption of Preferred Stock						8,372,697		(9,979,000)
Net Income								8,372,697
Balance, December 31, 2015	18,021	\$ 18,021,000	8,439,258	\$ 8,439,258	\$ 29,145,094	\$ 44,285,621	\$(4,434,351)	\$ 95,456,622
Change in Net Unrealized Gains (Losses) on Securities Available for Sale, Net of Reclassification Adjustment and Tax Effects							(587,789)	(587,789)
Dividends on Preferred Shares	(8,661)	(8,661,000)				(1,493,130)		(1,493,130)
Redemption of Preferred Stock						8,673,210		(8,661,000)
Net Income								8,673,210
Balance, December 31, 2016	9,360	\$ 9,360,000	8,439,258	\$ 8,439,258	\$ 29,145,094	\$ 51,465,521	\$(5,022,140)	\$ 93,387,733

See accompanying notes which are an integral part of these financial statements.

COLONY BANKCORP, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31

	2016	2015	2014
Cash Flows from Operating Activities			
Net Income	8,673,210	\$ 8,372,697	\$ 7,531,625
Adjustments to Reconcile Net Income to Net Cash Provided from Operating Activities			
Depreciation	1,574,249	1,657,229	1,595,253
Amortization and Accretion	1,609,339	1,797,152	1,312,857
Provision for Loan Losses	1,062,000	865,500	1,308,000
Deferred Income Taxes	222,120	625,436	1,932,950
Securities (Gains) Losses	(385,223)	11,466	(23,735)
(Gain) Loss on Sale of Premises and Equipment	80,329	11,047	(12,489)
Loss on Sale of Other Real Estate and Repossessions	160,682	600,663	828,411
Provision for Losses on Other Real Estate	501,736	453,148	1,006,827
Increase in Cash Surrender Value of Life Insurance	(589,408)	(299,010)	(590,674)
Change In			
Interest Receivable	176,766	(354,274)	55,786
Prepaid Expenses	(372,380)	278,637	(64,633)
Interest Payable	(46,284)	32,253	(1,099,756)
Accrued Expenses and Accounts Payable	(252,617)	(202,343)	197,195
Other	973,972	217,686	788,958
	13,388,491	14,067,287	14,766,575
Cash Flows from Investing Activities			
Interest-Bearing Deposits in Other Banks	(7,729,560)	(17,409,260)	754,252
Purchase of Investment Securities			
Available for Sale	(109,634,793)	(102,336,227)	(56,201,891)
Proceeds from Sale of Investment Securities			
Available for Sale	25,209,851	28,273,634	13,620,956
Proceeds from Maturities, Calls and Paydowns of Investment Securities			
Available for Sale	54,868,726	51,423,541	36,440,646
Held to Maturity	-	9,734	12,968
Proceeds from Sale of Premises and Equipment	89,551	28,608	14,376
Net Loans to Customers	(2,167,126)	(21,255,018)	(3,156,342)
Purchase of Premises and Equipment	(3,259,859)	(3,189,969)	(1,681,115)
Proceeds from Sale of Other Real Estate and Repossessions	7,529,131	8,154,596	7,233,497
Proceeds from Sale of Federal Home Loan Bank Stock	-	100,300	333,100
Purchase of Federal Home Loan Bank Stock	(279,500)	-	-
	(35,373,579)	(56,200,061)	(2,629,553)
Cash Flows from Financing Activities			
Interest-Bearing Customer Deposits	7,629,930	26,704,254	(21,305,068)
Noninterest-Bearing Customer Deposits	25,172,362	5,546,508	13,079,062
Proceeds from Other Borrowed Money	10,000,000	27,000,000	-
Principal Payments on Other Borrowed Money	(4,000,000)	(27,000,000)	-
Dividends Paid on Preferred Stock	(1,590,746)	(2,487,274)	(5,492,749)
Redemption of Preferred Stock	(8,661,000)	(9,979,000)	-
	28,550,546	19,784,488	(13,718,755)
Net Increase (Decrease) in Cash and Cash Equivalents	6,565,458	(22,348,286)	(1,581,733)
Cash and Cash Equivalents, Beginning	22,256,646	44,604,932	46,186,665
Cash and Cash Equivalents, Ending	\$28,822,104	\$ 22,256,646	\$ 44,604,932

See accompanying notes which are an integral part of these financial statements.

COLONY BANKCORP, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(1) Summary of Significant Accounting Policies

Principles of Consolidation

Colony Bankcorp, Inc. (the Company) is a bank holding company located in Fitzgerald, Georgia. The consolidated financial statements include the accounts of Colony Bankcorp, Inc. and its wholly-owned subsidiary, Colony Bank, Fitzgerald, Georgia. All significant intercompany accounts have been eliminated in consolidation. The accounting and reporting policies of Colony Bankcorp, Inc. conform to generally accepted accounting principles and practices utilized in the commercial banking industry.

Nature of Operations

The Company provides a full range of retail and commercial banking services for consumers and small- to medium-size businesses located primarily in central, south and coastal Georgia. Colony Bank is headquartered in Fitzgerald, Georgia with banking offices in Albany, Ashburn, Broxton, Centerville, Columbus, Cordele, Douglas, Eastman, Fitzgerald, Leesburg, Moultrie, Quitman, Rochelle, Savannah, Soperton, Statesboro, Sylvester, Thomaston, Tifton, Valdosta and Warner Robins. Lending and investing activities are funded primarily by deposits gathered through its retail banking office network.

Use of Estimates

In preparing the financial statements, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the balance sheet date and revenues and expenses for the period. Actual results could differ significantly from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses and the valuation of real estate acquired in connection with foreclosures or in satisfaction of loans.

Reclassifications

In certain instances, amounts reported in prior years' consolidated financial statements and note disclosures have been reclassified to conform to statement presentations selected for 2016. Such reclassifications had no effect on previously reported stockholders' equity or net income.

(1) Summary of Significant Accounting Policies (Continued)

Concentrations of Credit Risk

Concentrations of credit risk can exist in relation to individual borrowers or groups of borrowers, certain types of collateral, certain types of industries or certain geographic regions. The Company has a concentration in real estate loans as well as a geographic concentration that could pose an adverse credit risk, particularly with the current economic downturn in the real estate market. At December 31, 2016, approximately 87 percent of the Company's loan portfolio was concentrated in loans secured by real estate. A substantial portion of borrowers' ability to honor their contractual obligations is dependent upon the viability of the real estate economic sector. Declining collateral real estate values that secure land development, construction and speculative real estate loans in the Company's larger MSA markets have resulted in high loan loss provisions in recent years. In addition, a large portion of the Company's foreclosed assets are also located in these same geographic markets, making the recovery of the carrying amount of foreclosed assets susceptible to changes in market conditions. Management continues to monitor these concentrations and has considered these concentrations in its allowance for loan loss analysis.

The success of the Company is dependent, to a certain extent, upon the economic conditions in the geographic markets it serves. Adverse changes in the economic conditions in these geographic markets would likely have a material adverse effect on the Company's results of operations and financial condition. The operating results of the Company depend primarily on its net interest income. Accordingly, operations are subject to risks and uncertainties surrounding the exposure to changes in the interest rate environment.

At times, the Company may have cash and cash equivalents at financial institutions in excess of federal deposit insurance limits. The Company places its cash and cash equivalents with high credit quality financial institutions whose credit rating is monitored by management to minimize credit risk.

Investment Securities

The Company classifies its investment securities as trading, available for sale or held to maturity. Securities that are held principally for resale in the near term are classified as trading. Trading securities are carried at fair value, with realized and unrealized gains and losses included in noninterest income. Currently, no securities are classified as trading. Securities acquired with both the intent and ability to be held to maturity are classified as held to maturity and reported at amortized cost. All securities not classified as trading or held to maturity are considered available for sale. Securities available for sale are reported at estimated fair value. Unrealized gains and losses on securities available for sale are excluded from earnings and are reported, net of deferred taxes, in accumulated other comprehensive income (loss), a component of stockholders' equity. Gains and losses from sales of securities available for sale are computed using the specific identification method. Securities available for sale includes securities, which may be sold to meet liquidity needs arising from unanticipated deposit and loan fluctuations, changes in regulatory capital requirements, or unforeseen changes in market conditions.

(1) Summary of Significant Accounting Policies (Continued)

Investment Securities (Continued)

The Company evaluates each held to maturity and available for sale security in a loss position for other-than-temporary impairment (OTTI). In estimating other-than-temporary impairment losses, management considers such factors as the length of time and the extent to which the market value has been below cost, the financial condition of the issuer and the Company's intent to sell and whether it is more likely than not that the Company will be required to sell the security before anticipated recovery of the amortized cost basis. If the Company intends to sell or if it is more likely than not that the Company will be required to sell the security before recovery, the OTTI write-down is recognized in earnings. If the Company does not intend to sell the security or it is not more likely than not that it will be required to sell the security before recovery, the OTTI write-down is separated into an amount representing credit loss, which is recognized in earnings, and an amount related to all other factors, which is recognized in other comprehensive income (loss).

Federal Home Loan Bank Stock

Investment in stock of a Federal Home Loan Bank (FHLB) is required for every federally insured institution that utilizes its services. FHLB stock is considered restricted, as defined in the accounting standards. The FHLB stock is reported in the consolidated financial statements at cost. Dividend income is recognized when earned.

Loans

Loans that the Company has the ability and intent to hold for the foreseeable future or until maturity are recorded at their principal amount outstanding, net of unearned interest and fees. Loan origination fees, net of certain direct origination costs, are deferred and amortized over the estimated terms of the loans using the straight-line method. Interest income on loans is recognized using the effective interest method.

A loan is considered to be delinquent when payments have not been made according to contractual terms, typically evidenced by nonpayment of a monthly installment by the due date.

When management believes there is sufficient doubt as to the collectibility of principal or interest on any loan or generally when loans are 90 days or more past due, the accrual of applicable interest is discontinued and the loan is designated as nonaccrual, unless the loan is well secured and in the process of collection. Interest payments received on nonaccrual loans are either applied against principal or reported as income, according to management's judgment as to the collectibility of principal. Loans are returned to an accrual status when factors indicating doubtful collectibility on a timely basis no longer exist.

(1) Summary of Significant Accounting Policies (Continued)

Loans Modified in a Troubled Debt Restructuring (TDR)

Loans are considered to have been modified in a TDR when, due to a borrower's financial difficulty, the Company makes certain concessions to the borrower that it would not otherwise consider for new debt with similar risk characteristics. Modifications may include interest rate reductions, principal or interest forgiveness, forbearance, and other actions intended to minimize economic loss and to avoid foreclosure or repossession of the collateral. Generally, a nonaccrual loan that has been modified in a TDR remains on nonaccrual status for a period of six months to demonstrate that the borrower is able to meet the terms of the modified loan. However, performance prior to the modification, or significant events that coincide with the modification, are included in assessing whether the borrower can meet the new terms and may result in the loan being returned to accrual status at the time of loan modification or after a shorter performance period. If the borrower's ability to meet the revised payment schedule is uncertain, the loan remains on nonaccrual status. Once a loan is modified in a troubled debt restructuring, it is accounted for as an impaired loan, regardless of its accrual status, until the loan is paid in full, sold or charged off.

Allowance for Loan Losses

The allowance for loan losses is established as losses are estimated to have occurred through a provision for loan losses charged to earnings. Loan losses are charged against the allowance when management believes the uncollectibility of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance.

The allowance for loan losses is evaluated on a regular basis by management and is based upon management's periodic review of the collectibility of the loans in light of historical experience, the nature and volume of the loan portfolio, adverse situations that may affect the borrower's ability to repay, estimated value of any underlying collateral and prevailing economic conditions. This evaluation is inherently subjective, as it requires estimates that are susceptible to significant revisions as more information becomes available.

The allowance consists of specific, historical and general components. The specific component relates to loans that are classified as either doubtful, substandard or special mention. For such loans that are also classified as impaired, an allowance is established when the discounted cash flows (or collateral value or observable market price) of the impaired loan are lower than the carrying value of that loan. The historical component covers nonclassified loans and is based on historical loss experience adjusted for qualitative factors. A general component is maintained to cover uncertainties that could affect management's estimate of probable losses. The general component of the allowance reflects the margin of imprecision inherent in the underlying assumptions used in the methodologies for estimating specific and historical losses in the portfolio. General valuation allowances are based on internal and external qualitative risk factors such as (1) changes in lending policies and procedures, including changes in underwriting standards and collections, charge offs, and recovery practices, (2) changes in international, national, regional, and local conditions, (3) changes in the nature and volume of the portfolio and terms of loans, (4) changes in the experience, depth, and ability of lending management, (5) changes in the volume and severity of past due loans and other similar conditions, (6) changes in the quality of the organization's loan review system, (7) changes in the value of underlying collateral for collateral dependent loans, (8) the existence and effect of any concentrations of credit and changes in the levels of such concentrations, and (9) the effect of other external factors (i.e. competition, legal and regulatory requirements) on the level of estimated credit losses.

(1) Summary of Significant Accounting Policies (Continued)

Allowance for Loan Losses (Continued)

Loans identified as losses by management, internal loan review and/or Bank examiners are charged off. A loan is considered impaired when, based on current information and events, it is probable that the Company will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record and the amount of the shortfall in relation to the principal and interest owed. Impairment is measured on a loan-by-loan basis 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.

A significant portion of the Company's impaired loans are deemed to be collateral dependent. Management therefore measures impairment on these loans based on the fair value of the collateral. Collateral values are determined based on appraisals performed by qualified licensed appraisers hired by the Company or by senior members of the Company's credit administration staff. The decision whether to obtain an external third-party appraisal usually depends on the type of property being evaluated. External appraisals are usually obtained on more complex, income producing properties such as hotels, shopping centers and businesses. Less complex properties such as residential lots, farm land and single family houses may be evaluated internally by senior credit administration staff. When the Company does obtain appraisals from external third-parties, the values utilized in the impairment calculation are "as is" or current market values. The appraisals, whether prepared internally or externally, may utilize a single valuation approach or a combination of approaches including the comparable sales, income and cost approach. Appraised amounts used in the impairment calculation are typically discounted 10 percent to account for selling and marketing costs, if the repayment of the loan is to come from the sale of the collateral. Although appraisals may not be obtained each year on all impaired loans, the collateral values used in the impairment calculations are evaluated quarterly by management. Based on management's knowledge of the collateral and the current real estate market conditions, appraised values may be further discounted to reflect facts and circumstances known to management since the initial appraisal was performed.

Adjustments are routinely made in the appraisal process by the appraisers to adjust for differences between the comparable sales and income data available. Such adjustments are typically significant and result in a level 3 classification of the inputs for determining fair value. Because of the high degree of judgment required in estimating the fair value of collateral underlying impaired loans and because of the relationship between fair value and general economic conditions, we consider the fair value of impaired loans to be highly sensitive to changes in market conditions.

(1) Summary of Significant Accounting Policies (Continued)

Premises and Equipment

Premises and equipment are recorded at acquisition cost net of accumulated depreciation.

Depreciation is charged to operations over the estimated useful lives of the assets. The estimated useful lives and methods of depreciation are as follows:

<u>Description</u>	<u>Life in Years</u>	<u>Method</u>
Banking Premises	15-40	Straight-Line and Accelerated
Furniture and Equipment	5-10	Straight-Line and Accelerated

Expenditures for major renewals and betterments are capitalized. Maintenance and repairs are charged to operations as incurred. When property and equipment are retired or sold, the cost and accumulated depreciation are removed from the respective accounts and any gain or loss is reflected in other income or expense.

Other Intangible Assets

Intangible assets consist of core deposit intangibles acquired in connection with a business combination. The core deposit intangible is initially recognized based on an independent valuation performed as of the consummation date. The core deposit intangible is amortized by the straight-line method over the average remaining life of the acquired customer deposits.

Transfers of Financial Assets

Transfers of financial assets are accounted for as sales, when control over the assets has been surrendered. Control over transferred assets is deemed to be surrendered when (1) the assets have been isolated from the Company, (2) the transferee obtains the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred assets and (3) the Company does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity.

Statement of Cash Flows

For reporting cash flows, cash and cash equivalents include cash on hand, noninterest-bearing amounts due from banks, federal funds sold and securities purchased under agreement to resell. Cash flows from demand deposits, interest-bearing checking accounts, savings accounts, loans and certificates of deposit are reported net.

Advertising Costs

The Company expenses the cost of advertising in the periods in which those costs are incurred.

(1) Summary of Significant Accounting Policies (Continued)

Income Taxes

The provision for income taxes is based upon income for financial statement purposes, adjusted for nontaxable income and nondeductible expenses. Deferred income taxes have been provided when different accounting methods have been used in determining income for income tax purposes and for financial reporting purposes.

Deferred tax assets and liabilities are recognized based on future tax consequences attributable to differences arising from the financial statement carrying values of assets and liabilities and their tax basis. The differences relate primarily to depreciable assets (use of different depreciation methods for financial statement and income tax purposes) and allowance for loan losses (use of the allowance method for financial statement purposes and the direct write-off method for tax purposes). In the event of changes in the tax laws, deferred tax assets and liabilities are adjusted in the period of the enactment of those changes, with effects included in the income tax provision. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion or all of the deferred tax assets will not be realized. The Company and its subsidiary file a consolidated federal income tax return. The subsidiary pays its proportional share of federal income taxes to the Company based on its taxable income.

The Company's federal and state income tax returns for tax years 2016, 2015, 2014 and 2013 are subject to examination by the Internal Revenue Service (IRS) and the Georgia Department of Revenue, generally for three years after filing.

Positions taken in the Company's tax returns may be subject to challenge by the taxing authorities upon examination. Uncertain tax positions are initially recognized in the consolidated financial statements when it is more likely than not the position will be sustained upon examination by the tax authorities. Such tax positions are both initially and subsequently measured as the largest amount of tax benefit that is greater than 50 percent likely of being realized upon settlement with the tax authority, assuming full knowledge of the position and all relevant facts. The Company provides for interest and, in some cases, penalties on tax positions that may be challenged by the taxing authorities. Interest expense is recognized beginning in the first period that such interest would begin accruing. Penalties are recognized in the period that the Company claims the position in the tax return. Interest and penalties on income tax uncertainties are classified within income tax expense in the consolidated statements of operations.

Other Real Estate

Other real estate generally represents real estate acquired through foreclosure and is initially recorded at estimated fair value at the date of acquisition less the cost of disposal. Losses from the acquisition of property in full or partial satisfaction of debt are recorded as loan losses. Properties are evaluated regularly to ensure the recorded amounts are supported by current fair values, and valuation allowances are recorded as necessary to reduce the carrying amount to fair value less estimated cost of disposal. Routine holding costs and gains or losses upon disposition are included in foreclosed property expense.

(1) Summary of Significant Accounting Policies (Continued)

Bank-Owned Life Insurance

The Company has purchased life insurance on the lives of certain key members of management and directors. The life insurance policies are recorded at the amount that can be realized under the insurance contract at the balance sheet date, which is the cash surrender value adjusted for other charges or amounts due that are probable at settlement, if applicable. Increases in the cash surrender value are recorded as other income in the consolidated statements of income. The cash surrender value of the insurance contracts is recorded in other assets on the consolidated balance sheets in the amount of \$15,419,269 and \$14,829,861 as of December 31, 2016 and 2015, respectively.

Comprehensive Income

Accounting principles generally require that recognized revenue, expenses, gains and losses be included in net income. Certain changes in assets and liabilities, such as unrealized gains and losses on securities available for sale, represent equity changes from economic events of the period other than transactions with owners. Such items are considered components of other comprehensive income (loss). Accounting standards codification requires the presentation in the consolidated financial statements of net income and all items of other comprehensive income (loss) as total comprehensive income (loss).

Off-Balance Sheet Credit Related Financial Instruments

In the ordinary course of business, the Company has entered into commitments to extend credit, commercial letters of credit and standby letters of credit. Such financial instruments are recorded on the consolidated balance sheets when they are funded.

(1) Summary of Significant Accounting Policies (Continued)

Changes in Accounting Principles and Effects of New Accounting Pronouncements

ASU 2014-09, *Revenue from Contracts with Customers (Topic 606)*. The core principle of ASU 2014-09 is to recognize revenues when promised goods or services are transferred to customers in an amount that reflects the consideration to which an entity is expected to be entitled for those goods or services. ASU 2014-09 defines a five-step process to achieve this core principle and, in doing so, it is possible more judgment and estimates may be required within the revenue recognition process than required under existing U.S. GAAP, including identifying performance obligations in the contract, estimating the amount of variable consideration to include in the transaction price and allocating the transaction price to each performance obligation. ASU 2014-09, as deferred one year by ASU 2015-14, is effective for the Company in the first quarter of fiscal year 2018. The Company is currently evaluating the impact of the pending adoption of ASU 2014-09 on the consolidated financial statements.

ASU 2016-01, *Financial Instruments – Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities*. ASU 2016-01, among other things, (i) requires equity investments, with certain exceptions, to be measured at fair value with changes in fair value recognized in net income, (ii) simplifies the impairment assessment of equity investments without readily determinable fair values by requiring a qualitative assessment to identify impairment, (iii) eliminates the requirement for public business entities to disclose the methods and significant assumptions used to estimate the fair value that is required to be disclosed for financial instruments measured at amortized cost on the balance sheet, (iv) requires public business entities to use the exit price notion when measuring the fair value of financial instruments for disclosure purposes, (v) requires an entity to present separately in other comprehensive income the portion of the total change in the fair value of a liability resulting from a change in the instrument-specific credit risk when the entity has elected to measure the liability at fair value in accordance with the fair value option for financial instruments, (vi) requires separate presentation of financial assets and financial liabilities by measurement category and form of financial asset on the balance sheet or the accompanying notes to the financial statements and (viii) clarifies that an entity should evaluate the need for a valuation allowance on a deferred tax asset related to available-for-sale. ASU 2016-01 will be effective for the Company on January 1, 2018. The Company is currently evaluating the impact of the pending adoption of ASU 2016-01 on the consolidated financial statements.

ASU 2016-02, *Leases (Topic 842)*. This ASU requires lessees to put most leases on their balance sheets but recognize expenses in the income statement in a manner similar to current accounting treatment. This ASU changes the guidance on sale-leaseback transactions, initial direct costs and lease execution costs, and, for lessors, modifies the classification criteria and the accounting for sales-type and direct financing leases. For public business entities, this ASU is effective for annual periods beginning after December 15, 2018, and interim periods therein. Entities are required to use a modified retrospective approach for leases that exist or are entered into after the beginning of the earliest comparative period in the financial statements. The Company is evaluating the impact of this ASU on its financial statements and disclosures.

ASU 2016-09, *Compensation – Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting*. This ASU simplifies several aspects of the accounting for employee share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. For public business entities, this ASU is effective for financial statements issued for fiscal years beginning after December 15, 2016, and interim periods therein. The Company is evaluating the impact of this ASU on its financial statements and disclosures.

(1) Summary of Significant Accounting Policies (Continued)

Changes in Accounting Principles and Effects of New Accounting Pronouncements (Continued)

ASU 2016-13, *Financial Instruments – Credit Losses (Topic 326)*. This ASU sets forth a “current expected credit loss” (CECL) model which requires the Company to measure all expected credit losses for financial instruments held at the reporting date based on historical experience, current conditions and reasonable supported forecasts. This replaces the existing incurred loss model and is applicable to the measurement of credit losses on financial assets measured at amortized cost and applies to some off-balance sheet credit exposures. This ASU is effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. The Company is currently assessing the impact of the adoption of this ASU on its consolidated financial statements.

ASU 2016-15, *Statement of Cash Flows (Topic 230) - Classification of Certain Cash Receipts and Cash Payments*. ASU 2016-15 provides guidance related to certain cash flow issues in order to reduce the current and potential future diversity in practice. ASU 2016-15 will be effective for us on January 1, 2018 and is not expected to have a significant impact on our financial statements.

