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SOUTHWEST GEORGIA FINANCIAL CORPORATION

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2016 Annual Report

## Company Profile

Offering comprehensive financial services to consumer, business and government customers, Southwest Georgia Financial Corporation (NYSE MKT: SGB) is a state-chartered bank holding company with approximately \$448 million in assets. Our primary subsidiary, Southwest Georgia Bank, has served the community of Moultrie, Georgia since 1928. Over the years, Southwest Georgia Financial Corporation has continued to grow and advance, while constantly maintaining a strong leadership role in the communities we serve.

The current banking facilities include the main office, located in Colquitt County, branch offices located in Baker County, Worth County, and Lowndes County, and a loan production office located in Tift County. In addition to conventional banking services, the bank provides investment planning and management, trust management, and commercial and individual insurance products. Insurance products and advice are provided by Southwest Georgia Insurance Services, which is located in Colquitt County.

## Our Mission Statement

To grow the value of and enhance the long-term return on each stockholder's investment by providing high quality customer service through a staff of highly-trained, motivated, dedicated and well-managed employees, and by continuing a record of outstanding financial performance.

## Our Strategy

Our strategy for growth is to diversify our business base in order to broaden our revenue sources;

- *To strengthen our sales and marketing efforts in order to deliver quality service to our customers;*
- *To maintain our strong market share through commitment to our communities; and*
- *To expand our current geographic footprint.*

## > LETTER TO OUR SHAREHOLDERS

*Dear Fellow Shareholders,*



Our 2016 performance was a result of our commitment to a strategy of balancing profitability with growth. Growth in assets is being driven by exceptional results in Valdosta and Moultrie, and also by solid results in our newest market in Tifton. The Company earned a record \$1.58 per share, 20 percent higher than the prior year, and it marked the fifth consecutive year of earnings growth. We are committed to the same balanced strategy going forward, and believe the progress we made positions us well for continued success.

### **A Year of Outstanding Performance**

There were a number of highlights during the year. Total loans increased 17 percent to \$293 million. Deposits grew 10 percent to \$371 million and net income grew 20 percent to \$4.0 million. The changing mix of our assets to a higher level of loans and continued focus on building relationships that bring demand deposits with the loans are benefitting net interest income, which grew 12 percent to \$15.8 million. Non-interest bearing deposits were up 15 percent and now make up 31 percent of total deposits.

The economic environment appears to be improving. The Federal Reserve's gradual move toward a more normalized interest rate environment should help the banking industry. Due to wide spread practice of employing floors on loans, we may experience some short-term decrease in net interest margin as borrowing costs increase at a slightly higher pace than asset yields, at least until the floors are breached. However, our continued focus on managing asset and liability mix should allow us to maintain healthy levels of net interest income.

We continue to make significant progress on operational and risk systems. We have added key personnel to enhance and improve service levels. As we become a larger institution, we must ensure that the customer experience does not suffer. We continue to look for improvement in new account opening and banking floor operations, loan underwriting and credit administration, and deposit and loan operations. The significant investments we are making in people and systems are with an eye towards leveraging to drive asset growth and revenue expansion.

In 2016, our Board of Directors approved an increase in the dividend to an annual rate of \$0.44 per share. We are very proud that we have now paid a cash dividend for 89 consecutive years.

20%

year-over-year improvement  
in net income

\$1.58

record 2016 earnings per  
diluted share

1<sup>ST</sup> or 2<sup>ND</sup>

in market share in Colquitt,  
Worth and Baker counties

17%

increase in year-end  
total loan balances

15%

increase in  
noninterest-bearing deposits

89

consecutive years SGB has  
paid a cash dividend

### Well Positioned for Growth in 2017 and Beyond

Southwest Georgia Bank is a market leader in three of the four counties where we have a branch. We are now a top ten bank, in terms of deposits, in Lowndes County. We believe we can continue to leverage our strong reputation and, with an increased focus on customers' experiences, continue to see exceptional growth in Lowndes.

Further, we will be expanding our presence in Tift County, where we now have a loan production office. Early success in the market is encouraging and we have regulatory approval for a full service branch. We expect to be open during the first quarter of 2018.

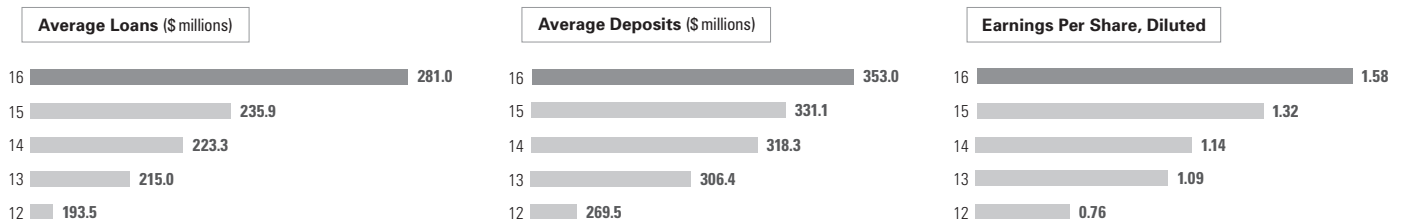
While we expect continued success in strengthening and growing in our core markets, we continue to evaluate expansion to contiguous markets. As always, any plans for expansion will be controlled, deliberate and strategic.

We have worked hard to build value for our shareholders. A consistent, prudent and strategic approach has allowed us to be successful. We look forward to many successful years ahead. On behalf of our Board and employees, thank you for your continued support.

Sincerely,



DeWitt Drew  
President and Chief Executive Officer



## Performance Highlights

<b>For The Year</b> <i>(in thousands, except per share data)</i>	2016	2015	2014	2013	2012
Interest income	\$ 17,413	\$ 15,428	\$ 14,712	\$ 14,475	\$ 13,734
Interest expense	1,612	1,317	1,355	1,663	1,898
Non-interest income	4,459	4,260	4,986	5,091	5,525
Non-interest expense	14,914	14,029	14,370	14,346	14,596
Net income	4,034	3,374	2,904	2,772	1,939
Earnings per share – diluted	\$ 1.58	\$ 1.32	\$ 1.14	\$ 1.09	\$ 0.76
Weighted average shares outstanding – diluted	2,548	2,548	2,548	2,548	2,548
Dividends paid per share	\$ 0.42	\$ 0.40	\$ 0.32	\$ 0.20	\$ 0.16
<b>At Year End</b>					
Total assets	\$ 448,501	\$ 414,855	\$ 374,280	\$ 373,895	\$ 347,181
Loans, less unearned income	292,524	250,786	224,400	218,688	204,137
Deposits	371,493	339,016	309,974	310,435	291,762
Shareholders' equity	38,422	36,097	34,335	31,420	29,875
Book value per share	15.08	14.17	13.48	12.33	11.73
Tangible book value per share	\$ 15.07	\$ 14.15	\$ 13.45	\$ 12.29	\$ 11.60
<b>Selected Average Balances</b>					
Average total assets	\$ 431,082	\$ 398,610	\$ 382,056	\$ 365,720	\$ 325,759
Average loans	281,006	235,939	223,295	215,040	193,532
Average deposits	353,005	331,140	318,267	306,370	269,480
Average shareholders' equity	\$ 38,370	\$ 35,957	\$ 33,225	\$ 30,749	\$ 29,287
<b>Asset Quality</b>					
Non-performing assets to total assets	0.08 %	0.39 %	0.28 %	0.36 %	0.53 %
Non-performing assets	\$ 373	\$ 1,629	\$ 1,060	\$ 1,363	\$ 1,849
Net loan charge-offs	\$ 68	\$ 223	\$ 293	\$ 187	\$ 700
Net loan charge-offs to average loans	0.02 %	0.09 %	0.13 %	0.09 %	0.36 %
Reserve for loan losses to loans	1.07 %	1.21 %	1.39 %	1.41 %	1.39 %
<b>Performance Ratios</b>					
Return on average total assets	0.94 %	0.85 %	0.76 %	0.76 %	0.60 %
Return on average shareholders' equity	10.51 %	9.38 %	8.74 %	9.02 %	6.62 %
Average shareholders' equity to average total assets	8.90 %	9.02 %	8.70 %	8.41 %	8.99 %
Efficiency ratio	70.64 %	73.03 %	75.43 %	77.00 %	81.15 %
Net interest margin	4.14 %	4.04 %	3.99 %	4.02 %	4.22 %
Dividend payout ratio	26.53 %	30.21 %	28.08 %	18.38 %	21.02 %

**U.S. Securities and Exchange Commission**

Washington, D. C. 20549

**Form 10-K**

Annual report pursuant to section 13 or 15(d) of the Securities Exchange Act of 1934

For the fiscal year ended December 31, 2016

Transition report pursuant to section 13 or 15(d) of the Securities Exchange Act of 1934

For the transition period from \_\_\_\_\_ to \_\_\_\_\_ .

Commission file number 001-12053

**Southwest Georgia Financial Corporation**

(Exact Name of Corporation as specified in its charter)

Georgia

(State Or Other Jurisdiction Of  
Incorporation Or Organization)

58-1392259

(I.R.S. Employer  
Identification No.)

201 First Street, S.E.  
Moultrie, Georgia

(Address of Principal Executive Offices)

31768

(Zip Code)

(Corporation's telephone number, including area code) (229) 985-1120

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

Common Stock \$1 Par Value

(Title of each class)

NYSE MKT LLC

(Name of each exchange on  
which registered)

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

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

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

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

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

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

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

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company

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

Aggregate market value of voting and non-voting stock held by nonaffiliates of the registrant as of June 30, 2016: \$28,189,421 based on 1,928,141 shares at the price of \$14.62 per share.

As of March 23, 2017, 2,547,437 shares of the \$1.00 par value common stock of Southwest Georgia Financial Corporation were outstanding.

**DOCUMENTS INCORPORATED BY REFERENCE**

Portions of the Registrant's definitive Proxy Statement for the 2017 annual meeting of shareholders, to be filed with the Commission are incorporated by reference into Part III.

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## PART I

### ITEM 1. BUSINESS

Southwest Georgia Financial Corporation (the “Corporation”) is a Georgia bank holding company organized in 1980, which, in 1981, acquired 100% of the outstanding shares of Southwest Georgia Bank (the “Bank”). The Bank commenced operations as Moultrie National Bank in 1928. Currently, it is a state-chartered bank insured by the Federal Deposit Insurance Corporation (the “FDIC”).

The Corporation’s primary business is providing banking services through the Bank to individuals and businesses principally in the following counties: Colquitt, Baker, Worth, Lowndes, and Tift as well as the surrounding counties of southwest Georgia. The Bank owns Empire Financial Services, Inc. (“Empire”), a provider of commercial mortgage banking services. The executive office of the Corporation is located at 25 Second Avenue, S. W., Moultrie, Georgia 31768, and its telephone number is (229) 985-1120.

All references herein to the Corporation include Southwest Georgia Financial Corporation, the Bank, and Empire, unless the context indicates a different meaning.

#### General

The Corporation is a registered bank holding company. The Bank is community-oriented and offers such customary banking services as consumer and commercial checking accounts, NOW accounts, savings accounts, certificates of deposit, lines of credit, VISA® business accounts, money transfers, and mortgage banking services. The Bank finances commercial and consumer transactions, makes secured and unsecured loans, and provides a variety of other banking services. The Bank has a Wealth Strategies division that performs corporate, pension, and personal trust services and acts as trustee, executor, and administrator for estates and as administrator or trustee of various types of employee benefit plans for corporations and other organizations. Also, the Wealth Strategies area has a securities sales department which offers full-service brokerage services through a third party service provider. The Bank’s Southwest Georgia Insurance Services Division offers property and casualty insurance, life, health, and disability insurance.

#### Markets

The Corporation conducts banking activities in four counties in southwest and south central Georgia. Population characteristics in these counties range from rural to more metropolitan. Our most recent and largest market is Lowndes County with a total population of 112,865 and the highest growth rate in our markets at 14.6% from 2005 to 2015. Due primarily to the location of a state university and a large air force base in Lowndes County, this market has a median age estimated at 29.4, younger than an average median age of 39.5 in the other three counties that the Bank primarily serves. These counties, Colquitt, Worth, and Baker, have an average total population of 23,241 and an average growth in population of 1.39% from 2005 to 2015. Per capita income is approximately \$19,000 in the Bank’s markets. Agriculture plays a major economic role in the Bank’s markets. Colquitt, Worth, Lowndes, and Baker Counties produce a large portion of our state’s crops, including cotton, peanuts, and a variety of vegetables.

At the beginning of 2016, the Corporation opened a loan production office in Tifton, the largest community in Tift County, Georgia. Tift County is an agricultural community as well as a major transportation hub where Interstate 75, U.S. Highway 82 and U.S. Highway 319 intersect.

#### Deposits

The Bank offers a full range of depository accounts and services to both consumers and businesses. At December 31, 2016, the Corporation’s deposit base, totaling \$371,492,987, consisted of \$116,648,264 in noninterest-bearing demand deposits (31.4% of total deposits), \$143,078,989 in interest-bearing demand deposits including money market accounts (38.6% of total deposits), \$29,006,734 in savings deposits (7.8% of total deposits), \$39,524,168 in time deposits in amounts less than \$100,000 (10.6% of total deposits), and \$43,234,832 in time deposits of \$100,000 or more (11.6% of total deposits).

#### Loans

The Bank makes both secured and unsecured loans to individuals, corporations, and other businesses. Both consumer and commercial lending operations include various types of credit for the Bank’s customers. Secured loans include first and second real estate mortgage loans. The Bank also makes direct installment loans to consumers on both a secured and unsecured basis. At December 31, 2016, consumer installment, real estate (including construction and mortgage loans), and commercial (including financial and agricultural) loans represented approximately 1.3%, 74.4% and 24.3%, respectively, of the Bank’s total loan portfolio.

#### Lending Policy

The current lending policy of the Bank is to offer consumer and commercial credit services to individuals and businesses that meet the Bank’s credit standards. The Bank provides each lending officer with written guidelines for lending activities. Lending authority is delegated by the Board of Directors of the Bank to loan officers, each of whom is limited in the amount of secured and unsecured loans which can be made to a single borrower or related group of borrowers.

The Loan Committee of the Bank’s Board of Directors is responsible for approving and monitoring the loan policy and providing guidance and counsel to all lending personnel. The committee approves all individual loan or relationship requests that exceed \$800,000. The Loan Committee is composed of the Chief Executive Officer and President, and other executive officers of the Bank, as well as certain Bank directors.

## **Mortgage Banking Services**

The Bank and Empire recognize mortgage banking income from secondary market loan origination fees and commercial mortgage banking fees, respectively. The Bank originates fixed rate mortgage loans for the secondary market. Empire recognizes as income in the current period fees collected on loans for investing participants. Empire does not directly fund any mortgages and acts as a service-oriented broker for participating mortgage lenders. In 2016, Bank revenue received from secondary market mortgage loan origination was \$295,581 compared with \$209,714 in 2015. Income from Empire's commercial mortgage banking was \$59,046 in 2016 and \$108,256 in 2015.

## **Loan Review and Nonperforming Assets**

The Bank regularly requires a review of its loan portfolio to determine deficiencies and corrective action to be taken. An independent loan review is conducted by an outside third party firm on a semiannual basis with their findings being reported annually to the Board's Loan Committee and the Audit Committee. Also, the Bank's external auditors as well as an outside third party firm conduct independent loan review adequacy tests and their findings are included annually as part of the overall report to the Audit Committee and to the Board of Directors.

Certain loans are monitored more often by the Credit Administration Department and the Loan Committee. These loans include non-accruing loans, loans more than 90 days past due, and other loans, regardless of size, that may be considered high risk based on factors defined within the Bank's loan review policy.

## **Asset/Liability Management**

The Asset/Liability Management Committee ("ALCO") is established by the Bank's Board of Directors and is charged with establishing policies to manage the assets and liabilities of the Bank. Its task is to manage asset growth, net interest margin, liquidity, and capital in order to maximize income and reduce interest rate risk. To meet these objectives while maintaining prudent management of risks, the ALCO manages the Bank's overall acquisition and allocation of funds. At its monthly meetings, the ALCO reviews and discusses the monthly asset and liability funds budget and income and expense budget in relation to the actual composition and flow of funds; the ratio of the amount of rate sensitive assets to the amount of rate sensitive liabilities; the ratio of loan loss reserve to outstanding loans; and other variables, such as expected loan demand, investment opportunities, core deposit growth within specified categories, regulatory changes, monetary policy adjustments, and the overall state of the local, state, and national economy. The Board of Directors reviews ALCO data quarterly.

## **Investment Policy**

The Bank's investment portfolio policy is to maximize income consistent with liquidity, asset quality, and regulatory constraints. The policy is reviewed periodically by the Board of Directors. Individual transactions, portfolio composition, and performance are reviewed and approved monthly by the Board of Directors.

## **Employees**

The Bank had 110 full-time employees and three part-time employees at December 31, 2016. The Bank is not a party to any collective bargaining agreement, and the Bank believes that its employee relations are good.

## **Competition**

The banking business is highly competitive. The Bank competes with other depository institutions and other financial service organizations, including brokers, finance companies, savings and loan associations, credit unions and certain governmental agencies. The Bank ranks third out of twenty-one banks in a five county region (Baker, Brooks, Colquitt, Lowndes, and Worth) in deposit market share.

## **Monetary Policies**

The results of operations of the Bank are affected by credit policies of monetary authorities, particularly the Board of Governors of the Federal Reserve System (the "Federal Reserve"). The instruments of monetary policy employed by the Federal Reserve include open market operations in U. S. government agency securities, changes in the discount rate on bank borrowings, and changes in reserve requirements against bank deposits. In view of changing conditions in the national economy and in the money markets, as well as the effect of action by monetary and fiscal authorities, including the Federal Reserve, no prediction can be made as to possible future changes in interest rates, deposit levels, loan demand, or the business and earnings of the Bank.

## **Payment of Dividends**

The Corporation is a legal entity separate and distinct from the Bank. Most of the revenue of the Corporation results from dividends paid to it by the Bank. There are statutory and regulatory requirements applicable to the payment of dividends by the Bank, as well as by the Corporation to its stockholders.

Under the regulations of the Georgia Department of Banking and Finance ("DBF"), a state bank with an accumulated deficit (negative retained earnings) may not declare dividends (reduction in capital) without first obtaining the written permission of the DBF and FDIC. If a state bank has positive retained earnings, it may declare dividends without DBF approval if it meets all the following requirements:

- (a) total classified assets as of the most recent examination of the bank do not exceed 80% of equity capital (as defined by regulation);



- (b) the aggregate amount of dividends declared or anticipated to be declared in the calendar year does not exceed 50% of the net profits after taxes but before dividends for the previous calendar year; and
- (c) the ratio of equity capital to adjusted assets is not less than 6%.

The payment of dividends by the Corporation and the Bank may also be affected or limited by other factors, such as the requirement to maintain adequate capital above regulatory guidelines. In addition, if, in the opinion of the applicable regulatory authority, a bank under its jurisdiction is engaged in or is about to engage in an unsafe or unsound practice (which, depending upon the financial condition of the bank, could include the payment of dividends), such authority may require, after notice and hearing, that such bank cease and desist from such practice. The FDIC has issued a policy statement providing that insured banks should generally only pay dividends out of current operating earnings. In addition to the formal statutes and regulations, regulatory authorities consider the adequacy of each of the Bank's total capital in relation to its assets, deposits and other such items. Capital adequacy considerations could further limit the availability of dividends to the Bank. At December 31, 2016, net assets available from the Bank to pay dividends without prior approval from regulatory authorities totaled \$2,049,022. For 2016, the Corporation's cash dividend payout to stockholders was \$1,070,047.

## Supervision and Regulation

The following is a brief summary of the supervision and regulation of the Corporation and the Bank as financial institutions and is not intended to be a complete discussion of all NYSE MKT LLC, state or federal rules, statutes and regulations affecting their operations, or that apply generally to business corporations or companies listed on NYSE MKT LLC. Changes in the rules, statutes and regulations applicable to the Corporation and the Bank can affect the operating environment in substantial and unpredictable ways.

**General.** The Corporation is a registered bank holding company subject to regulation by the Federal Reserve under the Bank Holding Company Act of 1956, as amended (the "Federal Reserve Act"). The Corporation is required to file annual and quarterly financial information with the Federal Reserve and is subject to periodic examination by the Federal Reserve.

The Federal Reserve Act requires every bank holding company to obtain the Federal Reserve's prior approval before (1) it may acquire direct or indirect ownership or control of more than 5% of the voting shares of any bank that it does not already control; (2) it or any of its non-bank subsidiaries may acquire all or substantially all of the assets of a bank; and (3) it may merge or consolidate with any other bank holding company. In addition, a bank holding company is generally prohibited from engaging in, or acquiring, direct or indirect control of the voting shares of any company engaged in non-banking activities. This prohibition does not apply to activities listed in the Federal Reserve Act or found by the Federal Reserve, by order or regulation, to be closely related to banking or managing or controlling banks as to be a proper incident thereto. Some of the activities that the Federal Reserve has determined by regulation or order to be closely related to banking are:

- making, acquiring or servicing loans and certain types of leases;
- performing certain data processing services;
- acting as fiduciary or investment or financial advisor;
- providing brokerage services;
- underwriting bank eligible securities;
- underwriting debt and equity securities on a limited basis through separately capitalized subsidiaries; and
- making investments in corporations or projects designed primarily to promote community welfare.

Although the activities of bank holding companies have traditionally been limited to the business of banking and activities closely related or incidental to banking (as discussed above), the Gramm-Leach-Bliley Act (the "GLB Act") relaxed the previous limitations and permitted bank holding companies to engage in a broader range of financial activities. Specifically, bank holding companies may elect to become financial holding companies which may affiliate with securities firms and insurance companies and engage in other activities that are financial in nature. Among the activities that are deemed "financial in nature" include:

- lending, exchanging, transferring, investing for others or safeguarding money or securities;
- insuring, guaranteeing, or indemnifying against loss, harm, damage, illness, disability, or death, or providing and issuing annuities, and acting as principal, agent, or broker with respect thereto;
- providing financial, investment, or economic advisory services, including advising an investment company;
- issuing or selling instruments representing interests in pools of assets permissible for a bank to hold directly; and
- underwriting, dealing in or making a market in securities.

Under this legislation, the Federal Reserve serves as the primary "umbrella" regulator of financial holding companies with supervisory authority over each parent company and limited authority over its subsidiaries. The primary regulator of each subsidiary of a financial holding company will depend on the type of activity conducted by the subsidiary. For example, broker-dealer subsidiaries will be regulated largely by securities regulators and insurance subsidiaries will be regulated largely by insurance authorities.

The Corporation has no current plans to register as a financial holding company.

The Corporation must also register with the DBF and file periodic information with the DBF. As part of such registration, the DBF requires information with respect to the financial condition, operations, management and intercompany relationships of the Corporation and the Bank and related matters. The DBF may also require such other information as is necessary to keep itself informed as to whether the provisions of Georgia law and the regulations and orders issued thereunder by the DBF have been complied with, and the DBF may examine the Corporation and the Bank.