(2) Cash and Balances Due from Banks

Components of cash and balances due from banks are as follows as of December 31:

	<u>2016</u>	<u>2015</u>
Cash on Hand and Cash Items	\$ 8,509,530	\$ 9,061,678
Noninterest-Bearing Deposits with Other Banks	20,312,574	13,194,968
	<u>\$28,822,104</u>	<u>\$22,256,646</u>

The Company is required to maintain reserve balances in cash or on deposit with the Federal Reserve Bank based on a percentage of deposits. Reserve balances totaled approximately \$1,417,000 and \$1,275,000 at December 31, 2016 and 2015, respectively.

(3) Investment Securities

Investment securities as of December 31, 2016 are summarized as follows:

	<u>Amortized Cost</u>	<u>Gross Unrealized Gains</u>	<u>Gross Unrealized Losses</u>	<u>Fair Value</u>
Securities Available for Sale				
U.S. Government Agencies				
Mortgage-Backed	\$ 326,694,417	\$ 75,743	\$ (7,672,786)	\$ 319,097,374
State, County and Municipal	<u>4,572,756</u>	<u>18,350</u>	<u>(30,610)</u>	<u>4,560,496</u>
	<u>\$ 331,267,173</u>	<u>\$ 94,093</u>	<u>\$ (7,703,396)</u>	<u>\$ 323,657,870</u>

The amortized cost and fair value of investment securities as of December 31, 2016, by contractual maturity, are shown hereafter. Expected maturities may differ from contractual maturities for certain investments because issuers may have the right to call or prepay obligations with or without call or prepayment penalties. This is often the case with mortgage-backed securities, which are disclosed separately in the table below.

	Securities Available for Sale	
	<u>Amortized Cost</u>	<u>Fair Value</u>
Due in One Year or Less	\$ 360,471	\$ 362,760
Due After One Year Through Five Years	1,618,395	1,610,940
Due After Five Years Through Ten Years	1,106,315	1,107,718
Due After Ten Years	<u>1,487,575</u>	<u>1,479,078</u>
	4,572,756	4,560,496
 Mortgage-Backed Securities	 <u>326,694,417</u>	 <u>319,097,374</u>
	<u>\$331,267,173</u>	<u>\$323,657,870</u>

Investment securities as of December 31, 2015 are summarized as follows:

	<u>Amortized Cost</u>	<u>Gross Unrealized Gains</u>	<u>Gross Unrealized Losses</u>	<u>Fair Value</u>
Securities Available for Sale				
U.S. Government Agencies				
Mortgage-Backed	\$297,778,875	\$62,815	\$(6,791,837)	\$291,049,853
State, County and Municipal	<u>5,089,137</u>	<u>30,542</u>	<u>(20,233)</u>	<u>5,099,446</u>
	<u>\$302,868,012</u>	<u>\$93,357</u>	<u>\$(6,812,070)</u>	<u>\$296,149,299</u>

(3) Investment Securities (Continued)

Proceeds from sales of investments available for sale were \$25,209,851 in 2016, \$28,273,634 in 2015, and 13,620,956 in 2014. Gross realized gains totaled \$391,976 in 2016, \$207,896 in 2015, and \$67,601 in 2014. Gross realized losses totaled \$6,753 in 2016, \$196,316 in 2015, and \$45,666 in 2014. Gross realized losses of \$23,046 in 2015 was due to a loss on a maturity for a held-to-maturity investment and gross realized gains of \$1,800 in 2014 was due to a gain on a call for a held-to-maturity investment.

Investment securities having a carrying value totaling \$144,853,885 and \$133,754,087 as of December 31, 2016 and 2015, respectively, were pledged to secure public deposits and for other purposes.

Information pertaining to securities with gross unrealized losses at December 31, 2016 and 2015 aggregated by investment category and length of time that individual securities have been in a continuous loss position, follows:

	Less Than 12 Months		12 Months or Greater		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
December 31, 2016						
U.S. Government Agencies						
Mortgage-Backed	\$174,200,881	\$(3,459,564)	\$107,481,698	\$(4,213,222)	\$281,682,579	\$(7,672,786)
State, County and Municipal	3,487,647	(30,610)	-	-	3,487,647	(30,610)
	<u>\$177,688,528</u>	<u>\$(3,490,174)</u>	<u>\$107,481,698</u>	<u>\$(4,213,222)</u>	<u>\$285,170,226</u>	<u>\$(7,703,396)</u>
December 31, 2015						
U.S. Government Agencies						
Mortgage-Backed	\$139,765,025	\$(1,270,011)	\$139,720,125	\$(5,521,826)	\$279,485,150	\$(6,791,837)
State, County and Municipal	1,034,613	(20,233)	-	-	1,034,613	(20,233)
	<u>\$140,799,638</u>	<u>\$(1,290,244)</u>	<u>\$139,720,125</u>	<u>\$(5,521,826)</u>	<u>\$280,519,763</u>	<u>\$(6,812,070)</u>

Management evaluates securities for other-than-temporary impairment at least on a quarterly basis, and more frequently when economic or market concerns warrant such evaluation. Consideration is given to (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer and (3) the intent and ability of the Company to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value.

(3) Investment Securities (Continued)

At December 31, 2016, 108 securities have unrealized losses which have depreciated 2.63 percent from the Company's amortized cost basis. These securities are guaranteed by either the U.S. Government, other governments or U.S. corporations. In analyzing an issuer's financial condition, management considers whether the securities are issued by the federal government or its agencies, whether downgrades by bond rating agencies have occurred and the results of reviews of the issuer's financial condition. The unrealized losses are largely due to increases in market interest rates over the yields available at the time the underlying securities were purchased. As management has the ability to hold debt securities until maturity, or for the foreseeable future if classified as available-for-sale, no declines are deemed to be other than temporary. However, the Company did own one asset-backed security at December 31, 2016 which was completely written off during prior years. This investment is comprised of one issuance of a trust preferred security and has no book value.

(4) Loans

The following table presents the composition of loans, segregated by class of loans, as of December 31:

	<u>2016</u>	<u>2015</u>
Commercial and Agricultural		
Commercial	\$ 47,024,878	\$ 47,781,689
Agricultural	17,079,579	19,193,497
Real Estate		
Commercial Construction	30,358,362	40,106,633
Residential Construction	11,830,447	9,413,263
Commercial	349,090,031	346,262,033
Residential	195,579,967	197,002,419
Farmland	66,877,197	61,779,859
Consumer and Other		
Consumer	19,695,241	20,605,465
Other	16,747,861	16,490,737
Total Loans	<u><u>\$754,283,563</u></u>	<u><u>\$758,635,595</u></u>

(4) Loans (Continued)

Commercial and agricultural loans are extended to a diverse group of businesses within the Company's market area. These loans are often underwritten based on the borrower's ability to service the debt from income from the business. Real estate construction loans often require loan funds to be advanced prior to completion of the project. Due to uncertainties inherent in estimating construction costs, changes in interest rates and other economic conditions, these loans often pose a higher risk than other types of loans. Consumer loans are originated at the bank level. These loans are generally smaller loan amounts spread across many individual borrowers to help minimize risk.

Credit Quality Indicators. As part of the ongoing monitoring of the credit quality of the loan portfolio, management tracks certain credit quality indicators including trends related to (1) the risk grade assigned to commercial and consumer loans, (2) the level of classified commercial loans, (3) net charge-offs, (4) nonperforming loans, and (5) the general economic conditions in the Company's geographic markets.

The Company uses a risk grading matrix to assign a risk grade to each of its loans. Loans are graded on a scale of 1 to 8. A description of the general characteristics of the grades is as follows:

- Grades 1 and 2 - Borrowers with these assigned grades range in risk from virtual absence of risk to minimal risk. Such loans may be secured by Company-issued and controlled certificates of deposit or properly margined equity securities or bonds. Other loans comprising these grades are made to companies that have been in existence for a long period of time with many years of consecutive profits and strong equity, good liquidity, excellent debt service ability and unblemished past performance, or to exceptionally strong individuals with collateral of unquestioned value that fully secures the loans. Loans in this category fall into the "pass" classification.
- Grades 3 and 4 - Loans assigned these "pass" risk grades are made to borrowers with acceptable credit quality and risk. The risk ranges from loans with no significant weaknesses in repayment capacity and collateral protection to acceptable loans with one or more risk factors considered to be more than average.
- Grade 5 - This grade includes "special mention" loans on management's watch list and is intended to be used on a temporary basis for pass grade loans where risk-modifying action is intended in the short-term.
- Grade 6 - This grade includes "substandard" loans in accordance with regulatory guidelines. This category includes borrowers with well-defined weaknesses that jeopardize the payment of the debt in accordance with the agreed terms. Loans considered to be impaired are assigned this grade, and these loans often have assigned loss allocations as part of the allowance for loan and lease losses. Generally, loans on which interest accrual has been stopped would be included in this grade.
- Grades 7 and 8 - These grades correspond to regulatory classification definitions of "doubtful" and "loss," respectively. In practice, any loan with these grades would be for a very short period of time, and generally the Company has no loans with these assigned grades. Management manages the Company's problem loans in such a way that uncollectible loans or uncollectible portions of loans are charged off immediately with any residual, collectible amounts assigned a risk grade of 6.

(4) Loans (Continued)

The following tables present the loan portfolio by credit quality indicator (risk grade) as of December 31. Those loans with a risk grade of 1, 2, 3 or 4 have been combined in the pass column for presentation purposes.

2016	Pass	Special Mention	Substandard	Total Loans
Commercial and Agricultural				
Commercial	\$ 44,249,874	\$ 1,861,757	\$ 913,247	\$ 47,024,878
Agricultural	16,585,646	192,445	301,488	17,079,579
Real Estate				
Commercial Construction	28,425,373	1,349,447	583,542	30,358,362
Residential Construction	11,630,165	-	200,282	11,830,447
Commercial	327,561,169	9,403,077	12,125,785	349,090,031
Residential	178,618,510	5,658,526	11,302,931	195,579,967
Farmland	65,074,715	839,362	963,120	66,877,197
Consumer and Other				
Consumer	19,071,739	225,959	397,543	19,695,241
Other	16,747,861	-	-	16,747,861
Total Loans	\$707,965,052	\$19,530,573	\$26,787,938	\$754,283,563
2015				
Commercial and Agricultural				
Commercial	\$ 44,273,407	\$ 1,927,198	\$ 1,581,084	\$ 47,781,689
Agricultural	18,970,328	17,843	205,326	19,193,497
Real Estate				
Commercial Construction	36,516,165	912,295	2,678,173	40,106,633
Residential Construction	9,413,263	-	-	9,413,263
Commercial	320,566,237	13,652,416	12,043,380	346,262,033
Residential	177,054,188	8,545,942	11,402,289	197,002,419
Farmland	56,798,365	929,814	4,051,680	61,779,859
Consumer and Other				
Consumer	20,037,996	156,739	410,730	20,605,465
Other	16,465,593	636	24,508	16,490,737
Total Loans	\$700,095,542	\$26,142,883	\$ 32,397,170	\$758,635,595

A loan's risk grade is assigned at the inception of the loan and is based on the financial strength of the borrower and the type of collateral. Loan risk grades are subject to reassessment at various times throughout the year as part of the Company's ongoing loan review process. Loans with an assigned risk grade of 6 or below and an outstanding balance of \$250,000 or more are reassessed on a quarterly basis. During this reassessment process individual reserves may be identified and placed against certain loans which are not considered impaired. In assessing the overall economic condition of the markets in which it operates, the Company monitors the unemployment rates for its major service areas. The unemployment rates are reviewed on a quarterly basis as part of the allowance for loan loss determination.

(4) Loans (Continued)

Loans are considered past due if the required principal and interest payments have not been received as of the date such payments were due. Generally, loans are placed on nonaccrual status if principal or interest payments become 90 days past due or when, in management's opinion, the borrower may be unable to meet payment obligations as they become due, as well as when required by regulatory provision. Loans may be placed on nonaccrual status regardless of whether such loans are considered past due.

The following table represents an age analysis of past due loans and nonaccrual loans, segregated by class of loans, as of December 31:

2016	Accruing Loans			Nonaccrual Loans	Current Loans	Total Loans
	30-89 Days Past Due	90 Days or More Past Due	Total Accruing Loans Past Due			
Commercial and Agricultural						
Commercial	\$ 419,969	\$ -	\$ 419,969	\$ 634,955	\$ 45,969,954	\$ 47,024,878
Agricultural	33,046	-	33,046	208,522	16,838,011	17,079,579
Real Estate						
Commercial Construction	54,001	-	54,001	190,494	30,113,867	30,358,362
Residential Construction	-	-	-	-	11,830,447	11,830,447
Commercial	491,468	-	491,468	6,360,176	342,238,387	349,090,031
Residential	3,178,833	-	3,178,833	3,944,337	188,456,797	195,579,967
Farmland	95,309	-	95,309	799,556	65,982,332	66,877,197
Consumer and Other						
Consumer	196,242	122	196,364	212,026	19,286,851	19,695,241
Other	-	-	-	-	16,747,861	16,747,861
Total Loans	\$4,468,868	\$ 122	\$4,468,990	\$12,350,066	\$737,464,507	\$754,283,563
2015						
Commercial and Agricultural						
Commercial	\$ 490,727	\$ -	\$ 490,727	\$ 576,940	\$ 46,714,022	\$ 47,781,689
Agricultural	71,416	-	71,416	178,021	18,944,060	19,193,497
Real Estate						
Commercial Construction	90,163	-	90,163	1,642,666	38,373,804	40,106,633
Residential Construction	-	-	-	-	9,413,263	9,413,263
Commercial	6,031,257	-	6,031,257	7,564,691	332,666,085	346,262,033
Residential	3,682,509	-	3,682,509	3,163,571	190,156,339	197,002,419
Farmland	122,696	-	122,696	1,103,354	60,553,809	61,779,859
Consumer and Other						
Consumer	469,839	7,799	477,638	178,336	19,949,491	20,605,465
Other	636	-	636	100	16,490,001	16,490,737
Total Loans	\$10,959,243	\$7,799	\$ 10,967,042	\$14,407,679	\$733,260,874	\$758,635,595

(4) Loans (Continued)

Had nonaccrual loans performed in accordance with their original contractual terms, the Company would have recognized additional interest income of approximately \$387,300, \$418,400, and \$591,900 for the years ended December 31, 2016, 2015 and 2014, respectively.

The following table details impaired loan data as of December 31, 2016:

	Unpaid Contractual Principal Balance	Impaired Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized	Interest Income Collected
With No Related Allowance Recorded						
Commercial	\$ 634,955	\$ 634,955	\$ -	\$ 539,099	\$ 24,563	\$ 27,142
Agricultural	229,182	208,522	-	210,372	8,794	12,412
Commercial Construction	190,494	190,494	-	697,893	6,630	7,127
Commercial Real Estate	14,357,601	14,276,688	-	14,274,719	567,349	560,354
Residential Real Estate	4,261,558	3,952,139	-	4,553,322	73,099	190,373
Farmland	920,666	799,556	-	1,016,395	21,526	26,012
Consumer	212,376	212,026	-	213,309	9,599	12,036
	\$20,806,832	\$ 20,274,380	\$ -	\$ 21,505,109	\$ 711,560	\$ 835,456
With An Allowance Recorded						
Commercial	-	-	-	30,270	-	-
Agricultural	-	-	-	-	-	-
Commercial Construction	72,296	72,296	21,135	74,098	1,532	1,416
Commercial Real Estate	8,557,582	8,467,135	3,021,943	8,339,666	238,684	235,749
Residential Real Estate	1,475,594	1,467,833	362,521	1,042,750	27,759	32,260
Farmland	379,851	379,851	29,173	384,056	21,098	21,310
Consumer	-	-	-	-	-	-
	\$10,485,323	\$ 10,387,115	\$ 3,434,772	\$ 9,870,840	\$ 289,073	\$ 290,735
Total						
Commercial	\$ 634,955	\$ 634,955	\$ -	\$ 569,369	\$ 24,563	\$ 27,142
Agricultural	229,182	208,522	-	210,372	8,794	12,412
Commercial Construction	262,790	262,790	21,135	771,991	8,162	8,543
Commercial Real Estate	22,915,183	22,743,823	3,021,943	22,614,385	806,033	796,103
Residential Real Estate	5,737,152	5,419,972	362,521	5,596,072	100,858	222,633
Farmland	1,300,517	1,179,407	29,173	1,400,451	42,624	47,322
Consumer	212,376	212,026	-	213,309	9,599	12,036
	\$31,292,155	\$ 30,661,495	\$ 3,434,772	\$ 31,375,949	\$ 1,000,633	\$1,126,191

(4) Loans (Continued)

The following table details impaired loan data as of December 31, 2015:

	Unpaid Contractual Principal Balance	Impaired Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized	Interest Income Collected
With No Related Allowance Recorded						
Commercial	\$ 454,423	\$ 454,013	-	\$ 534,814	\$ 17,259	\$ 21,253
Agricultural	195,654	178,021	-	163,078	(9,957)	10,334
Commercial Construction	6,887,522	1,896,938	-	2,867,061	25,788	27,007
Commercial Real Estate	15,569,340	15,122,486	-	15,430,252	529,376	530,699
Residential Real Estate	5,429,121	4,575,547	-	4,715,162	175,484	159,148
Farmland	1,104,887	1,103,353	-	1,339,863	583	2,076
Consumer	179,908	178,435	-	190,566	13,745	14,907
Other	-	-	-	48,438	-	-
	<u>\$29,820,855</u>	<u>\$23,508,793</u>	<u>-</u>	<u>\$ 25,289,234</u>	<u>\$ 752,278</u>	<u>\$ 765,424</u>
With An Allowance Recorded						
Commercial	\$ 122,928	\$ 122,928	\$ 94,538	\$ 99,749	\$ 2,275	\$ 2,438
Agricultural	-	-	-	-	-	-
Commercial Construction	76,644	76,644	25,344	92,200	375	375
Commercial Real Estate	8,969,329	8,955,503	1,607,962	6,673,087	213,693	208,657
Residential Real Estate	1,083,127	1,075,367	308,188	1,088,380	16,380	15,873
Farmland	387,968	387,969	37,386	391,060	20,880	20,954
Consumer	-	-	-	-	-	-
Other	-	-	-	-	-	-
	<u>\$10,639,996</u>	<u>\$10,618,411</u>	<u>\$ 2,073,418</u>	<u>\$ 8,344,476</u>	<u>\$ 253,603</u>	<u>\$ 248,297</u>
Total						
Commercial	\$ 577,351	\$ 576,941	\$ 94,538	\$ 634,563	\$ 19,534	\$ 23,691
Agricultural	195,654	178,021	-	163,078	(9,957)	10,334
Commercial Construction	6,964,166	1,973,582	25,344	2,959,261	26,163	27,382
Commercial Real Estate	24,538,669	24,077,989	1,607,962	22,103,339	743,069	739,356
Residential Real Estate	6,512,248	5,650,914	308,188	5,803,542	191,864	175,021
Farmland	1,492,855	1,491,322	37,386	1,730,923	21,463	23,030
Consumer	179,908	178,435	-	190,566	13,745	14,907
Other	-	-	-	48,438	-	-
	<u>\$40,460,851</u>	<u>\$34,127,204</u>	<u>\$2,073,418</u>	<u>\$33,633,710</u>	<u>\$1,005,881</u>	<u>\$1,013,721</u>

(4) Loans (Continued)

The following table details impaired loan data as of December 31, 2014:

	<u>Unpaid Contractual Principal Balance</u>	<u>Impaired Balance</u>	<u>Related Allowance</u>	<u>Average Recorded Investment</u>	<u>Interest Income Recognized</u>	<u>Interest Income Collected</u>
With No Related Allowance Recorded						
Commercial	\$ 310,447	\$ 308,817	\$ -	\$ 679,267	\$ 9,248	\$ 17,973
Agricultural	50,163	44,605	-	50,959	(6,029)	3,000
Commercial Construction	9,573,141	3,463,502	-	3,376,033	13,111	12,833
Commercial Real Estate	17,129,876	16,227,379	-	18,350,015	462,355	474,936
Residential Real Estate	9,136,987	7,600,073	-	5,690,573	312,024	306,859
Farmland	1,450,759	1,449,226	-	949,003	(8,518)	17,273
Consumer	201,695	201,695	-	211,775	14,455	15,495
Other	206,894	195,497	-	197,519	5,874	10,677
	<u>38,059,962</u>	<u>29,490,794</u>	<u>-</u>	<u>29,505,144</u>	<u>802,520</u>	<u>859,046</u>
With An Allowance Recorded						
Commercial	96,580	96,580	96,580	419,464	(299)	-
Agricultural	-	-	-	-	-	-
Commercial Construction	207,308	136,369	53,947	1,528,817	375	375
Commercial Real Estate	6,135,238	6,135,238	456,941	6,415,086	60,629	50,468
Residential Real Estate	2,072,919	2,065,158	414,684	1,829,102	84,177	86,472
Farmland	396,048	396,048	28,962	529,555	13,077	12,210
Consumer	-	-	-	-	-	-
Other	-	-	-	-	-	-
	<u>8,908,093</u>	<u>8,829,393</u>	<u>1,051,114</u>	<u>10,722,024</u>	<u>157,959</u>	<u>149,525</u>
Total						
Commercial	407,027	405,397	96,580	1,098,731	8,949	17,973
Agricultural	50,163	44,605	-	50,959	(6,029)	3,000
Commercial Construction	9,780,449	3,599,871	53,947	4,904,850	13,486	13,208
Commercial Real Estate	23,265,114	22,362,617	456,941	24,765,101	522,984	525,404
Residential Real Estate	11,209,906	9,665,231	414,684	7,519,675	396,201	393,331
Farmland	1,846,807	1,845,274	28,962	1,478,558	4,559	29,483
Consumer	201,695	201,695	-	211,775	14,455	15,495
Other	206,894	195,497	-	197,519	5,874	10,677
	<u>\$46,968,055</u>	<u>\$38,320,187</u>	<u>\$1,051,114</u>	<u>\$40,227,168</u>	<u>\$960,479</u>	<u>\$1,008,571</u>

(4) Loans (Continued)

Troubled Debt Restructurings (TDRs) are troubled loans on which the original terms of the loan have been modified in favor of the borrower due to deterioration in the borrower's financial condition. Each potential loan modification is reviewed individually and the terms of the loan are modified to meet the borrower's specific circumstances at a point in time. Not all loan modifications are TDRs. Loan modifications are reviewed and approved by the Company's senior lending staff, who then determine whether the loan meets the criteria for a TDR. Generally, the types of concessions granted to borrowers that are evaluated in determining whether a loan is classified as a TDR include:

- Interest rate reductions - Occur when the stated interest rate is reduced to a nonmarket rate or a rate the borrower would not be able to obtain elsewhere under similar circumstances.
- Amortization or maturity date changes - Result when the amortization period of the loan is extended beyond what is considered a normal amortization period for loans of similar type with similar collateral.
- Principal reductions - These are often the result of commercial real estate loan workouts where two new notes are created. The primary note is underwritten based upon the Company's normal underwriting standards and is structured so that the projected cash flows are sufficient to repay the contractual principal and interest of the newly restructured note. The terms of the secondary note vary by situation and often involve that note being charged off, or the principal and interest payments being deferred until after the primary note has been repaid. In situations where a portion of the note is charged off during modification, there is often no specific reserve allocated to those loans. This is due to the fact that the amount of the charge-off usually represents the excess of the original loan balance over the collateral value and the Company has determined there is no additional exposure on those loans.