The Corporation is an “affiliate” of the Bank under the Federal Reserve Act, which imposes certain restrictions on (1) loans by the Bank to the Corporation, (2) investments in the stock or securities of the Corporation by the Bank, (3) the Bank’s taking of the stock or securities of an “affiliate” as collateral for loans by the Bank to a borrower, and (4) the purchase of assets from the Corporation by the Bank. Further, a bank holding company and its subsidiaries are prohibited from engaging in certain tie-in arrangements in connection with any extension of credit, lease or sale of property or furnishing of services.

The Bank is regularly examined by the FDIC. As a state banking association organized under Georgia law, the Bank is subject to the supervision and the regular examination of the DBF. Both the FDIC and DBF must grant prior approval of any merger, consolidation or other corporation reorganization involving the Bank.

**Capital Adequacy.** Banks and bank holding companies are subject to various regulatory capital requirements administered by state and federal banking agencies. Capital adequacy guidelines involve quantitative measures of assets, liabilities and certain off-balance-sheet items calculated under regulatory accounting practices. Capital amounts and classifications are also subject to qualitative judgments by regulators about components, risk weighting and other factors.

The Federal Reserve and the FDIC have implemented substantially identical risk-based rules for assessing bank and bank holding company capital adequacy. These regulations establish minimum capital standards in relation to assets and off-balance sheet exposures as adjusted for credit risk. “Total capital” is composed of Tier 1 capital and Tier 2 capital. “Tier 1 capital” includes common equity, retained earnings, qualifying non-cumulative perpetual preferred stock, a limited amount of qualifying cumulative perpetual stock at the holding company level, minority interests in equity accounts of consolidated subsidiaries, less goodwill, most intangible assets and certain other assets. “Tier 2 capital” includes, among other things, perpetual preferred stock and related surplus not meeting the Tier 1 capital definition, qualifying mandatorily convertible debt securities, qualifying subordinated debt and allowances for possible loan and lease losses, subject to limitations. The Federal Reserve and the FDIC use the leverage ratio in tandem with the risk-based ratio to assess the capital adequacy of banks and bank holding companies. The Federal Reserve will require a bank holding company to maintain a leverage ratio well above minimum levels if it is experiencing or anticipating significant growth or is operating with less than well-diversified risks in the opinion of the Federal Reserve. The FDIC, the Office of the Comptroller of the Currency (the “OCC”) and the Federal Reserve also require banks to maintain capital well above minimum levels.

In July 2013, the Federal Reserve published the Basel III Capital Rules establishing a new comprehensive capital framework applicable to all depository institutions, bank holding companies with total consolidated assets above a certain threshold, and all savings and loan holding companies except for those that are substantially engaged in insurance underwriting or commercial activities (collectively, “banking organizations”). The rules implement the December 2010 framework proposed by the Basel Committee on Banking Supervision (the “Basel Committee”), known as “Basel III”, for strengthening international capital standards as well as certain provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the “Dodd-Frank Act”).

The Basel III Capital Rules substantially revised the risk-based capital requirements applicable to bank holding companies and depository institutions compared to the prior U.S. risk-based capital rules. The Basel III Capital Rules:

- defined the components of capital and address other issues affecting the numerator in banking institutions’ regulatory capital ratios;
- addressed risk weights and other issues affecting the denominator in banking institutions’ regulatory capital ratios and replaced the prior risk-weighting approach, which was derived from the Basel I capital accords of the Basel Committee, with a more risk-sensitive approach based, in part, on the standardized approach in the Basel Committee’s 2004 “Basel II” capital accords;
- introduced a new capital measure called “common equity Tier 1” (“CET1”);
- specified that Tier 1 capital consists of CET1 and “additional Tier 1 capital” instruments meeting specified requirements; and
- implemented the requirements of Section 939A of the Dodd-Frank Act to remove references to credit ratings from the federal banking agencies’ rules.

The Basel III Capital Rules became effective for the Bank on January 1, 2015, subject to a phase in period, but are not applicable to bank holding companies, like the Corporation, with less than \$1 billion in total consolidated assets that meet certain criteria.

The Basel III Capital Rules require the Bank to maintain;

- a minimum ratio of CET1 to risk-weighted assets of at least 4.5%, plus a 2.5% “capital conservation buffer” (which is added to the 4.5% CET1 ratio as that buffer is phased in over four years to 2.5%, effectively resulting in a minimum ratio of CET1 to risk-weighted assets of at least 7% upon full implementation);
- a minimum ratio of Tier 1 capital to risk-weighted assets of at least 6%, plus the capital conservation buffer (which is added to the 6% Tier 1 capital ratio as that buffer is phased in over four years to 2.5%, effectively resulting in a minimum Tier 1 capital ratio of 8.5% upon full implementation);
- a minimum ratio of Total capital (that is, Tier 1 plus Tier 2) to risk-weighted assets of at least 8%, plus the capital conservation buffer (which is added to the 8% Total capital ratio as that buffer is phased in over four years to 2.5%, effectively resulting in a minimum Total capital ratio of 10.5% upon full implementation); and
- a minimum leverage ratio of 4%, calculated as the ratio of Tier 1 capital to average assets.

In addition, Section 38 of the Federal Deposit Insurance Act implemented the prompt corrective action provisions that Congress enacted as a part of the Federal Deposit Insurance Corporation Improvement Act of 1991 (the “1991 Act”). The prompt corrective action provisions set forth five regulatory zones in which all banks are placed largely based on their capital positions. Regulators are permitted to take increasingly harsh action as a bank’s financial condition declines. The FDIC is required to resolve a bank when its ratio of tangible equity to total assets reaches 2%. Better capitalized institutions are generally subject to less onerous regulation and supervision than banks with lesser amounts of capital.

The FDIC has adopted regulations implementing the prompt corrective action provisions of the 1991 Act, as revised by the Basel III Capital Rules effective January 1, 2015, which place financial institutions in the following five categories based upon capitalization ratios: (1) a “well-capitalized” institution has a Total risk-based capital ratio of at least 10%, a Tier 1 risk-based ratio of at least 8%, a CET1 risk-based ratio of 6.5% and a leverage ratio of at least 5%; (2) an “adequately capitalized” institution has a Total risk-based capital ratio of at least 8%, a Tier 1 risk-based ratio of at least 6%, a CET1 risk-based ratio of 4.5% and a leverage ratio of at least 4%; (3) an “undercapitalized” institution has a Total risk-based capital ratio of under 8%, a Tier 1 risk-based ratio of under 6%, a CET1 risk-based ratio of under 4.5% or a leverage ratio of under 4%; (4) a “significantly undercapitalized” institution has a Total risk-based capital ratio of under 6%, a Tier 1 risk-based ratio of under 4%, a CET1 risk-based ratio of under 3% or a leverage ratio of under 3%; and (5) a “critically undercapitalized” institution has a ratio of tangible equity to total assets of 2% or less. Institutions in any of the three undercapitalized categories would be prohibited from declaring dividends or making capital distributions. The FDIC regulations also allow it to “downgrade” an institution to a lower capital category based on supervisory factors other than capital.

As of December 31, 2016, the most recent notifications from the FDIC categorized the Bank as “well-capitalized” under current regulations.

The Basel III Capital Rules provide for a number of deductions from and adjustments to CET1. These include, for example, the requirement that mortgage servicing rights, deferred tax assets arising from temporary differences that could not be realized through net operating loss carrybacks and significant investments in non-consolidated financial entities be deducted from CET1 to the extent that any one such category exceeds 10% of CET1 or all such categories in the aggregate exceed 15% of CET1. Under prior capital standards, the effects of certain accumulated other comprehensive income items included in capital were excluded for the purposes of determining regulatory capital ratios. Under the Basel III Capital Rules, the effects of certain accumulated other comprehensive items are not excluded; however, certain banking organizations, including the Bank, may make a one-time permanent election to continue to exclude these items. The Bank made this election in the first quarter of 2015 in order to avoid significant variations in the level of capital depending upon the impact of interest rate fluctuations on the fair value of the Bank’s available-for-sale securities portfolio.

The “capital conservation buffer” is designed to absorb losses during periods of economic stress. Banking organizations with a ratio of CET1 to risk-weighted assets above the minimum but below the conservation buffer (or below the combined capital conservation buffer and countercyclical capital buffer, when the latter is applied) will face constraints on dividends, equity repurchases and compensation based on the amount of the shortfall.

Implementation of the deductions and other adjustments to CET1 began on January 1, 2015, and will be phased-in over a four-year period (beginning at 4.5% on January 1, 2015, and an additional 0.625% per year thereafter). The implementation of the capital conservation buffer began on January 1, 2016, at the 0.625% level and will be phased in over a four-year period (increasing by that amount on each subsequent January 1, until it reaches 2.5% on January 1, 2019).

The Basel III Capital Rules prescribe a standardized approach for risk weightings that expand the risk-weighting categories from the current four Basel I-derived categories (0%, 20%, 50% and 100%) to a much larger and more risk-sensitive number of categories, depending on the nature of the assets, generally ranging from 0% for U.S. government agency securities, to 600% for certain equity exposures, and resulting in higher risk weights for a variety of asset categories. Consistent with the Dodd-Frank Act, the Basel III Capital Rules replace the ratings-based approach to securitization exposures, which is based on external credit ratings, with the simplified supervisory formula approach in order to determine the appropriate risk weights for these exposures. Alternatively, banking organizations may use the existing gross-up approach to assign securitization exposures to a risk weight category or choose to assign such exposures a 1,250% risk weight. In addition, the Basel III Capital Rules provide more advantageous risk weights for derivatives and repurchase-style transactions cleared through a qualifying central counterparty and increase the scope of eligible guarantors and eligible collateral for purposes of credit risk mitigation.

As of December 31, 2016, the Bank met all capital adequacy requirements under the Basel III Capital Rules on a fully phased-in basis as if such requirements were currently in effect.

**Consumer Protection Laws.** The Dodd-Frank Act centralized responsibility for consumer financial protection by creating a new agency, the Consumer Financial Protection Bureau (“CFPB”), and giving it the power to promulgate and enforce federal consumer protection laws. Depository institutions are subject to the CFPB’s rule writing authority, and existing federal bank regulatory agencies retain examination and enforcement authority for such institutions. The CFPB and the Corporation’s existing federal regulator, the FDIC, are focused on the following:

- risks to consumers and compliance with the federal consumer financial laws;
- the markets in which firms operate and risks to consumers posed by activities in those markets;
- depository institutions that offer a wide variety of consumer financial products and services;
- depository institutions with a more specialized focus; and
- non-depository companies that offer one or more consumer financial products or services.

**Volcker Rule.** The Dodd-Frank Act amended the Federal Reserve Act to require the federal bank regulatory agencies to adopt rules that prohibit banks and their affiliates from engaging in proprietary trading and investing in and sponsoring certain unregistered

investment companies (defined as hedge funds and private equity funds). The statutory provision is commonly called the “Volcker Rule”. The Federal Reserve adopted final rules implementing the Volcker Rule on December 10, 2013. Although the Corporation continues to evaluate the impact of the Volcker Rule and the final rules adopted by the Federal Reserve thereunder, the Corporation does not currently anticipate that the Volcker Rule will have a material effect on its operations and the operations of its subsidiaries, including the Bank, as the Corporation does not engage in businesses prohibited by the Volcker Rule. In the future, the Corporation may incur costs to adopt additional policies and systems to ensure compliance with the Volcker Rule.

**Commercial Real Estate.** The federal bank regulatory agencies, including the FDIC, restrict concentrations in commercial real estate lending and have noted that recent increases in banks’ commercial real estate concentrations have created safety and soundness concerns in the event of a significant economic downturn. The regulatory guidance mandates certain minimal risk management practices and categorizes banks with defined levels of such concentrations as banks requiring elevated examiner scrutiny. Although management believes that the Corporation’s credit processes and procedures meet the risk management standards dictated by this guidance, regulatory outcomes could effectively limit increases in the real estate concentrations in the Bank’s loan portfolio and require additional credit administration and management costs associated with those portfolios.

**Source of Strength Doctrine.** Federal Reserve regulations and policy requires bank holding companies to act as a source of financial and managerial strength to their subsidiary banks. Under this policy, the Corporation is expected to commit resources to support the Bank.

**Loans.** Inter-agency guidelines adopted by federal bank regulatory agencies mandate that financial institutions establish real estate lending policies with maximum allowable real estate loan-to-value limits, subject to an allowable amount of non-conforming loans as a percentage of capital.

**Transactions with Affiliates.** Under federal law, all transactions between and among a state nonmember bank and its affiliates, which include holding companies, are subject to Sections 23A and 23B of the Federal Reserve Act and Regulation W promulgated thereunder. Generally, these requirements limit these transactions to a percentage of the bank’s capital and require all of them to be on terms at least as favorable to the bank as transactions with non-affiliates. In addition, a bank may not lend to any affiliate engaged in non-banking activities not permissible for a bank holding company or acquire shares of any affiliate that is not a subsidiary. The FDIC is authorized to impose additional restrictions on transactions with affiliates if necessary to protect the safety and soundness of a bank. The regulations also set forth various reporting requirements relating to transactions with affiliates.

**Financial Privacy.** In accordance with the GLB Act, federal banking regulatory agencies adopted rules that limit the ability of banks and other financial institutions to disclose non-public information about consumers to non-affiliated third parties. These limitations require disclosure of privacy policies to consumers and, in some circumstances, allow consumers to prevent disclosure of certain personal information to a nonaffiliated third party. The privacy provisions of the GLB Act affect how consumer information is transmitted through diversified financial companies and conveyed to outside vendors.

**Anti-Money Laundering Initiatives and the USA Patriot Act.** A major focus of governmental policy on financial institutions in recent years has been aimed at combating terrorist financing. This has generally been accomplished by amending existing anti-money laundering laws and regulations. The United States Department of the Treasury has issued a number of implementing regulations which apply various requirements of the USA Patriot Act of 2001 to the Bank. These regulations impose obligations on financial institutions to maintain appropriate policies, procedures and controls to detect, prevent and report money laundering and terrorist financing and to verify the identity of their customers. Failure of a financial institution to maintain and implement adequate programs to combat terrorist financing, or to comply with all of the relevant laws or regulations, could have serious legal and reputational consequences for the institution.

**Incentive Compensation.** The federal banking agencies have issued guidance on incentive compensation policies (the “Incentive Compensation Guidance”) intended to ensure that the incentive compensation policies of financial institutions do not undermine the safety and soundness of such institutions by encouraging excessive risk-taking. The Incentive Compensation Guidance, which covers all employees that have the ability to materially affect the risk profile of an institution, either individually or as part of a group, is based upon the key principles that a financial institution’s incentive compensation arrangements should (i) provide incentives that do not encourage risk-taking beyond the institution ability to effectively identify and manage risks, (ii) be compatible with effective internal controls and risk management, and (iii) be supported by strong corporate governance, including active and effective oversight by the institution’s board of directors.

The Federal Reserve will review, as part of the regular, risk-focused examination process, the incentive compensation arrangements of financial institutions like the Corporation that are not “large, complex banking organizations.” These reviews will be tailored to each financial institution based on the scope and complexity of the institution’s activities and the prevalence of incentive compensation arrangements. The findings of the supervisory initiatives will be included in reports of examination. Deficiencies will be incorporated into the financial institution’s supervisory ratings, which can affect the institution’s ability to make acquisitions and take other actions. Enforcement actions may be taken against a financial institution if its incentive compensation arrangements, or related risk-management control or governance processes, pose a risk to the institution’s safety and soundness and the institution is not taking prompt and effective measures to correct the deficiencies.

The scope and content of banking regulators’ policies on executive compensation are continuing to develop and are likely to continue evolving in the near future. It cannot be determined at this time whether compliance with such policies will adversely affect our ability to hire, retain and motivate its key employees.

**Cybersecurity.** Recent cyber-attacks against banks and other financial institutions that resulted in unauthorized access to confidential customer information have prompted the federal bank regulatory agencies to issue extensive guidance on cybersecurity. These agencies are likely to devote more resources to this part of their safety and soundness examination than they may have in the past.

**Fair Value.** The Corporation's impaired loans and foreclosed assets may be measured and carried at "fair value", the determination of which requires management to make assumptions, estimates and judgments. When a loan is considered impaired, a specific valuation allowance is allocated or a partial charge-off is taken, if necessary, so that the loan is reported net, at the present value of estimated future cash flows using the loan's existing rate or at the fair value of collateral if repayment is expected solely from the collateral. In addition, foreclosed assets are carried at the lower of cost or "fair value", less cost to sell, following foreclosure. "Fair value" is defined by U.S. generally accepted accounting principles ("GAAP") "as the price that would be received to sell an asset in an orderly transaction between market participants at the measurement date." GAAP further defines an "orderly transaction" as "a transaction that assumes exposure to the market for a period prior to the measurement date to allow for marketing activities that are usual and customary for transactions involving such assets; it is not a forced transaction (for example, a forced liquidation or distress sale)." Recently in the Bank's markets, there have been very few transactions in the type of assets which represent the vast majority of the Bank's impaired loans and foreclosed properties which reflect "orderly transactions" as so defined. Instead, most transactions in comparable assets have been distressed sales not indicative of "fair value." Accordingly, the determination of fair value in the current environment is difficult and more subjective than it would be in a stable real estate environment. Although management believes its processes for determining the value of these assets are appropriate factors and allow the Corporation to arrive at a fair value, the processes require management judgment and assumptions and the value of such assets at the time they are revalued or divested may be significantly different from management's determination of fair value. Because of this increased subjectivity in fair value determinations, there is greater than usual grounds for differences in opinions, which may result in increased disagreements between management and the Bank's regulators, disagreements which could impair the relationship between the Bank and its regulators.

**Future Legislation.** Various legislation affecting financial institutions and the financial industry is, from time to time, introduced in Congress. Such legislation may change banking statutes and the operating environment of the Corporation and its subsidiaries in substantial and unpredictable ways, and could increase or decrease the cost of doing business, limit or expand permissible activities or affect the competitive balance depending upon whether any of this potential legislation will be enacted, and, if enacted, the effect that it or any implementing regulations would have on the financial condition or results of operations of the Corporation or any of its subsidiaries. With the current economic environment, the nature and extent of future legislative and regulatory changes affecting financial institutions is not known at this time.

#### **Available Information**

The Corporation's website where you can find more information is located at [www.sgfc.com](http://www.sgfc.com). We make available free of charge, through our website, our Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, proxy statements and other reports filed or furnished pursuant to Section 13(a) or 15(d) under the Securities Exchange Act of 1934 (the "Exchange Act"). These reports are available as soon as reasonably practicable after those materials are electronically filed with the Securities and Exchange Commission (the "SEC"). Our SEC filings are publicly available at the SEC's website located at [www.sec.gov](http://www.sec.gov). You may also read and copy any document we file with the SEC at its Public Reference Facilities at 100 F Street, N.E., Room 1580, Washington, D.C. 20549. You may obtain information about the Public Reference Room operations by calling the SEC at 1-800-SEC-0330.

Information provided on our website is not part of this report, and is not incorporated herein by reference unless otherwise specifically referenced as such in this report.

## Executive Officers of the Corporation

Executive officers are elected by the Board of Directors annually in May and hold office until the following May at the pleasure of the Board of Directors. The principal executive officers of the Corporation, Bank, and Empire and their ages, positions, and terms of office as of March 31, 2017, are as follows:

<u>Name (Age)</u>	<u>Principal Position</u>	<u>Executive Officer Since</u>
DeWitt Drew (60)	President and Chief Executive Officer of the Corporation and Bank	1999
John J. Cole, Jr. (67)	Executive Vice President and Chief Operating Officer of the Corporation and Bank	1984
Jeffery E. Hanson (51)	Executive Vice President and Chief Banking Officer of the Corporation and Bank and President and Chief Executive Officer of Empire	2011
George R. Kirkland (66)	Executive Vice President, Chief Financial Officer, and Treasurer of the Corporation and Bank	1991
Danny E. Singley (62)	Executive Vice President and Chief Credit Officer of the Bank	2002
Jeffrey (Jud) Moritz (40)	Senior Vice President of the Bank and Valdosta Region President	2011
David L. Shiver (67)	Senior Vice President of the Bank and Sylvester Region President	2006
Donna S. Lott (41)	Senior Vice President and Cashier of the Bank	2008
Karen T. Boyd (48)	Senior Vice President and Controller of the Bank	2010
Ross K. Dekle (35)	Senior Vice President of the Bank and Moultrie Region President	2011
Gregory P. Costin (42)	Senior Vice President of the Bank	2012
Pamela J. Yeager (48)	Senior Vice President of the Bank	2015
Chad J. Carpenter (43)	Senior Vice President of the Bank and Tifton Region President	2015

None of the above officers are related and there are no arrangements or understandings between them and any other person pursuant to which any of them was elected as an officer, other than arrangements or understandings with directors or officers of the Corporation, Bank or Empire acting solely in their capacities as such.

The following is a brief description of the business experience of the principal executive officers of the Corporation, Bank, and Empire. Except as otherwise indicated, each principal executive officer has been engaged in their present or last employment, in the same or similar position, for more than five years.

Mr. Drew is a director of Southwest Georgia Financial Corporation and Southwest Georgia Bank and was named President and Chief Executive Officer in May 2002. Previously, he served as President and Chief Operating Officer beginning in 2001 and Executive Vice President in 1999 of Southwest Georgia Financial Corporation and Southwest Georgia Bank.

Mr. Cole is a director of Southwest Georgia Financial Corporation and Southwest Georgia Bank and became Executive Vice President and Chief Operating Officer of the Corporation and Bank in 2011. He has been Executive and Senior Vice President of the Corporation and Bank since 1992 and has served in various other positions with the Bank since 1976 and the Corporation since 1981.

Mr. Hanson became Executive Vice President of the Corporation in 2012 and Executive Vice President and Chief Banking Officer of the Bank in 2011. He is also the President and Chief Executive Officer of Empire. Previously, he was employed by Park Avenue Bank in Valdosta, Georgia, as Valdosta Market President and various other positions since 1994.

Mr. Kirkland became Executive Vice President and Chief Financial Officer of the Corporation and Bank in 2013. Previously, he had been Senior Vice President of the Corporation and Bank and Treasurer of the Corporation and Comptroller of the Bank since 1993.

Mr. Singley became Executive Vice President and Chief Credit Officer of the Bank in 2014. Previously, he was appointed President Moultrie Region and Senior Vice President of the Bank in 2011 and served as Senior Vice President of the Bank since 2008. Prior to that, he had been Vice President of the Bank since 2002.

Mr. Moritz became Senior Vice President of the Bank and Valdosta Region President in 2011. Previously, he was employed by Park Avenue Bank in Valdosta, Georgia, for five years and Regions Bank for five years.

Mr. Shiver became Senior Vice President of the Bank and Sylvester Region President in 2011. Previously, he had been Vice President of the Bank since 2006 and, prior to that, Assistant Vice President of the Bank since 2005.

Ms. Lott became Senior Vice President of the Bank in 2014. She is also Cashier of the Bank. Previously, she served as Vice President of the bank since 2008 and, prior to that, Assistant Vice President of the Bank since 2007.

Ms. Boyd became Senior Vice President and Controller of the Bank in 2014. Previously, she served as Vice President of the Bank since 2010 and, prior to that, Assistant Vice President of the Bank since 2007.

Mr. Dekle became Senior Vice President of the Bank and Moultrie Region President in 2014. Previously, he served as Vice President of the Bank since 2011 and, prior to that, Assistant Vice President of the Bank since 2007.

Mr. Costin became Senior Vice President of the Bank in 2015. Previously, he served as Vice President of the Bank since 2012 and, prior to that, Assistant Vice President of the Bank since 2011.

Ms. Yeager became Senior Vice President of the Bank in 2015. Previously, she was employed for 11 years with Commercial Banking Company in Valdosta, Georgia. Prior to that, she was employed for 18 years with First State Bank and Trust in Valdosta, Georgia.

Mr. Carpenter became Senior Vice President of the Bank and Tifton Region President in 2015. Previously, he was employed by BB&T Bank in Tifton, Georgia, for 15 years where he most recently held the position of Area President for the communities of Tifton, Valdosta and Douglas.

**Table 1 - Distribution of Assets, Liabilities, and Stockholders' Equity; Interest Rates and Interest Differentials**

The following tables set forth, for the fiscal years ended December 31, 2016, 2015, and 2014, the daily average balances outstanding for the major categories of earning assets and interest-bearing liabilities and the average interest rate earned or paid thereon. Except for percentages, all data is in thousands of dollars.

	Year Ended December 31, 2016		
	Average Balance	Interest (Dollars in thousands)	Rate
<b>ASSETS</b>			
Cash and due from banks	\$ <u>7,479</u>	\$ _____	- %
Earning assets:			
Interest-bearing deposits with banks	19,759	103	0.52%
Loans, net (a) (b) (c)	277,908	14,863	5.35%
Certificates of deposit in other banks	17	0	0.00%
Taxable investment securities held to maturity	47,620	1,168	2.45%
Nontaxable investment securities held to maturity (c)	51,151	1,888	3.69%
Nontaxable investment securities available for sale (c)	3,696	151	4.09%
Other investment securities	<u>1,941</u>	<u>92</u>	4.74%
Total earning assets	<u>402,092</u>	\$ <u>18,265</u>	4.54%
Premises and equipment	11,355		
Other assets	<u>10,155</u>		
Total assets	\$ <u>431,081</u>		
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>			
Non-interest bearing demand deposits	\$ <u>113,122</u>	\$ _____	- %
Interest-bearing liabilities:			
NOW accounts	17,623	30	0.17%
Money market deposit accounts	112,434	285	0.25%
Savings deposits	29,621	50	0.17%
Time deposits	80,204	570	0.71%
Federal funds purchased	1	0	0.00%
Other borrowings	<u>35,861</u>	<u>677</u>	1.89%
Total interest-bearing liabilities	<u>275,744</u>	<u>1,612</u>	0.58%
Other liabilities	<u>3,845</u>		
Total liabilities	<u>392,711</u>		
Common stock	4,294		
Surplus	31,702		
Retained earnings	28,489		
Less treasury stock	( 26,115)		
Total stockholders' equity	<u>38,370</u>		
Total liabilities and stockholders' equity	\$ <u>431,081</u>		
Net interest income and margin		\$ <u>16,653</u>	4.14%

- (a) Average loans are shown net of unearned income and the allowance for loan losses. Nonperforming loans are included.  
(b) Interest income includes loan fees of \$1,045 million.  
(c) Reflects taxable equivalent adjustments using a tax rate of 34 %.



Year Ended December 31, 2015

ASSETS	Average Balance	Interest (Dollars in thousands)	Rate
Cash and due from banks	\$ 7,358	\$ _____	- %
Earning assets:			
Interest-bearing deposits with banks	20,244	62	0.31%
Loans, net (a) (b) (c)	232,791	12,767	5.48%
Certificates of deposit in other banks	1,293	12	0.93%
Taxable investment securities held to maturity	59,365	1,344	2.26%
Nontaxable investment securities held to maturity (c)	52,580	1,913	3.64%
Nontaxable investment securities available for sale (c)	1,990	95	4.77%
Other investment securities	<u>1,608</u>	<u>74</u>	4.60%
Total earning assets	<u>369,871</u>	\$ <u>16,267</u>	4.40%
Premises and equipment	11,525		
Other assets	<u>9,856</u>		
Total assets	<u>\$ 398,610</u>		
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>			
Non-interest bearing demand deposits	\$ <u>97,879</u>	\$ _____	- %
Interest-bearing liabilities:			
NOW accounts	16,963	30	0.18%
Money market deposit accounts	110,478	262	0.24%
Savings deposits	29,048	44	0.15%
Time deposits	76,772	460	0.60%
Federal funds purchased	42	0	0.00%
Other borrowings	<u>28,852</u>	<u>521</u>	1.81%
Total interest-bearing liabilities	<u>262,155</u>	<u>1,317</u>	0.50%
Other liabilities	<u>2,619</u>		
Total liabilities	<u>362,653</u>		
Common stock	4,294		
Surplus	31,702		
Retained earnings	26,075		
Less treasury stock	( 26,114)		
Total stockholders' equity	<u>35,957</u>		
Total liabilities and stockholders' equity	<u>\$ 398,610</u>		
Net interest income and margin		\$ <u>14,950</u>	4.04%

- (a) Average loans are shown net of unearned income and the allowance for loan losses. Nonperforming loans are included.
- (b) Interest income includes loan fees of \$797 thousand.
- (c) Reflects taxable equivalent adjustments using a tax rate of 34 %.

## Year Ended December 31, 2014

	Average Balance	Interest (Dollars in thousands)	Rate
ASSETS			
Cash and due from banks	\$ <u>7,714</u>	\$ <u>-</u>	-
Earning assets:			
Interest-bearing deposits with banks	19,988	52	0.26%
Loans, net (a) (b) (c)	220,164	12,191	5.54%
Certificates of deposit in other banks	3,066	33	1.08%
Taxable investment securities held to maturity	60,281	1,365	2.26%
Nontaxable investment securities held to maturity (c)	46,337	1,658	3.58%
Nontaxable investment securities available for sale (c)	924	49	5.30%
Other investment securities	<u>1,601</u>	<u>71</u>	4.44%
Total earning assets	<u>352,361</u>	\$ <u>15,419</u>	4.38%
Premises and equipment	11,427		
Other assets	<u>10,554</u>		
Total assets	\$ <u>382,056</u>		
LIABILITIES AND STOCKHOLDERS' EQUITY			
Non-interest bearing demand deposits	\$ <u>88,882</u>	\$ <u>-</u>	-
Interest-bearing liabilities:			
NOW accounts	17,212	32	0.19%
Money market deposit accounts	104,970	246	0.23%
Savings deposits	29,638	47	0.16%
Time deposits	77,565	425	0.55%
Federal funds purchased	45	0	0.00%
Other borrowings	<u>27,627</u>	<u>605</u>	2.19%
Total interest-bearing liabilities	<u>257,057</u>	<u>1,355</u>	0.53%
Other liabilities	<u>2,892</u>		
Total liabilities	<u>348,831</u>		
Common stock	4,294		
Surplus	31,702		
Retained earnings	23,343		
Less treasury stock	<u>( 26,114)</u>		
Total stockholders' equity	<u>33,225</u>		
Total liabilities and stockholders' equity	\$ <u>382,056</u>		
Net interest income and margin		\$ <u>14,064</u>	3.99%

- (a) Average loans are shown net of unearned income and the allowance for loan losses. Nonperforming loans are included.
- (b) Interest income includes loan fees of \$640 thousand.
- (c) Reflects taxable equivalent adjustments using a tax rate of 34 %.

**Table 2 – Rate/Volume Analysis**

The following table sets forth, for the indicated years ended December 31, a summary of the changes in interest paid resulting from changes in volume and changes in rate. The change due to volume is calculated by multiplying the change in volume by the prior year's rate. The change due to rate is calculated by multiplying the change in rate by the prior year's volume. The change attributable to both volume and rate is calculated by multiplying the change in volume by the change in rate.

	2016	2015	Increase (Decrease)	Due To Changes In (a)	
				Volume	Rate
(Dollars in thousands)					
Interest earned on:					
Interest-bearing deposits with banks	\$ 103	\$ 62	\$ 41	\$( 1)	\$ 42
Loans, net (b)	14,863	12,767	2,096	2,404	( 308)
Certificates of deposit in other banks	0	12	( 12)	( 6)	( 6)
Taxable investment securities held to maturity	1,168	1,344	( 176)	( 304)	128
Nontaxable investment securities held to maturity (b)	1,888	1,913	( 25)	( 54)	29
Nontaxable investment securities available for sale (b)	151	95	56	68	( 12)
Other investment securities	<u>92</u>	<u>74</u>	<u>18</u>	<u>16</u>	<u>2</u>
Total interest income	<u>18,265</u>	<u>16,267</u>	<u>1,998</u>	<u>2,123</u>	<u>( 125)</u>
Interest paid on:					
NOW accounts	30	30	0	0	0
Money market deposit accounts	285	262	23	5	18
Savings deposits	50	44	6	1	5
Time deposits	570	460	110	22	88
Other borrowings	<u>677</u>	<u>521</u>	<u>156</u>	<u>131</u>	<u>25</u>
Total interest expense	<u>1,612</u>	<u>1,317</u>	<u>295</u>	<u>159</u>	<u>136</u>
Net interest earnings	<u>\$16,653</u>	<u>\$14,950</u>	<u>\$ 1,703</u>	<u>\$1,964</u>	<u>\$( 261)</u>

- (a) Volume and rate components are in proportion to the relationship of the absolute dollar amounts of the change in each.  
(b) Reflects taxable equivalent adjustments using a tax rate of 34 % for 2016 and 2015 in adjusting interest on nontaxable loans and securities to a fully taxable basis.

	2015	2014	Increase (Decrease)	Due To Changes In (a)	
				Volume	Rate
(Dollars in thousands)					
Interest earned on:					
Interest-bearing deposits with banks	\$ 62	\$ 52	\$ 10	\$ 1	\$ 9
Loans, net (b)	12,767	12,191	576	691	( 115)
Certificates of deposit in other banks	12	33	( 21)	( 17)	( 4)
Taxable investment securities held to maturity	1,344	1,365	( 21)	( 21)	0
Nontaxable investment securities held to maturity (b)	1,913	1,658	255	227	28
Nontaxable investment securities available for sale (b)	95	49	46	51	( 5)
Other investment securities	<u>74</u>	<u>71</u>	<u>3</u>	<u>0</u>	<u>3</u>
Total interest income	<u>16,267</u>	<u>15,419</u>	<u>848</u>	<u>932</u>	<u>( 84)</u>
Interest paid on:					
NOW accounts	30	32	( 2)	0	( 2)
Money market deposit accounts	262	246	16	13	3
Savings deposits	44	47	( 3)	( 1)	( 2)
Time deposits	460	425	35	( 4)	39
Other borrowings	<u>521</u>	<u>605</u>	<u>( 84)</u>	<u>29</u>	<u>( 113)</u>
Total interest expense	<u>1,317</u>	<u>1,355</u>	<u>( 38)</u>	<u>37</u>	<u>( 75)</u>
Net interest earnings	<u>\$14,950</u>	<u>\$14,064</u>	<u>\$ 886</u>	<u>\$ 895</u>	<u>\$( 9)</u>

- (a) Volume and rate components are in proportion to the relationship of the absolute dollar amounts of the change in each.  
(b) Reflects taxable equivalent adjustments using a tax rate of 34 % for 2015 and 2014 in adjusting interest on nontaxable loans and securities to a fully taxable basis.

**Table 3 - Investment Portfolio**

The carrying values of investment securities for the indicated years are presented below:

	Year Ended December 31,		
	2016	2015	2014
	(Dollars in thousands)		
<u>Securities held to maturity:</u>			
State and municipal	\$ 50,436	\$ 54,775	\$ 53,059
Residential mortgage-backed	<u>4,167</u>	<u>6,114</u>	<u>8,529</u>
Total securities held to maturity	\$ <u>54,603</u>	\$ <u>60,889</u>	\$ <u>61,588</u>
<u>Securities available for sale:</u>			
U.S. government treasuries	\$ 962	\$ 0	\$ 0
U.S. government agencies	40,985	42,642	45,493
State and municipal	6,453	2,608	875
Residential mortgage-backed	2,529	3,741	4,971
Corporate notes	2,524	2,473	2,499
Equity securities	<u>112</u>	<u>12</u>	<u>0</u>
Total securities available for sale	\$ <u>53,565</u>	\$ <u>51,476</u>	\$ <u>53,838</u>

At year-end 2016, the total investment portfolio decreased to \$108,168,038, down \$4,197,177, compared with \$112,365,215 at year-end 2015. The decrease was mainly due to calls and maturities of \$14,132,941 of municipal securities and U.S. government agency securities, as well as residential mortgage-backed securities principal paydowns of \$2,173,667. Additionally, we sold \$11,933,634 of available for sale U.S. government agency and residential mortgage-backed securities and \$576,834 of held to maturity residential mortgage-backed securities resulting in a net gain of \$144,034 and \$24,885, respectively. These small lots of held to maturity mortgage-backed securities sold were paid down by over 85% of face value. Partially offsetting these calls, maturities and sales were purchases of \$25,608,386 of U.S. government agency securities and municipal securities.

The following table shows the contractual maturities of debt securities at December 31, 2016, and the weighted average yields (for nontaxable obligations on a fully taxable basis assuming a 34% tax rate) of such securities. Mortgage-backed securities amortize in accordance with the terms of the underlying mortgages, including prepayments as a result of refinancing and other early payoffs.

	MATURITY							
	Within One Year		After One But Within Five Years		After Five But Within Ten Years		After Ten Years	
	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield
	(Dollars in thousands)							
<u>Debt Securities:</u>								
U.S. government treasuries	\$ 0	0%	\$ 0	0%	\$ 962	2.25%	\$ 0	0%
U.S. government agencies	0	0%	9,466	2.29%	31,519	2.45%	0	0%
State and municipal	7,940	2.03%	26,524	3.57%	15,572	4.31%	6,853	4.32%
Residential mortgage-backed	0	0%	352	2.79%	4,609	3.26%	1,735	2.59%
Corporate notes	<u>0</u>	<u>0%</u>	<u>499</u>	<u>1.88%</u>	<u>2,025</u>	<u>1.91%</u>	<u>0</u>	<u>0%</u>
Total	\$ <u>7,940</u>	<u>2.03%</u>	\$ <u>36,841</u>	<u>3.21%</u>	\$ <u>54,687</u>	<u>3.03%</u>	\$ <u>8,588</u>	<u>3.97%</u>

The calculation of weighted average yields is based on the carrying value and effective yields of each security weighted for the scheduled maturity of each security. At December 31, 2016 and 2015, securities carried at approximately \$63,902,259 and \$74,772,674, respectively, were pledged to secure public and trust deposits as required by law. At year-end 2016, approximately \$9,400,000 was over pledged and could be released if necessary for liquidity needs. At December 31, 2016 and 2015, no securities were pledged to secure our Federal Home Loan Bank advances.

**Table 4 - Loan Portfolio**

The following table sets forth the amount of loans outstanding for the indicated years according to type of loan:

	2016	2015	Year Ended December 31,		2012
			2014	2013	
	(Dollars in thousands)				
Commercial, financial and agricultural	\$ 70,999	\$ 58,173	\$ 47,861	\$ 43,675	\$ 40,507
Real estate:					
Construction loans	25,999	19,831	12,257	15,859	16,989
Commercial mortgage loans	91,733	85,777	76,916	78,722	70,059
Residential loans	83,271	67,969	69,305	64,383	62,433
Agricultural loans	16,580	15,620	14,996	12,606	10,169
Consumer & other	<u>3,961</u>	<u>3,435</u>	<u>3,091</u>	<u>3,469</u>	<u>4,010</u>
Total loans	292,543	250,805	224,426	218,714	204,167
Less:					
Unearned interest and discount	19	19	26	26	30
Allowance for loan losses	<u>3,124</u>	<u>3,032</u>	<u>3,114</u>	<u>3,078</u>	<u>2,845</u>
Net loans	\$ <u>289,400</u>	\$ <u>247,754</u>	\$ <u>221,286</u>	\$ <u>215,610</u>	\$ <u>201,292</u>

The following table shows maturities of the commercial, financial, agricultural, and construction loan portfolio at December 31, 2016.

	Commercial, Financial, Agricultural and Construction
	(Dollars in thousands)
Distribution of loans which are due:	
In one year or less	\$ 24,006
After one year but within five years	48,236
After five years	<u>24,756</u>
Total	\$ <u>96,998</u>

The following table shows, for such loans due after one year, the amounts which have predetermined interest rates and the amounts which have floating or adjustable interest rates at December 31, 2016.

	Loans With Predetermined Rates	Loans With Floating Rates	Total
	(Dollars in thousands)		
Commercial, financial, agricultural and construction	\$ <u>66,212</u>	\$ <u>6,780</u>	\$ <u>72,992</u>

The following table presents information concerning outstanding balances of nonaccrual, past-due, and restructured loans as well as foreclosed assets for the indicated years. Respectively, they are defined as: (a) loans accounted for on a nonaccrual basis (“nonaccruals”); (b) loans which are contractually past due 90 days or more as to interest or principal payments and still accruing (“past-dues”); and (c) loans past due 30 days or more for which the terms have been modified to provide a reduction or deferral of interest or principal because of a deterioration in the financial position of the borrower (“troubled debt restructured”). The Corporation’s nonaccrual policy is located in Footnote 3.

	Nonaccrual Loans	Accruing Loans		Total	Foreclosed Assets
		90 Days Past-Due	Troubled Debt Restructured		
	(Dollars in thousands)				
December 31, 2016	\$ 246	\$ 0	\$ 914	\$1,160	\$ 127
December 31, 2015	\$1,546	\$ 1	\$2,290	\$3,837	\$ 82
December 31, 2014	\$ 786	\$ 0	\$ 215	\$1,001	\$ 274
December 31, 2013	\$ 913	\$ 0	\$ 256	\$1,169	\$ 406
December 31, 2012	\$ 25	\$ 0	\$ 199	\$ 224	\$1,690

In 2016, nonaccrual loans decreased due primarily to one \$906,504 agricultural real estate relationship. Items in foreclosed assets includes two residential properties totaling \$126,713.

The Bank performs an internal analysis of the loan portfolio in order to identify and quantify loans with higher than normal risk. Loans having a higher risk profile are assigned a risk rating corresponding to the level of weakness identified in the loan. All loans risk rated Watch, Other Assets Especially Mentioned (OAEM), Substandard or Doubtful are listed on the Bank’s “watchlist.” Management monitors these loans closely and reviews their performance on a regular basis to assess the level of risk and to ensure that appropriate actions are

being taken to minimize potential loss exposure. Loans identified as being Loss are fully charged off. In addition, the Bank maintains a listing of “classified loans,” of which some loans may be potential problem loans, consisting of Substandard and Doubtful loans which totaled \$5,614,548 at December 31, 2016. Potential problem loans are loans other than nonaccruals, past-dues and troubled debt restructured loans which management has doubt as to the borrower’s ability to comply with the present loan repayment terms.

Management closely monitors the watchlist for signs of deterioration to mitigate the growth in nonaccrual loans. At December 31, 2016, watchlist loans, inclusive of the “classified loans”, totaled \$13,391,639, of which \$9,830,738 are not considered impaired. See Footnote 3, Loans and Allowance for Loan Losses, elsewhere in this report for further discussion on classification of potential problem loans.

### Summary of Loan Loss Experience

The following table is a summary of average loans outstanding during the reported periods, changes in the allowance for loan losses arising from loans charged off and recoveries on loans previously charged off by loan category, and additions to the allowance which have been charged to operating expenses.

	Year Ended December 31,				
	2016	2015	2014	2013	2012
	(Dollars in thousands)				
Average loans outstanding	<u>\$281,006</u>	<u>\$235,939</u>	<u>\$223,295</u>	<u>\$215,040</u>	<u>\$193,532</u>
Amount of allowance for loan losses at beginning of period	<u>\$ 3,032</u>	<u>\$ 3,114</u>	<u>\$ 3,078</u>	<u>\$ 2,845</u>	<u>\$ 3,100</u>
Amount of loans charged off during period:					
Commercial, financial and agricultural	103	264	37	18	286
Real estate:					
Construction	0	0	121	0	249
Commercial	0	0	0	161	9
Residential	4	33	158	46	241
Agricultural	0	0	0	0	0
Consumer & other	<u>9</u>	<u>22</u>	<u>26</u>	<u>9</u>	<u>12</u>
Total loans charged off	<u>116</u>	<u>319</u>	<u>342</u>	<u>234</u>	<u>797</u>
Amount of recoveries during period:					
Commercial, financial and agricultural	28	42	12	23	60
Real estate:					
Construction	0	0	0	0	0
Commercial	0	0	0	5	11
Residential	17	22	30	13	19
Agricultural	0	0	0	0	0
Consumer & other	<u>3</u>	<u>32</u>	<u>6</u>	<u>6</u>	<u>7</u>
Total loans recovered	<u>48</u>	<u>96</u>	<u>48</u>	<u>47</u>	<u>97</u>
Net loans charged off during period	<u>68</u>	<u>223</u>	<u>294</u>	<u>187</u>	<u>700</u>
Additions to allowance for loan losses charged to operating expense during period	<u>160</u>	<u>141</u>	<u>330</u>	<u>420</u>	<u>445</u>
Amount of allowance for loan losses at end of period	<u>\$ 3,124</u>	<u>\$ 3,032</u>	<u>\$ 3,114</u>	<u>\$ 3,078</u>	<u>\$ 2,845</u>
Ratio of net charge-offs during period to average loans outstanding for the period	<u>.02%</u>	<u>.09%</u>	<u>.13%</u>	<u>.09%</u>	<u>.36%</u>

The allowance is based upon management’s analysis of the portfolio under current economic conditions. This analysis includes a study of loss experience, a review of delinquencies, and an estimate of the possibility of loss in view of the risk characteristics of the portfolio. Based on the above factors, management considers the current allowance to be adequate.

### Allocation of Allowance for Loan Losses

Management has allocated the allowance for loan losses within the categories of loans set forth in the table below based on historical experience of net charge-offs. The allowance for loan losses allocated to each category is not necessarily indicative of future losses in any particular category and does not restrict the use of the allowance to absorb losses in other categories. The amount of the allowance applicable to each category and the percentage of loans in each category to total loans are presented below.