(4) Loans (Continued)

As discussed in Note 1, Summary of Significant Accounting Policies, once a loan is identified as a TDR, it is accounted for as an impaired loan. The Company had no unfunded commitments to lend to a customer that has a troubled debt restructured loan as of December 31, 2016. The following tables present the number of loan contracts restructured during the 12 months ended December 31, 2016, 2015 and 2014. It shows the pre- and post-modification recorded investment as well as the number of contracts and the recorded investment for those TDRs modified during the previous 12 months which subsequently defaulted during the period. Loans modified in a troubled debt restructuring are considered to be in default once the loan becomes 90 days past due. A TDR may cease being classified as impaired if the loan is subsequently modified at market terms, has performed according to the modified terms for at least six months, and has not had any prior principal forgiveness on a cumulative basis.

Troubled Debt Restructurings

2016	# of Contracts	Pre-Modification	Post-Modification
Commercial Real Estate	1	\$ 91,280	\$ 91,097
Residential Real Estate	1	354,784	354,784
Total Loans	2	\$ 446,064	\$ 445,881
2015			
Commercial Real Estate	1	\$ 513,868	\$ 505,978
Residential Real Estate	2	1,106,345	1,035,590
Total Loans	3	\$1,620,213	\$1,541,568
2014			
Farmland	1	\$ 400,778	\$ 400,778
Commercial Construction	1	349,976	349,976
Commercial Real Estate	1	1,771,395	1,775,407
Residential Real Estate	1	49,194	49,194
Total Loans	4	\$2,571,343	\$2,575,355

(4) Loans (Continued)

Troubled debt restructurings that subsequently defaulted as of December 31 are as follows:

	<u>2016</u>		<u>2015</u>		<u>2014</u>	
	<u># of Contracts</u>	<u>Recorded Investment</u>	<u># of Contracts</u>	<u>Recorded Investment</u>	<u># of Contracts</u>	<u>Recorded Investment</u>
Residential Real Estate	<u>1</u>	<u>\$ 89,297</u>	<u>-</u>	<u>\$ -</u>	<u>-</u>	<u>\$ -</u>
Total Loans	<u>1</u>	<u>\$ 89,297</u>	<u>-</u>	<u>\$ -</u>	<u>-</u>	<u>\$ -</u>

During 2016, a restructured loan totaling \$89,297 failed to continue to perform as agreed and was charged off in June 2016. At December 31, 2015 and 2014, all restructured loans were performing as agreed.

(5) Allowance for Loan Losses

Changes in the allowance for loan losses for the years ended December 31 are as follows:

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Balance, Beginning of Year	\$8,603,905	\$8,802,316	\$ 11,805,986
Provision for Loan Losses	1,062,000	865,500	1,308,000
Loans Charged Off	(2,087,850)	(2,083,347)	(5,104,491)
Recoveries of Loans Previously Charged Off	1,345,238	1,019,436	792,821
Balance, End of Year	<u>\$8,923,293</u>	<u>\$8,603,905</u>	<u>\$ 8,802,316</u>

(5) Allowance for Loan Losses (Continued)

The following tables detail activity in the allowance for loan losses, segregated by class of loan, for the years ended December 31. Allocation of a portion of the allowance to one category of loans does not preclude its availability to absorb losses in other loan categories and periodically may result in reallocation within the provision categories.

2016	<u>Beginning Balance</u>	<u>Charge-Offs</u>	<u>Recoveries</u>	<u>Provision</u>	<u>Ending Balance</u>
Commercial and Agricultural					
Commercial	\$ 855,364	\$ (304,918)	\$ 66,738	\$ (160,987)	\$ 456,197
Agricultural	203,091	(19,258)	4,150	(20,291)	167,692
Real Estate					
Commercial Construction	690,766	(25,318)	814,586	(1,157,309)	322,725
Residential Construction	19,890	-	-	(6,399)	13,491
Commercial	3,850,527	(992,067)	206,154	2,686,384	5,750,998
Residential	1,990,355	(361,630)	49,660	(282,286)	1,396,099
Farmland	911,692	(119,576)	145,000	(214,785)	722,331
Consumer and Other					
Consumer	63,377	(265,083)	52,629	229,342	80,265
Other	18,843	-	6,321	(11,669)	13,495
	<u>\$ 8,603,905</u>	<u>\$ (2,087,850)</u>	<u>\$1,345,238</u>	<u>\$ 1,062,000</u>	<u>\$ 8,923,293</u>
2015					
Commercial and Agricultural					
Commercial	\$ 497,561	\$ (454,971)	\$ 52,111	\$760,663	\$ 855,364
Agricultural	304,172	(5,000)	3,600	(99,681)	203,091
Real Estate					
Commercial Construction	1,222,695	(97,698)	485,834	(920,065)	690,766
Residential Construction	138,092	-	-	(118,202)	19,890
Commercial	3,664,777	(275,297)	270,003	191,044	3,850,527
Residential	2,425,327	(929,668)	109,626	385,070	1,990,355
Farmland	103,800	(40,000)	20,000	827,892	911,692
Consumer and Other					
Consumer	66,914	(255,062)	61,976	189,549	63,377
Other	378,978	(25,651)	16,286	(350,770)	18,843
	<u>\$8,802,316</u>	<u>\$ (2,083,347)</u>	<u>\$1,019,436</u>	<u>\$865,500</u>	<u>\$8,603,905</u>

(5) Allowance for Loan Losses (Continued)

2014	Beginning Balance	Charge-Offs	Recoveries	Provision	Ending Balance
Commercial and Agricultural					
Commercial	\$ 1,017,073	\$ (624,944)	\$ 76,002	\$ 29,430	\$ 497,561
Agricultural	293,886	-	2,700	7,586	304,172
Real Estate					
Commercial Construction	1,782,179	(1,543,099)	485,005	498,610	1,222,695
Residential Construction	138,092	-	-	-	138,092
Commercial	4,379,276	(1,326,825)	90,042	522,284	3,664,777
Residential	3,278,269	(1,033,966)	31,127	149,897	2,425,327
Farmland	311,494	(233,580)	20,000	5,886	103,800
Consumer and Other					
Consumer	243,253	(342,077)	72,477	93,261	66,914
Other	362,464	-	15,468	1,046	378,978
	<u>\$11,805,986</u>	<u>\$(5,104,491)</u>	<u>\$792,821</u>	<u>\$1,308,000</u>	<u>\$8,802,316</u>

The Company's allowance for loan losses consists of specific valuation allowances established for probable losses on specific loans and historical valuation allowances for other loans with similar risk characteristics. During the first quarter of 2016 Company management implemented a change to its allowance for loan loss methodology by expanding the historical loss period from a rolling 8 quarters to 16 quarters. Management believes the longer historical loss period better reflects the current and expected loss behavior of the loan portfolio within the current credit cycle. The transition to a rolling 16 quarter loss period will be complete in the first quarter of 2017. As of December 31, 2016, this change in the historical loss period resulted in an increase to the allowance for loan losses of \$804,000. The loss history period used at December 31, 2015 and 2014 was based on the loss rate from the eight quarters ended September 30, 2015 and 2014, respectively.

Effective with the quarter ended June 30, 2015, the calculation of the amount needed in the Allowance for Loan Losses changed. Management determined that the segmentation method for the ASC 450-20 portion of the loan portfolio should be changed to bank call report categories. Prior to this change, the ASC 450-20 segmentation categorized loans by various non-owner occupied commercial real estate loan types and risk grades for the remainder of the ASC 450-20 portion of the portfolio. On the date of change, June 30, 2015, the change in methodology resulted in an increase to the calculated allowance for loan loss reserve of \$1,621,424.

During 2014, management changed its methodology for calculating the allowance for loan losses to better reflect the estimated losses inherent in the portfolio. Specific changes included:

- Reducing the historical loss ratios by including loan loss recoveries in the calculation. Previously, management included only the loan charge-off amount and did not consider the effect of subsequent recoveries.
- Reducing the balance of those loans which are guaranteed by government agencies, such as SBA loans. Previously, the entire balance of such loans was considered in the calculation of the general reserves; however, beginning in 2014, only the nonguaranteed portion of these loans is subject to the loss calculation.

(5) Allowance for Loan Losses (Continued)

Management feels these changes better align the calculation of the allowance for loan losses with the direction of the loan portfolio. These changes did not result in a significant change to the recorded allowance for loan loss balance.

The Company determines its individual reserves during its quarterly review of substandard loans. This process involves reviewing all loans with a risk grade of 6 or greater and an outstanding balance of \$250,000 or more, regardless of the loans impairment classification.

Since not all loans in the substandard category are considered impaired, this quarterly review process may result in the identification of specific reserves on nonimpaired loans. Management considers those loans graded substandard, but not classified as impaired, to be higher risk loans and, therefore, makes specific allocations to the allowance for those loans if warranted. The total of such loans is \$10,786,699 and \$11,155,813 as of December 31, 2016 and 2015, respectively. Specific allowance allocations were made for these loans totaling \$632,706 and \$276,731 as of December 31, 2016 and 2015, respectively. Since these loans are not considered impaired, both the loan balance and related specific allocation are included in the “Collectively Evaluated for Impairment” column of the following tables.

At December 31, 2016, there were 160 impaired loans totaling \$4,204,156 below the \$250,000 review threshold which were not individually reviewed for impairment. Those loans were subject to the Bank’s general loan loss reserve methodology and are included in the “Collectively Evaluated for Impairment” column of the following tables. Likewise, at December 31, 2015 and 2014, impaired loans totaling \$3,744,733 and \$3,885,411, respectively, were below the \$250,000 review threshold and were subject to the Bank’s general loan loss reserve methodology and are included in the “Collectively Evaluated for Impairment” column of the following tables.

2016	Ending Allowance Balance			Ending Loan Balance		
	Individually Evaluated for Impairment	Collectively Evaluated for Impairment	Total	Individually Evaluated for Impairment	Collectively Evaluated for Impairment	Total
Commercial and Agricultural						
Commercial	\$ -	\$ 456,197	\$ 456,197	\$ 6,671	\$ 47,018,207	\$ 47,024,878
Agricultural	-	167,692	167,692	-	17,079,579	17,079,579
Real Estate						
Commercial Construction	21,135	301,590	322,725	72,296	30,286,066	30,358,362
Residential Construction	-	13,491	13,491	-	11,830,447	11,830,447
Commercial	3,021,943	2,729,055	5,750,998	22,422,451	326,667,580	349,090,031
Residential	362,522	1,033,577	1,396,099	2,911,874	192,668,093	195,579,967
Farmland	29,172	693,159	722,331	1,044,047	65,833,150	66,877,197
Consumer and Other						
Consumer	-	80,265	80,265	-	19,695,241	19,695,241
Other	-	13,495	13,495	-	16,747,861	16,747,861
Total End of Year Balance	\$3,434,772	\$5,488,521	\$8,923,293	\$26,457,339	\$727,826,224	\$754,283,563

(5) Allowance for Loan Losses (Continued)

2015	Ending Allowance Balance			Ending Loan Balance		
	Individually Evaluated for Impairment	Collectively Evaluated for Impairment	Total	Individually Evaluated for Impairment	Collectively Evaluated for Impairment	Total
Commercial and Agricultural						
Commercial	\$ 94,538	\$ 760,826	\$ 855,364	\$ 122,928	\$ 47,658,761	\$ 47,781,689
Agricultural	-	203,091	203,091	8,445	19,185,052	19,193,497
Real Estate						
Commercial Construction	25,344	665,422	690,766	1,622,560	38,484,073	40,106,633
Residential Construction	-	19,890	19,890	-	9,413,263	9,413,263
Commercial	1,607,962	2,242,565	3,850,527	23,628,213	322,633,820	346,262,033
Residential	308,188	1,682,167	1,990,355	3,597,386	193,405,033	197,002,419
Farmland	37,386	874,306	911,692	1,402,939	60,376,920	61,779,859
Consumer and Other						
Consumer	-	63,377	63,377	-	20,605,465	20,605,465
Other	-	18,843	18,843	-	16,490,737	16,490,737
Total End of Year Balance	\$2,073,418	\$6,530,487	\$8,603,905	\$30,382,471	\$728,253,124	\$758,635,595
2014						
Commercial and Agricultural						
Commercial	\$ 96,580	\$ 400,981	\$ 497,561	\$ 96,580	\$ 50,863,685	\$ 50,960,265
Agricultural	-	304,172	304,172	-	16,689,444	16,689,444
Real Estate						
Commercial Construction	53,947	1,168,748	1,222,695	3,384,377	47,874,593	51,258,970
Residential Construction	-	138,092	138,092	-	11,220,683	11,220,683
Commercial	456,941	3,207,836	3,664,777	21,693,061	310,537,786	332,230,847
Residential	414,684	2,010,643	2,425,327	7,559,965	196,192,655	203,752,620
Farmland	28,962	74,838	103,800	1,700,793	48,250,191	49,950,984
Consumer and Other						
Consumer	-	66,914	66,914	-	22,820,314	22,820,314
Other	-	378,978	378,978	-	7,209,682	7,209,682
Total End of Year Balance	\$1,051,114	\$7,751,202	\$8,802,316	\$34,434,776	\$711,659,033	\$746,093,809

(6) Premises and Equipment

Premises and equipment are comprised of the following as of December 31:

	<u>2016</u>	<u>2015</u>
Land	\$ 9,668,722	\$ 9,696,723
Building	25,239,165	23,927,467
Furniture, Fixtures and Equipment	12,461,043	12,154,375
Leasehold Improvements	653,939	993,618
Construction in Progress	1,530,359	1,170,050
	<u>49,553,228</u>	<u>47,942,233</u>
Accumulated Depreciation	<u>(21,583,968)</u>	<u>(21,488,703)</u>
	<u>\$27,969,260</u>	<u>\$ 26,453,530</u>

Depreciation charged to operations totaled \$1,574,249 in 2016, \$1,657,229 in 2015, and \$1,595,253 in 2014.

Certain Company facilities and equipment are leased under various operating leases. Rental expense approximated \$437,000 for 2016, \$560,000 for 2015, and \$613,000 for 2014.

Future minimum rental payments as of December 31, 2016 are as follows:

<u>Year Ending December 31</u>	<u>Amount</u>
2017	<u>\$39,820</u>
	<u>\$39,820</u>

(7) Other Real Estate Owned

The aggregate carrying amount of Other Real Estate Owned (OREO) at December 31, 2016, 2015 and 2014 was \$6,439,226, \$8,839,103, and \$10,401,832, respectively. All of the Company's other real estate owned represents properties acquired through foreclosure or deed in lieu of foreclosure. The following table details the change in OREO during 2016, 2015 and 2014 as of December 31:

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Balance, Beginning of Year	\$ 8,839,103	\$10,401,832	\$15,502,462
Additions	5,664,554	7,536,165	3,852,848
Sales of OREO	(7,416,293)	(8,054,675)	(7,102,136)
Loss on Sale	(146,402)	(591,071)	(844,515)
Provision for Losses	(501,736)	(453,148)	(1,006,827)
Balance, End of Year	\$ 6,439,226	\$ 8,839,103	\$10,401,832

At December 31, 2016, the Company held \$431,194 of residential real estate property as foreclosed property. Also at December 31, 2016, \$204,403 of consumer mortgage loans collateralized by residential real estate property was in the process of foreclosure according to local requirements of the applicable jurisdictions.

(8) Other Intangible Assets

The following is an analysis of the core deposit intangible activity for the years ended December 31:

	<u>Core Deposit Intangible</u>	<u>Accumulated Amortization</u>	<u>Net Core Deposit Intangible</u>
Core Deposit Intangible			
Balance, December 31, 2014	\$1,056,693	(904,681)	152,012
Amortization Expense	-	(35,748)	(35,748)
Balance, December 31, 2015	\$1,056,693	\$(940,429)	\$116,264
Amortization Expense	-	(35,749)	(35,749)
Balance, December 31, 2016	<u>\$1,056,693</u>	<u>\$(976,178)</u>	<u>\$ 80,515</u>

Amortization expense related to the core deposit intangible was \$35,749, \$35,748, and \$35,749 for the years ended December 31, 2016, 2015 and 2014. Amortizations expense will continue at an annual rate of approximately \$35,749 through the first quarter of 2019, at which point the core deposit will be fully amortized.

(9) Income Taxes

The components of income tax expense for the years ended December 31 are as follows:

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Current Federal Expense	\$3,629,213	\$3,162,367	\$1,335,337
Deferred Federal Expense	222,120	625,436	1,932,950
Federal Income Tax Expense	3,851,333	3,787,803	3,268,287
Current State Income Tax Expense	-	-	-
Federal and State Income Tax Expense	<u>\$3,851,333</u>	<u>\$3,787,803</u>	<u>\$3,268,287</u>

The federal income tax expense of \$3,851,333 in 2016, \$3,787,803 in 2015, and \$3,268,287 in 2014 is different than the income taxes computed by applying the federal statutory rates to income before income taxes. The reasons for the differences are as follows:

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Statutory Federal Income Taxes	\$4,283,394	\$4,134,570	\$3,671,971
Tax-Exempt Interest	(109,759)	(83,903)	(74,138)
Premiums on Officers' Life Insurance	(182,532)	(232,988)	(186,712)
Meal and Entertainment Disallowance	16,813	21,600	14,044
Other	(156,583)	(51,476)	(156,878)
Actual Federal Income Taxes	<u>\$3,851,333</u>	<u>\$3,787,803</u>	<u>\$3,268,287</u>

(9) Income Taxes (Continued)

Deferred taxes in the accompanying consolidated balance sheets as of December 31 include the following:

	<u>2016</u>	<u>2015</u>
Deferred Tax Assets		
Allowance for Loan Losses	\$3,033,920	\$2,925,328
Other Real Estate	688,162	537,914
Deferred Compensation	280,704	308,128
Investments	340,000	340,000
Goodwill	167,666	212,190
Other	379,304	418,165
	<u>4,889,756</u>	<u>4,741,725</u>
Deferred Tax Liabilities		
Premises and Equipment	(1,553,460)	(1,183,309)
Other	(4,185)	(4,185)
	<u>(1,557,645)</u>	<u>(1,187,494)</u>
Deferred Tax Assets (Liabilities) on Unrealized Securities Gains (Losses)	<u>2,587,163</u>	<u>2,284,362</u>
Net Deferred Tax Assets	<u>\$5,919,274</u>	<u>\$5,838,593</u>

The deferred tax assets are included in Other Assets in the consolidated balance sheets. As discussed in Note 1, certain positions taken in the Company's tax returns may be subject to challenge by the taxing authorities. An analysis of activity related to unrecognized taxes as of December 31 follows.

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Balance, Beginning	\$ -	\$ -	\$ 42,327
Positions Taken During the Current Year	-	-	-
Reductions Resulting from Lapse of Statutes of Limitation	-	-	42,327
Balance, Ending	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>

The net decrease of \$42,327 is included in income tax expense for the year ended December 31, 2014.

(10) Deposits

The aggregate amount of overdrawn deposit accounts reclassified as loan balances totaled \$413,563 and \$272,110 as of December 31, 2016 and 2015, respectively.

Components of interest-bearing deposits as of December 31 are as follows:

	<u>2016</u>	<u>2015</u>
Interest-Bearing Demand	\$448,003,985	\$412,959,430
Savings	70,066,140	64,976,174
Time, \$100,000 and Over	183,610,778	202,800,899
Other Time	183,616,992	196,931,462
	<u>\$885,297,895</u>	<u>\$877,667,965</u>

At December 31, 2016 and December 31, 2015, the Company had brokered deposits of \$49,303,139 and \$25,576,524, respectively. All of these brokered deposits represent Certificate of Deposit Account Registry Service (CDARS) reciprocal deposits. The CDARS deposits are ones in which customers placed core deposits into the CDARS program for FDIC insurance coverage and the Company receives reciprocal brokered deposits in a like amount. The aggregate amount of short-term jumbo certificates of deposit, each with a minimum denomination of \$100,000 was \$123,612,962 and \$141,900,102 as of December 31, 2016 and December 31, 2015, respectively. The aggregate amount of jumbo certificates of deposit, each with a minimum denomination of \$250,000 was \$32,168,191 and \$31,755,483 as of December 31, 2016 and December 31, 2015, respectively.

As of December 31, 2016, the scheduled maturities of certificates of deposit are as follows:

<u>Year</u>	<u>Amount</u>
2017	\$256,886,186
2018	63,055,100
2019	22,738,969
2020	15,858,433
2021 and Thereafter	8,689,082
	<u>\$367,227,770</u>

(11) Other Borrowed Money

Other borrowed money at December 31 is summarized as follows:

	<u>2016</u>	<u>2015</u>
Federal Home Loan Bank Advances	<u>\$ 46,000,000</u>	<u>\$ 40,000,000</u>

Advances from the Federal Home Loan Bank (FHLB) have maturities ranging from 2018 to 2026 and interest rates ranging from 0.98 percent to 3.51 percent. As collateral on the outstanding FHLB advances, the Company has provided a blanket lien on its portfolio of qualifying residential first mortgage loans and commercial loans. At December 31, 2016, the book value of those loans pledged is \$104,769,821. At

(11) Other Borrowed Money (Continued)

December 31, 2016, the Company had remaining credit availability from the FHLB of \$241,746,000. The Company may be required to pledge additional qualifying collateral in order to utilize the full amount of the remaining credit line.

The aggregate stated maturities of other borrowed money at December 31, 2016 are as follows:

<u>Year</u>	<u>Amount</u>
2018	\$ 2,500,000
2019	5,000,000
2020	2,500,000
2021	-
2022 and Thereafter	<u>36,000,000</u>
	<u><u>\$46,000,000</u></u>

At December 31, 2016, \$13,000,000 of FHLB advances are subject to fixed rates of interest, while the remaining \$33,000,000 is subject to floating interest rates which will convert to fixed rates of interests in the next few years.

The Company also has available federal funds lines of credit with various financial institutions totaling \$43,500,000, of which there were none outstanding at December 31, 2016.

The Company has the ability to borrow funds from the Federal Reserve Bank (FRB) of Atlanta utilizing the discount window. The discount window is an instrument of monetary policy that allows eligible institutions to borrow money from the FRB on a short-term basis to meet temporary liquidity shortages caused by internal or external disruptions. At December 31, 2016, the Company had borrowing capacity available under this arrangement, with no outstanding balances. The Company would be required to pledge certain available-for-sale investment securities as collateral under this agreement.

(12) Subordinated Debentures (Trust Preferred Securities)

<u>Description</u>	<u>Date</u>	<u>Amount</u>	<u>3-Month Libor Rate</u>	<u>Added Points</u>	<u>Total Interest Rate</u>	<u>Maturity</u>	<u>5-Year Call Option</u>
(In Thousands)							
Colony Bankcorp Statutory Trust III	6/17/2004	\$4,640	0.99317	2.68	3.67317	6/14/2034	6/17/2009
Colony Bankcorp Capital Trust I	4/13/2006	5,155	0.99789	1.50	2.49789	4/13/2036	4/13/2011
Colony Bankcorp Capital Trust II	3/12/2007	9,279	0.99817	1.65	2.64817	3/12/2037	3/12/2012
Colony Bankcorp Capital Trust III	9/14/2007	5,155	0.88733	1.40	2.28733	9/14/2037	9/14/2012

The Trust Preferred Securities are recorded as subordinated debentures on the consolidated balance sheets, and subject to certain limitations, qualify as Tier 1 Capital for regulatory capital purposes. The proceeds from these offerings were used to fund certain acquisitions, pay off holding company debt and inject capital into the Bank subsidiary.

The Trust Preferred Securities pay interest quarterly.

(12) Subordinated Debentures (Trust Preferred Securities) (Continued)

Quarterly interest payments on the Trust Preferred Securities were suspended from February 13, 2012 until November 17, 2014, at which time the Company reinstated the interest payments and paid \$1,069,695 of interest payments in arrears.