Category	December 31, 2016		December 31, 2015		December 31, 2014	
	Allocation	% of Total Loans	Allocation	% of Total Loans	Allocation	% of Total Loans
Commercial, financial and agricultural	\$ 191	24.3%	\$ 145	23.2%	\$ 300	21.3%
Real estate:						
Construction	1,043	8.9%	1,043	7.9%	1,043	5.4%
Commercial	1,192	31.3%	1,192	34.2%	1,192	34.3%
Residential	420	28.5%	382	27.1%	313	30.9%
Agricultural	87	5.7%	86	6.2%	86	6.7%
Consumer & other	<u>191</u>	<u>1.3%</u>	<u>184</u>	<u>1.4%</u>	<u>180</u>	<u>1.4%</u>
Total	\$ <u>3,124</u>	<u>100.0%</u>	\$ <u>3,032</u>	<u>100.0%</u>	\$ <u>3,114</u>	<u>100.0%</u>

Category	December 31, 2013		December 31, 2012	
	Allocation	% of Total Loans	Allocation	% of Total Loans
Commercial, financial and agricultural	\$ 298	20.0%	\$ 310	19.8%
Real estate:				
Construction	1,032	7.3%	1,032	8.3%
Commercial	1,192	36.0%	1,047	34.3%
Residential	301	29.3%	285	30.6%
Agricultural	77	5.8%	0	5.0%
Consumer & other	<u>178</u>	<u>1.6%</u>	<u>171</u>	<u>2.0%</u>
Total	\$ <u>3,078</u>	<u>100.0%</u>	\$ <u>2,845</u>	<u>100.0%</u>

The calculation is based upon total loans including unearned interest and discount. Management believes that the portfolio is diversified and, to a large extent, secured without undue concentrations in any specific risk area. Control of loan quality is regularly monitored by management, the loan committee, and is reviewed by the Bank's Board of Directors which meets monthly. Independent external review of the loan portfolio is provided by examinations conducted by regulatory authorities. The amount of additions to the allowance for loan losses charged to operating expense for the periods indicated were based upon many factors, including actual charge-offs and evaluations of current economic conditions in the market area. Management believes the allowance for loan losses is adequate to cover any potential loan losses.

#### Table 5 - Deposits

The average amounts of deposits for the last three years are presented below.

	Year Ended December 31,		
	2016	2015	2014
		(Dollars in thousands)	
Noninterest-bearing demand deposits	\$113,122	\$ 97,879	\$ 88,882
NOW accounts	17,623	16,963	17,212
Money market deposit accounts	112,435	110,478	104,970
Savings	29,621	29,048	29,638
Time deposits	<u>80,204</u>	<u>76,772</u>	<u>77,565</u>
Total interest-bearing deposits	<u>239,883</u>	<u>233,261</u>	<u>229,385</u>
Total average deposits	\$ <u>353,005</u>	\$ <u>331,140</u>	\$ <u>318,267</u>

The maturity of certificates of deposit of \$100,000 or more as of December 31, 2016, are presented below.

	(Dollars in thousands)
3 months or less	\$ 9,149
Over 3 months through 6 months	12,697
Over 6 months through 12 months	15,115
Over 12 months	<u>6,274</u>
Total outstanding certificates of deposit of \$100,000 or more	\$ <u>43,235</u>

## Return on Equity and Assets

Certain financial ratios are presented below.

	Year Ended December 31,		
	<u>2016</u>	<u>2015</u>	<u>2014</u>
Return on average assets	0.94%	0.85%	0.76%
Return on average equity	10.51%	9.38%	8.74%
Dividend payout (dividends paid divided by net income)	26.53%	30.21%	28.08%
Average equity to average assets	8.90%	9.02%	8.70%

## Forward-Looking Statements

This Annual Report on Form 10-K contains forward-looking statements within the meaning of the federal securities laws. These forward-looking statements are intended to be covered by the safe harbor for forward-looking statements provided by the Private Securities Litigation Reform Act of 1995. Forward-looking statements are not statements of historical fact, and can be identified by the use of forward-looking terminology such as “believes”, “expects”, “may”, “will”, “could”, “should”, “projects”, “plans”, “goal”, “targets”, “potential”, “estimates”, “pro forma”, “seeks”, “intends”, or “anticipates” or the negative thereof or comparable terminology. Forward-looking statements include discussions of strategy, financial projections, guidance and estimates (including their underlying assumptions), statements regarding plans, objectives, expectations or consequences of various transactions, and statements about the future performance, operations, products and services of the Corporation and its subsidiaries. We caution our stockholders and other readers not to place undue reliance on such statements.

The Corporation cautions that there are various factors that could cause actual results to differ materially from the anticipated results or other expectations expressed in any forward-looking statements; accordingly, there can be no assurance that such indicated results will be realized. These factors include risks related to:

- the conditions in the banking system, financial markets, and general economic conditions;
- the Corporation’s ability to raise capital;
- the Corporation’s ability to maintain liquidity or access other sources of funding;
- the Corporation’s construction and land development loans;
- asset quality;
- the adequacy of the allowance for loan losses;
- technology difficulties or failures;
- the Corporation’s ability to execute its business strategy;
- the loss of key personnel;
- competition from financial institutions and other financial service providers;
- the impact of the Dodd-Frank Act and related regulations and other changes in financial services laws and regulations;
- changes in regulatory capital and other requirements;
- changes in regulation and monetary policy;
- losses due to fraudulent and negligent conduct of customers, service providers or employees;
- acquisitions or dispositions of assets or internal restructuring that may be pursued by the Corporation;
- changes in or application of environmental and other laws and regulations to which the Corporation is subject;
- political, legal and local economic conditions and developments;
- financial market conditions and the results of financing efforts;
- changes in commodity prices and interest rates;
- a cybersecurity incident involving the misappropriation, loss or unauthorized disclosure or use of confidential information of our customers; and
- weather, natural disasters and other catastrophic events and other factors discussed in the Corporation’s other filings with the SEC.

The foregoing list of factors is not exclusive, and readers are cautioned not to place undue reliance on any forward-looking statements. The Corporation undertakes no obligation to update or revise any forward-looking statements. Additional information with respect to factors that may cause results to differ materially from those contemplated by such forward-looking statements is included in the Corporation’s current and subsequent filings with the SEC.

## ITEM 1A. RISK FACTORS

An investment in the Corporation’s common stock and the Corporation’s financial results are subject to a number of risks. Investors should carefully consider the risks described below and all other information contained in this Annual Report on Form 10-K and the documents incorporated by reference. Additional risks and uncertainties, including those generally affecting the industry in which the Corporation operates and risks that management currently deems immaterial, may arise or become material in the future and affect the Corporation’s business.



**As a bank holding company, adverse conditions in the general business or economic environment could have a material adverse effect on the Corporation's financial condition and results of operation.**

Weaknesses or adverse changes in business and economic conditions generally or specifically in the markets in which the Corporation operates could adversely impact our business, including causing one or more of the following negative developments:

- a decrease in the demand for loans and other products and services offered by the Corporation;
- a decrease in the value of the Corporation's loans secured by consumer or commercial real estate;
- an impairment of the Corporation's assets, such as its intangible assets, goodwill, or deferred tax assets; or
- an increase in the number of customers or other counterparties who default on their loans or other obligations to the Corporation, which could result in a higher level of nonperforming assets, net charge-offs and provision for loan losses.

For example, if the Corporation is unable to continue to generate, or demonstrate that it can continue to generate, sufficient taxable income in the near future, then it may not be able to fully realize the benefits of its deferred tax assets. Such a development, or one or more other negative developments resulting from adverse conditions in the general business or economic environment, some of which are described above, could have a material adverse effect on the Corporation's financial condition and results of operations.

**The Corporation's ability to raise capital could be limited, affect its liquidity, and could be dilutive to existing stockholders.**

Current conditions in the capital markets are such that traditional sources of capital may not be available to the Corporation on reasonable terms if it needed to raise capital. In such case, there is no guarantee that the Corporation will be able to borrow funds or successfully raise additional capital at all or on terms that are favorable or otherwise not dilutive to existing stockholders.

**Liquidity is essential to the Corporation's businesses and it relies on external sources to finance a significant portion of its operations.**

Liquidity is essential to the Corporation's businesses. The Corporation's capital resources and liquidity could be negatively impacted by disruptions in its ability to access these sources of funding. Factors that the Corporation cannot control, such as disruption of the financial markets or negative views about the financial services industry generally, could impair its ability to raise funding. Other financial institutions may be unwilling to extend credit to banks because of concerns about the banking industry and the economy generally and there may not be a viable market for raising short or long-term debt or equity capital. In addition, the Corporation's ability to raise funding could be impaired if lenders develop a negative perception of its long-term or short-term financial prospects. Such negative perceptions could be developed if the Corporation is downgraded or put on (or remains on) negative watch by the rating agencies, suffers a decline in the level of its business activity or regulatory authorities take significant action against it, among other reasons. If the Corporation is unable to raise funding using the methods described above, it would likely need to finance or liquidate unencumbered assets to meet maturing liabilities. The Corporation may be unable to sell some of its assets, or it may have to sell assets at a discount from market value, either of which could adversely affect its results of operations and financial condition.

**The Corporation's construction and land development loans are subject to unique risks that could adversely affect earnings.**

The Corporation's construction and land development loan portfolio was \$26.0 million at December 31, 2016, comprising 8.9% of total loans. Construction and land development loans are often riskier than home equity loans or residential mortgage loans to individuals. In the event of a general economic slowdown, they would represent higher risk due to slower sales and reduced cash flow that could impact the borrowers' ability to repay on a timely basis. In addition, although regulations and regulatory policies affecting banks and financial services companies undergo continuous change and we cannot predict when changes will occur or the ultimate effect of any changes, there has been recent regulatory focus on construction, development and other commercial real estate lending. Federal policies applicable to construction, development or other commercial real estate loans make us subject to substantial limitations with respect to making such loans, increase the costs of making such loans, and require us to have a greater amount of capital to support this kind of lending, all of which could have a material adverse effect on our profitability or financial condition.

**Recent performance may not be indicative of future performance.**

Various factors, such as economic conditions, regulatory and legislative considerations, competition and the ability to find and retain talented people, may impede the Corporation's ability to remain profitable.

**Deterioration in asset quality could have an adverse impact on the Corporation.**

A significant source of risk for the Corporation arises from the possibility that losses will be sustained because borrowers, guarantors and related parties may fail to perform in accordance with the terms of their loans. With respect to secured loans, the collateral securing the repayment of these loans includes a wide variety of diverse real and personal property that may be affected by changes in prevailing economic, environmental and other conditions, including declines in the value of real estate, changes in interest rates, changes in monetary and fiscal policies of the federal government, environmental contamination and other external events. In addition, decreases in real estate property values due to the nature of the Bank's loan portfolio, over 74% of which is secured by real estate, could affect the ability of customers to repay their loans. The Bank's loan policies and procedures may not prevent unexpected losses that could have a material adverse effect on the Corporation's business, financial condition, results of operations, or liquidity.

**Changes in prevailing interest rates may negatively affect the results of operations of the Corporation and the value of its assets.**

The Corporation's earnings depend largely on the relationship between the yield on earning assets, primarily loans and investments, and the cost of funds, primarily deposits and borrowings. This relationship, known as the interest rate spread, is subject to fluctuation and is affected by economic and competitive factors which influence interest rates, the volume and mix of interest-earning assets and interest-bearing liabilities and the level of nonperforming assets. Fluctuations in interest rates affect the demand of customers for the Corporation's products and services. In addition, interest-bearing liabilities may re-price or mature more slowly or more rapidly or on a different basis than interest-earning assets. Significant fluctuations in interest rates could have a material adverse effect on the Corporation's business, financial condition, results of operations or liquidity.

Changes in the level of interest rates may also negatively affect the value of the Corporation's assets and its ability to realize book value from the sale of those assets, all of which ultimately affect earnings.

**If the Corporation's allowance for loan losses is not sufficient to cover actual loan losses, earnings would decrease.**

The Bank's loan customers may not repay their loans according to their terms and the collateral securing the payment of these loans may be insufficient to assure repayment. The Bank may experience significant loan losses which would have a material adverse effect on the Corporation's operating results. Management makes various assumptions and judgments about the collectability of the loan portfolio, including the creditworthiness of borrowers and the value of the real estate and other assets serving as collateral for the repayment of loans. The Corporation maintains an allowance for loan losses in an attempt to cover any loan losses inherent in the portfolio. In determining the size of the allowance, management relies on an analysis of the loan portfolio based on historical loss experience, volume and types of loans, trends in classification, volume and trends in delinquencies and nonaccruals, national and local economic conditions and other pertinent information. As a result of these considerations, the Corporation has from time to time increased its allowance for loan losses. For the year ended December 31, 2016, the Corporation recorded an allowance for possible loan losses of \$3.12 million, compared with \$3.03 million for the year ended December 31, 2015. If those assumptions are incorrect, the allowance may not be sufficient to cover future loan losses and adjustments may be necessary to allow for different economic conditions or adverse developments in the loan portfolio.

**The Corporation may be subject to losses due to fraudulent and negligent conduct of the Bank's loan customers, third party service providers and employees.**

When the Bank make loans to individuals or entities, they rely upon information supplied by borrowers and other third parties, including information contained in the applicant's loan application, property appraisal reports, title information and the borrower's net worth, liquidity and cash flow information. While they attempt to verify information provided through available sources, they cannot be certain all such information is correct or complete. The Bank's reliance on incorrect or incomplete information could have a material adverse effect on the Corporation's profitability or financial condition.

**Technology difficulties or failures or cyber security breaches of our network security could have a material adverse effect on the Corporation.**

The Corporation depends upon data processing, software, and communication and information exchange on a variety of computing platforms and networks. The computer platforms and network infrastructure we use could be vulnerable to unforeseen hardware and cyber security issues. The Corporation cannot be certain that all of its systems are entirely free from vulnerability to cyber-attack or other technological difficulties or failures. The Corporation relies on the services of a variety of vendors to meet its data processing and communication needs. If information security is breached or other technology difficulties or failures occur, information may be lost or misappropriated, services and operations may be interrupted and the Corporation could subject us to additional regulatory scrutiny, damage our reputation, result in a loss of customers and expose us to claims from customers. Any of these results could have a material adverse effect on the Corporation's business, financial condition, results of operations or liquidity.

**The Corporation's business is subject to the success of the local economies and real estate markets in which it operates.**

The Corporation's banking operations are located in southwest Georgia. Because of the geographic concentration of its operations, the Corporation's success depends largely upon economic conditions in this area, which include volatility in the agricultural market, influx and outflow of major employers in the area, and minimal population growth throughout the region. Deterioration in economic conditions in the communities in which the Corporation operates could adversely affect the quality of the Corporation's loan portfolio and the demand for its products and services, and accordingly, could have a material adverse effect on the Corporation's business, financial condition, results of operations or liquidity. The Corporation is less able than a larger institution to spread the risks of unfavorable local economic conditions across a large number of more diverse economies.

**The Corporation may face risks with respect to its ability to execute its business strategy.**

The financial performance and profitability of the Corporation will depend on its ability to execute its strategic plan and manage its future growth. Moreover, the Corporation's future performance is subject to a number of factors beyond its control, including pending and future federal and state banking legislation, regulatory changes, unforeseen litigation outcomes, inflation, lending and deposit rate changes, interest rate fluctuations, increased competition and economic conditions. Accordingly, these issues could have a material adverse effect on the Corporation's business, financial condition, results of operations or liquidity.

**The Corporation depends on its key personnel, and the loss of any of them could adversely affect the Corporation.**

The Corporation's success depends to a significant extent on the management skills of its existing executive officers and directors, many of whom have held officer and director positions with the Corporation for many years. The loss or unavailability of any of its key personnel,

including DeWitt Drew, President and CEO; John J. Cole, Jr., Executive Vice President and COO; Jeffery E. Hanson, Executive Vice President and CBO; George R. Kirkland, Executive Vice President & CFO; and Danny E. Singley, Executive Vice President and CCO, could have a material adverse effect on the Corporation's business, financial condition, and results of operations or liquidity.

**Competition from financial institutions and other financial service providers may adversely affect the Corporation.**

The banking business is highly competitive, and the Corporation experiences competition in its markets from many other financial institutions. The Corporation competes with these other financial institutions both in attracting deposits and in making loans. Many of its competitors are well-established, larger financial institutions that are able to operate profitably with a narrower net interest margin and have a more diverse revenue base. The Corporation may face a competitive disadvantage as a result of its smaller size, lack of geographic diversification and inability to spread costs across broader markets. There can be no assurance that the Corporation will be able to compete effectively in its markets. Furthermore, developments increasing the nature or level of competition could have a material adverse effect on the Corporation's business, financial condition, results of operations or liquidity.

**The short-term and long-term impact of the changing regulatory capital requirements is uncertain.**

The Basel III Capital Rules include new minimum risk-based capital and leverage ratios, which are being phased in and modify the capital and asset definitions for purposes of calculating those ratios. Among other things, the Basel III Capital Rules established a new common equity Tier 1 minimum capital requirement of 4.5%, a higher minimum Tier 1 capital to risk-weighted assets requirement of 6% and Total capital to risk-weighted assets of 8%. In addition, the final rules provided, to be considered "well-capitalized", a new common equity Tier 1 capital requirement of 6.5% or greater and a higher Tier 1 capital to risk-weighted assets requirement of 8% or greater. Moreover, the final rules limit a banking organization's capital distributions and certain discretionary bonus payments if such banking organization does not hold a "capital conservation buffer" consisting of a 2.5% of common equity Tier 1 capital in addition to the 4.5% minimum common equity Tier 1 requirement and the other amounts necessary to meet the minimum risk-based capital requirements that will be phased in and fully effective in 2019.

The application of the more stringent capital requirements described above could, among other things, result in lower returns on invested capital, require the raising of additional capital, and result in additional regulatory actions if we were to be unable to comply with such requirements. Implementation of changes to asset risk weightings for risk based capital calculations, items included or deducted in calculating regulatory capital and/or additional capital conservation buffers could result in us modifying our business strategy and could limit our ability to make dividends.

**Changes in government regulation or monetary policy could adversely affect the Corporation.**

The Corporation and the banking industry are subject to extensive regulation and supervision under federal and state laws and regulations. The restrictions imposed by such laws and regulations limit the manner in which the Corporation conducts its banking business, undertakes new investments and activities and obtains financing. These regulations are designed primarily for the protection of the deposit insurance funds and consumers and not to benefit holders of the Corporation's securities. Financial institution regulation has been the subject of significant legislation in recent years and may be the subject of further significant legislation in the future, none of which is in the control of the Corporation. Significant new laws or changes in, or repeals of, existing laws could have a material adverse effect on the Corporation's business, financial condition, results of operations or liquidity. Further, federal monetary policy, particularly as implemented through the Federal Reserve, significantly affects credit conditions for the Corporation, and any unfavorable change in these conditions could have a material adverse effect on the Corporation's business, financial condition, results of operations or liquidity. See Part I, Item 1, "Supervision and Regulation."

**ITEM 1B. UNRESOLVED STAFF COMMENTS**

There are no unresolved comments from the SEC staff regarding the Corporation's periodic or current reports under the Exchange Act.

**ITEM 2. PROPERTIES**

The executive offices of the Corporation are located in the SGB Wealth Strategies office at 25 Second Avenue S.W. Moultrie, Georgia. The main banking office and operations center of the Bank are located in a 22,000 square foot facility at 201 First Street, S.E., Moultrie, Georgia. The Trust and Brokerage area are located in the SGB Wealth Strategies office. The Bank's Administrative Services office is located across the street from the main office at 205 Second Street, S.E., Moultrie, Georgia. This building is also used for training and meeting rooms, record storage, and a drive-thru teller facility. The Bank sold Empire's property in Milledgeville, Georgia, in 2016.

<u>Name</u>	<u>Address</u>	<u>Square Feet</u>
Main Office	201 First Street, SE, Moultrie, GA 31768	22,000
Old Operations Center	11 Second Avenue, SW, Moultrie, GA 31768	5,000
SGB Wealth Strategies Office	25 Second Avenue, SW, Moultrie, GA 31768	9,400
Administrative Services	205 Second Street, SE, Moultrie, GA 31768	15,000
Southwest Georgia Ins. Services	501 South Main Street, Moultrie, GA 31768	5,600
Baker County Branch	168 Georgia Highway 91, Newton, GA 39870	4,400
Sylvester Branch	300 North Main Street, Sylvester, GA 31791	12,000
North Valdosta Branch	3500 North Valdosta Road, Valdosta, GA 31602	5,900
Valdosta Commercial Banking Center	3520 North Valdosta Road, Valdosta, GA 31602	10,700
Baytree Branch	1404 Baytree Road, Valdosta, GA 31602	3,000

All of the buildings and land, which include parking and drive-thru teller facilities, are owned by the Bank. There are two automated teller machines on the Bank's main office premises and one in each of the Baker County, Sylvester, North Valdosta and Baytree branch offices. These automated teller machines are linked to the STAR network of automated teller machines. The commercial banking center in Valdosta, Georgia, was completed and opened in August of 2014. The Bank also leases space for a loan production office in Tifton, Georgia. Land has been purchased and regulatory approval was recently received to build a full-service branch office in Tifton, Georgia. The Bank owns a property in Pavo, Georgia, that was formerly a branch office. It is considered bank property held for sale.

### ITEM 3. LEGAL PROCEEDINGS

In the ordinary course of operations, the Corporation, the Bank and Empire are defendants in various legal proceedings. Additionally, in the ordinary course of business, the Corporation, the Bank and Empire are subject to regulatory examinations and investigations. In the opinion of management, there is no pending or threatened proceeding in which an adverse decision will result in a material adverse change in the consolidated financial condition or results of operations of the Corporation. No material proceedings terminated in the fourth quarter of 2016.

### ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

## PART II

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

#### Market Information

The Corporation's common stock trades on the NYSE MKT LLC under the symbol "SGB". The closing price on December 31, 2016, was \$19.99. Below is a schedule of the high and low stock prices for each quarter of 2016 and 2015.

<u>For the Quarter</u>	<u>Fourth</u>	<u>2016</u>		
		<u>Third</u>	<u>Second</u>	<u>First</u>
High	\$19.99	\$17.00	\$15.25	\$15.95
Low	\$15.33	\$14.51	\$14.00	\$13.27
<u>For the Quarter</u>	<u>Fourth</u>	<u>2015</u>		
		<u>Third</u>	<u>Second</u>	<u>First</u>
High	\$15.95	\$15.95	\$16.40	\$15.85
Low	\$14.24	\$13.02	\$13.21	\$12.83

As of December 31, 2016, there were 416 record holders of the Corporation's common stock. Also, there were approximately 485 additional stockholders who held shares through trusts and brokerage firms.

#### Dividends

Cash dividends paid on the Corporation's common stock were \$0.42 per share in 2016 and \$0.40 per share in 2015. Our dividend policy objective is to pay out a portion of earnings in dividends to our stockholders in a consistent manner over time. However, no assurance can be given that dividends will be declared in the future. The amount and frequency of dividends is determined by the Corporation's Board of Directors after consideration of various factors, which include the Corporation's financial condition and results of operations, investment opportunities available to the Corporation, capital requirements, tax considerations and general economic conditions. The primary source of funds available to the parent company is the payment of dividends by its subsidiary bank. Federal and State banking laws restrict the amount of dividends that can be paid without regulatory approval. See Part I, Item 1, "Business – Payment of Dividends." The Corporation and its predecessors have paid cash dividends for the past eighty-eight consecutive years.

#### Share Repurchases

On October 26, 2016, the Corporation announced that its Board of Directors had authorized a program to repurchase up to \$1.75 million of its outstanding shares of common stock through October 31, 2017. Under the program, the shares may be repurchased periodically in open market transactions at prevailing market prices, in privately negotiated transactions, or by other means in accordance with federal securities laws. The actual timing, number and value of shares repurchased under the program depends on a number of factors, including the market price of the Corporation's common stock, general market and economic conditions, and applicable legal requirements. As of December 31, 2016, \$1.74 million of the Corporation's outstanding common stock may be repurchased under the program.

The following table contains information for shares repurchased during the fourth quarter of 2016.

	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number (or Approximate Dollar Value) of Shares that May Yet Be Purchased Under the Plans or Programs
(Dollars in thousands, except for per share amounts)				
October 26, 2016 – October 31, 2016	0	\$ 0.00	0	\$ 1,750
November 1, 2016 – November 30, 2016	400	16.64	400	1,743
December 1, 2016 – December 31, 2016	0	0.00	0	1,743
Total	<u>400</u>	<u>\$ 16.64</u>	<u>400</u>	<u>\$ 1,743</u>

#### Securities Authorized for Issuance Under Equity Compensation Plans

The following table presents information as of December 31, 2016, with respect to shares of common stock of the Corporation that may be issued under the Key Individual Stock Option Plan, the Director's and Executive Officers Stock Purchase Plan, and the 2013 Omnibus Incentive Plan. No additional option shares can be granted under the Key Individual Stock Option Plan.

Plan Category	Number of Securities to be Issued upon Exercise of Outstanding Options	Weighted Average Exercise Price of Outstanding Options	Number of Securities Remaining Available for Future Issuance Under Equity Compensation Plans
Equity compensation plans approved by stockholders <sup>(1)</sup>	0	\$0.00	379,217
Equity compensation plans not approved by stockholders <sup>(2)</sup>	0	0.00	0
Total	<u>0</u>	<u>\$0.00</u>	<u>379,217</u>

(1) The Key Individual Stock Option Plan, the Directors and Executive Officers Stock Purchase Plan, and the 2013 Omnibus Incentive Plan.

(2) Excludes shares issued under the 401(k) Plan.

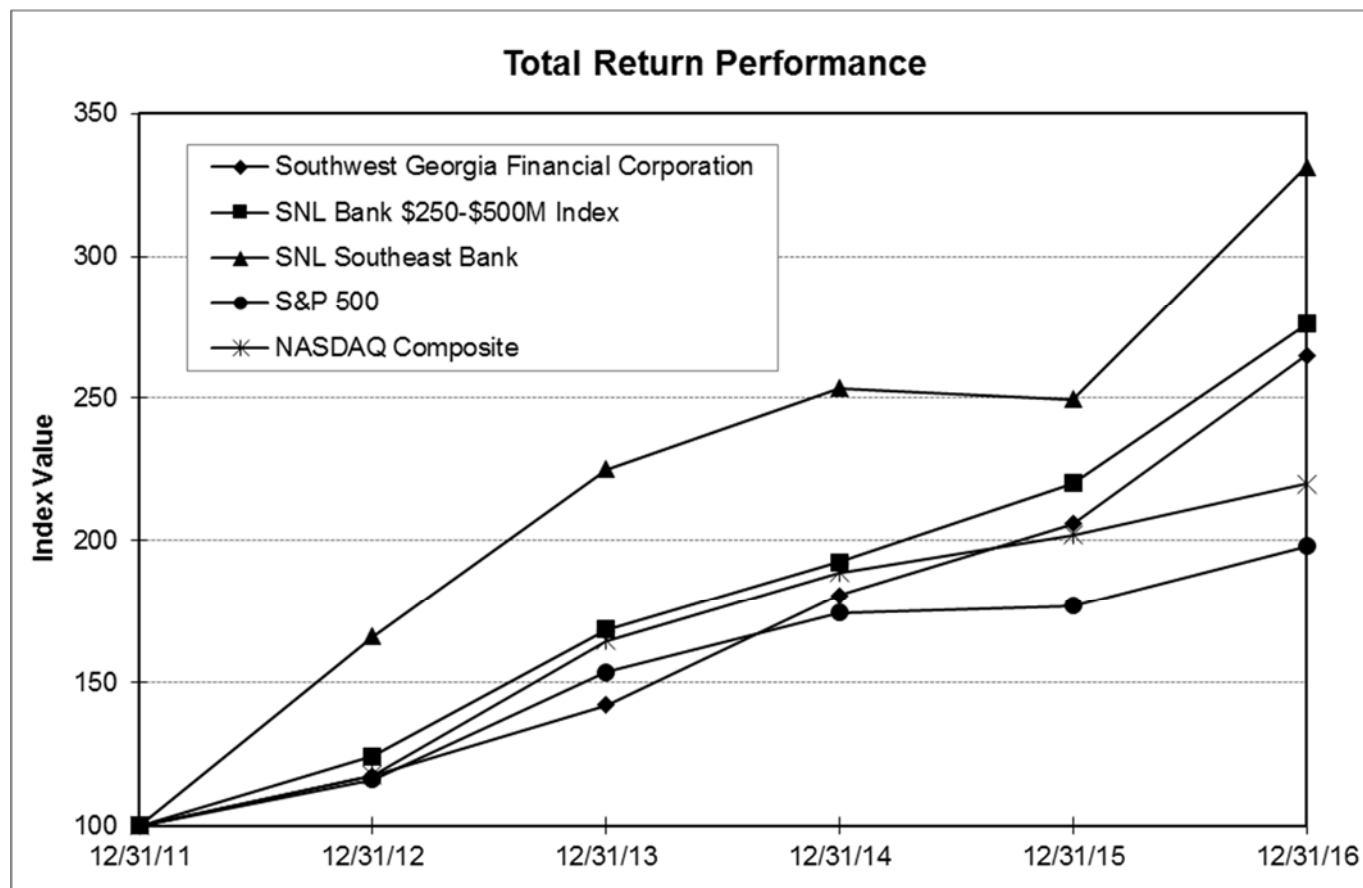
#### Sales of Unregistered Securities

The Corporation has not sold any unregistered securities in the past three years.

## Performance Graph

The following graph compares the cumulative total stockholder return of the Corporation's common stock with SNL's Southeast Bank Index, SNL Bank \$250M-\$500M Index, the S&P 500 Index and the NASDAQ Composite Index. SNL's Southeast Bank Index is a compilation of the total return to stockholders over the past five years of a group of 85 banks located in the southeastern states of Alabama, Arkansas, Florida, Georgia, Mississippi, North Carolina, South Carolina, Tennessee, Virginia, and West Virginia. The SNL Bank \$250M-\$500M Index is a compilation of the total return to stockholders over the past five years of a group of eight banks in the United States with assets between \$250 million and \$500 million. The comparison assumes \$100 was invested January 1, 2011, and that all semi-annual and quarterly dividends were reinvested each period. The comparison takes into consideration changes in stock price, cash dividends, stock dividends, and stock splits since December 31, 2010.

The comparisons in the graph are required by the SEC and are not intended to forecast or be indicative of possible future performance of the Corporation's Common Stock.



Index	Period Ending					
	12/31/11	12/31/12	12/31/13	12/31/14	12/31/15	12/31/16
Southwest Georgia Financial Corporation	100.00	117.35	142.06	180.55	205.84	265.00
SNL Bank \$250M-\$500M Index	100.00	124.13	168.55	192.33	220.05	276.11
SNL Southeast Bank Index	100.00	166.11	225.10	253.52	249.57	331.30
S&P 500 Index	100.00	116.00	153.57	174.60	177.01	198.18
NASDAQ Composite Index	100.00	117.45	164.57	188.84	201.98	219.89

## ITEM 6. SELECTED FINANCIAL DATA

Not applicable.

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

### **Overview**

The Corporation is a full-service community bank holding company headquartered in Moultrie, Georgia. The community of Moultrie has been served by the Bank since 1928. We provide comprehensive financial services to consumer, business and governmental customers, which, in addition to conventional banking products, include a full range of mortgage banking, trust, retail brokerage and insurance services. Our primary market area incorporates Colquitt County, where we are headquartered, as well as Baker, Lowndes, Tift and Worth Counties, each contiguous with Colquitt County, and the surrounding counties of southwest Georgia. We have five full service banking facilities, six automated teller machines, and a loan production office in Tifton, Georgia.

Our strategy is to:

- maintain the diversity of our revenue, including both interest and noninterest income through a broad base of business;
- strengthen our sales and marketing efforts while developing our employees to provide the best possible service to our customers;
- expand our market share where opportunity exists; and
- grow outside of our current geographic market either through de-novo branching or acquisitions into areas proximate to our current market area.

We believe that investing in sales and marketing in this challenging market will provide us with a competitive advantage. To that end, about six years ago, we began expanding geographically in Valdosta, Georgia, with two full-service banking centers, a mortgage origination office, and most recently added a commercial banking center in August 2014. Continuing to expand our geographical footprint, in January 2016, a loan production office was opened in the neighboring community of Tifton, Georgia. We recently received regulatory approval to add a full-service branch in Tifton, Georgia.

The Corporation's profitability, like most financial institutions, is dependent to a large extent upon net interest income, which is the difference between the interest received on earning assets and the interest paid on interest-bearing liabilities. The Corporation's earning assets are primarily loans, securities, and short-term interest-bearing deposits with banks, and the interest-bearing liabilities are principally customer deposits and borrowings. Net interest income is highly sensitive to fluctuations in interest rates. To address interest rate fluctuations, we manage our balance sheet in an effort to diminish the impact should interest rates suddenly change.

Broadening our revenue sources helps to reduce the risk and exposure of our financial results to the impact of changes in interest rates, which are outside of our control. Sources of noninterest income include our insurance agency, fees on customer accounts, and trust and retail brokerage services through our Wealth Strategies division. In 2016, noninterest income, at 20.4% of the Corporation's total revenue, increased mostly due to gains on the sale of securities and increased income from insurance services when compared with 2015.

Our profitability is also impacted by operating expenses such as salaries, employee benefits, occupancy, and income taxes. Our lending activities are significantly influenced by regional and local factors such as changes in population, competition among lenders, interest rate conditions and prevailing market rates on competing uses of funds and investments, customer preferences and levels of personal income and savings in the Corporation's primary market area.

Although the economy is slowly recovering, regulatory burdens continue to outpace growth opportunities. Despite those challenges, we will continue to focus on our customers and believe that our strategic positioning, strong balance sheet and capital levels position us to sustain our franchise, capture market share and build customer loyalty.

At the end of 2016, the Corporation's nonperforming assets decreased to \$373 thousand from \$1.629 million at December 31, 2015, due to decreases of \$1.3 million in nonaccrual loans which were partially offset by an increase of \$45 thousand in foreclosed assets when compared to the end of 2015.

### **Critical Accounting Policies**

In the course of the Corporation's normal business activity, management must select and apply many accounting policies and methodologies that lead to the financial results presented in the consolidated financial statements of the Corporation. Management considers the accounting policy relating to the allowance for loan losses to be a critical accounting policy because of the uncertainty and subjectivity inherent in estimating the levels of allowance needed to cover probable credit losses within the loan portfolio and the material effect that these estimates have on the Corporation's results of operations. We believe that the allowance for loan losses as of December 31, 2016, is adequate; however, under adverse conditions or assumptions, future additions to the allowance may be necessary. There have been no significant changes in the methods or assumptions used in our accounting policies that would have resulted in material estimates and assumptions changes. Note 1 to the Consolidated Financial Statements provides a description of our significant accounting policies and contributes to the understanding of how our financial performance is reported.

### **Results of Operations**

#### *Performance Summary*

For the year ended December 31, 2016, net income was \$4.03 million, up \$660 thousand from net income of \$3.37 million for 2015. The improvement in net income was primarily due to a \$1.67 million increase in net interest income after provision for loan losses. Interest income and fees on loans increased \$2.10 million due to a \$45.1 million increase in average loan volume. Also, positively impacting our

net income was a \$199 thousand increase in noninterest income compared to 2015. Partially offsetting these improvements in net earnings was an increase in salaries and employee benefits of \$852 thousand due to investment in personnel for the expanding Valdosta and Tifton markets compared with the prior year. Interest expense also increased \$295 thousand mainly due to increased average borrowings and higher interest rates on deposits. On a per share basis, we had a net income of \$1.58 per diluted share for 2016 compared with a net income of \$1.32 per diluted share for 2015.

For the year ended December 31, 2015, net income was \$3.37 million, up \$470 thousand from net income of \$2.90 million for 2014. The improvement in net income was primarily due to a \$943 thousand increase in net interest income after provision for loan losses. Interest income and fees on loans increased \$560 thousand due to greater loan volume while interest expense declined \$39 thousand due to lower interest paid on borrowings. Also, positively impacting our net income was a \$189 thousand decrease in the provision for loan losses and lower salaries and employee benefits of \$445 thousand compared to 2014. The decrease in salaries and employee benefits is a result of duties and responsibilities of retirees being absorbed by other personnel as well as a decrease in contributions to employee benefit plans. Partially offsetting these improvements in net earnings was declining income from mortgage banking services of \$327 thousand as well as lower gains on sale of securities compared with 2014. On a per share basis, we had a net income of \$1.32 per diluted share for 2015 compared with a net income of \$1.14 per diluted share for 2014.

We measure our performance on selected key ratios, which are provided in the following table:

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Return on average total assets	0.94%	0.85%	0.76%
Return on average stockholders' equity	10.51%	9.38%	8.74%
Average stockholders' equity to average total assets	8.90%	9.02%	8.70%
Net interest margin (tax equivalent)	4.14%	4.04%	3.99%

### **Net Interest Income**

Net interest income after provision for loan losses increased \$1.67 million, or 12.0%, to \$15.64 million for 2016 when compared with 2015. Total interest income increased \$2.0 million which more than offset an increase in total interest expense of \$295 thousand. The Corporation recognized a \$160 thousand provision for loan losses in 2016, a \$19 thousand increase compared with \$141 thousand in 2015. Interest income and fees on loans increased \$2.1 million when compared with 2015 resulting from growth in average loans of \$45.1 million. Interest on deposits in other banks also increased \$41 thousand compared with the same period last year. Partially offsetting these increases in net interest income, interest paid on total borrowings increased by \$156 thousand when compared with the prior year, and interest paid on deposits increased \$139 thousand to \$935 thousand at the end of 2016. The average rate paid on average time deposits of \$80.2 million increased 11 basis points when compared with 2015. Also, decreases of \$146 thousand in interest income on investment securities were mainly due to a decline in average investment securities volume of \$11.1 million compared with 2015.

For the year 2015, net interest income after provision for loan losses increased \$943 thousand, or 7.2%, to \$13.97 million when compared with 2014. While total interest income increased \$716 thousand, total interest expense decreased \$39 thousand. The Corporation recognized a \$141 thousand provision for loan losses in 2015, a \$189 thousand decrease compared with \$330 thousand in 2014. Interest income and fees on loans increased \$560 thousand when compared with 2014 resulting from an average increase in loans of \$12.6 million. Interest income on investment securities increased \$146 thousand mainly due to an increase in overall yield of 9 basis points compared with 2014. Also contributing to the increase in net interest income, interest paid on total borrowings declined by \$85 thousand when compared with 2014, and interest paid on deposits increased \$46 thousand to \$796 thousand at the end of 2014. The average rate paid on average time deposits of \$76.8 million increased 5 basis points when compared with 2014.

### **Net Interest Margin**

Net interest margin, which is the net return on earning assets, is a key performance ratio for evaluating net interest income. It is computed by dividing net interest income by average total earning assets.

Net interest margin increased 10 basis points to 4.14% for 2016 when compared with 2015. The increase in net interest margin was primarily impacted by the large increase in loan volume. Net interest margin was 4.04% for 2015, a 5 basis point increase from 3.99% in 2014.



## Noninterest Income

Noninterest income is an important contributor to net earnings. The following table summarizes the changes in noninterest income during the past three years:

	2016		2015		2014	
	Amount	% Change	Amount	% Change	Amount	% Change
Service charges on deposit accounts	\$ 1,086	(3.1)%	\$ 1,121	(12.1)%	\$ 1,275	(0.2)%
Income from trust services	210	(14.3)	245	1.7	241	5.7
Income from retail brokerage services	342	(18.8)	421	12.0	376	11.2
Income from insurance services	1,478	7.7	1,373	3.7	1,324	(0.3)
Income from mortgage banking services	354	11.3	318	(50.7)	645	(31.4)
Gain on the sale or disposition of assets	38	72.7	22	(75.3)	89	230.9
Gain on the sale of securities	169	NM	4	(98.6)	293	(6.1)
Other income	<u>782</u>	3.4	<u>756</u>	1.7	<u>743</u>	1.1
Total noninterest income	\$ <u>4,459</u>	4.7 %	\$ <u>4,260</u>	(14.6)%	\$ <u>4,986</u>	(2.1)%

\*NM = not meaningful

For 2016, noninterest income was \$4.46 million, up from \$4.26 million in the same period of 2015. The increase was primarily attributed to a \$169 thousand gain on the sale of securities compared with a \$4 thousand gain in 2015. Also, income from insurance services and mortgage banking services increased \$105 thousand and \$36 thousand, respectfully, when compared with last year. These increases were partially offset by decreases in income from retail brokerage services, trust services and service charges on deposit accounts of \$79 thousand, \$35 thousand, and \$35 thousand, respectfully, when compared with 2015.

For 2015, noninterest income was \$4.26 million, down from \$4.99 million in the same period of 2014. The decrease was primarily attributed to a \$327 thousand decrease in income from mortgage banking services. Also, net gains on the sale of securities, service charges on deposit accounts, and net gains on the sale or disposition of assets were less than 2014 by \$290 thousand, \$153 thousand and \$66 thousand, respectfully, when compared with 2014. These decreases were partially offset by increases in income from insurance, retail brokerage, and trust services of \$49 thousand, \$45 thousand, and \$4 thousand, respectfully, when compared with 2014.

## Noninterest Expense

Noninterest expense includes all expenses of the Corporation other than interest expense, provision for loan losses and income tax expense. The following table summarizes the changes in the noninterest expenses for the past three years:

	2016		2015		2014	
	Amount	% Change	Amount	% Change	Amount	% Change
Salaries and employee benefits	\$ 8,766	10.8 %	\$ 7,914	(5.3)%	\$ 8,359	(1.1)%
Occupancy expense	1,140	1.7	1,121	5.7	1,061	3.5
Equipment expense	861	(6.7)	923	3.0	896	(0.7)
Data processing expense	1,368	11.8	1,224	8.3	1,130	3.0
Amortization of intangible assets	16	0.0	16	(64.4)	45	(79.2)
Other operating expenses	<u>2,763</u>	(2.4)	<u>2,832</u>	(1.6)	<u>2,879</u>	8.6
Total noninterest expense	\$ <u>14,914</u>	6.3 %	\$ <u>14,030</u>	(2.4) %	\$ <u>14,370</u>	0.2 %

Noninterest expense increased \$884 thousand to \$14.91 million in 2016 compared with the same period in 2015. Salaries and employee benefits increased \$852 thousand when compared with 2015 as a result of new personnel in our Valdosta and Tifton markets as well as new staff needed in connection with the upcoming retirement of critical staff. Data processing and occupancy expense also increased \$144 thousand and \$19 thousand, respectively, compared with 2015. Partially offsetting these increases were decreases in other operating and equipment expense of \$69 thousand and \$62 thousand, respectively, compared with 2015.

For 2015, noninterest expense decreased \$340 thousand to \$14.03 million in 2015 compared with the same period in 2014. Salaries and employee benefits, other operating, and amortization of intangible assets decreased \$445 thousand, \$48 thousand, and \$29 thousand, respectively, when compared with 2014. The decrease in salaries and employee benefits is a result of duties and responsibilities of retirees being absorbed by other personnel as well as a decrease in contribution to the employee benefit plan. Partially offsetting these decreases were increases in data processing, occupancy, and equipment expense of \$95 thousand, \$60 thousand and \$27 thousand, respectively, compared with 2014.

The efficiency ratio, (noninterest expense divided by total noninterest income plus tax equivalent net interest income), a measure of productivity, decreased to 70.6% for 2016 when compared with 73.0% and 75.4% for the years 2015 and 2014, respectively. The improvement in the efficiency ratio for 2016 resulted from growth in interest income which more than offset the increase in noninterest expense compared with 2015. The improvement in the efficiency ratio for 2015 resulted from growth in interest income while noninterest expense declined when compared with 2014.

## Federal Income Tax Expense

The Corporation had an expense of \$1.15 million for federal income taxes in 2016 compared with an expense of \$827 thousand in 2015

and \$740 thousand for the year ending December 31, 2014. These amounts resulted in an effective tax rate of 22.2%, 19.7%, and 20.3%, for 2016, 2015, and 2014, respectively. See Note 10 of the Corporation's Notes to Consolidated Financial Statements for further details of tax expense.

## Uses and Sources of Funds

The Corporation, primarily through the Bank, acts as a financial intermediary. As such, our financial condition should be considered in terms of how we manage our sources and uses of funds. Our primary sources of funds are deposits and borrowings. We invest our funds in assets, and our earning assets are what provide us income.

Total average assets increased \$32.5 million to \$431.1 million in 2016 compared with 2015. The increase in total average assets is primarily attributable to an increase in average loans of \$45.1 million partially offset by a decrease in average investment securities of \$11.1 million. The Corporation's earning assets, which include loans, investment securities, certificates of deposit with other banks and interest-bearing deposits with banks, averaged \$402.1 million in 2016, a 9% increase from \$369.9 million in 2015. The average volume for total deposits increased \$21.9 million mostly due to an increase in non-interest bearing deposits of \$15.2 million compared with the prior year. For 2016, average earning assets were comprised of 69% loans, 26% investment securities, and 5% deposit balances with banks. The ratio of average earning assets to average total assets increased to 93.3% for 2016 compared with 92.8% for 2015.

## Loans

Loans are one of the Corporation's largest earning assets and uses of funds. Because of the importance of loans, most of the other assets and liabilities are managed to accommodate the needs of the loan portfolio. During 2016, average net loans represented 69% of average earning assets and 64% of average total assets.

The composition of the Corporation's loan portfolio at December 31, 2016, 2015, and 2014 was as follows:

Category	2016		2015		2014	
	Amount	% Change	Amount	% Change	Amount	% Change
Commercial, financial, and agricultural	\$ 70,999	22.1 %	\$ 58,173	21.5 %	\$ 47,861	9.6 %
Real estate:						
Construction	25,999	31.1	19,831	61.8	12,257	(22.7)
Commercial	91,733	6.9	85,777	11.5	76,916	(2.3)
Residential	83,271	22.5	67,969	(1.9)	69,305	7.6
Agricultural	16,580	6.2	15,620	4.2	14,996	19.0
Consumer & other	<u>3,961</u>	15.3	<u>3,435</u>	11.1	<u>3,091</u>	(10.9)
Total loans	\$292,543	16.6	\$250,805	11.8	\$224,426	2.6
Unearned interest and discount	(19)	0.0	(19)	(26.9)	(26)	0.0
Allowance for loan losses	<u>(3,124)</u>	3.0	<u>(3,032)</u>	(2.6)	<u>(3,114)</u>	(1.2)
Net loans	<u>\$289,400</u>	16.8 %	<u>\$247,754</u>	11.9 %	<u>\$221,286</u>	2.6 %

Total year-end balances of loans increased \$41.6 million while average total loans increased \$45.1 million in 2016 compared with 2015. All real estate loan categories as well as commercial, financial and agricultural, and consumer loans experienced growth in 2016. The ratio of total loans to total deposits at year end increased to 78.7% in 2016 compared with 73.9% in 2015. The loan portfolio mix at year-end 2016 consisted of 8.9% loans secured by construction real estate, 31.4% loans secured by commercial real estate, 28.4% of loans secured by residential real estate, and 5.7% of loans secured by agricultural real estate. The loan portfolio also included other commercial, financial, and agricultural purposes of 24.3% and installment loans to individuals for consumer purposes of 1.3%.