(13) Preferred Stock

The Company had 9,360 shares and 18,021 shares of Fixed Rate Cumulative Perpetual Preferred Stock, Series A (the Preferred Stock) issued and outstanding with private investors as of December 31, 2016 and 2015, respectively. The Company redeemed 8,661 shares of Preferred Stock at \$1,000 per share during 2016. The Company also had a warrant (the Warrant) to purchase up to 500,000 shares of the Company's common stock outstanding with private investors. Both the Preferred Stock and the Warrant originated in 2009 through transactions with the United States Department of the Treasury and were subsequently sold to the public through an auction process during 2013.

The Preferred Stock qualifies as Tier 1 capital and is nonvoting, other than class voting rights on certain matters that could adversely affect the Preferred Stock. The Preferred Stock may be redeemed by the Company at the liquidation preference of \$1,000 per share, plus any accrued and unpaid dividends. The Warrant may be exercised on or before January 9, 2019 at an exercise price of \$8.40 per share. No voting rights may be exercised with respect to the shares of the Warrant until the Warrant has been exercised.

The Preferred Stock requires a cumulative cash dividend be paid quarterly at a rate of 9 percent per annum. Prior to January 9, 2014, the annual dividend rate for the Preferred Stock was 5 percent. Unpaid dividends on the Preferred Stock must be declared and set aside for the benefit of the holders of the Preferred Stock before any dividend may be declared on common stock. On February 13, 2012, the Company announced the suspension of dividends on Preferred Stock. On November 17, 2014, the Company reinstated dividend payments on the Preferred Stock and paid \$5,492,749 of accumulated dividends in arrears to the holders of the Preferred Stock.

(14) Employee Benefit Plan

The Company offers a defined contribution 401(k) Profit Sharing Plan (the Plan) which covers substantially all employees who meet certain age and service requirements. The Plan allows employees to make voluntary pre-tax salary deferrals to the Plan. The Company, at its discretion, may elect to make an annual contribution to the Plan equal to a percentage of each participating employee's salary. Such discretionary contributions must be approved by the Company's board of directors. Employees are fully vested in the Company contributions after six years of service. In 2016, 2015 and 2014, the Company made total contributions of \$408,303, \$385,453 and \$401,497 to the Plan.

(15) Commitments and Contingencies

Credit-Related Financial Instruments. The Company is a party to credit-related financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit, standby letters of credit and commercial letters of credit. Such commitments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the consolidated balance sheets.

(15) Commitments and Contingencies (Continued)

The Company's exposure to credit loss is represented by the contractual amount of these commitments. The Company follows the same credit policies in making commitments as it does for on-balance sheet instruments.

At December 31, 2016 and 2015, the following financial instruments were outstanding whose contract amounts represent credit risk:

	Contract Amount	
	2016	2015
Commitments to Extend Credit	\$71,359,000	\$67,889,000
Standby Letters of Credit	1,551,000	1,588,212

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

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

Standby and performance letters of credit are conditional lending commitments issued by the Company to guarantee the performance of a customer to a third party. Those letters of credit are primarily issued to support public and private borrowing arrangements. Essentially all letters of credit issued have expiration dates within one year. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers.

Legal Contingencies. In the ordinary course of business, there are various legal proceedings pending against Colony and its subsidiary. The aggregate liabilities, if any, arising from such proceedings would not, in the opinion of management, have a material adverse effect on Colony's consolidated financial position.

(16) Deferred Compensation Plan

Colony Bank, the wholly-owned subsidiary, has deferred compensation plans covering certain former directors and certain officers choosing to participate through individual deferred compensation contracts. In accordance with terms of the contracts, the Bank is committed to pay the participant's deferred compensation over a specified number of years, beginning at age 65. In the event of a participant's death before age 65, payments are made to the participant's named beneficiary over a specified number of years, beginning on the first day of the month following the death of the participant.

Liabilities accrued under the plans totaled \$825,599 and \$906,259 as of December 31, 2016 and 2015, respectively. Benefit payments under the contracts were \$135,885 in 2016 and \$131,652 in 2015.

(16) Deferred Compensation Plan (Continued)

Provisions charged to operations totaled \$57,125 in 2016, \$196,869 in 2015 and \$69,653 in 2014.

The Company has purchased life insurance policies on the plans' participants and uses the cash flow from these policies to partially fund the plan. Fee income recognized with these plans totaled \$165,128 in 2016, \$174,675 in 2015 and \$167,911 in 2014. In addition death benefits recognized as income totaled \$137,058 in 2015.

(17) Supplemental Cash Flow Information

Cash payments for the following were made during the years ended December 31:

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Interest Expense	<u>\$ 6,529,615</u>	<u>\$ 6,536,994</u>	<u>\$7,898,543</u>
Income Taxes	<u>\$ 3,365,000</u>	<u>\$ 4,738,000</u>	<u>\$ 113,000</u>

Noncash financing and investing activities for the years ended December 31 are as follows:

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Acquisitions of Real Estate Through Loan Foreclosures	<u>\$ 5,664,554</u>	<u>\$ 7,536,165</u>	<u>\$ 3,852,848</u>
Change in Unrealized Gain (Loss) on AFS Investment Securities	<u>\$ (890,590)</u>	<u>\$ 622,155</u>	<u>\$ 6,409,171</u>

(18) Related Party Transactions

The following table reflects the activity and aggregate balance of direct and indirect loans to directors, executive officers or principal holders of equity securities of the Company. All such loans were made on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with other persons and do not involve more than a normal risk of collectibility. A summary of activity of related party loans is shown below:

	<u>2016</u>	<u>2015</u>
Balance, Beginning	\$ 1,816,609	\$ 3,233,949
New Loans	2,379,026	4,900,932
Repayments	(3,170,092)	(6,065,098)
Transactions Due to Changes in Directors	<u>-</u>	<u>(253,174)</u>
Balance, Ending	<u>\$ 1,025,543</u>	<u>\$ 1,816,609</u>

(19) Fair Value of Financial Instruments and Fair Value Measurements

Generally accepted accounting standards in the U.S. require disclosure of fair value information about financial instruments, whether or not recognized on the face of the balance sheet, for which it is practicable to estimate that value. The assumptions used in the estimation of the fair value of Colony Bankcorp, Inc. and Subsidiary's financial instruments are detailed hereafter. Where quoted prices are not available, fair values are based on estimates using discounted cash flows and other valuation techniques. The use of discounted cash flows can be significantly affected by the assumptions used, including the discount rate and estimates of future cash flows.

Generally accepted accounting principles related to Fair Value Measurements define fair value, establish a framework for measuring fair value, establish a three-level valuation hierarchy for disclosure of fair value measurement and enhance disclosure requirements for fair value measurements. The valuation hierarchy is based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date. The three levels are defined as follows:

- Level 1 inputs to the valuation methodology are quoted prices (unadjusted) for identical assets or liabilities in active markets.
- Level 2 inputs to the valuation methodology include quoted prices for similar assets and liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument.
- Level 3 inputs to the valuation methodology are unobservable and represent the Company's own assumptions about the assumptions that market participants would use in pricing the assets or liabilities.

The following disclosures should not be considered a surrogate of the liquidation value of the Company, but rather a good-faith estimate of the increase or decrease in value of financial instruments held by the Company since purchase, origination or issuance.

Cash and Short-Term Investments - For cash, due from banks, bank-owned deposits and federal funds sold, the carrying amount is a reasonable estimate of fair value and is classified Level 1.

Investment Securities - Fair values for investment securities are based on quoted market prices where available and classified as Level 1. If quoted market prices are not available, estimated fair values are based on quoted market prices of comparable instruments and classified as Level 2. If a comparable is not available, the investment securities are classified as Level 3.

Federal Home Loan Bank Stock - The fair value of Federal Home Loan Bank stock approximates carrying value and is classified as Level 1.

Loans - The fair value of fixed rate loans is estimated by discounting the future cash flows using the current rates at which similar loans would be made to borrowers with similar credit ratings. For variable rate loans, the carrying amount is a reasonable estimate of fair value. Most loans are classified as Level 2, but impaired loans with a related allowance are classified as Level 3.

(19) Fair Value of Financial Instruments and Fair Value Measurements (Continued)

Bank-Owned Life Insurance - The carrying value of bank-owned life insurance policies approximates fair value and is classified as Level 1.

Deposit Liabilities - The fair value of demand deposits, savings accounts and certain money market deposits is the amount payable on demand at the reporting date and is classified as Level 1. The fair value of fixed maturity certificates of deposit is estimated by discounting the future cash flows using the rates currently offered for deposits of similar remaining maturities and is classified as Level 2.

Subordinated Debentures – The fair value of subordinated debentures is estimated by discounting the future cash flows using the current rates at which similar advances would be obtained. Subordinated debentures are classified as Level 2.

Other Borrowed Money - The fair value of other borrowed money is calculated by discounting contractual cash flows using an estimated interest rate based on current rates available to the Company for debt of similar remaining maturities and collateral terms. Other borrowed money is classified as Level 2 due to their expected maturities.

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

2016	Carrying Amount	Estimated Fair Value	Level		
			1	2	3
			(in Thousands)		
Assets					
Cash and Short-Term Investments	\$ 75,167	\$ 75,167	\$ 75,167	\$ -	\$ -
Investment Securities Available for Sale	323,658	323,658	-	323,082	576
Federal Home Loan Bank Stock	3,010	3,010	3,010	-	-
Loans, Net	744,999	745,240	-	738,288	6,952
Bank-Owned Life Insurance	15,419	15,419	15,419	-	-
Liabilities					
Deposits	1,044,357	1,045,726	677,129	368,597	-
Subordinated Debentures	24,229	24,229	-	24,229	-
Other Borrowed Money	46,000	46,232	-	46,232	-
2015					
Assets					
Cash and Short-Term Investments	\$ 60,872	\$ 60,872	\$ 60,872	\$ -	\$ -
Investment Securities Available for Sale	296,149	296,149	-	295,219	930
Federal Home Loan Bank Stock	2,731	2,731	2,731	-	-
Loans, Net	749,675	750,412	-	741,867	8,545
Bank-Owned Life Insurance	14,830	14,830	14,830	-	-
Liabilities					
Deposits	1,011,554	1,013,111	611,822	401,289	-
Subordinated Debentures	24,229	24,229	-	24,229	-
Other Borrowed Money	40,000	40,421	-	40,421	-

(19) Fair Value of Financial Instruments and Fair Value Measurements (Continued)

Fair value estimates are made at a specific point in time, based on relevant market information and information about the financial instrument. These estimates do not reflect any premium or discount that could result from offering for sale at one time the Company's entire holdings of a particular financial instrument. Because no market exists for a significant portion of the Company's financial instruments, fair value estimates are based on many judgments. These estimates are subjective in nature and involve uncertainties and matters of significant judgment and therefore cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

Fair value estimates are based on existing on- and off-balance sheet financial instruments without attempting to estimate the value of anticipated future business and the value of assets and liabilities that are not considered financial instruments. Significant assets and liabilities that are not considered financial instruments include deferred income taxes and premises and equipment. In addition, the tax ramifications related to the realization of the unrealized gains and losses can have a significant effect on fair value estimates and have not been considered in the estimates.

Following is a description of the valuation methodologies used for instruments measured at fair value on a recurring and nonrecurring basis, as well as the general classification of such instruments pursuant to the valuation hierarchy:

Assets

Securities - Where quoted prices are available in an active market, securities are classified within Level 1 of the valuation hierarchy. Level 1 inputs include securities that have quoted prices in active markets for identical assets. If quoted market prices are not available, then fair values are estimated by using pricing models, quoted prices of securities with similar characteristics, or discounted cash flow. Examples of such instruments, which would generally be classified within level 2 of the valuation hierarchy, include certain collateralized mortgage and debt obligations and certain high-yield debt securities. In certain cases where there is limited activity or less transparency around inputs to the valuation, securities are classified within level 3 of the valuation hierarchy. When measuring fair value, the valuation techniques available under the market approach, income approach and/or cost approach are used. The Company's evaluations are based on market data and the Company employs combinations of these approaches for its valuation methods depending on the asset class.

(19) Fair Value of Financial Instruments and Fair Value Measurements (Continued)

Assets (Continued)

Impaired Loans - Impaired loans are those loans which the Company has measured impairment generally based on the fair value of the loan's collateral. Fair value is generally determined based upon independent third-party appraisals of the properties, or discounted cash flows based upon the expected proceeds. These assets are included as level 3 fair values, based upon the lowest level of input that is significant to the fair value measurements.

Other Real Estate - Other real estate owned assets are adjusted to fair value less estimated selling costs upon transfer of the loans to other real estate owned. Typically, an external, third-party appraisal is performed on the collateral upon transfer into the other real estate owned account to determine the asset's fair value. Subsequent adjustments to the collateral's value may be based upon either updated third-party appraisals or management's knowledge of the collateral and the current real estate market conditions. Appraised amounts used in determining the asset's fair value, whether internally or externally prepared, are discounted 10 percent to account for selling and marketing costs. Adjustments are routinely made in the appraisal process by the appraisers to adjust for differences between the comparable sales and income data available. Such adjustments are typically significant and result in a level 3 classification of the inputs for determining fair value. Because of the high degree of judgment required in estimating the fair value of other real estate owned assets and because of the relationship between fair value and general economic conditions, we consider the fair value of other real estate owned assets to be highly sensitive to changes in market conditions.

Assets and Liabilities Measured at Fair Value on a Recurring and Nonrecurring Basis - The following table presents the recorded amount of the Company's assets measured at fair value on a recurring and nonrecurring basis as of December 31, 2016 and 2015, aggregated by the level in the fair value hierarchy within which those measurements fall. The table below includes only impaired loans with a specific reserve and only other real estate properties with a valuation allowance at December 31, 2016 and 2015. Those impaired loans and other real estate properties are shown net of the related specific reserves and valuation allowances.

(19) Fair Value of Financial Instruments and Fair Value Measurements (Continued)**Assets (Continued)**

	2016	Total Fair Value	Fair Value Measurements at Reporting Date Using		
			Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Recurring					
Securities Available for Sale					
U.S. Government Agencies					
Mortgage-Backed		\$319,097,374	\$ -	\$319,097,374	\$ -
State, County and Municipal		4,560,496	-	3,984,112	576,384
		<u>\$323,657,870</u>	<u>\$ -</u>	<u>\$323,081,486</u>	<u>\$ 576,384</u>
Nonrecurring					
Impaired Loans		<u>\$ 6,952,343</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 6,952,343</u>
Other Real Estate		<u>\$ 2,505,188</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 2,505,188</u>
2015					
Recurring					
Securities Available for Sale					
U.S. Government Agencies					
Mortgage-Backed		\$291,049,853	\$ -	\$291,049,853	\$ -
State, County and Municipal		5,099,446	-	4,169,135	930,311
		<u>\$296,149,299</u>	<u>\$ -</u>	<u>\$295,218,988</u>	<u>\$ 930,311</u>
Nonrecurring					
Impaired Loans		<u>\$ 8,544,993</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 8,544,993</u>
Other Real Estate		<u>\$ 2,535,884</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 2,535,884</u>

Liabilities

The Company did not identify any liabilities that are required to be presented at fair value.

(19) Fair Value of Financial Instruments and Fair Value Measurements (Continued)

Fair Value Measurements Using Significant Unobservable Inputs (Level 3)

The following tables present quantitative information about the significant unobservable inputs used in the fair value measurements for assets in level 3 of the fair value hierarchy measured on a nonrecurring basis at December 31, 2016 and 2015. These tables are comprised primarily of collateral dependent impaired loans and other real estate owned:

	December 31, 2016	Valuation Techniques	Unobservable Inputs	Range Weighted Avg
Real Estate				
Commercial Construction	\$ 51,161	Sales Comparison	Adjustment for Differences Between the Comparable Sales	(5.00)% - 99.00% 47.00%
			Management Adjustments for Age of Appraisals and/or Current Market Conditions	0.00% - 10.00% 5.00%
Residential Real Estate	1,105,312	Sales Comparison	Adjustment for Differences Between the Comparable Sales	(22.00)% - 0.00% (11.00)%
			Management Adjustments for Age of Appraisals and/or Current Market Conditions	0.00% - 40.00% 20.00%
Commercial Real Estate	5,445,192	Sales Comparison	Adjustment for Differences Between the Comparable Sales	(14.08)% - 24.62% 5.27%
			Management Adjustments for Age of Appraisals and/or Current Market Conditions	0.00% - 100.00% 50.00%
		Income Approach	Capitalization Rate	10.67%
Farmland	350,678	Sales Comparison	Adjustment for Differences Between the Comparable Sales	(27.00)% - 15.00% (6.00)%
			Management Adjustments for Age of Appraisals and/or Current Market Conditions	10.00% - 75.00% 42.50%
Other Real Estate Owned	2,505,188	Sales Comparison	Adjustment for Differences Between the Comparable Sales	(50.80)% - 316.00% 132.60%
			Management Adjustments for Age of Appraisals and/or Current Market Conditions	6.25% - 76.92% 36.31%
		Income Approach	Discount Rate	12.50%

(19) Fair Value of Financial Instruments and Fair Value Measurements (Continued)***Fair Value Measurements using Significant Unobservable Inputs (Level 3) (Continued)***

	December 31, 2015	Valuation Techniques	Unobservable Inputs	Range Weighted Avg
Commercial	\$ 28,390	Sales Comparison	Adjustment for Differences Between the Comparable Sales	(31.77)% - 34.00% 1.12%
			Management Adjustments for Age of Appraisals and/or Current Market Conditions	0.00% - 10.00% 5.00%
		Income Approach	Capitalization Rate	11.00%
Real Estate				
Commercial Construction	51,300	Sales Comparison	Adjustment for Differences Between the Comparable Sales	(5.00)% - 99.00% 47.00%
			Management Adjustments for Age of Appraisals and/or Current Market Conditions	0.00% - 10.00% 5.00%
Residential Real Estate	767,179	Sales Comparison	Adjustment for Differences Between the Comparable Sales	(22.00)% - 10.80% (5.60)%
			Management Adjustments for Age of Appraisals and/or Current Market Conditions	0.00% - 25.00% 12.50%
Commercial Real Estate	7,347,541	Sales Comparison	Adjustment for Differences Between the Comparable Sales	(31.77)% - 34.00% 1.12%
			Management Adjustments for Age of Appraisals and/or Current Market Conditions	0.00% - 10.00% 5.00%
		Income Approach	Capitalization Rate	10.25%
Farmland	350,583	Sales Comparison	Adjustment for Differences Between the Comparable Sales	(27.00)% - 15.00% (6.00)%
			Management Adjustments for Age of Appraisals and/or Current Market Conditions	10.00% - 75.00% 42.50%
Other Real Estate Owned	2,535,884	Sales Comparison	Adjustment for Differences Between the Comparable Sales	(50.80)% - 142.90% 46.05%
			Management Adjustments for Age of Appraisals and/or Current Market Conditions	15.53% - 72.75% 43.37%
		Income Approach	Discount Rate	12.50%

(19) Fair Value of Financial Instruments and Fair Value Measurements (Continued)

Fair Value Measurements Using Significant Unobservable Inputs (Level 3) (Continued)

The following table presents a reconciliation and statement of income classification of gains and losses for all assets measured at fair value on a recurring basis using significant unobservable inputs (level 3) for the years ended December 31, 2016, 2015 and 2014:

	Available for Sale Securities		
	2016	2015	2014
Balance, Beginning	\$ 930,311	\$ 948,390	\$ 941,265
Transfers into Level 3		-	-
Transfers out of Level 3		-	-
Securities Purchased During the Year		-	-
Securities Matured During the Year	(330,000)	-	-
Loss on OTTI Impairment Included in Noninterest Income		-	-
Unrealized Gains(Losses) Included in Other Comprehensive Income	(23,927)	(18,079)	7,125
Balance, Ending	\$ 576,384	\$ 930,311	\$ 948,390

The Company's policy is to recognize transfers in and transfers out of levels 1, 2 and 3 as of the end of a reporting period. There were no transfers of securities between level 1 and level 2 or level 3 for the years ended December 31, 2016, 2015 or 2014.

The following table presents quantitative information about recurring level 3 fair value measurements as of December 31, 2016 and 2015:

December 31, 2016	Fair Value	Valuation Techniques	Unobservable Inputs	Range (Weighted Avg)
State, County and Municipal	\$ 576,384	Discounted Cash Flow	Discount Rate or Yield	N/A*
December 31, 2015				
State, County and Municipal	\$ 930,311	Discounted Cash Flow	Discount Rate or Yield	N/A*

* The Company relies on a third-party pricing service to value its municipal securities. The details of the unobservable inputs and other adjustments used by the third-party pricing service were not readily available to the Company.

(20) Regulatory Capital Matters

The amount of dividends payable to the parent company from the subsidiary bank is limited by various banking regulatory agencies. Upon approval by regulatory authorities, the Bank may pay cash dividends to the parent company in excess of regulatory limitations. Additionally, the Company suspended the payment of dividends to its stockholders in the third quarter of 2009.

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

Quantitative measures established by regulation to ensure capital adequacy require the Company to maintain minimum amounts and ratios of total and Tier I capital to risk-weighted assets, and of Tier I capital to average assets. As of December 31, 2016, the interim final Basel III rules (Basel III) require the Company to also maintain minimum amounts and ratios of common equity Tier 1 capital to risk weighted assets. These amounts and ratios as defined in regulations are presented hereafter. Management believes, as of December 31, 2016, the Company meets all capital adequacy requirements to which it is subject under the regulatory framework for prompt corrective action. In the opinion of management, there are no conditions or events since prior notification of capital adequacy from the regulators that have changed the institution's category.

The Basel III rules also require the implementation of a new capital conservation buffer comprised of common equity Tier 1 capital. The capital conservation buffer will be phased in beginning January 1, 2016 at 0.625% of risk-weighted assets and increase each subsequent year by 0.625% until reaching its final level of 2.5% on January 1, 2019.

The following table summarizes regulatory capital information as of December 31, 2016 and December 31, 2015 on a consolidated basis and for the subsidiary, as defined. Regulatory capital ratios for December 31, 2016 and 2015 were calculated in accordance with the Basel III rules.

(20) Regulatory Capital Matters (Continued)

The following table summarizes regulatory capital information as of December 31, 2016 and 2015 on a consolidated basis and for its wholly-owned subsidiary, as defined:

	<u>Actual</u>		<u>For Capital Adequacy Purposes</u>		<u>To Be Well Capitalized Under Prompt Corrective Action Provisions</u>	
	<u>Amount</u>	<u>Ratio</u>	<u>Amount</u>	<u>Ratio</u>	<u>Amount</u>	<u>Ratio</u>
As of December 31, 2016			(In Thousands)			
Total Capital to Risk-Weighted Assets						
Consolidated	\$130,785	16.64%	\$ 62,880	8.00%	N/A	N/A
Colony Bank	127,646	16.26	62,796	8.00	\$78,495	10.00%
Tier I Capital to Risk-Weighted Assets						
Consolidated	121,862	15.50	47,160	6.00	N/A	N/A
Colony Bank	118,723	15.12	47,097	6.00	62,796	8.00
Common Equity Tier 1 Capital to Risk-Weighted Assets						
Consolidated	89,002	11.32	35,370	4.50	N/A	N/A
Colony Bank	118,723	15.12	35,323	4.50	51,022	6.50
Tier I Capital to Average Assets						
Consolidated	121,862	10.29	47,368	4.00	N/A	N/A
Colony Bank	118,723	10.04	47,290	4.00	59,113	5.00
As of December 31, 2015						
Total Capital to Risk-Weighted Assets						
Consolidated	\$131,948	16.60%	\$63,602	8.00%	N/A	N/A
Colony Bank	126,939	15.99	63,500	8.00	\$79,375	10.00%
Tier I Capital to Risk-Weighted Assets						
Consolidated	123,344	15.51	47,702	6.00	N/A	N/A
Colony Bank	118,335	14.91	47,625	6.00	63,500	8.00
Common Equity Tier 1 Capital to Risk-Weighted Assets						
Consolidated	81,823	10.29	35,776	4.50	N/A	N/A
Colony Bank	118,335	14.91	35,719	4.50	51,594	6.50
Tier I Capital to Average Assets						
Consolidated	123,344	10.69	46,149	4.00	N/A	N/A
Colony Bank	118,335	10.27	46,074	4.00	57,592	5.00

(20) Regulatory Capital Matters (Continued)

In 2016, the Bank obtained approval of its regulators and paid a \$9,100,000 dividend to the Company. The dividend was utilized to redeem 8,661 shares of Preferred Stock. In 2015, the Bank obtained approval of its regulators and paid a \$10,000,000 dividend to the Company. The dividend was utilized to redeem 9,979 shares of Preferred Stock.

Effective October 22, 2014, the Board Resolution (BR) the Bank had been operating under was lifted. The BR required that, prior to declaring or paying any cash dividend to the Company, the Bank must obtain written consent of its regulators. In November 2014, the Bank paid a \$12,000,000 dividend to the Company. This dividend was utilized to bring the interest payments of the Trust Preferred Securities and the dividend payments of the Preferred Stock to a current status and to fund holding company operations for the coming year.

(21) Financial Information of Colony Bankcorp, Inc. (Parent Only)

The parent company's balance sheets as of December 31, 2016 and 2015 and the related statements of operations and comprehensive income (loss) and cash flows for each of the years in the three-year period then ended are as follows:

**COLONY BANKCORP, INC. (PARENT ONLY)
BALANCE SHEETS
DECEMBER 31**

ASSETS

	<u>2016</u>	<u>2015</u>
Cash	\$ 2,307,008	\$ 4,100,860
Premises and Equipment, Net	1,074,884	1,134,524
Investment in Subsidiary, at Equity	114,478,277	114,677,455
Other	<u>20,990</u>	<u>170,801</u>
Total Assets	<u>\$117,881,159</u>	<u>\$120,083,640</u>

LIABILITIES AND STOCKHOLDERS' EQUITY

Liabilities

Dividends Payable	\$ 105,300	\$ 202,736
Other	<u>159,126</u>	<u>195,282</u>
	<u>\$ 264,426</u>	<u>398,018</u>
Subordinated Debt	<u>24,229,000</u>	<u>24,229,000</u>

Stockholders' Equity

Preferred Stock, Stated Value \$1,000; 10,000,000 Shares Authorized, 9,360 and 18,021 Shares Issued and Outstanding as of December 31, 2016 and 2015	9,360,000	18,021,000
Common Stock, Par Value \$1; 20,000,000 Shares Authorized, 8,439,258 Shares Issued and Outstanding as of December 31, 2016 and 2015	8,439,258	8,439,258
Paid-In Capital	29,145,094	29,145,094
Retained Earnings	51,465,521	44,285,621
Accumulated Other Comprehensive Loss, Net of Tax	<u>(5,022,140)</u>	<u>(4,434,351)</u>
	<u>93,387,733</u>	<u>95,456,622</u>
Total Liabilities and Stockholders' Equity	<u>\$117,881,159</u>	<u>\$120,083,640</u>

(21) Financial Information of Colony Bankcorp, Inc. (Parent Only) (Continued)**COLONY BANKCORP, INC. (PARENT ONLY)
STATEMENTS OF OPERATIONS
FOR THE YEARS ENDED DECEMBER 31**

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Income			
Dividends from Subsidiary	\$ 9,118,104	\$10,015,147	\$12,015,572
Management Fees	601,080	581,334	581,334
Other	103,612	112,876	100,269
	<u>\$ 9,822,796</u>	<u>\$10,709,357</u>	<u>\$12,697,175</u>
Expenses			
Interest	601,567	503,286	517,381
Amortization	-	-	938
Salaries and Employee Benefits	840,130	811,150	782,152
Other	554,434	666,872	538,847
	<u>1,996,131</u>	<u>1,981,308</u>	<u>1,839,318</u>
Income Before Taxes and Equity in Undistributed Earnings of Subsidiary	7,826,665	8,728,049	10,857,857
Income Tax Benefits	457,934	444,764	396,738
Income Before Equity in Undistributed Earnings of Subsidiary	8,284,599	9,172,813	11,254,595
Dividends Received in Excess of Earnings of Subsidiary	-	(800,116)	(3,722,970)
Equity in Undistributed Earnings of Subsidiary	388,611	-	-
Net Income	8,673,210	8,372,697	7,531,625
Preferred Stock Dividends	1,493,310	2,375,010	2,688,604
Net Income Available to Common Stockholders	<u>\$ 7,179,900</u>	<u>\$ 5,997,687</u>	<u>\$4,843,021</u>

(21) Financial Information of Colony Bankcorp, Inc. (Parent Only) (Continued)

**COLONY BANKCORP, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
FOR THE YEARS ENDED DECEMBER 31**

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Net Income	<u>\$8,673,210</u>	<u>\$8,372,697</u>	<u>\$ 7,531,625</u>
Other Comprehensive Income (Loss)			
Gains (Losses) on Securities Arising During the Year	(505,367)	610,689	6,432,906
Tax Effect	171,825	(207,634)	(2,187,189)
Realized (Gains) Losses on Sale of AFS Securities	(385,223)	11,466	(23,735)
Tax Effect	130,976	(3,898)	8,070
Impairment Loss on Securities	-	-	-
Tax Effect	-	-	-
Change in Unrealized Gains (Losses) on Securities Available for Sale, Net of Reclassification Adjustment and Tax Effects	<u>(587,789)</u>	<u>410,623</u>	<u>4,230,052</u>
Comprehensive Income	<u><u>\$8,085,421</u></u>	<u><u>\$8,783,320</u></u>	<u><u>\$11,761,677</u></u>

(21) Financial Information of Colony Bankcorp, Inc. (Parent Only) (Continued)**COLONY BANKCORP, INC. (PARENT ONLY)
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31**

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Cash Flows from Operating Activities			
Net Income	\$ 8,673,210	\$ 8,372,697	\$ 7,531,625
Adjustments to Reconcile Net Income to Net Cash Provided by Operating Activities			
Depreciation and Amortization	66,476	73,999	75,347
Equity in Undistributed Earnings of Subsidiary	(388,611)	-	-
Dividends Received in Excess of Earnings of Subsidiary	-	800,116	3,722,970
Change in Interest Payable	5,367	23,072	(1,069,695)
Other	108,288	1,555,482	(437,115)
	<u>8,464,730</u>	<u>10,825,366</u>	<u>9,823,132</u>
Cash Flows from Investing Activities			
Purchases of Premises and Equipment	<u>(6,836)</u>	<u>(8,884)</u>	<u>(2,020)</u>
Cash Flows from Financing Activities			
Dividends Paid on Preferred Stock	(1,590,746)	(2,487,274)	(5,492,749)
Redemption of Preferred Stock	(8,661,000)	(9,979,000)	-
	<u>(10,251,746)</u>	<u>(12,466,274)</u>	<u>(5,492,749)</u>
Increase (Decrease) in Cash	(1,793,852)	(1,649,792)	4,328,363
Cash, Beginning	<u>4,100,860</u>	<u>5,750,652</u>	<u>1,422,289</u>
Cash, Ending	<u>\$ 2,307,008</u>	<u>\$ 4,100,860</u>	<u>\$ 5,750,652</u>

(22) Earnings Per Share

Basic earnings per share is computed by dividing net income available to common stockholders by the weighted average number of common shares outstanding during each period. Diluted earnings per share reflects the potential dilution of common stock warrants. Net income available to common stockholders represents net income after preferred stock dividends. The following table presents earnings per share for the years ended December 31, 2016, 2015 and 2014:

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Numerator			
Net Income Available to Common Stockholders	<u>\$ 7,179,900</u>	<u>\$ 5,997,687</u>	<u>\$ 4,843,021</u>
Denominator			
Weighted Average Number of Common Shares Outstanding for Basic Earnings Per Common Share	8,439,258	8,439,258	8,439,258
Dilutive Effect of Potential Common Stock Stock Warrants	<u>74,037</u>	19,203	-
Weighted-Average Number of Shares Outstanding for Diluted Earnings Per Common Share	<u>8,513,295</u>	<u>8,458,461</u>	<u>8,439,258</u>
Earnings Per Share - Basic	<u>\$ 0.85</u>	<u>\$ 0.71</u>	<u>\$ 0.57</u>
Earnings Per Share - Diluted	<u>\$ 0.84</u>	<u>\$ 0.71</u>	<u>\$ 0.57</u>

For the year ended December 31, 2014, the Company has excluded 500,000 shares of common stock equivalents because the strike price of the common stock equivalents would cause them to have an anti-dilutive effect.

(23) Accumulated Other Comprehensive Income (Loss)

Changes in accumulated other comprehensive income (loss) for unrealized gains and losses securities available for sale for the years ended December 31, 2016, 2015 and 2014 are as follows:

	<u>Years Ended December 31,</u>		
	<u>2016</u>	<u>2015</u>	<u>2014</u>
Beginning Balance	<u>\$ (4,434,351)</u>	<u>\$ (4,844,974)</u>	<u>\$ (9,075,026)</u>
Other Comprehensive Income Before Reclassification	(333,542)	403,055	4,245,717
Amounts Reclassified from Accumulated Other Comprehensive Income	<u>(254,247)</u>	7,568	<u>(15,665)</u>
Net Current Period Other Comprehensive Income	<u>(587,789)</u>	<u>410,623</u>	<u>4,230,052</u>
Ending Balance	<u>\$ (5,022,140)</u>	<u>\$ (4,434,351)</u>	<u>\$ (4,844,974)</u>

Management's Discussion and Analysis of Financial Condition and Results of Operations

Forward-Looking Statements and Factors that Could Affect Future Results

Certain statements contained in this Annual Report that are not statements of historical fact constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 (the Act), notwithstanding that such statements are not specifically identified. In addition, certain statements may be contained in the Company's future filings with the SEC, in press releases, and in oral and written statements made by or with the approval of the Company that are not statements of historical fact and constitute forward-looking statements within the meaning of the Act. Examples of forward-looking statements include, but are not limited to: (i) projections of revenues, income or loss, earnings or loss per share, the payment or nonpayment of dividends, capital structure and other financial items; (ii) statements of plans and objectives of Colony Bankcorp, Inc. or its management or Board of Directors, including those relating to products or services; (iii) statements of future economic performance; and (iv) statements of assumptions underlying such statements. Words such as "believes," "anticipates," "expects," "intends," "targeted" and similar expressions are intended to identify forward-looking statements but are not the exclusive means of identifying such statements.

Forward-looking statements involve risks and uncertainties that may cause actual results to differ materially from those in such statements. Factors that could cause actual results to differ from those discussed in the forward-looking statements include, but are not limited to:

- Local and regional economic conditions and the impact they may have on the Company and its customers and the Company's assessment of that impact;
- Changes in estimates of future reserve requirements based upon the periodic review thereof under relevant regulatory and accounting requirements;
- The effects of and changes in trade, monetary and fiscal policies and laws, including interest rate policies of the Federal Reserve Board;
- Inflation, interest rate, market and monetary fluctuations;
- Political instability;
- Acts of war or terrorism;
- The timely development and acceptance of new products and services and perceived overall value of these products and services by users;
- Changes in consumer spending, borrowings and savings habits;
- Technological changes;
- Acquisitions and integration of acquired businesses;
- The ability to increase market share and control expenses;

- The effect of changes in laws and regulations (including laws and regulations concerning taxes, banking, securities and insurance) with which the Company and its subsidiaries must comply;
- The effect of changes in accounting policies and practices, as may be adopted by the regulatory agencies, as well as the Financial Accounting Standards Board and other accounting standard setters;
- Changes in the Company's organization, compensation and benefit plans;
- The costs and effects of litigation and of unexpected or adverse outcomes in such litigation;
- Greater than expected costs or difficulties related to the integration of new lines of business; and
- The Company's success at managing the risks involved in the foregoing items.

Forward-looking statements speak only as of the date on which such statements are made. The Company undertakes no obligation to update any forward-looking statement to reflect events or circumstances after the date on which such statement is made, or to reflect the occurrence of unanticipated events.

Future Outlook

During the recent financial crisis, the financial industry experienced tremendous adversities as a result of the collapse of the real estate markets across the country. Colony, like most banking companies, has been affected by these economic challenges that started with a rapid stall of real estate sales and developments throughout the county. While much has been accomplished in addressing problem assets the past several years, there is still work to be done in bringing our problem assets to an acceptable level. A focus in 2017 will be directed toward further reduction of problem assets.

As we look forward to 2017 we are committed to improving earnings, reducing problem assets and redeeming TARP preferred stock. We plan to seek approval from the Federal Reserve and the Department of Finance to completely eliminate the Preferred Stock during 2017. Given the improved condition of the company we are also considering product and market expansion. In 2016 we opened new offices in Tifton and Statesboro, while closing four offices in smaller rural markets. In January 2017, the Company opened its third office in Savannah.

While the Company has improved earnings, reduced problem assets and maintained strong capital levels, we have reinstated dividend payments beginning first quarter 2017. The Company's board of directors suspended the payment of dividends in the third quarter of 2009.

We continue to explore opportunities to improve core non-interest income. Revenue enhancement initiatives to accomplish this include new product lines and services. The Company will also invest in new technology with implementation of a new loan platform which will offer much efficiency with our "back-office" operations.

In addition, we continue to make efforts to attract and retain top talent to improve business operations. To that end, the Company entered into Retention Agreements with members of management in the first quarter of 2015. The Company expects that these agreements will facilitate the retention of key individuals responsible for maintaining current operations and spearheading future product and market expansion.

Non-GAAP Financial Measures

Our accounting and reporting policies conform to generally accepted accounting principles (GAAP) in the United States and prevailing practices in the banking industry. However, certain non-GAAP measures are used by management to supplement the evaluation of our performance. These include the fully-taxable equivalent measures: tax-equivalent net interest income, tax-equivalent net interest margin, and tax-equivalent net interest spread, which include the effects of taxable-equivalent adjustments using a federal income tax rate of 34% to increase tax-exempt interest income to a tax-equivalent basis. Tax-equivalent adjustments are reported in Notes 1 and 2 to the Average Balances with Average Yields and Rates table under Rate/Volume Analysis. Tangible book value per common share is also a non-GAAP measure used in the selected Financial Data Section.

Tax-equivalent net interest income, net interest margin and net interest spread. Net interest income on a tax-equivalent basis is a non-GAAP measure that adjusts for the tax-favored status of net interest income from loans and investments. We believe this measure to be the preferred industry measurement of net interest income and it enhances comparability of net interest income arising from taxable and tax-exempt sources. The most directly comparable financial measure calculated in accordance with GAAP is our net interest income. Net interest margin on a tax-equivalent basis is net interest income on a tax-equivalent basis divided by average interest-earning assets on a tax-equivalent basis. The most directly comparable financial measure calculated in accordance with GAAP is our net interest margin. Net interest spread on a tax-equivalent basis is the difference in the average yield on average interest-earning assets on a tax equivalent basis and the average rate paid on average interest-bearing liabilities. The most directly comparable financial measure calculated in accordance with GAAP is our net interest spread.

These non-GAAP financial measures should not be considered alternatives to GAAP-basis financial statements, and other bank holding companies may define or calculate these non-GAAP measures or similar measures differently.

A reconciliation of these performance measures to GAAP performance measures is included in the tables below.

Non-GAAP Performance Measures Reconciliation

	Years Ended December 31,				
	2016	2015	2014	2013	2012
	(Dollars in Thousands, except per share data)				
Interest Income Reconciliation					
	\$			\$	
Interest Income – Taxable Equivalent	44,762	\$ 44,407	44,879	\$ 45,356	\$ 47,433
Tax Equivalent Adjustment	173	132	117	170	144
Interest Income (GAAP)	<u>\$ 44,589</u>	<u>\$ 44,275</u>	<u>\$ 44,762</u>	<u>\$ 45,186</u>	<u>\$ 47,289</u>
Net Interest Income Reconciliation					
	\$			\$	
Net Interest Income – Taxable Equivalent	38,279	\$ 37,838	38,080	\$ 37,859	\$ 36,417
Tax Equivalent Adjustment	173	132	117	170	144
Net Interest Income (GAAP)	<u>\$ 38,106</u>	<u>\$ 37,706</u>	<u>\$ 37,963</u>	<u>\$ 37,689</u>	<u>\$ 36,273</u>
Net Interest Margin Reconciliation					
Net Interest Margin – Taxable Equivalent	3.51%	3.52%	3.60%	3.61%	3.42%
Tax Equivalent Adjustment	.02	.01	.01	.02	.01
Net Interest Margin (GAAP)	<u>3.49%</u>	<u>3.51%</u>	<u>3.59%</u>	<u>3.59%</u>	<u>3.41%</u>
Interest Rate Spread Reconciliation					
Interest Rate Spread – Taxable Equivalent	3.40%	3.41%	3.49%	3.50%	3.27%
Tax Equivalent Adjustment	.02	.01	.01	.02	.01
Interest Rate Spread (GAAP)	<u>3.38%</u>	<u>3.40%</u>	<u>3.48%</u>	<u>3.48%</u>	<u>3.26%</u>
Selected Financial Data					
Tangible Book Value Per Common Share	\$ 9.95	\$ 9.16	\$ 8.40	\$ 7.32	\$ 8.02
Effect of Other Intangible Assets	0.01	0.02	0.02	0.02	0.03
Book Value Per Common Share (GAAP)	<u>\$ 9.96</u>	<u>\$ 9.18</u>	<u>\$ 8.42</u>	<u>\$ 7.34</u>	<u>\$ 8.05</u>

The Company

Colony Bankcorp, Inc. (“Colony” or the “Company”) is a bank holding company headquartered in Fitzgerald, Georgia that provides, through its wholly-owned subsidiary Colony Bank (collectively referred to as the Company), a broad array of products and services throughout central, south and coastal Georgia markets. The Company offers commercial, consumer and mortgage banking services.

Overview

The following discussion and analysis presents the more significant factors affecting the Company’s financial condition as of December 31, 2016 and 2015, and results of operations for each of the years in the three-year period ended December 31, 2016. This discussion and analysis should be read in conjunction with the Company’s consolidated financial statements, notes thereto and other financial information appearing elsewhere in this report.

Taxable-equivalent adjustments are the result of increasing income from tax-free loans and investments by an amount equal to the taxes that would be paid if the income were fully taxable based on a 34 percent federal tax rate, thus making tax-exempt yields comparable to taxable asset yields.

Dollar amounts in tables are stated in thousands, except for per share amounts.

Results of Operations

The Company's results of operations are determined by its ability to effectively manage interest income and expense, to minimize loan and investment losses, to generate noninterest income and to control noninterest expense. Since market forces and economic conditions beyond the control of the Company determine interest rates, the ability to generate net interest income is dependent upon the Company's ability to obtain an adequate spread between the rate earned on interest-earning assets and the rate paid on interest-bearing liabilities. Thus, the key performance for net interest income is the interest margin or net yield, which is taxable-equivalent net interest income divided by average interest-earning assets. Net income available to common shareholders totaled \$7.18 million, or \$0.84 per diluted common share in 2016, compared to \$6.00 million, or \$0.71 per diluted common share in 2015 and compared to \$4.84 million, or \$0.57 per diluted common share in 2014.

Selected income statement data, returns on average assets and average equity and dividends per share for the comparable periods were as follows:

			\$	%			\$	%
	2016	2015	Variance	Variance	2015	2014	Variance	Variance
Taxable-equivalent net interest income	\$ 38,279	\$ 37,838	\$ 441	1.17%	\$ 37,838	\$ 38,080	\$ (242)	(0.64)%
Taxable-equivalent adjustment	173	132	41	31.06	132	117	15	12.82
Net interest income	38,106	37,706	400	1.06	37,706	37,963	(257)	(0.68)
Provision for loan losses	1,062	866	196	22.63	866	1,308	(442)	(33.79)
Noninterest income	9,553	9,045	508	5.62	9,045	9,125	(80)	(0.88)
Noninterest expense	34,073	33,724	349	1.03	33,724	34,980	(1,256)	(3.59)
Income before income taxes	\$ 12,524	\$ 12,161	\$ 363	2.98%	\$ 12,161	\$ 10,800	\$ 1,361	12.60%
Income Taxes	3,851	3,788	63	1.66	3,788	3,268	520	15.91
Net income	\$ 8,673	\$ 8,373	\$ 300	3.58%	\$ 8,373	\$ 7,532	\$ 841	11.17%
Preferred stock dividends	\$ 1,493	\$ 2,375	\$ (882)	(37.14)%	\$ 2,375	\$ 2,689	\$ (314)	(11.68)%
Net income available to common shareholders	\$ 7,180	\$ 5,998	\$ 1,182	19.71%	\$ 5,998	\$ 4,843	\$ 1,155	23.85%
Net income available to common shareholders:								
Basic	\$ 0.85	\$ 0.71	\$ 0.14	19.72%	\$ 0.71	\$ 0.57	\$ 0.14	24.56%
Diluted	\$ 0.84	\$ 0.71	\$ 0.13	18.31%	\$ 0.71	\$ 0.57	\$ 0.14	24.56%
Return on average assets (1)	0.62%	0.52%	0.10%	19.23%	0.52%	0.43%	0.09%	20.93%
Return on average common equity (1)	7.17%	5.90%	1.27%	21.53%	5.90%	5.11%	0.79%	15.46%

(1) Computed using net income available to common shareholders.

Net Interest Income

Net interest income is the difference between interest income on earning assets, such as loans and securities, and interest expense on liabilities, such as deposits and borrowings, which are used to fund those assets. Net interest income is the Company's largest source of revenue, representing 79.96 percent of total revenue during 2016, 80.65 percent of total revenue during 2015 and 80.62 percent during 2014.

Net interest margin is the taxable-equivalent net interest income as a percentage of average interest-earning assets for the period. The level of interest rates and the volume and mix of interest-earning assets and interest-bearing liabilities impact net interest income and net interest margin.

The Company's loan portfolio is significantly affected by changes in the prime interest rate. The prime interest rate, which is the rate offered on loans to borrowers with strong credit, is currently 3.75 percent. The Federal Reserve Board sets general market rates of interest, including the deposit and loan rates offered by many financial institutions. For the first time in several years, the prime interest rate increased by 25 basis points in the fourth quarter of 2015, followed by a similar 25-point increase in the fourth quarter of 2016. We anticipate that the prime interest rate will again rise in 2017. Given that the federal funds rate moves in accordance with the movement of the prime interest rate, we anticipate that the federal funds rate will also increase from its current 0.75 percent.

The following table presents the changes in taxable-equivalent net interest income and identifies the changes due to differences in the average volume of interest-earning assets and interest-bearing liabilities and the changes due to changes in the average interest rate on those assets and liabilities. The changes in net interest income due to changes in both average volume and average interest rate have been allocated to the average volume change or the average interest rate change in proportion to the absolute amounts of the change in each. The Company's consolidated average balance sheets along with an analysis of taxable-equivalent net interest earnings are presented in the Rate/Volume Analysis.

Rate/Volume Analysis

The rate/volume analysis presented hereafter illustrates the change from year to year for each component of the taxable equivalent net interest income separated into the amount generated through volume changes and the amount generated by changes in the yields/rates.