## Allowance and Provision for Possible Loan Losses

The allowance for loan losses represents our estimate of the amount required for probable loan losses in the Corporation's loan portfolio. Loans, or portions thereof, which are considered to be uncollectible are charged against this allowance and any subsequent recoveries are credited to the allowance. There can be no assurance that the Corporation will not sustain losses in future periods which could be substantial in relation to the size of the allowance for loan losses at December 31, 2016.

We have a loan review program in place which provides for the regular examination and evaluation of the risk elements within the loan portfolio. The adequacy of the allowance for loan losses is regularly evaluated based on the review of all significant loans with particular emphasis on non-accruing, past due, and other potentially impaired loans that have been identified as possible problems.

The allowance for loan losses was \$3.124 million, or 1.1% of total loans outstanding, as of December 31, 2016. This level represented a \$92 thousand increase from the corresponding 2015 year-end amount, which was 1.2% of total loans outstanding.

There was a provision for loan losses of \$160 thousand in 2016 compared with a provision for loan losses of \$141 thousand in 2015. See Part I, Item 1, "Table 4 – Loan Portfolio" of the Guide 3 for details of the changes in the allowance for loan losses.

## Investment Securities

The investment portfolio serves several important functions for the Corporation. Investments in securities are used as a source of income

for excess liquidity that is not needed for loan demand and to satisfy pledging requirements in the most profitable way possible. The investment portfolio is a source of liquidity when loan demand exceeds funding availability, and is a vehicle for adjusting balance sheet sensitivity to cushion against adverse rate movements. Our investment policy attempts to provide adequate liquidity by maintaining a portfolio with significant cash flow for reinvestment. The Corporation's investment securities represent 24.5% of our assets and 53% of the portfolio includes largely state, county and municipal securities. Also, the portfolio includes 38% of U.S. government agency securities, 6% of U.S. government sponsored pass-thru residential mortgage-backed securities, 2% of corporate notes, and 1% of U.S. government treasury securities.

The following table summarizes the contractual maturity of investment securities at their carrying values as of December 31, 2016:

<u>Amounts Maturing In:</u>	<u>Securities Available for Sale</u>	<u>Securities Held to Maturity</u> (Dollars in thousands)	<u>Total</u>
One year or less	\$ 0	\$ 7,940	\$ 7,940
After one through five years	10,304	26,537	36,841
After five through ten years	39,508	15,179	54,687
After ten years	<u>3,641</u>	<u>4,947</u>	<u>8,588</u>
Total debt investment securities	53,453	54,603	108,056
Equity securities	<u>112</u>	<u>0</u>	<u>112</u>
Total investment securities	<u>\$ 53,565</u>	<u>\$ 54,603</u>	<u>\$ 108,168</u>

At year-end 2016, the total investment portfolio decreased to \$108.2 million, down \$4.2 million, compared with \$112.4 million at year-end 2015. The decrease was mainly due to calls and maturities of \$14.1 million of municipal securities and U.S. government agency securities as well as residential mortgage-backed securities principal paydowns of \$2.2 million. Additionally, we sold \$11.9 million of available for sale U.S. government agency securities and residential mortgage-backed securities and \$577 thousand of held to maturity residential mortgage-backed securities resulting in a net gain of \$144 thousand and \$25 thousand, respectively. These small lots of held to maturity mortgage-backed securities sold were paid down by over 85% of face value. Partially offsetting these calls, maturities and sales were purchases of \$25.6 million of U.S. government agency securities and municipal securities.

We will continue to actively manage the size, components, and maturity structure of the investment securities portfolio. Future investment strategies will continue to be based on profit objectives, economic conditions, interest rate risk objectives, and balance sheet liquidity demands.

### **Nonperforming Assets**

Nonperforming assets are defined as nonaccrual loans, loans that are 90 days past due and still accruing, other-than-temporarily impaired preferred stock, and property acquired by foreclosure. The level of nonperforming assets decreased \$1.3 million at year-end 2016 compared with year-end 2015 due to a decrease of \$1.3 million in nonaccrual loans. Partially offsetting this decrease was an increase of \$45 thousand in foreclosed assets. Nonperforming assets were approximately \$373 thousand, or 0.08% of total assets as of December 31, 2016, compared with \$1.629 million or 0.39% of total assets at year-end 2015.

### **Deposits and Other Interest-Bearing Liabilities**

Our primary source of funds is deposits. The Corporation offers a variety of deposit accounts having a wide range of interest rates and terms. We rely primarily on competitive pricing policies and customer service to attract and retain these deposits.

In 2016, average deposits increased from \$331.1 million in 2015 to \$353.0 million. This average deposit growth occurred primarily in noninterest bearing deposits. As of December 31, 2016, the Corporation's balance of certificates of deposit of \$100,000 or more increased to \$43.2 million from \$25.2 million at the end of 2015.

We have used borrowings from the Federal Home Loan Bank to support our residential mortgage lending activities. During 2016, the Corporation borrowed \$6 million in principal reducing credit advances, \$3 million in fixed rate credit advances, repaid \$3 million of the fixed-rate advances, and made an annual installment payments of \$7.6 million on two principal reducing credit advances from the Federal Home Loan Bank. During 2017, we expect to make annual installment payments totaling \$8.4 million on principal reducing credit advances. Total long-term advances with the Federal Home Loan Bank were \$26.0 million at December 31, 2016. Two of these advances totaling \$10 million have convertible options by the issuer to convert the rates to a 3-month LIBOR. The Corporation intends to pay off these advances at the conversion dates. Details on the Federal Home Loan Bank advances are presented in Notes 7 and 8 to the financial statements.

### **Liquidity**

Liquidity is managed to assume that the Bank can meet the cash flow requirements of customers who may be either depositors wanting to withdraw their funds or borrowers needing funds to meet their credit needs. Many factors affect the ability to accomplish liquidity objectives successfully. Those factors include the economic environment, our asset/liability mix and our overall reputation and credit standing in the marketplace. In the ordinary course of business, our cash flows are generated from deposits, interest and fee income, loan repayments and the maturity or sale of other earning assets.

The Corporation is a separate entity from the Bank and provides for its own liquidity. The Corporation is responsible for the payment of dividends declared for stockholders, and interest and principal on its outstanding debt. Substantially, all of the Corporation's liquidity is

obtained from dividends from the Bank.

The Consolidated Statement of Cash Flows details the Corporation's cash flows from operating, investing, and financing activities. During 2016, operating and financing activities provided cash flows of \$35.0 million, while investing activities used \$39.6 million resulting in a decrease in cash and cash equivalents balances of \$4.6 million.

Liability liquidity represents our ability to renew or replace our short-term borrowings and deposits as they mature or are withdrawn. The Bank's deposit mix includes a significant amount of core deposits. Core deposits are defined as total deposits less time deposits of \$100,000 or more. These funds are relatively stable because they are generally accounts of individual customers who are concerned not only with rates paid, but with the value of the services they receive, such as efficient operations performed by helpful personnel. Total core deposits were 88.4% of total deposits on December 31, 2016, compared with 92.6% in 2015.

Asset liquidity is provided through ordinary business activity, such as cash received from interest and fee payments as well as from maturing loans and investments. Additional sources include marketable securities and short-term investments that are easily converted into cash without significant loss. The Bank had \$7.9 million of investment securities maturing within one year or less on December 31, 2016, which represented 7.4% of the investment debt securities portfolio. Also, the Bank has \$4.6 million of U.S. government agency securities callable at the option of the issuer within one year and approximately \$1.5 million of expected annual cash flow in principal reductions from payments of mortgage-backed securities. In 2016, \$9.6 million of our callable U.S. government agency securities were called and \$3.0 million were called in 2015. We have reinvested these proceeds from called investment securities in new loans and new investment securities. We are not aware of any other known trends, events, or uncertainties that will have or that are reasonably likely to have a material adverse effect on the Corporation's liquidity or operations.

### Contractual Obligations

The chart below shows the Corporation's contractual obligations and its scheduled future cash payments under those obligations as of December 31, 2016.

The majority of the Corporation's outstanding contractual obligations are long-term debt. The remaining contractual are comprised of purchase obligations for data processing services and a rental agreement for our loan production office in Tifton, Georgia. We have no capital lease obligations.

	Payments Due by Period				
	(Dollars in thousands)				
	Total	Less than 1 Year	1-3 Years	4-5 Years	After 5 Years
Contractual Obligations					
Long-term debt	\$26,029	\$ 0	\$18,429	\$5,029	\$2,571
Operating leases	36	21	10	5	0
Total contractual obligations	<u>\$26,065</u>	<u>\$ 21</u>	<u>\$18,439</u>	<u>\$5,034</u>	<u>\$2,571</u>

### Off-Balance Sheet Arrangements

We are a party to financial instruments with off-balance-sheet risk which arise in the normal course of business to meet the financing needs of our customers. These financial instruments include commitments to extend credit in the form of loans or through letters of credit. The instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amounts recognized in the financial statements. Since many of the commitments to extend credit and standby letters of credit are expected to expire without being drawn upon, the contractual amounts do not necessarily represent future cash requirements.

Financial instruments whose contract amounts represent credit risk:	2016	2015
	(Dollars in thousands)	
Commitments to extend credit	\$ 34,031	\$ 24,780
Standby letters of credit	\$ 2,660	\$ 960

The Corporation does not have any special purpose entities or off-balance sheet financing payment obligations.

### Capital Resources and Dividends

Our average equity to average assets ratio was 8.90% in 2016 and 9.02% in 2015. The Federal Reserve Board and the FDIC have issued rules regarding risk-based capital requirements for U.S. banks and bank holding companies. The Basel III Capital Rules set forth changes in the methods of calculating certain risk-weighted assets, which in turn affect the calculation of risk-based ratios. The new risk weightings are more punitive for assets held by banks that are deemed to be of higher risk. The minimum capital level requirements applicable to the Bank under the Basel III Capital Rules are: (i) a common equity Tier 1 risk-based capital ratio of 4.5%; (ii) a Tier 1 risk-based capital ratio of 6%; (iii) a Total risk-based capital ratio of 8%; and (iv) Tier 1 leverage ratio of 4%. Common equity Tier 1 capital consists of retained earnings and common stock instruments, subject to certain adjustments. At year-end 2016, we were well in excess of the minimum requirements under the guidelines with a common equity Tier 1 capital ratio of 13.03%, Tier 1 risk-based capital ratio of 13.03%, Total risk-based capital ratio of 14.04%, and a leverage ratio of 8.87%. To continue to conduct its business as currently conducted, the Corporation and the Bank will need to maintain capital well above the minimum levels.

The following table presents the risk-based capital and leverage ratios at December 31, 2016 and 2015 in comparison to both the minimum regulatory guidelines and the minimum for well capitalized:

<u>Risk Based Capital Ratios</u>	<u>Southwest Georgia Financial Corporation</u>		<u>Southwest Georgia Bank</u>		<u>Minimum Regulatory Guidelines</u>	<u>Minimum For Well Capitalized</u>
	<u>2016</u>	<u>2015</u>	<u>2016</u>	<u>2015</u>		
Common Equity Tier 1	13.03%	14.07%	12.47%	12.99%	5.13%	≥ 6.50%
Tier I capital	13.03%	14.07%	12.47%	12.99%	6.63%	≥ 8.00%
Total risk-based capital	14.04%	15.22%	13.48%	14.14%	8.63%	≥ 10.00%
Leverage	8.87%	9.13%	8.49%	8.43%	4.00%	≥ 5.00%

### **Interest Rate Sensitivity**

The Corporation's most important element of asset/liability management is the monitoring of its sensitivity and exposure to interest rate movements which is the Corporation's primary market risk. We have no foreign currency exchange rate risk, commodity price risk, or any other material market risk. The Corporation has no trading investment portfolio, nor do we have any interest rate swaps or other derivative instruments.

Our primary source of earnings, net interest income, can fluctuate with significant interest rate movements. To lessen the impact of these movements, we seek to maximize net interest income while remaining within prudent ranges of risk by practicing sound interest rate sensitivity management. We attempt to accomplish this objective by structuring the balance sheet so that the differences in repricing opportunities between assets and liabilities are minimized. Interest rate sensitivity refers to the responsiveness of earning assets and interest-bearing liabilities to changes in market interest rates. The Corporation's interest rate risk management is carried out by the Asset/Liability Management Committee which operates under policies and guidelines established by the Bank's Board of Directors. The principal objective of asset/liability management is to manage the levels of interest-sensitive assets and liabilities to minimize net interest income fluctuations in times of fluctuating market interest rates. To effectively measure and manage interest rate risk, the Corporation uses computer simulations that determine the impact on net interest income of numerous interest rate scenarios, balance sheet trends and strategies. These simulations cover the following financial instruments: short-term financial instruments, investment securities, loans, deposits, and borrowings. These simulations incorporate assumptions about balance sheet dynamics, such as loan and deposit growth and pricing, changes in funding mix, and asset and liability repricing and maturity characteristics. Simulations are run under various interest rate scenarios to determine the impact on net income and capital. From these computer simulations, interest rate risk is quantified and appropriate strategies are developed and implemented. The Corporation also maintains an investment portfolio which receives monthly cash flows from mortgage-backed securities principal payments, and staggered maturities and provides flexibility over time in managing exposure to changes in interest rates. Any imbalances in the repricing opportunities at any point in time constitute a financial institution's interest rate sensitivity.

### **ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

Not applicable.

### **ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA**

The information required by this item is filed herewith.

## Management's Report on Internal Control over Financial Reporting

Management of the Corporation is responsible for establishing and maintaining effective internal control over financial reporting. Internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with GAAP.

Under the supervision and with the participation of management, including the principal executive officer and principal financial officer, the Corporation conducted an evaluation of the effectiveness of internal control over financial reporting based on the framework in *Internal Control over Financial Reporting - Guidance for Smaller Public Companies* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this evaluation under the above framework, management of the Corporation has concluded the Corporation maintained effective internal control over financial reporting, as such term is defined in Securities Exchange Act of 1934 Rule 13a-15(f), as of December 31, 2016. Internal control over financial reporting cannot provide absolute assurance of achieving financial reporting objectives because of its inherent limitations. Internal control over financial reporting is a process that involves human diligence and compliance and is subject to lapses in judgment and breakdowns resulting from human failures. Internal control over financial reporting can also be circumvented by collusion or improper management override. Because of such limitations, there is a risk that material misstatements may not be prevented or detected on a timely basis by internal control over financial reporting. However, these inherent limitations are known features of the financial reporting process. Therefore, it is possible to design into the process safeguards to reduce, though not eliminate, this risk.

Management is also responsible for the preparation and fair presentation of the consolidated financial statements and other financial information contained in this report. The accompanying consolidated financial statements were prepared in conformity with GAAP and include, as necessary, best estimates and judgments by management.

/s/ DeWitt Drew

DeWitt Drew  
President and  
Chief Executive Officer

/s/ George R. Kirkland

George R. Kirkland  
Executive Vice President and  
Chief Financial Officer

March 31, 2017



**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

To the Board of Directors and Stockholders  
Southwest Georgia Financial Corporation

We have audited the accompanying consolidated balance sheets of Southwest Georgia Financial Corporation and subsidiary as of December 31, 2016 and 2015, and the related consolidated statements of income, comprehensive income, stockholders' equity, and cash flows for the years then ended. These consolidated 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 audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall 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 Southwest Georgia Financial Corporation and subsidiary as of December 31, 2016 and 2015, and the results of its operations and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

*TJS Deemer Dana LLP*

Dublin, Georgia  
March 31, 2017

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SOUTHWEST GEORGIA FINANCIAL CORPORATION  
CONSOLIDATED BALANCE SHEETS  
December 31, 2016 and 2015

	<u>2016</u>	<u>2015</u>
<b>ASSETS</b>		
Cash and due from banks	\$ 7,700,522	\$ 6,156,818
Interest-bearing deposits in other banks	<u>18,819,394</u>	<u>24,923,455</u>
Cash and cash equivalents	<u>26,519,916</u>	<u>31,080,273</u>
Certificates of deposit in other banks	0	245,000
Investment securities available for sale, at fair value	53,565,503	51,476,411
Investment securities to be held to maturity (fair value approximates \$55,123,073 and \$62,198,699)	54,602,535	60,888,804
Federal Home Loan Bank stock, at cost	1,874,200	1,869,200
Loans, net of allowance for loan losses of \$3,124,611 and \$3,032,242	289,399,625	247,754,093
Premises and equipment, net	11,209,285	11,157,444
Bank property held for sale	211,500	0
Foreclosed assets, net	126,713	81,750
Intangible assets	35,156	50,781
Bank owned life insurance	5,356,683	5,231,393
Other assets	<u>5,600,114</u>	<u>5,020,321</u>
Total assets	<u>\$ 448,501,230</u>	<u>\$ 414,855,470</u>

**LIABILITIES AND STOCKHOLDERS' EQUITY**

Liabilities:		
Deposits:		
NOW accounts	\$ 47,420,335	\$ 25,382,480
Money market	95,658,654	108,226,017
Savings	29,006,734	27,720,845
Certificates of deposit \$100,000 and over	43,234,832	25,189,020
Other time accounts	<u>39,524,168</u>	<u>50,728,148</u>
Total interest-bearing deposits	254,844,723	237,246,510
Noninterest-bearing deposits	<u>116,648,264</u>	<u>101,769,333</u>
Total deposits	<u>371,492,987</u>	<u>339,015,843</u>
Short-term borrowed funds	8,447,619	7,590,476
Long-term debt	26,028,571	28,476,190
Other liabilities	<u>4,109,719</u>	<u>3,675,271</u>
Total liabilities	<u>410,078,896</u>	<u>378,757,780</u>
Stockholders' equity:		
Common stock – \$1 par value, 5,000,000 shares authorized, 4,293,835 shares for 2016 and 2015 issued	4,293,835	4,293,835
Additional paid-in capital	31,701,533	31,701,533
Retained earnings	30,333,410	27,369,480
Accumulated other comprehensive loss	( 1,785,991)	( 1,153,363)
Treasury stock, at cost 1,746,398 shares for 2016 and 1,745,998 for 2015	<u>( 26,120,453)</u>	<u>( 26,113,795)</u>
Total stockholders' equity	<u>38,422,334</u>	<u>36,097,690</u>
Total liabilities and stockholders' equity	<u>\$ 448,501,230</u>	<u>\$ 414,855,470</u>

See accompanying notes to consolidated financial statements.



SOUTHWEST GEORGIA FINANCIAL CORPORATION  
CONSOLIDATED STATEMENTS OF INCOME  
for the years ended December 31, 2016, 2015, and 2014

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Interest income:			
Interest and fees on loans	\$ 14,796,649	\$ 12,695,520	\$ 12,135,221
Interest on debt securities: Taxable	1,170,259	1,345,549	1,366,591
Interest on debt securities: Tax-exempt	1,253,064	1,240,706	1,055,727
Dividends	89,840	72,619	69,343
Interest on deposits in other banks	103,244	62,138	51,995
Interest on certificates of deposit in other banks	<u>52</u>	<u>11,795</u>	<u>33,327</u>
Total interest income	<u>17,413,108</u>	<u>15,428,327</u>	<u>14,712,204</u>
Interest expense:			
Deposits	935,291	795,850	749,854
Federal funds purchased	10	426	258
Other short-term borrowings	103,567	67,274	169,661
Long-term debt	<u>573,225</u>	<u>453,258</u>	<u>435,686</u>
Total interest expense	<u>1,612,093</u>	<u>1,316,808</u>	<u>1,355,459</u>
Net interest income	15,801,015	14,111,519	13,356,745
Provision for loan losses	<u>160,000</u>	<u>141,300</u>	<u>330,000</u>
Net interest income after provision for loan losses	<u>15,641,015</u>	<u>13,970,219</u>	<u>13,026,745</u>
Noninterest income:			
Service charges on deposit accounts	1,086,268	1,121,240	1,274,726
Income from trust services	209,755	245,279	241,131
Income from brokerage services	342,051	420,695	375,699
Income from insurance services	1,477,663	1,372,872	1,324,183
Income from mortgage banking services	354,627	317,970	645,241
Net gain on sale or disposition of assets	38,165	22,382	88,631
Net gain on sale of securities	168,919	3,587	293,508
Other income	<u>781,811</u>	<u>756,152</u>	<u>743,319</u>
Total noninterest income	<u>4,459,259</u>	<u>4,260,177</u>	<u>4,986,438</u>
Noninterest expense:			
Salaries and employee benefits	8,765,865	7,914,155	8,359,019
Occupancy expense	1,140,600	1,120,940	1,060,822
Equipment expense	860,935	923,267	896,416
Data processing expense	1,367,569	1,224,177	1,129,617
Amortization of intangible assets	15,625	15,625	44,931
Other operating expenses	<u>2,763,227</u>	<u>2,831,433</u>	<u>2,878,991</u>
Total noninterest expenses	<u>14,913,821</u>	<u>14,029,597</u>	<u>14,369,796</u>
Income before income taxes	5,186,453	4,200,799	3,643,387
Provision for income taxes	<u>1,152,476</u>	<u>827,164</u>	<u>739,557</u>
Net income	<u>\$ 4,033,977</u>	<u>\$ 3,373,635</u>	<u>\$ 2,903,830</u>
Basic earnings per share:			
Net income	<u>\$ 1.58</u>	<u>\$ 1.32</u>	<u>\$ 1.14</u>
Weighted average shares outstanding	<u>2,547,778</u>	<u>2,547,837</u>	<u>2,547,837</u>
Diluted earnings per share:			
Net income	<u>\$ 1.58</u>	<u>\$ 1.32</u>	<u>\$ 1.14</u>
Weighted average shares outstanding	<u>2,547,778</u>	<u>2,547,837</u>	<u>2,547,837</u>

See accompanying notes to consolidated financial statements.

SOUTHWEST GEORGIA FINANCIAL CORPORATION  
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME  
for the years ended December 31, 2016, 2015, and 2014

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Net income	\$ 4,033,977	\$ 3,373,635	\$ 2,903,830
Other comprehensive income (loss), net of tax:			
Unrealized gain (loss) on securities available for sale	(704,188)	116,782	1,490,640
Reclassification adjustment for (gain) loss realized in income on securities available for sale	(144,034)	17,992	(293,508)
Unrealized gain (loss) on pension plan benefits	(110,306)	(1,032,035)	55,700
Federal income tax expense (benefit)	<u>(325,900)</u>	<u>(305,069)</u>	<u>425,963</u>
Other comprehensive income (loss), net of tax	<u>(632,628)</u>	<u>(592,192)</u>	<u>826,869</u>
Total comprehensive income	<u>\$ 3,401,349</u>	<u>\$ 2,781,443</u>	<u>\$ 3,730,699</u>

See accompanying notes to consolidated financial statements.

SOUTHWEST GEORGIA FINANCIAL CORPORATION  
CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY  
for the years ended December 31, 2016, 2015, and 2014

	Common Stock	Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Treasury Stock	Total Stockholders' Equity
Balance at Dec. 31, 2013	\$ 4,293,835	\$ 31,701,533	\$ 22,926,458	\$ (1,388,040)	\$ (26,113,795)	\$ 31,419,991
Net Income	-	-	2,903,830	-	-	2,903,830
Comprehensive income:						
Changes in net gain on securities available for sale	-	-	-	790,107	-	790,107
Changes in net gain on pension plan benefits	-	-	-	36,762	-	36,762
Cash dividend declared \$ .32 per share	-	-	(815,308)	-	-	(815,308)
Balance at Dec. 31, 2014	4,293,835	31,701,533	25,014,980	(561,171)	(26,113,795)	34,335,382
Net Income	-	-	3,373,635	-	-	3,373,635
Comprehensive income (loss):						
Changes in net gain on securities available for sale	-	-	-	88,951	-	88,951
Changes in net loss on pension plan benefits	-	-	-	(681,143)	-	(681,143)
Cash dividend declared \$ .40 per share	-	-	(1,019,135)	-	-	(1,019,135)
Balance at Dec. 31, 2015	4,293,835	31,701,533	27,369,480	(1,153,363)	(26,113,795)	36,097,690
Net Income	-	-	4,033,977	-	-	4,033,977
Comprehensive income (loss):						
Changes in net gain on securities available for sale	-	-	-	(559,826)	-	(559,826)
Changes in net loss on pension plan benefits	-	-	-	(72,802)	-	(72,802)
Cash dividend declared \$ .42 per share	-	-	(1,070,047)	-	-	(1,070,047)
Purchase of treasury stock	-	-	-	-	(6,658)	(6,658)
Balance at Dec. 31, 2016	<u>\$ 4,293,835</u>	<u>\$ 31,701,533</u>	<u>\$ 30,333,410</u>	<u>\$ (1,785,991)</u>	<u>\$ (26,120,453)</u>	<u>\$ 38,422,334</u>

See accompanying notes to consolidated financial statements.

SOUTHWEST GEORGIA FINANCIAL CORPORATION  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
for the years ended December 31, 2016, 2015, and 2014

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Cash flows from operating activities:			
Net income	\$ 4,033,977	\$ 3,373,635	\$ 2,903,830
Adjustments to reconcile net income to net cash provided by operating activities:			
Provision for loan losses	160,000	141,300	330,000
Depreciation	923,578	961,964	890,812
Net amortization of investment securities	309,185	307,861	324,209
Income on cash surrender value of bank owned life insurance	(125,290)	(147,601)	(123,784)
Amortization of intangibles	15,625	15,625	44,931
Gain on sale/writedown of foreclosed assets	0	(13,077)	(84,898)
Net gain on sale of securities	(168,919)	(3,587)	(293,508)
Net gain on disposal of other assets	(36,701)	(9,305)	(3,733)
Change in:			
Other assets	(253,894)	52,322	640,249
Other liabilities	324,142	(208,670)	(213,747)
Net cash provided by operating activities	<u>5,181,703</u>	<u>4,470,467</u>	<u>4,414,361</u>
Cash flows from investing activities:			
Proceeds from calls, paydowns and maturities of securities HTM	5,952,271	5,115,703	3,983,421
Proceeds from calls, paydowns and maturities of securities AFS	10,354,337	4,143,139	2,460,175
Proceeds from Federal Home Loan Bank Stock repurchase	413,700	141,600	1,115,000
Proceeds from sale of securities available for sale	11,933,634	4,044,500	2,208,318
Proceeds from sale of securities held to maturity	576,834	516,746	0
Proceeds from maturity of certificates of deposit in other banks	245,000	1,225,000	1,960,000
Purchase of securities held to maturity	(478,559)	(5,207,650)	(6,239,587)
Purchase of securities available for sale	(25,129,827)	(5,709,379)	(20,586,864)
Purchase of Federal Home Loan Bank Stock	(418,700)	(450,800)	(954,000)
Net change in loans	(41,850,494)	(26,517,707)	(6,362,332)
Proceeds from bank owned life insurance	0	30,011	0
Purchase of premises and equipment	(1,455,043)	(370,837)	(2,311,767)
Proceeds from sales of other assets	304,825	201,000	578,067
Net cash used by investing activities	<u>(39,552,022)</u>	<u>(22,838,674)</u>	<u>(24,149,569)</u>
Cash flows from financing activities:			
Net change in deposits	32,477,143	29,042,251	(460,947)
Payment of short-term portion of long-term debt	(7,590,476)	(5,133,333)	(11,800,000)
Proceeds from issuance of short-term debt	857,143	2,457,143	0
Proceeds from issuance of long-term debt	5,142,857	11,542,857	10,000,000
Cash dividends paid	(1,070,047)	(1,019,135)	(815,308)
Payment for treasury stock	(6,658)	0	0
Net cash provided (used) by financing activities	<u>29,809,962</u>	<u>36,889,783</u>	<u>(3,076,255)</u>
Increase (decrease) in cash and cash equivalents	(4,560,357)	18,521,576	(22,811,463)
Cash and cash equivalents - beginning of period	<u>31,080,273</u>	<u>12,558,697</u>	<u>35,370,160</u>
Cash and cash equivalents - end of period	<u>\$ 26,519,916</u>	<u>\$ 31,080,273</u>	<u>\$ 12,558,697</u>
Cash paid during the year for:			
Income taxes	\$ 964,000	\$ 725,000	\$ 255,000
Interest paid	\$ 1,600,593	\$ 1,314,156	\$ 1,414,059

See accompanying notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS, continued

	<u>2016</u>	<u>2015</u>	<u>2014</u>
NONCASH ITEMS:			
Increase in foreclosed properties and decrease in loans	\$ 44,963	\$ 241,980	\$ 357,013
Unrealized gain (loss) on securities AFS	\$ (848,222)	\$ 134,774	\$ 1,197,132
Unrealized gain (loss) on pension plan benefits	\$ (110,306)	\$ (1,032,035)	\$ 55,700
Net reclass between short and long-term debt	\$ 7,590,476	\$ 5,133,333	\$ 5,133,333
Sale of foreclosed properties through loans	\$ 0	\$ (334,000)	\$ 0
Property moved from fixed assets to property held for sale	\$ 211,500	\$ 0	\$ 0

See accompanying notes to consolidated financial statements.

SOUTHWEST GEORGIA FINANCIAL CORPORATION  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting and reporting policies of Southwest Georgia Financial Corporation (the “Corporation”) and its direct and indirect subsidiaries, including its wholly-owned banking subsidiary, Southwest Georgia Bank (the “Bank”), conform to U.S. generally accepted accounting principles (“GAAP”) and to general practices within the banking industry. The following is a description of the more significant of those policies.

Principles of Consolidation

The consolidated financial statements include the accounts of the Corporation and its direct and indirect subsidiaries. All significant intercompany accounts and transactions have been eliminated in the consolidation.

Nature of Operations

The Corporation offers comprehensive financial services to consumer, business, and governmental entity customers through its banking offices in southwest Georgia. Its primary deposit products are money market, NOW, savings and certificates of deposit, and its primary lending products are consumer and commercial mortgage loans. In addition to conventional banking services, the Corporation provides investment planning and management, trust management, mortgage banking, and commercial and individual insurance products. Insurance products and advice are provided by the Bank’s Southwest Georgia Insurance Services Division.

The Corporation’s primary business is providing banking services through the Bank to individuals and businesses principally in the counties of Colquitt, Baker, Worth, Lowndes and the surrounding counties of southwest Georgia. The Corporation has two full-service banking centers, a commercial banking center and a mortgage origination office in Valdosta, Georgia. The Corporation expanded its geographical footprint in to neighboring Tift County, Georgia, by opening a loan production office in January 2016.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Material estimates that are particularly susceptible to significant change 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. In connection with these evaluations, management obtains independent appraisals for significant properties.

A substantial portion of the Corporation’s loans are secured by real estate located primarily in Georgia. Accordingly, the ultimate collection of these loans is susceptible to changes in the real estate market conditions of this market area.

Cash and Cash Equivalents and Statement of Cash Flows

For purposes of reporting cash flows, the Corporation considers cash and cash equivalents to include all cash on hand, deposit amounts due from banks, interest-bearing deposits in other banks, and federal funds sold. The Corporation maintains its cash balances in several financial institutions. Accounts at the financial institutions are secured by the Federal Deposit Insurance Corporation (the “FDIC”) up to \$250,000. There were uninsured deposits of \$953,956 at December 31, 2016.

Investment Securities

Debt securities that management has the positive intent and ability to hold to maturity are classified as “held to maturity” and recorded at amortized cost. Securities not classified as held to maturity or trading, including equity securities with readily determinable fair values, are classified as “available for sale” and recorded at fair value with unrealized gains and losses reported in other comprehensive income.

Purchase premiums and discounts are recognized in interest income using the interest method over the terms of the securities. Declines in the fair value of held to maturity and available for sale securities below their cost that are deemed to be other-than-temporarily impaired are reflected in earnings as realized losses. In estimating other-than-temporary impairment losses, management considers (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 Corporation to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value. Gains and losses on the sale of securities are recorded on the trade date and are determined using the specific identification method.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, continued

### Premises and Equipment

Premises and equipment are stated at cost, less accumulated depreciation and amortization. Depreciation has been calculated primarily using the straight-line method for buildings and building improvements over the assets estimated useful lives. Equipment and furniture are depreciated using the modified accelerated recovery system method over the assets estimated useful lives for financial reporting and income tax purposes for assets purchased on or before December 31, 2003. For assets acquired after 2003, the Corporation used the straight-line method of depreciation. The following estimated useful lives are used for financial statement purposes:

Land improvements	5 – 31 years
Building and improvements	10 – 40 years
Machinery and equipment	5 – 10 years
Computer equipment	3 – 5 years
Office furniture and fixtures	5 – 10 years

All of the Corporation's leases are operating leases and are not capitalized as assets for financial reporting purposes. Maintenance and repairs are charged to expense and betterments are capitalized.

Long-lived assets are evaluated regularly for other-than-temporary impairment. If circumstances suggest that their value may be impaired and the write-down would be material, an assessment of recoverability is performed prior to any write-down of the asset. Impairment on intangibles is evaluated at each balance sheet date or whenever events or changes in circumstances indicate that the carrying amount should be assessed. Impairment, if any, is recognized through a valuation allowance with a corresponding charge recorded in the income statement.

### Bank Property Held for Sale

During 2016, the Bank's former branch in Pavo, Georgia, was transferred from premises to bank property held for sale and depreciation was discontinued. The property was booked at the lower of cost or market value based on a current appraisal of \$211,500. The Corporation has this property available for sale.

### Loans and Allowances for Loan Losses

Loans are stated at principal amounts outstanding less unearned income and the allowance for loan losses. Interest income is credited to income based on the principal amount outstanding at the respective rate of interest except for interest on certain installment loans made on a discount basis which is recognized in a manner that results in a level-yield on the principal outstanding.

Accrual of interest income is discontinued on loans when, in the opinion of management, collection of such interest income becomes doubtful. Accrual of interest on such loans is resumed when, in management's judgment, the collection of interest and principal becomes probable.

Fees on loans and costs incurred in origination of most loans are recognized at the time the loan is placed on the books. Because loan fees are not significant, the results on operations are not materially different from the results which would be obtained by accounting for loan fees and costs as amortized over the term of the loan as an adjustment of the yield.

A loan is considered impaired when, based on current information and events, it is probable that the Corporation 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 for commercial and construction loans by either the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's obtainable market price, or the fair value of the collateral if the loan is collateral dependent.

Large groups of smaller balance homogeneous loans are collectively evaluated for impairment. Accordingly, the Corporation does not separately identify individual consumer and residential loans for impairment disclosures.

The allowance for loan losses is established through a provision for loan losses charged to expense. Loans are charged against the allowance for loan losses when management believes the collection of the principal is unlikely. The allowance is an amount which management believes will be adequate to absorb estimated losses on existing loans that may become uncollectible based on evaluation of the collectability of loans and prior loss experience. This evaluation takes into consideration such factors as changes in the nature and

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, continued

volume of the loan portfolios, current economic conditions that may affect the borrowers' ability to pay, overall portfolio quality, and review of specific problem loans.

Management believes that the allowance for loan losses is adequate. While management uses available information to recognize losses on loans, future additions to the allowance may be necessary based upon changes in economic conditions. Also, various regulatory agencies, as an integral part of their examination process, periodically review the Corporation's allowance for loan losses. Such agencies may require the Corporation to recognize additions to the allowance based on their judgments of information available to them at the time of their examination.

### Foreclosed Assets

In accordance with policy guidelines and regulations, properties acquired through, or in lieu of, loan foreclosure are held for sale and are initially recorded at the lower of cost or fair value at the date of foreclosure, establishing a new cost basis. Subsequent to foreclosure, valuations are periodically performed by management and the assets are carried at the lower of carrying amount or fair value less cost to sell. A valuation allowance is established to record market value changes in foreclosed assets. Revenue and expenses from operations and changes in the valuation allowance are included in net expenses from foreclosed assets. There was no allowance for foreclosed asset losses at December 31, 2016. Foreclosed assets totaled \$126,713 at December 31, 2016, up from \$81,750 at December 31, 2015.

### Intangible Assets

Intangible assets are amortized over a determined useful life using the straight-line basis. These assets are evaluated annually as to the recoverability of the carrying value. The remaining intangibles have a remaining life of less than three years.

### Credit Related Financial Instruments

In the ordinary course of business, the Corporation has entered into commitments to extend credit, including commitments under credit card arrangements, commercial letters of credit, and standby letters of credit. Such financial instruments are recorded when they are funded.

### Retirement Plans

The Corporation and its direct and indirect subsidiaries have post-retirement plans covering substantially all employees. The Corporation makes annual contributions to the plans in amounts not exceeding the regulatory requirements.

### Bank Owned Life Insurance

The Bank owns life insurance policies on a group of employees. Banking laws and regulations allow the Bank to purchase life insurance policies on certain employees in order to help offset the Bank's overall employee compensation costs. The beneficial aspects of these life insurance policies are tax-free earnings and a tax free death benefit, which are realized by the Bank as the owner of the policies. The cash surrender value of these policies is included as an asset on the balance sheet, and any increases in cash surrender value are recorded as noninterest income on the statement of income. At December 31, 2016 and 2015, the policies had a value of \$5,356,683 and \$5,231,393, respectively, and were 13.9% and 14.5%, respectively, of stockholders' equity. These values are within regulatory guidelines.

### Income Taxes

The Corporation and its direct and indirect subsidiaries file a consolidated income tax return. Each subsidiary computes its income tax expense as if it filed an individual return except that it does not receive any portion of the surtax allocation. Any benefits or disadvantages of the consolidation are absorbed by the parent company. Each subsidiary pays its allocation of federal income taxes to the parent company or receives payment from the parent company to the extent that tax benefits are realized.

The Corporation reports income under the Financial Accounting Standards Board Accounting Standards Codification ("ASC") Topic 740, Income Taxes, which requires recognition of deferred tax liabilities and assets for the expected future tax consequences of events that have been included in the financial statements or tax returns. Under this method, deferred tax liabilities and assets are determined based on the difference between the financial statement and tax bases of assets and liabilities using enacted tax rates in effect for the year in which the differences are expected to reverse. Recognition of deferred tax assets is based on management's belief that it is more likely than not that the tax benefit associated with certain temporary differences and tax credits will be realized.

The Corporation will recognize a tax position as a benefit only if it is more likely than not that the tax position would be sustained in a tax examination, with an examination being presumed to occur. The amount recognized is the largest amount of a tax benefit that is greater than fifty percent likely of being realized on examination. No benefit is recorded for tax positions that do not meet the more than likely than not test.



## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, continued

The Corporation recognizes penalties related to income tax matters in income tax expense. The Corporation is subject to U.S. federal and Georgia state income tax audit for returns for the tax period ending December 31, 2014 and subsequent years.

### Accumulated Other Comprehensive Income (Loss)

Accumulated other comprehensive income (loss) includes all changes in stockholders' equity during a period, except those resulting from transactions with stockholders. Besides net income, other components of the Corporation's accumulated other comprehensive income (loss) includes the after tax effect of changes in the net unrealized gain/loss on securities available for sale and the unrealized gain/loss on pension plan benefits.

### Trust Department

Trust income is included in the accompanying consolidated financial statements on the cash basis in accordance with established industry practices. Reporting of such fees on the accrual basis would have no material effect on reported income.

### Advertising Costs

It is the policy of the Corporation to expense advertising costs as they are incurred. The Corporation does not engage in any direct-response advertising and accordingly has no advertising costs reported as assets on its balance sheet. Costs that were expensed during 2016, 2015, and 2014 were \$173,595, \$153,423, and \$161,994, respectively.

### Regulatory Developments

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

Quantitative measures established by regulation to ensure capital adequacy require the Corporation and the Bank to maintain minimum Tier 1 leverage, Tier 1 risk-based capital and Total risk-based capital ratios. In July 2013, the Board of Governors of the Federal Reserve System published the Basel III Capital Rules. These rules establish a comprehensive capital framework applicable to all depository institutions, certain bank holding companies with total consolidated assets below a certain threshold and all savings and loan holding companies except for those that are substantially engaged in insurance underwriting or commercial activities. These rules implement higher minimum capital requirements for banks and certain bank holding companies, include a new common equity Tier 1 capital requirement and establish criteria that instruments must meet to be considered common equity Tier 1 capital, additional Tier 1 capital or Tier 2 capital.

The Basel III Capital Rules became effective for the Bank on January 1, 2015, subject to a phase in period, but are not applicable to bank holding companies, like the Corporation, with less than \$1 billion in total consolidated assets that meet certain criteria.

The minimum capital level requirements applicable to the Bank under the Basel III Capital Rules are: (i) a common equity Tier 1 risk-based capital ratio of 4.5%; (ii) a Tier 1 risk-based capital ratio of 6% (increased from 4%); (iii) a Total risk-based capital ratio of 8% (unchanged from the rules effective for the year ended December 31, 2014); and (iv) a Tier 1 leverage ratio of 4% for all institutions. Common equity Tier 1 capital will consist of retained earnings and common stock instruments, subject to certain adjustments.

The Basel III Capital Rules set forth changes in the methods of calculating certain risk-weighted assets, which in turn affect the calculation of risk-based ratios. The new risk weightings are more punitive for assets held by banks that are deemed to be of higher risk. These changes were also effective beginning January 1, 2015.

The Basel III Capital Rules also introduce a "capital conservation buffer," which is in addition to each capital ratio and is phased-in over a three-year period beginning in January 2016.

As of December 31, 2016, the Bank is considered to be well-capitalized under the Basel III Capital Rules. There have been no conditions or events since December 31, 2016, that management believes has changed the Bank's status as "well-capitalized." The capital ratios of the Corporation and Bank are presented in Footnote 15.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, continued

### Recent Accounting Pronouncements

In October 2016, the FASB issued ASU 2016-16, *Intra-Entity Transfers of Assets other than Inventory*. This ASU eliminates the exception for all intra-entity sales of assets other than inventory. As a result, a reporting entity would recognize the tax expense from the sale of the asset in the seller's tax jurisdiction when the transfer occurs, even though the pre-tax effects of that transaction are eliminated in consolidation. Any deferred tax asset that arises in the buyer's jurisdiction would also be recognized at the time of the transfer. For public business entities, this ASU is effective for financial statements issued for fiscal years beginning after December 15, 2017, and interim periods therein. The adoption of ASU No. 2016-16 is not expected to have a material impact on the Corporation's consolidated financial statements.

In August 2016, the FASB issued ASU 2016-15, *Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments*, to address diversity in how certain cash receipts and cash payments are presented and classified in the statement of cash flows. The amendments provide guidance on the following eight specific cash flow issues: 1) debt prepayment or debt extinguishment costs; 2) settlement of zero-coupon debt instruments or other debt instruments with coupon interest rates that are insignificant in relation to the effective interest rate of the borrowing; 3) contingent consideration payments made after a business combination; 4) proceeds from the settlement of insurance claims; 5) proceeds from the settlement of corporate-owned life insurance policies, including bank-owned life insurance policies; 6) distributions received from equity method investees; 7) beneficial interests in securitization transactions; and 8) separately identifiable cash flows and application of the predominance principle. The amendments are effective for public companies for fiscal years beginning after December 31, 2017, and interim periods within those fiscal years. Early adoption is permitted, including adoption in an interim period. The adoption of ASU No. 2016-15 is not expected to have a material impact on the Corporation's consolidated financial statements.

In June 2016, the FASB issued ASU No. 2016-13, *Financial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments*, which is essentially the final rule on use of the so-called CECL model, or current expected credit losses. Among other things, the amendments in this ASU require the measurement of all expected credit losses for financial assets held at the reporting date based on historical experience, current conditions, and reasonable and supportable forecasts. Financial institutions and other organizations will now use forward-looking information to better inform their credit loss estimates. Many of the loss estimation techniques applied today will still be permitted, although the inputs to those techniques will change to reflect the full amount of expected credit losses. In addition, the ASU amends the accounting for credit losses on available-for-sale debt securities and purchased financial assets with credit deterioration. For SEC filers, the amendments in this ASU are effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2019, with later effective dates for non-SEC registrant public companies and other organizations. Early adoption will be permitted for all organizations for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018. The adoption of ASU No. 2016-13 is being reviewed for any material impact on the Corporation's consolidated financial statements.

In March 2016, the FASB issued ASU No. 2016-09 - *Compensation - Stock Compensation: Improvements to Employee Share-Based Payment Accounting*. The objective of the Simplification Initiative is to identify, evaluate, and improve areas of GAAP for which cost and complexity can be reduced while maintaining or improving the usefulness of the information provided to users of financial statements. The areas for simplification involve several aspects of the accounting for 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. Amendments related to the timing of when excess tax benefits are recognized, minimum statutory withholding requirements, forfeitures, and intrinsic value should be applied using a modified retrospective transition method by means of a cumulative-effect adjustment to equity as of the beginning of the period in which the guidance is adopted. For public entities, the amendments are effective for annual periods beginning after December 15, 2016, and interim periods within those annual periods. The adoption of ASU No. 2016-09 is being reviewed for any material impact on the Corporation's consolidated financial statements.

In March 2016, the FASB issued ASU No. 2016-07: *Investments —Equity Method and Joint Ventures*. The amendments in this update eliminate the requirement that when an investment qualifies for use of the equity method as a result of an increase in the level of ownership interest or degree of influence. The amendments require that the equity method investor add the cost of acquiring the additional interest in the investee to the current basis of the investor's previously held interest and adopt the equity method of accounting as of the date the investment becomes qualified for equity method accounting. The amendments in this update are effective for all entities for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2016. The adoption of ASU No. 2016-07 is not expected to have a material impact on the Corporation's consolidated financial statements.