	Changes From 2015 to 2016 (a)			Changes From 2014 to 2015 (a)		
	Volume	Rate	Total	Volume	Rate	Total
Interest Income						
Loans, Net-Taxable	\$ 221	\$ (951)	\$ (730)	\$ 831	\$ (831)	\$ -
Investment Securities						
Taxable	381	669	1,050	(89)	(396)	(485)
Tax-Exempt	12	(15)	(3)	(12)	(3)	(15)
Total Investment Securities	393	654	1,047	(101)	(399)	(500)
Interest-Bearing Deposits in						
Other Banks	(18)	62	44	35	3	38
Federal Funds Sold	(15)	-	(15)	(16)	(1)	(17)
Other Interest - Earning Assets	4	5	9	(6)	13	7
Total Interest Income	585	(230)	355	743	(1,215)	(472)
Interest Expense						
Interest-Bearing Demand and						
Savings Deposits	137	62	199	126	(29)	97
Time Deposits	(271)	(4)	(275)	(240)	(113)	(353)
Total Interest Expense						
On Deposits	(134)	58	(76)	(114)	(142)	(256)
Other Interest-Bearing Liabilities						
Subordinated Debentures	-	98	98	-	(15)	(15)
Other Debt	74	(183)	(109)	-	41	41
Federal Funds Purchased	-	1	1	-	-	-
Total Interest Expense	(60)	(26)	(86)	(114)	(116)	(230)
Net Interest Income (Loss)	\$ 645	\$ (204)	\$ 441	\$ 857	\$ (1,099)	\$ (242)

- (a) Changes in net interest income for the periods, based on either changes in average balances or changes in average rates for interest-earning assets and interest-bearing liabilities, are shown on this table. During each year there are numerous and simultaneous balance and rate changes; therefore, it is not possible to precisely allocate the changes between balances and rates. For the purpose of this table, changes that are not exclusively due to balance changes or rate changes have been attributed to rates.

The Company maintains about 21.2 percent of its loan portfolio in adjustable rate loans that reprice with prime rate changes, while the bulk of its other loans mature within 3 years. The liabilities to fund assets are primarily in non-maturing core deposits and short term certificates of deposit that mature within one year. The Federal Reserve rates have remained flat since 2008 until the 25 basis point increase in the fourth quarter of 2015 followed by the 25 basis point increase in the fourth quarter of 2016. We have seen the net interest margin change to 3.51 percent for 2016, compared to 3.52 percent for 2015 and 3.60 percent for 2014. We have seen our net interest margin reach a low of 3.39 percent in fourth quarter 2016 to a high of 3.59 percent in second quarter 2016.

Taxable-equivalent net interest income for 2016 increased by \$441 thousand, or 1.17 percent, compared to 2015 while taxable-equivalent net interest income for 2015 decreased by \$242 thousand, or 0.64 percent compared to 2014. The average volume of interest-earning assets during 2016 increased \$16.41 million compared to 2015 while over the same period the net interest margin dropped to 3.51 percent from 3.52 percent. The average volume of interest-earning assets during 2015 increased \$16.95 million compared to 2014 while over the same period the net interest margin dropped to 3.52 percent from 3.60 percent. The change in the net interest margin in 2016 and 2015 was primarily driven by reduction in the cost of funds and a higher level of low yielding assets. The increase in average interest-earning assets in 2016 was in loans, investments and other interest-earning assets. The increase in average interest-earning assets in 2015 was in loans and interest-bearing deposits.

The average volume of loans increased \$4.20 million in 2016 compared to 2015, and increased \$15.47 million in 2015 compared to 2014. The average yield on loans decreased 13 basis points in 2016 compared to 2015 and decreased 11 basis points in 2015 compared to 2014. The average volume of deposits increased \$17.35 million in 2016 compared to 2015. The average volume of deposits increased \$17.29 million in 2015 compared to 2014. Demand deposits made up \$11.80 million of the increase in average deposits in 2016 compared to \$10.09 million of the increase in average deposits in 2015.

Accordingly, the ratio of average interest-bearing deposits to total average deposits was 85.9 percent in 2016, 86.8 percent in 2015 and 87.6 percent in 2014. This deposit mix, combined with a general decrease in interest rates, had the effect of (i) decreasing the average cost of total deposits by 2 basis points in 2016 compared to 2015 and decreasing the average cost of total deposits by 3 basis points in 2015 compared to 2014, and (ii) mitigating a portion of the impact of decreasing yields on interest-earning assets on the Company's net interest income.

The Company's net interest spread, which represents the difference between the average rate earned on interest-earning assets and the average rate paid on interest-bearing liabilities, was 3.40 percent in 2016 compared to 3.41 percent in 2015 and 3.49 percent in 2014. The net interest spread, as well as the net interest margin, will be impacted by future changes in short-term and long-term interest rate levels, as well as the impact from the competitive environment. A discussion of the effects of changing interest rates on net interest income is set forth in *Market Risk and Interest Rate Sensitivity* included elsewhere in this report.

Rate/Volume Analysis (Continued)

AVERAGE BALANCE SHEETS

	2016			2015			2014		
	Average Balances	Income/ Expense	Yields/ Rates	Average Balances	Income/ Expense	Yields/ Rates	Average Balances	Income/ Expense	Yields/ Rates
Assets									
Interest-Earning Assets									
Loans, Net of Unearned Income (1)	\$ 761,149	\$ 39,084	5.13%	\$ 756,953	\$ 39,814	5.26%	\$ 741,484	\$ 39,814	5.37%
Investment Securities									
Taxable	301,357	5,328	1.77	276,807	4,278	1.55	282,056	4,763	1.69
Tax-Exempt (2)	2,440	95	3.89	2,171	98	4.51	2,418	113	4.67
Total Investment Securities	303,797	5,423	1.79	278,978	4,376	1.57	284,474	4,876	1.71
Interest-Bearing Deposits	23,167	124	0.54	29,815	80	0.27	16,193	42	0.26
Federal Funds Sold	-	-	-	6,056	15	0.25	12,551	32	0.25
Other Interest-Earning Assets	2,854	131	4.59	2,754	122	4.43	2,906	115	3.96
Total Interest-Earning Assets	1,090,967	44,762	4.10	1,074,556	44,407	4.13	1,057,608	44,879	4.24
Noninterest-Earning Assets									
Cash	19,208			19,049			9,698		
Allowance for Loan Losses	(9,372)			(8,587)			(10,841)		
Other Assets	63,060			61,966			71,587		
Total Noninterest-Earning Assets	72,896			72,428			70,444		
Total Assets	\$ 1,163,863			\$ 1,146,984			\$ 1,128,052		
Liabilities and Stockholders' Equity									
Interest-Bearing Liabilities									
Interest-Bearing Demand and Savings	\$ 469,740	\$ 1,694	0.36%	\$ 430,731	\$ 1,495	0.35%	\$ 394,615	\$ 1,398	0.35%
Other Time	383,628	3,087	0.80	417,080	3,362	0.81	445,993	3,715	0.83
Total Interest-Bearing Deposits	853,368	4,781	0.56	847,811	4,857	0.57	840,608	5,113	0.61
Other Interest-Bearing Liabilities									
Other Borrowed Money	42,470	1,100	2.59	40,000	1,209	3.02	40,000	1,168	2.92
Subordinated Debentures	24,229	601	2.48	24,229	503	2.08	24,229	518	2.14
Federal Funds Purchased and									
Repurchase Agreements	35	1	2.86	3	-	-	2	-	-
Total Other Interest-Bearing									
Liabilities	66,734	1,702	2.55	64,232	1,712	2.67	64,231	1,686	2.62
Total Interest-Bearing Liabilities	920,102	6,483	0.70	912,043	6,569	0.72	904,839	6,799	0.75
Noninterest-Bearing Liabilities and									
Stockholders' Equity									
Demand Deposits	140,338			128,541			118,452		
Other Liabilities	3,309			4,690			10,010		
Stockholders' Equity	100,114			101,710			94,751		
Total Noninterest-Bearing									
Liabilities and Stockholders' Equity	243,761			234,941			223,213		
Total Liabilities and									
Stockholders' Equity	\$ 1,163,863			\$ 1,146,984			\$ 1,128,052		
Interest Rate Spread			3.40%			3.41%			3.49%
Net Interest Income	\$ 38,279			\$ 37,838			\$ 38,080		
Net Interest Margin			3.51%			3.52%			3.60%

- (1) The average balance of loans includes the average balance of nonaccrual loans. Income on such loans is recognized and recorded on the cash basis. Taxable equivalent adjustments totaling \$141, \$99 and \$79 for 2016, 2015 and 2014, respectively, are included in interest on loans. The adjustments are based on a federal tax rate of 34 percent.
- (2) Taxable-equivalent adjustments totaling \$32, \$33 and \$38 for 2016, 2015 and 2014, respectively, are included in tax-exempt interest on investment securities. The adjustments are based on a federal tax rate of 34 percent with appropriate reductions for the effect of disallowed interest expense incurred in carrying tax-exempt obligations.

Provision for Loan Losses

The provision for loan losses is determined by management as the amount to be added to the allowance for loan losses after net charge-offs have been deducted to bring the allowance to a level which, in management's best estimate, is necessary to absorb probable losses within the existing loan portfolio. The provision for loan losses totaled \$1.06 million in 2016 compared to \$866 thousand in 2015 and \$1.31 million in 2014. See the section captioned "Allowance for Loan Losses" elsewhere in this discussion for further analysis of the provision for loan losses.

Noninterest Income

The components of noninterest income were as follows:

			\$	%			\$	%
	2016	2015	Variance	Variance	2015	2014	Variance	Variance
Service Charges on Deposit Accounts	\$ 4,307	\$ 4,269	\$ 38	0.89%	\$ 4,269	\$ 4,649	\$ (380)	(8.17)%
Other Charges, Commissions and Fees	2,803	2,627	176	6.70	2,627	2,388	239	10.01
Mortgage Fee Income	682	527	155	29.41	527	420	107	25.48
Securities Gains (Losses)	385	(11)	396	3,600.00	(11)	24	(35)	(145.83)
Other	1,377	1,633	(256)	(15.68)	1,633	1,644	(11)	(0.67)
Total	<u>\$ 9,554</u>	<u>\$ 9,045</u>	<u>\$ 509</u>	<u>5.63%</u>	<u>\$ 9,045</u>	<u>\$ 9,125</u>	<u>\$ (80)</u>	<u>(0.88)%</u>

Other Charges, Commissions and Fees. Significant amounts impacting the comparable periods was primarily attributed to ATM and debit card interchange fees which increased \$184 thousand in 2016 compared to 2015 and \$251 thousand in 2015 compared to 2014.

Mortgage Fee Income. The increase in mortgage fee income in 2016 compared to the same period in 2015 is due to an increase in the volume of mortgage loans.

Securities Gains (Losses). The increase in 2016 is attributable to the gain on sale of securities compared to 2015 with a loss on sale of securities.

Other. Significant amounts impacting the comparable periods was primarily attributed to having income from the sale of a tax credit of \$66 thousand and life insurance benefits of \$137 that did not occur in 2016. The Bank did not have any significant changes for 2015 compared to 2014.

Noninterest Expense

The components of noninterest expense were as follows:

	<u>2016</u>	<u>2015</u>	<u>\$</u> <u>Variance</u>	<u>%</u> <u>Variance</u>	<u>2015</u>	<u>2014</u>	<u>\$</u> <u>Variance</u>	<u>%</u> <u>Variance</u>
Salaries and Employee Benefits	\$ 18,483	\$ 17,590	\$ 893	5.08%	\$ 17,590	\$ 17,508	\$ 82	0.47%
Occupancy and Equipment	3,970	3,989	(19)	(0.48)	3,989	4,063	(74)	(1.82)
Directors' Fees	349	358	(9)	(2.51)	358	392	(34)	(8.67)
Legal and Professional Fees	792	738	54	7.32	738	786	(48)	(6.11)
Foreclosed Property	1,143	1,683	(540)	(32.09)	1,683	2,701	(1,018)	(37.69)
FDIC Assessment	604	899	(295)	(32.81)	899	966	(67)	(6.94)
Advertising	610	625	(15)	(2.40)	625	652	(27)	(4.14)
Software	1,112	993	119	11.98	993	925	68	7.35
Telephone	737	710	27	3.80	710	736	(26)	(3.53)
ATM/Card Processing	1,136	1,061	75	7.07	1,061	906	155	17.11
Other	5,137	5,078	59	1.16	5,078	5,345	(267)	(5.00)
Total	<u>\$ 34,073</u>	<u>\$ 33,724</u>	<u>\$ 349</u>	<u>1.03%</u>	<u>\$ 33,724</u>	<u>\$ 34,980</u>	<u>\$ (1,256)</u>	<u>(3.59)%</u>

Salaries and Employee Benefits. The increase in salary and employee benefits for 2016 is due to merit pay increases. Salary and employee benefits remained flat in 2015 compared to 2014.

Foreclosed Property. The decrease in foreclosed property and repossession expense for 2016 and 2015 is primarily attributable to the decrease in the volume of OREO.

Sources and Uses of Funds

The following table illustrates, during the years presented, the mix of the Company's funding sources and the assets in which those funds are invested as a percentage of the Company's average total assets for the period indicated. Average assets totaled \$1.16 billion in 2016 compared to \$1.15 billion in 2015 and \$1.13 billion in 2014.

	2016		2015		2014	
Sources of Funds:						
Deposits:						
Noninterest-Bearing	\$ 140,338	12.1%	\$ 128,541	11.2%	\$ 118,452	10.5%
Interest-Bearing	853,368	73.3%	847,811	73.9%	840,608	74.5%
Federal Funds Purchased and Repurchase Agreements	35	- %	3	- %	2	- %
Subordinated Debentures and Other Borrowed Money	66,699	5.7%	64,229	5.6%	64,229	5.7%
Other Noninterest-Bearing Liabilities	3,309	0.3%	4,690	0.4%	10,010	0.9%
Equity Capital	100,114	8.6%	101,710	8.9%	94,751	8.4%
Total	<u>\$ 1,163,863</u>	<u>100.0%</u>	<u>\$ 1,146,984</u>	<u>100.0%</u>	<u>\$ 1,128,052</u>	<u>100.0%</u>
Uses of Funds:						
Loans (Net of Allowance)	\$ 751,777	64.6%	\$ 748,366	65.3%	\$ 730,643	64.8%
Investment Securities	303,797	26.1%	278,978	24.3%	284,474	25.2%
Federal Funds Sold	-	- %	6,056	0.5%	12,551	1.1%
Interest-Bearing Deposits	23,167	2.0%	29,815	2.6%	16,193	1.4%
Other Interest-Earning Assets	2,854	0.2%	2,754	0.2%	2,906	0.3%
Other Noninterest-Earning Assets	82,268	7.1%	81,015	7.1%	81,285	7.2%
Total	<u>\$ 1,163,863</u>	<u>100.0%</u>	<u>\$ 1,146,984</u>	<u>100.0%</u>	<u>\$ 1,128,052</u>	<u>100.0%</u>

Deposits continue to be the Company's primary source of funding. Over the comparable periods, the relative mix of deposits continues to be high in interest-bearing deposits. Interest-bearing deposits totaled 85.9 percent of total average deposits in 2016 compared to 86.8 percent in 2015 and 87.6 percent in 2014.

The Company primarily invests funds in loans and securities. Loans continue to be the largest component of the Company's mix of invested assets. Loan demand decreased in 2016 as total loans were \$754.3 million at December 31, 2016, down 0.57 percent, compared to loans of \$758.6 million at December 31, 2015, which went up 1.68 percent, compared to loans of \$746.1 million at December 31, 2014. See additional discussion regarding the Company's loan portfolio in the section captioned "Loans" on the following page. The majority of funds provided by deposits have been invested in loans and securities.

Loans

The following table presents the composition of the Company's loan portfolio as of December 31 for the past five years.

	<u>2016</u>	<u>2015</u>	<u>2014</u>	<u>2013</u>	<u>2012</u>
Commercial and Agricultural					
Commercial	\$ 47,025	\$ 47,782	\$ 50,960	\$ 48,107	\$ 55,684
Agricultural	17,080	19,193	16,689	10,666	6,211
Real Estate					
Commercial Construction	30,358	40,107	51,259	52,739	53,808
Residential Construction	11,830	9,413	11,221	6,549	5,852
Commercial	349,090	346,262	332,231	341,783	334,386
Residential	195,580	197,002	203,753	206,258	203,845
Farmland	66,877	61,780	49,951	47,034	49,057
Consumer and Other					
Consumer	19,695	20,605	22,820	25,676	29,778
Other	16,748	16,492	7,210	12,406	8,429
	<u>754,283</u>	<u>758,636</u>	<u>746,094</u>	<u>751,218</u>	<u>747,050</u>
Unearned Interest and Fees	(361)	(357)	(362)	(360)	(234)
Allowances for Loan Losses	<u>(8,923)</u>	<u>(8,604)</u>	<u>(8,802)</u>	<u>(11,806)</u>	<u>(12,737)</u>
Loans	<u>\$ 744,999</u>	<u>\$ 749,675</u>	<u>\$ 736,930</u>	<u>\$ 739,052</u>	<u>\$ 734,079</u>

The following table presents total loans as of December 31, 2016 according to maturity distribution and/or repricing opportunity on adjustable rate loans.

Maturity and Repricing Opportunity

One Year or Less	\$ 264,807
After One Year through Three Years	287,713
After Three Years through Five Years	149,866
Over Five Years	<u>51,897</u>
	<u>\$ 754,283</u>

Overview. Loans totaled \$754.3 million at December 31, 2016, down 0.57 percent from \$758.6 million at December 31, 2015. The majority of the Company's loan portfolio is comprised of the real estate loans. Commercial and residential real estate which is primarily 1-4 family residential properties and nonfarm nonresidential properties, made up 72.21 percent and 71.61 percent of total loans, real estate construction loans made up 5.59 percent and 6.53 percent while commercial and agricultural loans made up 8.50 percent and 8.83 percent of total loans at December 31, 2016 and December 31, 2015, respectively.

Loan Origination/Risk Management. In accordance with the Company's decentralized banking model, loan decisions are made at the local bank level. The Company utilizes both an Executive Loan Committee and a Director Loan Committee to assist lenders with the decision making and underwriting process of larger loan requests. Due to the diverse economic markets served by the Company, evaluation and underwriting criterion may vary slightly by market. Overall, loans are extended after a review of the borrower's repayment ability, collateral adequacy, and overall credit worthiness.

Commercial purpose, commercial real estate, and agricultural loans are underwritten similarly to how other loans are underwritten throughout the Company. The properties securing the Company's commercial real estate portfolio are diverse in terms of type and geographic location. In addition, the Company restricts total loans to \$10 million per borrower, subject to exception and approval by the Director Loan Committee. This diversity helps reduce the company's exposure to adverse economic events that affect any single market or industry. Management monitors and evaluates commercial real estate loans monthly based on collateral, geography, and risk grade criteria. The Company also utilizes information provided by third-party agencies to provide additional insight and guidance about economic conditions and trends affecting the markets it serves.

The Company extends loans to builders and developers that are secured by non-owner occupied properties. In such cases, the Company reviews the overall economic conditions and trends for each market to determine the desirability of loans to be extended for residential construction and development. Sources of repayment for these types of loans may be pre-committed permanent loans from approved long-term lenders, sales of developed property or an interim mini-perm loan commitment from the Company until permanent financing is obtained. In some cases, loans are extended for residential loan construction for speculative purposes and are based on the perceived present and future demand for housing in a particular market served by the Company. These loans are monitored by on-site inspections and are considered to have higher risks than other real estate loans due to their ultimate repayment being sensitive to interest rate changes, general economic conditions and trends, the demand for the properties, and the availability of long-term financing.

The Company originates consumer loans at the bank level. Due to the diverse economic markets served by the Company, underwriting criterion may vary slightly by market. The Company is committed to serving the borrowing needs of all markets served and, in some cases, adjusts certain evaluation methods to meet the overall credit demographics of each market. Consumer loans represent relatively small loan amounts that are spread across many individual borrowers to help minimize risk. Additionally, consumer trends and outlook reports are reviewed by management on a regular basis.

The Company utilizes an independent third party company for loan review and validation of the credit risk program on an ongoing quarterly basis. Results of these reviews are presented to management and the audit committee. The loan review process complements and reinforces the risk identification and assessment decisions made by lenders and credit personnel, as well as the Company's policies and procedures.

Commercial and Agricultural. Commercial and agricultural loans at December 31, 2016 decreased 4.3 percent to \$64.1 million from December 31, 2015 at \$67.0 million. The Company's commercial and agricultural loans are a diverse group of loans to small, medium and large businesses. The purpose of these loans varies from supporting seasonal working capital needs to term financing of equipment. While some short-term loans may be made on an unsecured basis, most are secured by the assets being financed with collateral margins that are consistent with the Company's loan policy guidelines.

Real Estate. Commercial and residential construction loans decreased by \$7.3 million, or 14.8 percent, at December 31, 2016 to \$42.2 million from \$49.52 million at December 31, 2015. This decrease is partially due to completion of construction and the new loans transferring to the commercial real estate category. Therefore, commercial real estate increased \$2.8 million or 0.8 percent at December 31, 2016 to \$349.09 million from \$346.26 million at December 31, 2015.

Other. Other loans at December 31, 2016 increased 1.5 percent to \$16.75 million from \$16.49 million in December 31, 2015.

Industry Concentrations. As of December 31, 2016 and December 31, 2015, there were no concentrations of loans within any single industry in excess of 10 percent of total loans, as segregated by Standard Industrial Classification code (“SIC code”). The SIC code is a federally designed standard industrial numbering system used by the Company to categorize loans by the borrower’s type of business. The Company has established industry-specific guidelines with respect to maximum loans permitted for each industry with which the Company does business.

Collateral Concentrations. Concentrations of credit risk can exist in relation to individual borrowers or groups of borrowers, certain types of collateral, certain types of industries, or certain geographic regions. The Company has a concentration in real estate loans as well as a geographic concentration that could pose an adverse credit risk, particularly with the current economic downturn in the real estate market. At December 31, 2016, approximately 87 percent of the Company’s loan portfolio was concentrated in loans secured by real estate. A substantial portion of borrowers’ ability to honor their contractual obligations is dependent upon the viability of the real estate economic sector. In addition, a large portion of the Company’s foreclosed assets are also located in these same geographic markets, making the recovery of the carrying amount of foreclosed assets susceptible to changes in market conditions. Management continues to monitor these concentrations and has considered these concentrations in its allowance for loan loss analysis.

Large Credit Relationships. The Company is currently in eighteen counties in central, south and coastal Georgia and includes metropolitan markets in Dougherty, Lowndes, Houston, Chatham and Muscogee counties. As a result, the Company originates and maintains large credit relationships with several commercial customers in the ordinary course of business. The Company considers large credit relationships to be those with commitments equal to or in excess of \$5.0 million prior to any portion being sold. Large relationships also include loan participations purchased if the credit relationship with the agent is equal to or in excess of \$5.0 million. In addition to the Company’s normal policies and procedures related to the origination of large credits, the Company’s Executive Loan Committee and Director Loan Committee must approve all new and renewed credit facilities which are part of large credit relationships. The following table provides additional information on the Company’s large credit relationships outstanding at December 31, 2016 and December 31, 2015.

	December 31, 2016			December 31, 2015		
	Number of Relationships	Period End Balances		Number of Relationships	Period End Balances	
Committed		Outstanding	Committed		Outstanding	
Large Credit Relationships: \$5 million to \$9.9 million	14	\$ 96,807	\$ 86,712	16	\$ 108,432	\$ 99,126

Maturities and Sensitivities of Loans to Changes in Interest Rates. The following table presents the maturity distribution of the Company's loans at December 31, 2016. The table also presents the portion of loans that have fixed interest rates or variable interest rates that fluctuate over the life of the loans in accordance with changes in an interest rate index such as the prime rate.

	<u>Due in One Year or Less</u>	<u>After One, but Within Three Years</u>	<u>After Three, but Within Five Years</u>	<u>After Five Years</u>	<u>Total</u>
Loans with fixed interest rates	\$ 181,178	\$ 263,748	\$ 98,267	\$ 51,151	\$ 594,344
Loans with floating interest rates	<u>83,629</u>	<u>23,965</u>	<u>51,599</u>	<u>746</u>	<u>159,939</u>
Total	<u>\$ 264,807</u>	<u>\$ 287,713</u>	<u>\$ 149,866</u>	<u>\$ 51,897</u>	<u>\$ 754,283</u>

The Company may renew loans at maturity when requested by a customer whose financial strength appears to support such renewal or when such renewal appears to be in the Company's best interest. In such instances, the Company generally requires payment of accrued interest and may adjust the rate of interest, require a principal reduction or modify other terms of the loan at the time of renewal.

Nonperforming Assets and Potential Problem Loans

Year-end nonperforming assets and accruing past due loans were as follows:

	<u>2016</u>	<u>2015</u>	<u>2014</u>	<u>2013</u>	<u>2012</u>
Loans Accounted for on Nonaccrual	\$ 12,350	\$ 14,408	\$18,334	\$24,114	\$29,851
Loans Accruing Past Due 90 Days or More	-	8	7	4	4
Other Real Estate Foreclosed	6,439	8,839	10,402	15,502	15,941
Securities Accounted for on Nonaccrual	-	-	-	-	366
Total Nonperforming Assets	<u>\$ 18,789</u>	<u>\$ 23,255</u>	<u>\$28,743</u>	<u>\$39,620</u>	<u>\$46,162</u>
Nonperforming Assets by Segment					
Construction and Land Development	3,376	7,106	9,655	17,323	23,832
1-4 Family Residential	4,375	4,197	8,237	5,926	7,153
Multifamily Residential	-	-	173	335	627
Nonfarm Residential	9,182	9,908	8,375	12,441	10,421
Farmland	800	1,103	1,449	1,629	2,413
Commercial and Consumer	1,056	941	854	1,966	1,716
Total Nonperforming Assets	<u>\$ 18,789</u>	<u>\$ 23,255</u>	<u>\$28,743</u>	<u>\$39,620</u>	<u>\$46,162</u>
Nonperforming Assets as a Percentage of:					
Total Loans and Foreclosed Assets	2.47%	3.03%	3.80%	5.17%	6.05%
Total Assets	1.55%	1.98%	2.51%	3.45%	4.05%
Nonperforming Loans as a Percentage of:					
Total Loans	1.64%	1.90%	2.46%	3.21%	4.00%
Supplemental Data:					
Trouble Debt Restructured Loans					
In Compliance with Modified Terms	\$ 17,992	\$ 19,375	\$19,229	\$20,715	\$24,870
Trouble Debt Restructured Loans					
Past Due 30-89 Days	319	344	757	435	1,377
Accruing Past Due Loans:					
30-89 Days Past Due	4,469	10,959	9,701	9,366	14,911
90 or More Days Past Due	-	8	7	4	4
Total Accruing Past Due Loans	<u>\$ 4,469</u>	<u>\$ 10,967</u>	<u>\$9,708</u>	<u>\$ 9,370</u>	<u>\$ 14,915</u>
Allowance for Loan Losses	\$ 8,923	\$ 8,604	\$ 8,802	\$ 11,806	\$ 12,737
ALLL as a Percentage of:					
Total Loans	1.18%	1.13%	1.18%	1.57%	1.70%
Nonperforming Loans	72.25%	59.68%	47.99%	48.95%	42.66%

Nonperforming assets include nonaccrual loans, loans past due 90 days or more, foreclosed real estate and nonaccrual securities. Nonperforming assets at December 31, 2016 decreased 19.20 percent from December 31, 2015.

Generally, loans are placed on nonaccrual status if principal or interest payments become 90 days past due and/or management deems the collectibility of the principal and/or interest to be in question, as well as when required by regulatory requirements. Loans to a customer whose financial condition has deteriorated are considered for nonaccrual status whether or not the loan is 90 days or more past due. For consumer loans, collectibility and loss are generally determined before the loan reaches 90 days past due. Accordingly, losses on consumer loans are recorded at the time they are determined. Consumer loans that are 90 days or more past due are generally either in liquidation/payment status or bankruptcy awaiting confirmation of a plan. Once interest accruals are discontinued, accrued but uncollected interest is charged to current year operations. Subsequent receipts on nonaccrual loans are recorded as a reduction of principal, and interest income is recorded only after principal recovery is reasonably assured. Classification of a loan as nonaccrual does not preclude the ultimate collection of loan principal or interest.

Troubled debt restructured loans are loans on which, due to deterioration in the borrower's financial condition, the original terms have been modified in favor of the borrower or either principal or interest has been forgiven.

Foreclosed assets represent property acquired as the result of borrower defaults on loans. Foreclosed assets are recorded at estimated fair value, less estimated selling costs, at the time of foreclosure. Write-downs occurring at foreclosure are charged against the allowance for loan losses. On an ongoing basis, properties are appraised as required by market indications and applicable regulations. Write-downs are provided for subsequent declines in value and are included in other non-interest expense along with other expenses related to maintaining the properties.

Allowance for Loan Losses

The allowance for loan losses is a reserve established through a provision for loan losses charged to expense, which represents management's best estimate of probable losses that have been incurred within the existing portfolio of loans. The allowance, in the judgment of management, is necessary to reserve for estimated loan losses and risks inherent in the loan portfolio. The allowance for loan losses includes allowance allocations calculated in accordance with current U.S. accounting standards. The level of the allowance reflects management's continuing evaluation of industry concentrations, specific credit risks, loan loss experience, current loan portfolio quality, present economic, political and regulatory conditions and unidentified losses inherent in the current loan portfolio. Portions of the allowance may be allocated for specific credits; however, the entire allowance is available for any credit that, in management's judgment, should be charged off. While management utilizes its best judgment and information available, the ultimate adequacy of the allowance is dependent upon a variety of factors beyond the Company's control, including the performance of the Company's loan portfolio, the economy, changes in interest rates and the view of the regulatory authorities toward loan classifications.

The Company's allowance for loan losses consists of specific valuation allowances established for probable losses on specific loans and historical valuation allowances for other loans with similar risk characteristics. During the first quarter of 2016 Company management implemented a change to its allowance for loan loss methodology by expanding the historical loss period from a rolling 8 quarters to 16 quarters. Management believes the longer historical loss period better reflects the current and expected loss behavior of the loan portfolio within the current credit cycle. The transition to a rolling 16 quarter loss period will be complete in the first quarter of 2017. As of December 31, 2016, this change in the historical loss period resulted in an increase to the allowance for loan losses of \$804,000. The loss history period used at December 31, 2015 and 2014 was based on the loss rate from the eight quarters ended September 30, 2015 and 2014, respectively.

Effective with the quarter ended June 30, 2015, the calculation of the amount needed in the Allowance for Loan Losses changed. Management determined that the segmentation method for the ASC 450-20 portion of the loan portfolio should be changed to bank call report categories. Prior to this change, the ASC 450-20 segmentation categorized loans by various non-owner occupied commercial real estate loan types and risk grades for the remainder of the ASC 450-20 portion of the portfolio. On the date of change, June 30, 2015, the change in methodology resulted in an increase to the calculated allowance for loan loss reserve of \$1,621,424.

The allowances established for probable losses on specific loans are the result of management's quarterly review of substandard loans with an outstanding balance of \$250,000 or more. This review process usually involves regional credit officers along with local lending officers reviewing the loans for impairment. Specific valuation allowances are determined after considering the borrower's financial condition, collateral deficiencies, and economic conditions affecting the borrower's industry, among other things. In the case of collateral dependent loans, collateral shortfall is most often based upon local market real estate value estimates. This review process is performed at the subsidiary bank level and is reviewed at the parent Company level.

Once the loan becomes impaired, it is removed from the pool of loans covered by the general reserve and reviewed individually for exposure as described above. In cases where the individual review reveals no exposure, no reserve is recorded for that loan, either through an individual reserve or through a general reserve. If, however, the individual review of the loan does indicate some exposure, management often charges off this exposure, rather than recording a specific reserve. In these instances, a loan which becomes nonperforming could actually reduce the allowance for loan losses. Those loans deemed uncollectible are transferred to our problem loan department for workout, foreclosure and/or liquidation. The problem loan department obtains a current appraisal on the property in order to record the fair market value (less selling expenses) when the property is foreclosed on and moved into other real estate.

The allowances established for the remainder of the loan portfolio are based on historical loss factors, adjusted for certain qualitative factors, which are applied to groups of loans with similar risk characteristics. Loans are segregated into fifteen separate groups based on call codes. Most of the Company's charge-offs during the past two years have been real estate dependent loans. The historical loss ratios applied to these groups of loans are updated quarterly based on actual charge-off experience. The historical loss ratios are further adjusted by qualitative factors.

Management evaluates the adequacy of the allowance for each of these components on a quarterly basis. Peer comparisons, industry comparisons, and regulatory guidelines are also used in the determination of the general valuation allowance. Loans identified as losses by management, internal loan review, and/or bank examiners are charged off. Additional information about the Company's allowance for loan losses is provided in the Notes to the Consolidated Financial Statements for Allowance for Loan Losses.

The following table sets forth the breakdown of the allowance for loan losses by loan category for the periods indicated. The allocation of the allowance to each category is subjective and is not necessarily indicative of future losses and does not restrict the use of the allowance to absorb losses in any other category.

	<u>2016</u>		<u>2015</u>		<u>2014</u>		<u>2013</u>		<u>2012</u>	
	<u>Reserve</u>	<u>%*</u>	<u>Reserve</u>	<u>%*</u>	<u>Reserve</u>	<u>%*</u>	<u>Reserve</u>	<u>%*</u>	<u>Reserve</u>	<u>%*</u>
Commercial and Agricultural										
Commercial	\$ 456	6%	\$ 855	6%	\$ 497	7%	1,017	6%	981	7%
Agricultural	168	2%	203	3%	304	2%	294	2%	296	1%
Real Estate										
Commercial Construction	323	4%	691	5%	1,223	7%	1,782	7%	1,890	7%
Residential Construction	13	2%	20	1%	138	1%	138	1%	138	1%
Commercial	5,751	46%	3,851	46%	3,665	45%	4,380	46%	5,163	45%
Residential	1,396	26%	1,990	26%	2,425	27%	3,278	27%	3,406	27%
Farmland	722	9%	912	8%	104	7%	312	6%	291	7%
Consumer and Other										
Consumer	80	3%	63	3%	67	3%	243	3%	228	4%
Other	14	2%	19	2%	379	1%	362	2%	344	1%
	<u>\$ 8,923</u>	<u>100%</u>	<u>\$ 8,604</u>	<u>100%</u>	<u>\$ 8,802</u>	<u>100%</u>	<u>\$ 11,806</u>	<u>100%</u>	<u>\$ 12,737</u>	<u>100%</u>

* Percentage represents the loan balance in each category expressed as a percentage of total end of period loans.

The following table presents an analysis of the Company's loan loss experience for the periods indicated.

	<u>2016</u>	<u>2015</u>	<u>2014</u>	<u>2013</u>	<u>2012</u>
Allowance for Loan Losses at Beginning of Year	\$ 8,604	\$ 8,802	\$ 11,806	\$12,737	\$15,650
Charge-Offs					
Commercial	305	455	625	121	653
Agricultural	19	5	-	34	3
Commercial Construction	25	98	1,543	2,071	4,106
Residential Construction	-	-	-	-	-
Commercial	992	275	1,327	2,873	4,326
Residential	362	930	1,034	706	961
Farmland	120	40	233	21	225
Consumer	265	255	342	398	169
Other	-	25	-	4	11
	<u>2,088</u>	<u>2,083</u>	<u>5,104</u>	<u>6,228</u>	<u>10,454</u>
Recoveries					
Commercial	67	52	76	56	140
Agricultural	4	3	3	6	-
Commercial Construction	814	486	485	253	209
Residential Construction	-	-	-	-	-
Commercial	206	270	90	298	233
Residential	50	110	31	65	47
Farmland	145	20	20	22	5
Consumer	53	62	72	94	82
Other	6	16	15	18	40
	<u>1,345</u>	<u>1,019</u>	<u>792</u>	<u>812</u>	<u>756</u>
Net Charge-Offs	<u>743</u>	<u>1,064</u>	<u>4,312</u>	<u>5,416</u>	<u>9,698</u>
Provision for Loans Losses	<u>1,062</u>	<u>866</u>	<u>1,308</u>	<u>4,485</u>	<u>6,785</u>
Allowance for Loan Losses at End of Year	<u>\$ 8,923</u>	<u>\$ 8,604</u>	<u>\$ 8,802</u>	<u>\$11,806</u>	<u>\$12,737</u>
Ratio of Net Charge-Offs to Average Loans	<u>0.10%</u>	<u>0.14%</u>	<u>0.58%</u>	<u>0.73%</u>	<u>1.34%</u>

The allowance for loan losses increased from \$8.60 million, or 1.13 percent of total loans at December 31, 2015 to \$8.92 million, or 1.18 percent at December 31, 2016. The provision for loan losses reflects loan quality trends, including the level of net charge-offs or recoveries, among other factors. Significant changes in the allowance during 2016 was the reduction in the net charge-offs in 2016 to \$743 thousand from \$1.06 million in 2015, or a reduction of \$321 thousand. Significant changes in the allowance during 2015 was the reduction in the net charge-offs in 2015 to \$1.06 million from \$4.31 million in 2014. The Company believes that collection efforts have reduced impaired loans and the reduction in net charge-offs runs parallel with the improvement in the substandard assets. As we begin to see stabilization in the economy and the housing and real estate market, we expect continued improvement in our substandard assets, including net charge-offs. There were no charge-offs or recoveries related to foreign loans during any of the periods presented.

Investment Portfolio

The following table presents carrying values of investment securities held by the Company as of December 31, 2016, 2015 and 2014.

	<u>2016</u>	<u>2015</u>	<u>2014</u>
State, County and Municipal	\$ 4,561	\$ 5,099	\$ 3,560
Mortgage-Backed Securities	<u>319,097</u>	<u>291,050</u>	<u>271,064</u>
Total Investment Securities and Mortgage-Backed Securities	<u><u>\$323,658</u></u>	<u><u>\$296,149</u></u>	<u><u>\$274,624</u></u>

The following table represents expected maturities and weighted-average yields of investment securities held by the Company as of December 31, 2016. (Mortgage-backed securities are based on the average life at the projected speed, while State and Political Subdivisions reflect anticipated calls being exercised.)

	<u>Within 1 Year</u>		<u>After 1 Year But Within 5 Years</u>		<u>After 5 Years But Within 10 Years</u>		<u>After 10 Years</u>	
	<u>Amount</u>	<u>Yield</u>	<u>Amount</u>	<u>Yield</u>	<u>Amount</u>	<u>Yield</u>	<u>Amount</u>	<u>Yield</u>
Mortgage-Backed Securities	\$ 32,166	1.54%	\$ 191,290	1.57%	\$ 73,706	2.40%	\$ 21,935	2.33%
Obligations of State and Political Subdivisions	<u>363</u>	<u>3.72</u>	<u>2,570</u>	<u>2.15</u>	<u>1,391</u>	<u>2.94</u>	<u>237</u>	<u>4.03</u>
Total Investment Portfolio	<u><u>\$ 32,529</u></u>	<u><u>1.56%</u></u>	<u><u>\$ 193,860</u></u>	<u><u>1.58%</u></u>	<u><u>\$ 75,097</u></u>	<u><u>2.41%</u></u>	<u><u>\$ 22,172</u></u>	<u><u>2.35%</u></u>

Securities are classified as held to maturity and carried at amortized cost when management has the positive intent and ability to hold them to maturity. Securities are classified as available for sale when they might be sold before maturity. Securities available for sale are carried at fair value, with unrealized holding gains and losses reported in other comprehensive income. The Company has 100 percent of its portfolio classified as available for sale.

At December 31, 2016, there were no holdings of any one issuer, other than the U.S. government and its agencies, in an amount greater than 10 percent of the Company's stockholders' equity.

The average yield of the securities portfolio was 1.79 percent in 2016 compared to 1.57 percent in 2015 and 1.71 percent in 2014. The increase in the average yield from 2015 to 2016 was primarily attributed to the adjustment in amortization resulting from the deceleration of prepayment speeds. The decrease in the average yield from 2014 to 2015 was primarily attributed to the adjustment in amortization resulting from the acceleration of prepayment speeds.

Deposits

The following table presents the average amount outstanding and the average rate paid on deposits by the Company for the years 2016, 2015 and 2014.

	2016		2015		2014	
	Average Amount	Average Rate	Average Amount	Average Rate	Average Amount	Average Rate
Noninterest-Bearing Demand Deposits	\$ 140,338		\$ 128,541		\$ 118,452	
Interest-Bearing Demand and Savings Time Deposits	469,740	0.36%	430,731	0.35%	394,615	0.35%
	383,628	0.80%	417,080	0.81%	445,993	0.83%
Total Deposits	<u>\$ 993,706</u>	<u>0.48%</u>	<u>\$ 976,352</u>	<u>0.50%</u>	<u>\$ 959,060</u>	<u>0.53%</u>

The following table presents the maturities of the Company's time deposits as of December 31, 2016.

Months to Maturity	Time Deposits \$100,000 or Greater	Time Deposits Less Than \$100,000	Total
3 or Less	\$ 31,113	\$ 43,150	\$ 74,263
Over 3 through 6	30,844	33,443	64,287
Over 6 through 12	61,656	56,680	118,336
Over 12 Months	59,998	50,344	110,342
	<u>\$ 183,611</u>	<u>\$ 183,617</u>	<u>\$ 367,228</u>

Average deposits increased \$17.35 million in 2016 compared to 2015 and increased \$17.29 million in 2015 compared to 2014. The increase in 2016 included \$39.01 million, or 9.06 percent in interest-bearing demand and savings deposits while, at the same time noninterest bearing deposits increased \$11.80 million, or 9.18 percent and time deposits decreased \$33.45 million, or 8.02 percent. The increase in 2015 included \$36.12 million, or 9.15 percent in interest-bearing demand and savings deposits while, at the same time noninterest bearing deposits increased \$10.09 million, or 8.52 percent and time deposits decreased \$28.91 million, or 6.48 percent. Accordingly, the ratio of average noninterest-bearing deposits to total average deposits was 14.12 percent in 2016, 13.17 percent in 2015 and 12.35 percent in 2014. The general decrease in market rates in 2016 had the effect of (i) decreasing the average cost of interest-bearing deposits by 2 basis points in 2016 compared to 2015 and (ii) mitigating a portion of the impact of decreasing yields on interest-earning assets in the Company's net interest income in 2016. The general decrease in market rates in 2015 had the effect of (i) decreasing the average cost of interest-bearing deposits by 3 basis points in 2015 compared to 2014 and (ii) mitigating a portion of the impact of decreasing yields on interest-earning assets in the Company's net interest income in 2015.

Total average interest-bearing deposits increased \$5.56 million, or 0.66 percent in 2016 compared to 2015 and increased \$7.20 million, or 0.86 percent in 2015 compared to 2014. This increase was primarily attributable to the increase in interest-bearing demand and savings accounts in 2016 and in 2015 as well.

The Company supplements deposit sources with brokered deposits. As of December 31, 2016, the Company had \$49.30 million, or 4.72 percent of total deposits, in brokered certificates of deposit attracted by external third parties. Additional information is provided in the Notes to Consolidated Financial Statements for Deposits.

Off-Balance-Sheet Arrangements, Commitments, Guarantees, and Contractual Obligations

The following table summarizes the Company's contractual obligations and other commitments to make future payments as of December 31, 2016. Payments for borrowings do not include interest. Payments related to leases are based on actual payments specified in the underlying contracts. Loan commitments and standby letters of credit are presented at contractual amounts; however, since many of these commitments are expected to expire unused or only partially used, the total amounts of these commitments do not necessarily reflect future cash requirements. The off-balance-sheet arrangements for loan commitments consist of approximately \$10 million in 1-4 residential home equity and construction loans, \$4 million in commercial real estate construction loans, \$19 million in commercial/industrial loans and \$38 million in the overdraft privilege program.

	<u>Payments Due by Period</u>				Total
	1 Year or Less	More than 1 Year but Less Than 3 Years	3 Years or More but Less Than 5 Years	5 Years or More	
Contractual Obligations:					
Subordinated Debentures	\$ -	\$ -	\$ -	\$ 24,229	\$ 24,229
Federal Home Loan Bank Advances	-	7,500	2,500	36,000	46,000
Operating Leases	40	-	-	-	40
Deposits with Stated Maturity Dates	256,886	85,794	15,859	8,689	367,228
	<u>\$256,926</u>	<u>93,294</u>	<u>18,359</u>	<u>68,918</u>	<u>\$437,497</u>
Other Commitments:					
Loan Commitments	71,359	-	-	-	71,359
Standby Letters of Credit	1,551	-	-	-	1,551
	<u>72,910</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>72,910</u>
Total Contractual Obligations and Other Commitments	<u>\$329,836</u>	<u>\$ 93,294</u>	<u>\$ 18,359</u>	<u>\$ 68,918</u>	<u>\$510,407</u>

In the ordinary course of business, the Company has entered into off-balance sheet financial instruments which are not reflected in the consolidated financial statements. These instruments include commitments to extend credit, standby letters of credit, performance letters of credit, guarantees and liability for assets held in trust.

Such financial instruments are recorded in the financial statements when funds are disbursed or the instruments become payable. The Company uses the same credit policies for these off-balance sheet financial instruments as they do for instruments that are recorded in the consolidated financial statements.

Loan Commitments. The Company enters into contractual commitments to extend credit, normally with fixed expiration dates or termination clauses, at specified rates and for specific purposes. Substantially all of the Company's commitments to extend credit are contingent upon customers maintaining specific credit standards at the time of loan funding. The Company minimizes its exposure to loss under these commitments by subjecting them to credit approval and monitoring procedures. Management assesses the credit risk associated with certain commitments to extend credit in determining the level of the allowance for loan losses. Loan commitments outstanding at December 31, 2016 are included in the preceding table.

Standby Letters of Credit. Letters of credit are written conditional commitments issued by the Company to guarantee the performance of a customer to a third party. In the event the customer does not perform in accordance with the terms of the agreement with the third party, the Company would be required to fund the commitment. The maximum potential amount of future payments the Company could be required to make is represented by the contractual amount of the commitment. If the commitment is funded, the Company would be entitled to seek recovery from the customer. The Company's policies generally require that standby letters of credit arrangements contain security and debt covenants similar to those contained in loan agreements. Standby letters of credit outstanding at December 31, 2016 are included in the preceding table.

Capital and Liquidity

At December 31, 2016, shareholders' equity totaled \$93.39 million compared to \$95.46 million at December 31, 2015. In addition to net income of \$8.67 million, other significant changes in shareholders' equity during 2016 included \$1.49 million of dividends declared on preferred stock and \$8.66 million redemption of preferred stock. The accumulated other comprehensive loss component of stockholders' equity totaled \$(5.02) million at December 31, 2016 compared to \$(4.43) million at December 31, 2015. This fluctuation was mostly related to the after-tax effect of changes in the fair value of securities available for sale. Under regulatory requirements, the unrealized gain or loss on securities available for sale does not increase or reduce regulatory capital and is not included in the calculation of risk-based capital and leverage ratios. Regulatory agencies for banks and bank holding companies utilize capital guidelines designed to measure Tier 1 and total capital and take into consideration the risk inherent in both on-balance sheet and off-balance sheet items. Tier 1 capital consists of common stock and qualifying preferred stockholders' equity less goodwill and disallowed deferred tax assets. Tier 2 capital consists of certain convertible, subordinated and other qualifying debt and the allowance for loan losses up to 1.25 percent of risk-weighted assets. The Company has no Tier 2 capital other than the allowance for loan losses.

Using the capital requirements presently in effect, the Tier 1 ratio as of December 31, 2016 was 15.50 percent and total Tier 1 and 2 risk-based capital was 16.64 percent. Both of these measures compare favorably with the regulatory minimum of 6 percent for Tier 1 and 8 percent for total risk-based capital. The Company's common equity Tier 1 ratio as of December 31, 2016 was 11.32, which exceeds the regulatory minimum of 4.50 percent. The Company's Tier 1 leverage ratio as of December 31, 2016 was 10.29 percent, which exceeds the required ratio standard of 4 percent.

For 2016, average capital was \$100.11 million, representing 8.60 percent of average assets for the year. This compares to 8.87 percent for 2015.

For 2016, the Company did not have any material commitments for capital expenditures.

The Company did not pay any common stock dividends in 2016 or 2015. The Company suspended common stock dividend payments beginning in the third quarter of 2009 for capital retention purposes.

The Company declared dividends of \$1,493 and \$2,375 on preferred stock during 2016 and 2015, respectively. On November 17, 2014 the Company reinstated dividend payments after being on deferral since February 12, 2012, on the Preferred Stock and paid \$5.5 million of accumulated dividends in arrears to the holders of the Preferred Stock. Additional information is provided in the Notes to the Consolidated Financial Statements for Preferred Stock.

The Company, primarily through the actions of its subsidiary bank, engages in liquidity management to ensure adequate cash flow for deposit withdrawals, credit commitments and repayments of borrowed funds. Needs are met through loan repayments, net interest and fee income and the sale or maturity of existing assets. In addition, liquidity is continuously provided through the acquisition of new deposits, the renewal of maturing deposits and external borrowings.

Management monitors deposit flow and evaluates alternate pricing structures to retain and grow deposits. To the extent needed to fund loan demand, traditional local deposit funding sources are supplemented by the use of FHLB borrowings, brokered deposits and other wholesale deposit sources outside the immediate market area. Internal policies have been updated to monitor the use of various core and non-core funding sources, and to balance ready access with risk and cost. Through various asset/liability management strategies, a balance is maintained among goals of liquidity, safety and earnings potential. Internal policies that are consistent with regulatory liquidity guidelines are monitored and enforced by the Bank.

The investment portfolio provides a ready means to raise cash if liquidity needs arise. As of December 31, 2016, the available for sale bond portfolio totaled \$323.7 million. At December 31, 2015, the available for sale bond portfolio totaled \$296.2 million. Only marketable investment grade bonds are purchased. Although most of the Banks' bond portfolios are encumbered as pledges to secure various public funds deposits, repurchase agreements, and for other purposes, management can restructure and free up investment securities for sale if required to meet liquidity needs.

Management continually monitors the relationship of loans to deposits as it primarily determines the Company's liquidity posture. Colony had ratios of loans to deposits of 72.2 percent as of December 31, 2016 and 75.0 percent as of December 31, 2015. Management employs alternative funding sources when deposit balances will not meet loan demands. The ratios of loans to all funding sources (excluding Subordinated Debentures) at December 31, 2016 and December 31, 2015 were 69.2 percent and 72.1 percent, respectively. Management continues to emphasize programs to generate local core deposits as our Company's primary funding sources. The stability of the Banks' core deposit base is an important factor in Colony's liquidity position. A heavy percentage of the deposit base is comprised of accounts of individuals and small businesses with comprehensive banking relationships and limited volatility. At December 31, 2016 and December 31, 2015, the Bank had \$184 million and \$203 million, respectively, in certificates of deposit of \$100,000 or more. These larger deposits represented 17.6 percent and 20.1 percent of respective total deposits. Management seeks to monitor and control the use of these larger certificates, which tend to be more volatile in nature, to ensure an adequate supply of funds as needed. Relative interest costs to attract local core relationships are

compared to market rates of interest on various external deposit sources to help minimize the Company's overall cost of funds.

The Company supplemented deposit sources with brokered deposits. As of December 31, 2016, the Company had \$49.3 million or 4.7 percent of total deposits in CDARS. Additional information is provided in the Notes to the Consolidated Financial Statements regarding these brokered deposits. Additionally, the Company uses external deposit listing services to obtain out-of-market certificates of deposit at competitive interest rates when funding is needed. The deposits obtained from listing services are often referred to as wholesale or Internet CDs. As of December 31, 2016, the Company had \$15.6 million, or 1.5 percent of total deposits, in internet certificates of deposit obtained through deposit listing services.

To plan for contingent sources of funding not satisfied by both local and out-of-market deposit balances, Colony and its subsidiary have established multiple borrowing sources to augment their funds management. The Company has borrowing capacity through membership of the Federal Home Loan Bank program. The Bank has also established overnight borrowing for Federal Funds Purchased through various correspondent banks. Management believes the various funding sources discussed above are adequate to meet the Company's liquidity needs in the future without any material adverse impact on operating results.

Liquidity measures the ability to meet current and future cash flow needs as they become due. The liquidity of a financial institution reflects its ability to meet loan requests, to accommodate possible outflows in deposits and to take advantage of interest rate market opportunities. The ability of a financial institution to meet its current financial obligations is a function of balance sheet structure, the ability to liquidate assets, and the availability of alternative sources of funds. The Company seeks to ensure its funding needs are met by maintaining a level of liquid funds through asset/liability management.

Asset liquidity is provided by liquid assets which are readily marketable or pledgeable or which will mature in the near future. Liquid assets include cash, interest-bearing deposits in banks, securities available for sale and federal funds sold and securities purchased under resale agreements.

Liability liquidity is provided by access to funding sources which include core deposits. Should the need arise, the Company also maintains relationships with the Federal Home Loan Bank, Federal Reserve Bank, two correspondent banks and repurchase agreement lines that can provide funds on short notice.

Since Colony is a bank holding Company and does not conduct operations, its primary sources of liquidity are dividends up streamed from the subsidiary bank and borrowings from outside sources.

The liquidity position of the Company is continuously monitored and adjustments are made to the balance between sources and uses of funds as deemed appropriate. Management is not aware of any events that are reasonably likely to have a material adverse effect on the Company's liquidity, capital resources or operations. In addition, management is not aware of any regulatory recommendations regarding liquidity, which if implemented, would have a material adverse effect on the Company.

Impact of Inflation and Changing Prices

The Company's financial statements included herein have been prepared in accordance with accounting principles generally accepted in the United States (GAAP). GAAP presently requires the Company to measure financial position and operating results primarily in terms of historic dollars. Changes in the relative value of money due to inflation or recession are generally not considered. The primary effect of inflation on the operations of the Company is reflected in increased operating costs, though given recent economic conditions, the Company has not experienced any material effects of inflation during the last three fiscal years. In management's opinion, changes in interest rates affect the financial condition of a financial institution to a far greater degree than changes in the inflation rate. While interest rates are greatly influenced by changes in the inflation rate, they do not necessarily change at the same rate or in the same magnitude as the inflation rate. Interest rates are highly sensitive to many factors that are beyond the control of the Company, including changes in the expected rate of inflation, the influence of general and local economic conditions and the monetary and fiscal policies of the United States government, its agencies and various other governmental regulatory authorities, among other things, as further discussed in the next section.

Regulatory and Economic Policies

The Company's business and earnings are affected by general and local economic conditions and by the monetary and fiscal policies of the United States government, its agencies and various other governmental regulatory authorities, among other things. The Federal Reserve Board regulates the supply of money in order to influence general economic conditions. Among the instruments of monetary policy available to the Federal Reserve Board are (i) conducting open market operations in United States government obligations, (ii) changing the discount rate on financial institution borrowings, (iii) imposing or changing reserve requirements against financial institution deposits, and (iv) restricting certain borrowings and imposing or changing reserve requirements against certain borrowings by financial institutions and their affiliates. These methods are used in varying degrees and combinations to affect directly the availability of bank loans and deposits, as well as the interest rates charged on loans and paid on deposits. For that reason alone, the policies of the Federal Reserve Board have a material effect on the earnings of the Company.

Governmental policies have had a significant effect on the operating results of commercial banks in the past and are expected to continue to do so in the future; however, the Company cannot accurately predict the nature, timing or extent of any effect such policies may have on its future business and earnings.

Recently Issued Accounting Pronouncements

See Note 1 - Summary of Significant Accounting Policies under the section headed Changes in Accounting Principles and Effects of New Accounting Pronouncements included in the Notes to Consolidated Financial Statements.

Market Risk and Interest Rate Sensitivity

Our financial performance is impacted by, among other factors, interest rate risk and credit risk. We do not utilize derivatives to mitigate our credit risk, relying instead on an extensive loan review process and our allowance for loan losses.

Interest rate risk is the change in value due to changes in interest rates. The Company is exposed only to U.S. dollar interest rate changes and, accordingly, the Company manages exposure by considering the possible changes in the net interest margin. The Company does not have any trading instruments nor does it classify any portion of its investment portfolio as held for trading. The Company does not engage in any hedging activity or utilize any derivatives. The Company has no exposure to foreign currency exchange rate risk, commodity price risk and other market risks. Interest rate risk is addressed by our Asset & Liability Management Committee (ALCO) which includes senior management representatives. The ALCO monitors interest rate risk by analyzing the potential impact to the net portfolio of equity value and net interest income from potential changes to interest rates and considers the impact of alternative strategies or changes in balance sheet structure.

Interest rates play a major part in the net interest income of financial institutions. The repricing of interest earnings assets and interest-bearing liabilities can influence the changes in net interest income. The timing of repriced assets and liabilities is Gap management and our Company has established its policy to maintain a Gap ratio in the one-year time horizon of .80 to 1.20.

Our exposure to interest rate risk is reviewed at least quarterly by our Board of Directors and the ALCO. Interest rate risk exposure is measured using interest rate sensitivity analysis to determine our change in net portfolio value in the event of assumed changes in interest rates. In order to reduce the exposure to interest rate fluctuations, we have implemented strategies to more closely match our balance sheet composition. The Company has engaged FTN Financial to run a quarterly asset/liability model for interest rate risk analysis. We are generally focusing our investment activities on securities with terms or average lives in the 3 ½ - 5 ½ year range.

Market risk reflects the risk of economic loss resulting from adverse changes in market prices and interest rates. This risk of loss can be reflected in either reduced current market values or reduced current and potential net income. Colony's most significant market risk is interest rate risk. This risk arises primarily from Colony's extension of loans and acceptance of deposits.

Managing interest rate risk is a primary goal of the asset liability management function. Colony attempts to achieve stability in net interest income while limiting volatility arising from changes in interest rates. Colony seeks to achieve this goal by balancing the maturity and repricing characteristics of assets and liabilities. Colony manages its exposure to fluctuations in interest rates through policies established by ALCO and approved by the Board of Directors. ALCO meets at least quarterly and has responsibility for developing asset liability management policies, reviewing the interest rate sensitivity of Colony, and developing and implementing strategies to improve balance sheet structure and interest rate risk positioning.

Colony measures the sensitivity of net interest income to changes in market interest rates through the utilization of Asset/Liability simulation modeling. On at least a quarterly basis, the following twenty-four month time period is simulated to determine a baseline net interest income forecast and the sensitivity of this forecast to changes in interest rates. These simulations include all of Colony's earning assets and liabilities. Forecasted balance sheet changes, primarily reflecting loan and deposit growth and forecasts, are included in the periods modeled. Projected rates for loans and deposits are based on management's outlook and local market conditions.

The magnitude and velocity of rate changes among the various asset and liability groups exhibit different characteristics for each possible interest rate scenario; additionally, customer loan and deposit preferences can vary in response to changing interest rates. Simulation modeling enables Colony to capture the expected effect of these differences. Assumptions utilized in the model are updated on an ongoing basis and are reviewed and approved by the ALCO Committee of the Board of Directors.

Colony has modeled its baseline net interest income forecast assuming a flat interest rate environment with the federal funds rate at the Federal Reserve's current targeted range of 0.50% to 0.25% and the current prime rate of 3.75%. Colony has modeled the impact of a gradual increase in short-term rates of 100 and 200 basis points and a decline of 100 basis points to determine the sensitivity of net interest income for the next twelve months. As illustrated in the table below, the net interest income sensitivity model indicates that, compared with a net interest income forecast assuming stable rates, net interest income is projected to increase by 1.88% and increase by 3.35% if interest rates increased by 100 and 200 basis points, respectively. Net interest income is projected to decline by 3.67% if interest rates decreased by 100 basis points. These changes were within Colony's policy limit of a maximum 15% negative change.

Twelve Month Net Interest Income Sensitivity

Change in Short-term Interest Rates (in basis points)	Estimated Change in Net Interest Income As of December 31,	
	2016	2015
+200	3.35%	-0.32%
+100	1.88%	0.13%
Flat	- %	- %
-100	-3.67%	-1.16%

The measured interest rate sensitivity indicates an asset sensitive position over the next year, which could serve to improve net interest income in a rising interest rate environment. The actual realized change in net interest income would depend on several factors, some of which could serve to reduce or eliminate the asset sensitivity noted above. These factors include a higher than projected level of deposit customer migration to higher cost deposits, such as certificates of deposit, which would increase total interest expense and serve to reduce the realized level of asset sensitivity. Another factor which could impact the realized interest rate sensitivity in a rising rate environment is the repricing behavior of interest bearing non-maturity deposits. Assumptions for repricing are expressed as a beta relative to the change in the prime rate. For instance, a 25% beta would correspond to a deposit rate that would increase 0.25% for every 1% increase in the prime rate. Projected betas for interest bearing non-maturity deposit repricing are a key component of determining the Company's interest rate risk position. Should realized betas be higher than projected betas, the expected benefit from higher interest rates would be reduced.

The net interest income simulation model is the primary tool utilized to evaluate potential interest rate risks over a shorter term time horizon. Colony also evaluates potential longer term interest rate risk through modeling and evaluation of economic value of equity (EVE). This EVE modeling allows Colony to capture longer-term repricing risk and options risk embedded in the balance sheet. Simulation modeling is utilized to measure the economic value of equity and its sensitivity to immediate changes in interest rates. These simulations value only the current balance sheet and do not incorporate growth assumptions used in the net interest income simulation. The economic value of equity is the net fair value of assets and liabilities derived from the present value of future cash flows discounted at current market interest rates. From this baseline valuation, Colony evaluates changes in the value of each of these items in various interest rate scenarios to determine the net impact on the economic value of equity. Key assumptions utilized in the model, namely loan prepayments, deposit pricing betas, and non-maturity deposit durations have a significant impact on the results of the EVE simulations.

As illustrated in the table below, the economic value of equity model indicates that, compared with a valuation assuming stable rates, EVE is projected to increase by 9.59% and 16.27%, assuming an immediate and sustained increase in interest rates of 100 and 200 basis points, respectively. The primary reason for the increase in asset sensitivity from the prior year is a more aggressive assumption regarding non-maturity deposit durations. Assuming an immediate 100 basis point decline in rates, EVE is projected to decrease by 12.44%. These changes were within Colony’s policy except in the -100 basis point change, which limits the maximum negative change in EVE to 10% of the base EVE. We believe this projection outside of policy is mitigated by the unlikely reduction in interest rates due to the current rate environment.

Economic Value of Equity Sensitivity

Immediate Change in Interest Rates (in basis points)	Estimated Change in EVE As of December 31,	
	2016	2015
+200	16.27%	13.43%
+100	9.59%	8.62%
-100	-12.44%	-7.74%

Colony is also subject to market risk in certain of its fee income business lines. Financial management services revenues, which include trust, brokerage, and asset management fees, can be affected by risk in the securities markets, primarily the equity securities market. A significant portion of the fees in this unit are determined based upon a percentage of asset values. Weaker securities markets and lower equity values have an adverse impact on the fees generated by these operations. Trading account assets, maintained to facilitate brokerage customer activity, are also subject to market risk. This risk is not considered significant, as trading activities are limited and subject to risk policy limits. Mortgage banking income is also subject to market risk. Mortgage loan originations are sensitive to levels of mortgage interest rates and therefore, mortgage banking income could be negatively impacted during a period of rising interest rates. The extension of commitments to customers to fund mortgage loans also subjects Colony to market risk. This risk is primarily created by the time period between making the commitment and closing and delivering the loan. Colony seeks to minimize this exposure by utilizing various risk management tools, the primary of which are forward sales commitments and best efforts commitments.

The following table is an analysis of the Company's interest rate-sensitivity position at December 31, 2016. The interest-bearing rate-sensitivity gap, which is the difference between interest-earning assets and interest-bearing liabilities by repricing period, is based upon maturity or first repricing opportunity, along with a cumulative interest rate-sensitivity gap. It is important to note that the table indicates a position at a specific point in time and may not be reflective of positions at other times during the year or in subsequent periods. Major changes in the gap position can be, and are, made promptly as market outlooks change.

	Assets and Liabilities Repricing Within					Total
	3 Months or Less	4 to 12 Months	1 Year	1 to 5 Years	Over 5 Years	
INTEREST-EARNING ASSETS:						
Interest-Bearing Deposits	\$ 46,345	\$ -	\$ 46,345	\$ -	\$ -	\$ 46,345
Investment Securities	3,298	4,494	7,792	198,173	117,693	323,658
Loans, Net of Unearned Income	133,589	131,037	264,626	437,399	51,897	753,922
Other Interest- Earning Assets	3,010	-	3,010	-	-	3,010
Total Interest-Earning Assets	<u>186,242</u>	<u>135,531</u>	<u>\$321,773</u>	<u>635,572</u>	<u>169,590</u>	<u>\$1,126,935</u>
INTEREST-BEARING LIABILITIES:						
Interest-Bearing Demand Deposits (1)	448,004	-	448,004	-	-	448,004
Savings (1)	70,066	-	70,066	-	-	70,066
Time Deposits	74,263	182,623	256,886	101,653	8,689	367,228
Other Borrowings	-	-	-	10,000	36,000	46,000
Subordinated Debentures	24,229	-	24,229	-	-	24,229
Total Interest-Bearing Liabilities	<u>616,562</u>	<u>182,623</u>	<u>799,185</u>	<u>111,653</u>	<u>44,689</u>	<u>955,527</u>
Interest Rate-Sensitivity Gap	<u>(430,320)</u>	<u>(47,092)</u>	<u>(477,412)</u>	<u>523,919</u>	<u>124,901</u>	<u>\$ 171,408</u>
Cumulative Interest-Sensitivity Gap	<u>\$(430,320)</u>	<u>\$(477,412)</u>	<u>\$(477,412)</u>	<u>\$ 46,507</u>	<u>\$171,408</u>	
Interest Rate-Sensitivity Gap as a Percentage of Interest-Earning Assets	<u>(38.18)%</u>	<u>(4.18)%</u>	<u>(42.36)%</u>	<u>46.49%</u>	<u>11.08%</u>	
Cumulative Interest Rate-Sensitivity as a Percentage of Interest-Earning Assets	<u>(38.18)%</u>	<u>(42.36)%</u>	<u>(42.36)%</u>	<u>4.13%</u>	<u>15.21%</u>	

(1) Interest-bearing Demand and Savings Accounts for repricing purposes are considered to reprice within 3 months or less.

The foregoing table indicates that we had a one year negative gap of \$477.4 million, or 42.36 percent of total interest-earning assets at December 31, 2016. In theory, this would indicate that at December 31, 2016, \$477.4 million more in liabilities than assets would reprice if there were a change in interest rates over the next 365 days. Thus, if interest rates were to decline, the gap would indicate a resulting increase in net interest margin. However, changes in the mix of interest-earning assets or supporting liabilities can either increase or decrease the net interest margin without affecting interest rate sensitivity. In addition, the interest rate spread between an asset and our supporting liability can vary significantly while the timing of repricing of both the assets and our supporting liability can remain the same, thus impacting net interest income. This characteristic is referred to as a basis risk and,

generally, relates to the repricing characteristics of short-term funding sources such as certificates of deposits.

Gap analysis has certain limitations. Measuring the volume of repricing or maturing assets and liabilities does not always measure the full impact on the portfolio value of equity or net interest income. Gap analysis does not account for rate caps on products; dynamic changes such as increasing prepay speeds as interest rates decrease, basis risk, or the benefit of non-rate funding sources. The majority of our loan portfolio reprices quickly and completely following changes in market rates, while non-term deposit rates in general move slowly and usually incorporate only a fraction of the change in rates. Products categorized as nonrate sensitive, such as our noninterest-bearing demand deposits, in the gap analysis behave like long term fixed rate funding sources. Both of these factors tend to make our actual behavior more asset sensitive than is indicated in the gap analysis. In fact, we experience higher net interest income when rates rise, opposite what is indicated by the gap analysis. Therefore, management uses gap analysis, net interest margin analysis and market value of portfolio equity as our primary interest rate risk management tools. The Company has established its one year gap to be 80 percent to 120 percent. The most recent analysis as of December 31, 2016 indicates a one year gap of 122 percent. The analysis reflects slight net interest margin compression in both a declining and increasing interest rate environment. Given that interest rates have basically “bottomed-out” with the recent Federal Reserve action, the Company is anticipating interest rates to increase in the future though we believe that interest rates will remain flat most of 2016. The Company is focusing on areas to minimize margin compression in the future by minimizing longer term fixed rate loans, shortening on the yield curve with investments, securing longer term FHLB advances, securing certificates of deposit for longer terms and focusing on reduction of nonperforming assets.

The Company utilizes FTN Financial Asset/Liability Management Analysis for a more dynamic analysis of balance sheet structure. The Company has established policies for rate shock per basis point (bp) for earnings at risk for net interest income and for equity at risk. The following table shows the policy limits with the rate shock for earnings at risk and equity at risk as of December 31, 2016.

	Rate Shock	Policy Limit	Immediate Shock (-) decrease bp	Immediate Shock (+) increase bp
Net Interest Income –				
Earnings at Risk	+/- 100 bp	+/- 10%	-3.83%	2.01%
	+/- 200 bp	+/- 15%	-9.39	3.35
	+/- 300 bp	+/- 20%	-10.90	4.75
	+/- 400 bp	+/- 25%	-12.53	4.82
Equity at Risk	+/- 100 bp	+/- 10%	-12.44	9.59
	+/- 200 bp	+/- 20%	-28.91	16.27
	+/- 300 bp	+/- 30%	-36.87	20.52
	+/- 400 bp	+/- 40%	-37.08	23.18

Return on Assets and Stockholder's Equity

The following table presents selected financial ratios for each of the periods indicated.

	Years Ended December 31		
	2016	2015	2014
Return on Average Assets(1)	0.62%	0.52%	0.43%
Return on Average Equity(1)	7.17%	5.90%	5.11%
Equity to Assets	7.72%	8.13%	8.63%
Common Stock Dividends Declared	\$0.00	\$0.00	\$0.00

(1) Computed using net income available to common shareholders.



Colony Bankcorp, Inc. common stock is quoted on the NASDAQ Global Market under the symbol "CBAN."

**COLONY BANKCORP, INC.
SHAREHOLDER INFORMATION**

CORPORATE HEADQUARTERS:

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P.O. Box 989
115 South Grant Street
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229-426-6000

ANNUAL MEETING

Tuesday, May 23, 2017 at 2:00 p.m.
Colony Bankcorp, Inc.
115 South Grant Street
Fitzgerald, Georgia 31750

INDEPENDENT AUDITORS:

McNair, McLemore, Middlebrooks & Co., LLC
P.O. Box One
Macon, Georgia 31202

SHAREHOLDER SERVICES:

Shareholders who want to change the name, address or ownership of stock; to report lost, stolen or destroyed certificates; or to consolidate accounts should contact:

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