In January 2016, the FASB issued ASU No. 2016-01, *Recognition and Measurement of Financial Assets*. The new standard significantly revises an entity's accounting related to (1) the classification and measurement of investments in equity securities and (2) the presentation of certain fair value changes for financial liabilities measured as fair value. It also amends certain disclosure requirements associated with the fair value of financial instruments. This ASU is effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. The adoption of ASU No. 2016-01 is being reviewed for any material impact there may be on the Corporation's consolidated financial statements.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, continued**

**2. INVESTMENT SECURITIES**

Debt and equity securities have been classified in the consolidated balance sheets according to management's intent. The amortized costs of securities as shown in the consolidated balance sheets and their estimated fair values at December 31 were as follows:

Securities Available For Sale:

<u>December 31, 2016</u>	Amortized <u>Cost</u>	Unrealized <u>Gains</u>	Unrealized <u>Losses</u>	Estimated <u>Fair Value</u>
U.S. government treasury securities	\$ 977,967	\$ 0	\$ 15,817	\$ 962,150
U.S. government agency securities	41,117,402	697,811	830,316	40,984,897
State and municipal securities	6,537,093	25,170	109,666	6,452,597
Residential mortgage-backed securities	2,454,282	76,284	1,252	2,529,314
Corporate notes	<u>2,497,016</u>	<u>27,944</u>	<u>795</u>	<u>2,524,165</u>
Total debt securities AFS	53,583,760	827,209	957,846	53,453,123
Equity securities	<u>112,380</u>	<u>0</u>	<u>0</u>	<u>112,380</u>
Total securities AFS	<u>\$53,696,140</u>	<u>\$ 827,209</u>	<u>\$ 957,846</u>	<u>\$53,565,503</u>

<u>December 31, 2015</u>	Amortized <u>Cost</u>	Unrealized <u>Gains</u>	Unrealized <u>Losses</u>	Estimated <u>Fair Value</u>
U.S. government agency securities	\$42,074,712	\$ 782,567	\$ 214,957	\$42,642,322
State and municipal securities	2,573,844	33,840	0	2,607,684
Residential mortgage-backed securities	3,601,949	140,934	1,438	3,741,445
Corporate notes	<u>2,496,320</u>	<u>0</u>	<u>23,360</u>	<u>2,472,960</u>
Total debt securities AFS	50,746,825	957,341	239,755	51,464,411
Equity securities	<u>12,000</u>	<u>0</u>	<u>0</u>	<u>12,000</u>
Total securities AFS	<u>\$50,758,825</u>	<u>\$ 957,341</u>	<u>\$ 239,755</u>	<u>\$51,476,411</u>

Securities Held to Maturity:

<u>December 31, 2016</u>	Amortized <u>Cost</u>	Unrealized <u>Gains</u>	Unrealized <u>Losses</u>	Estimated <u>Fair Value</u>
State and municipal securities	\$50,435,624	\$ 508,109	\$ 117,077	\$50,826,656
Residential mortgage-backed securities	<u>4,166,911</u>	<u>129,506</u>	<u>0</u>	<u>4,296,417</u>
Total securities HTM	<u>\$54,602,535</u>	<u>\$ 637,615</u>	<u>\$ 117,077</u>	<u>\$55,123,073</u>

<u>December 31, 2015</u>	Amortized <u>Cost</u>	Unrealized <u>Gains</u>	Unrealized <u>Losses</u>	Estimated <u>Fair Value</u>
State and municipal securities	\$54,775,093	\$1,124,007	\$ 41,153	\$55,857,947
Residential mortgage-backed securities	<u>6,113,711</u>	<u>227,041</u>	<u>0</u>	<u>6,340,752</u>
Total securities HTM	<u>\$60,888,804</u>	<u>\$1,351,048</u>	<u>\$ 41,153</u>	<u>\$62,198,699</u>

At December 31, 2016, securities with a carrying value of \$63,902,259 and a market value of \$64,141,934 were pledged as collateral for public deposits and other purposes as required by law. Of these amounts, approximately \$9,400,000 was over pledged and could be released if necessary for liquidity needs. At December 31, 2015, securities with a carrying value of \$74,772,674 and a market value of \$75,959,402 were pledged as collateral for public deposits and other purposes as required by law. At December 31, 2016 and 2015, we had both 1 – 4 family and multifamily mortgage loans pledged to secure Federal Home Loan Bank ("FHLB") advances. The FHLB requires the Bank to hold a minimum investment of stock, based on membership and the level of activity. As of December 31, 2016, this stock investment was \$1,874,200.

There were no investments in obligations of any state or municipal subdivisions which exceeded 10% of the Corporation's stockholders' equity at December 31, 2016.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, continued

The amortized cost and estimated fair value of securities at December 31, 2016 and 2015, by contractual maturity, are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without penalties.

### December 31, 2016

<u>Available for Sale:</u>	<u>Amortized Cost</u>	<u>Estimated Fair Value</u>
Amounts maturing in:		
One year or less	\$ 0	\$ 0
After one through five years	10,130,179	10,303,973
After five through ten years	39,818,677	39,507,820
After ten years	<u>3,634,904</u>	<u>3,641,330</u>
Total debt securities AFS	53,583,760	53,453,123
Equity securities	<u>112,380</u>	<u>112,380</u>
Total securities AFS	<u>\$53,696,140</u>	<u>\$53,565,503</u>

<u>Held to Maturity:</u>	<u>Amortized Cost</u>	<u>Estimated Fair Value</u>
Amounts maturing in:		
One year or less	\$ 7,939,740	\$ 7,941,397
After one through five years	26,537,314	26,786,525
After five through ten years	15,178,560	15,493,803
After ten years	<u>4,946,921</u>	<u>4,901,348</u>
Total securities HTM	<u>\$54,602,535</u>	<u>\$55,123,073</u>

### December 31, 2015

<u>Available for Sale:</u>	<u>Amortized Cost</u>	<u>Estimated Fair Value</u>
Amounts maturing in:		
One year or less	\$ 0	\$ 0
After one through five years	22,374,572	22,310,228
After five through ten years	22,553,504	23,222,962
After ten years	<u>5,818,749</u>	<u>5,931,221</u>
Total debt securities AFS	50,746,825	51,464,411
Equity securities	<u>12,000</u>	<u>12,000</u>
Total securities AFS	<u>\$50,758,825</u>	<u>\$51,476,411</u>

<u>Held to Maturity:</u>	<u>Amortized Cost</u>	<u>Estimated Fair Value</u>
Amounts maturing in:		
One year or less	\$ 3,956,629	\$ 3,968,196
After one through five years	27,302,169	27,617,796
After five through ten years	21,412,080	22,253,863
After ten years	<u>8,217,926</u>	<u>8,358,844</u>
Total securities HTM	<u>\$60,888,804</u>	<u>\$62,198,699</u>

For the years ended December 31, 2016, 2015, and 2014, proceeds from sales of securities available for sale amounted to \$11,933,634, \$4,044,500, and \$2,208,318, respectively. In 2016, \$576,834 of securities held to maturity were sold. Reported net realized gains amounted to \$168,919, \$3,587, and \$293,508, respectively. The net gain in 2016 was due to selling \$11,933,634 in U. S. government agency securities and available for sale mortgage-backed securities and \$576,834 in held to maturity mortgage-backed securities in order to provide liquidity and remove small lots of mortgage-backed securities. These small lots of held to maturity mortgage-backed securities sold were paid down by over 85% of face value. The net gain in 2015 was due to selling \$4,044,500 in short-term U. S. government agency securities and \$516,746 in mortgage-backed securities. In 2015, \$516,746 of mortgage-backed securities held to maturity were sold. These small lots were paid down by over 85% of face value. The net gain in 2014 was due to the sale of \$2,208,318 of small lots of mortgage-backed securities and the remaining government sponsored entity preferred stock.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, continued**

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

<u>December 31, 2016</u>	<u>Less Than Twelve Months</u>		<u>Twelve Months or More</u>	
	<u>Gross Unrealized Losses</u>	<u>Fair Value</u>	<u>Gross Unrealized Losses</u>	<u>Fair Value</u>
<u>Securities Available for Sale</u>				
Temporarily impaired debt securities:				
U.S. government treasury securities	\$ 15,817	\$ 962,150	\$ 0	\$ 0
U.S. government agency securities	830,316	19,330,575	0	0
State and municipal securities	109,666	4,676,685	0	0
Residential mortgage-backed securities	1,252	311,851	0	0
Corporate notes	0	0	795	499,205
Total debt securities available for sale	<u>\$ 957,051</u>	<u>\$ 25,281,261</u>	<u>\$ 795</u>	<u>\$ 499,205</u>
<u>Securities Held to Maturity</u>				
Temporarily impaired debt securities:				
State and municipal securities	\$ 117,077	\$ 16,162,203	\$ 0	\$ 0
Residential mortgage-backed securities	0	0	0	0
Total securities held to maturity	<u>\$ 117,077</u>	<u>\$ 16,162,203</u>	<u>\$ 0</u>	<u>\$ 0</u>
<u>December 31, 2015</u>	<u>Less Than Twelve Months</u>		<u>Twelve Months or More</u>	
	<u>Gross Unrealized Losses</u>	<u>Fair Value</u>	<u>Gross Unrealized Losses</u>	<u>Fair Value</u>
<u>Securities Available for Sale</u>				
Temporarily impaired debt securities:				
U.S. government agency securities	\$ 73,907	\$ 11,885,323	\$ 141,050	\$ 5,858,950
State and municipal securities	0	0	0	0
Residential mortgage-backed securities	1,438	441,997	0	0
Corporate notes	22,360	1,973,960	1,000	499,000
Total debt securities available for sale	<u>\$ 97,705</u>	<u>\$ 14,301,280</u>	<u>\$ 142,050</u>	<u>\$ 6,357,950</u>
<u>Securities Held to Maturity</u>				
Temporarily impaired debt securities:				
State and municipal securities	\$ 26,435	\$ 7,250,634	\$ 14,718	\$ 994,476
Residential mortgage-backed securities	0	0	0	0
Total securities held to maturity	<u>\$ 26,435</u>	<u>\$ 7,250,634</u>	<u>\$ 14,718</u>	<u>\$ 994,476</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 Corporation to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value.

At December 31, 2016, sixty nine debt securities had unrealized losses with aggregate depreciation of 2.50% from the Corporation's amortized cost basis. At December 31, 2015, thirty seven debt securities had unrealized losses with aggregate depreciation of .96%. These unrealized losses relate principally to current interest rates for similar types of securities. In analyzing an issuer's financial condition, management considers whether the securities are issued by the federal government, its agencies, or other governments, whether downgrades by bond rating agencies have occurred, and the results of reviews of the issuer's financial condition. Management has the ability to hold debt securities until maturity, or for the foreseeable future if classified as available for sale. Also, no declines in debt securities are deemed to be other-than-temporary.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, continued**

**3. LOANS AND ALLOWANCE FOR LOAN LOSSES**

The composition of the Corporation's loan portfolio at December 31, 2016 and 2015 was as follows:

	<u>2016</u>	<u>2015</u>
Commercial, financial and agricultural loans	\$ 70,999,423	\$ 58,173,187
Real estate		
Construction loans	25,999,295	19,831,070
Commercial mortgage loans	91,732,812	85,777,359
Residential loans	83,270,983	67,969,119
Agricultural loans	16,580,126	15,620,266
Consumer & other loans	<u>3,960,492</u>	<u>3,434,380</u>
Loans outstanding	292,543,131	250,805,381
Unearned interest and discount	( 18,895)	( 19,046)
Allowance for loan losses	<u>( 3,124,611)</u>	<u>( 3,032,242)</u>
Net loans	<u>\$ 289,399,625</u>	<u>\$ 247,754,093</u>

The Corporation's only significant concentration of credit at December 31, 2016, occurred in real estate loans which totaled approximately \$218 million. However, this amount was not concentrated in any specific segment within the market or geographic area.

At December 31, 2016, \$57,611,388 1-4 family and multifamily mortgage loans were pledged to FHLB to secure outstanding advances.

**Appraisal Policy**

When a loan is first identified as a problem loan, the appraisal is reviewed to determine if the appraised value is still appropriate for the collateral. For the duration that a loan is considered a problem loan, the appraised value of the collateral is monitored on a quarterly basis. If significant changes occur in market conditions or in the condition of the collateral, a new appraisal will be obtained.

**Nonaccrual Policy**

The Corporation does not accrue interest on any loan (1) that is maintained on a cash basis due to the deteriorated financial condition of the borrower, (2) for which payment in full of principal or interest is not expected, or (3) upon which principal or interest has been past due for ninety days or more unless the loan is well secured and in the process of collection.

A loan subsequently placed on nonaccrual status may be returned to accrual status if (1) all past due interest and principal is paid with expectations of any remaining contractual principal and interest being repaid or (2) the loan becomes well secured and in the process of collection.

Loans placed on nonaccrual status amounted to \$246,320 and \$1,545,599 at December 31, 2016 and 2015, respectively. There were no past due loans over 90 days and still accruing at December 31, 2016 and one past due loan over ninety days and still accruing in the amount of \$521 at December 31, 2015. The accrual of interest is discontinued when the loan is placed on nonaccrual. Interest income that would have been recorded on these nonaccrual loans in accordance with their original terms totaled \$476 and \$40,346 as of year-end 2016 and 2015, respectively. The following tables present an age analysis of past due loans and nonaccrual loans segregated by class of loans.

Age Analysis of Past Due Loans  
As of December 31, 2016

	30-89 Days <u>Past Due</u>	Greater than 90 <u>Days</u>	Total Past Due <u>Loans</u>	Nonaccrual <u>Loans</u>	<u>Current Loans</u>	<u>Total Loans</u>
Commercial, financial and agricultural loans	\$1,264,998	\$ 0	\$1,264,998	\$ 38,798	\$ 69,695,627	\$ 70,999,423
Real estate:						
Construction loans	66,931	0	66,931	207,522	25,724,842	25,999,295
Commercial mortgage loans	1,268,405	0	1,268,405	0	90,464,407	91,732,812
Residential loans	1,376,671	0	1,376,671	0	81,894,312	83,270,983
Agricultural loans	0	0	0	0	16,580,126	16,580,126
Consumer & other loans	<u>65,127</u>	<u>0</u>	<u>65,127</u>	<u>0</u>	<u>3,895,365</u>	<u>3,960,492</u>
Total loans	<u>\$4,042,132</u>	<u>\$ 0</u>	<u>\$4,042,132</u>	<u>\$ 246,320</u>	<u>\$288,254,679</u>	<u>\$292,543,131</u>

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, continued

Age Analysis of Past Due Loans  
As of December 31, 2015

	30-89 Days Past Due	Greater than 90 Days	Total Past Due Loans	Nonaccrual Loans	Current Loans	Total Loans
Commercial, financial and agricultural loans	\$ 449,618	\$ 521	\$ 450,139	\$ 0	\$ 57,723,048	\$ 58,173,187
Real estate:						
Construction loans	121,694	0	121,694	0	19,709,376	19,831,070
Commercial mortgage loans	810,515	0	810,515	0	84,966,844	85,777,359
Residential loans	2,238,684	0	2,238,684	639,094	65,091,341	67,969,119
Agricultural loans	148,761	0	148,761	906,505	14,565,000	15,620,266
Consumer & other loans	<u>84,342</u>	<u>0</u>	<u>84,342</u>	<u>0</u>	<u>3,350,038</u>	<u>3,434,380</u>
Total loans	<u>\$3,853,614</u>	<u>\$ 521</u>	<u>\$3,854,135</u>	<u>\$ 1,545,599</u>	<u>\$245,405,647</u>	<u>\$250,805,381</u>

Impaired Loans

A loan is considered impaired when, based on current information and events, it is probable that the Corporation 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 for commercial and construction loans by either the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's obtainable market price, or the fair value of the collateral if the loan is collateral dependent.

At December 31, 2016 and 2015, impaired loans amounted to \$3,560,901 and \$5,558,615, respectively. A reserve amount of \$549,429 and \$304,114, respectively, was recorded in the allowance for loan losses for these impaired loans as of December 31, 2016 and 2015.

The following tables present impaired loans, segregated by class of loans as of December 31, 2016 and 2015:

	Unpaid Principal Balance	Recorded Investment			Related Allowance	Year-to-date Average Recorded Investment	Interest Income Received During Impairment
		With No Allowance	With Allowance	Total			
<u>December 31, 2016</u>							
Commercial, financial and agricultural loans	\$ 102,086	\$ 4,798	\$ 97,288	\$ 102,086	\$ 12,021	\$ 21,154	\$ 2,464
Real estate:							
Construction loans	247,015	126,215	0	126,215	0	168,432	12,691
Commercial mortgage loans	880,670	0	880,670	880,670	245,472	4,005,175	46,195
Residential loans	2,223,421	230,610	1,971,899	2,202,509	291,936	3,272,528	122,370
Agricultural loans	246,175	246,175	0	246,175	0	851,740	8,150
Consumer & other loans	<u>3,246</u>	<u>3,246</u>	<u>0</u>	<u>3,246</u>	<u>0</u>	<u>6,501</u>	<u>201</u>
Total loans	<u>\$3,702,613</u>	<u>\$ 611,044</u>	<u>\$2,949,857</u>	<u>\$3,560,901</u>	<u>\$549,429</u>	<u>\$8,325,530</u>	<u>\$192,071</u>

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, continued**

<u>December 31, 2015</u>	Unpaid Principal Balance	Recorded Investment			Related Allowance	Year-to-date Average Recorded Investment	Interest Income Received During Impairment
		With No Allowance	With Allowance	Total			
Commercial, financial and agricultural loans	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0
Real estate:							
Construction loans	193,524	72,724	0	72,724	0	133,693	15,049
Commercial mortgage loans	3,256,589	496,159	2,760,430	3,256,589	212,283	2,096,082	89,947
Residential loans	1,988,434	662,523	1,304,999	1,967,522	91,831	3,832,546	107,070
Agricultural loans	257,211	257,211	0	257,211	0	422,099	25,823
Consumer & other loans	<u>4,569</u>	<u>4,569</u>	<u>0</u>	<u>4,569</u>	<u>0</u>	<u>0</u>	<u>0</u>
Total loans	<u>\$5,700,327</u>	<u>\$1,493,186</u>	<u>\$4,065,429</u>	<u>\$5,558,615</u>	<u>\$304,114</u>	<u>\$6,484,420</u>	<u>\$237,889</u>

For the period ending December 31, 2014, the average recorded investment for impaired loans was \$4,279,301 and the interest income received during impairment was \$251,495.

At December 31, 2016 and 2015, included in impaired loans were \$914,378 and \$2,290,411, respectively, of troubled debt restructurings.

Troubled Debt Restructurings

Loans are considered to have been modified in a troubled debt restructuring, or TDR, when due to a borrower's financial difficulty the Corporation 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. 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. 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.

Loan modifications are reviewed and recommended by the Corporation's senior credit officer, who determines whether the loan meets the criteria for a TDR. Generally, the types of concessions granted to borrowers that are evaluated in determining whether the 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 – Arise when the Corporation charges off a portion of the principal that is not fully collateralized and collectability is uncertain; however, this portion of principal may be recovered in the future under certain circumstances.

The following tables present the amount of troubled debt restructuring by loan class, classified separately as accrual and nonaccrual at December 31, 2016 and 2015, as well as those currently paying under restructured terms and those that have defaulted under restructured terms as of December 31, 2016 and 2015. Loans modified in a troubled debt restructuring are considered to be in default once the loan becomes 30 or more days past due.



NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, continued

December 31, 2016

			Under restructured terms			
	Accruing	Non-accruing	#	Current	#	Default
Commercial, financial, and agricultural loans	\$ 0	\$ 0	0	\$ 0	0	\$ 0
Real estate:						
Construction loans	0	0	0	0	0	0
Commercial mortgage loans	0	0	0	0	0	0
Residential loans	4,853	0	1	4,853	0	0
Agricultural loans	906,279	0	3	906,279	0	0
Consumer & other loans	3,246	0	1	3,246	0	0
Total TDR's	\$ 914,378	\$ 0	5	\$ 914,378	0	\$ 0

December 31, 2015

			Under restructured terms			
	Accruing	Non-accruing	#	Current	#	Default
Commercial, financial, and agricultural loans	\$ 0	\$ 0	0	\$ 0	0	\$ 0
Real estate:						
Construction loans	0	0	0	0	0	0
Commercial mortgage loans	2,280,466	0	1	2,280,466	0	0
Residential loans	5,376	0	1	5,376	0	0
Agricultural loans	0	0	0	0	0	0
Consumer & other loans	4,569	0	1	4,569	0	0
Total TDR's	\$ 2,290,411	\$ 0	3	\$ 2,290,411	0	\$ 0

The following table presents the amount of troubled debt restructurings by types of concessions made, classified separately as accrual and nonaccrual at December 31, 2016 and 2015.

	December 31, 2016				December 31, 2015			
	#	Accruing Balance	#	Nonaccruing Balance	#	Accruing Balance	#	Nonaccruing Balance
Type of concession:								
Payment modification	0	\$ 0	0	\$ 0	0	\$ 0	0	\$ 0
Rate reduction	0	0	0	0	0	0	0	0
Rate reduction, payment modification	5	914,378	0	0	3	2,290,411	0	0
Forbearance of interest	0	0	0	0	0	0	0	0
Total	5	\$ 914,378	0	\$ 0	3	\$ 2,290,411	0	\$ 0

As of December 31, 2016 and 2015, the Corporation had a balance of \$914,378 and \$2,290,411, respectively, in troubled debt restructurings. The Corporation had no charge-offs on such loans as of December 31, 2016, and no charge-offs as of December 31, 2015. The Corporation's balance in the allowance for loan losses allocated to such troubled debt restructurings was \$0 and \$130,441 at December 31, 2016 and 2015, respectively. The Corporation had no unfunded commitment to lend to a customer that has a troubled debt restructured loan as of December 31, 2016.

Credit Risk Monitoring and Loan Grading

The Corporation employs several means to monitor the risk in the loan portfolio including volume and severity of loan delinquencies, nonaccrual loans, internal grading of loans, historical loss experience and economic conditions.

Loans are subject to an internal risk grading system which indicates the risk and acceptability of that loan. The loan grades used by the Corporation are for internal risk identification purposes and do not directly correlate to regulatory classification categories or any financial reporting definitions.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, continued

The general characteristics of the risk grades are as follows:

*Grade 1 – Exceptional* – Loans graded 1 are characterized as having a very high credit quality, exhibit minimum risk to the Corporation and have low administrative cost. These loans are usually secured by highly liquid and marketable collateral and a strong primary and secondary source of repayment is available.

*Grade 2 – Above Average* – Loans graded 2 are basically sound credits secured by sound assets and/or backed by the financial strength of borrowers of integrity with a history of satisfactory payments of credit obligations.

*Grade 3 – Acceptable* – Loans graded 3 are secured by sound assets of sufficient value and/or supported by the sufficient financial strength of the borrower. The borrower will have experience in their business area or employed a reasonable amount of time at their current employment. The borrower will have a sound primary source of repayment, and preferably a secondary source, which will allow repayment in a prompt and reasonable period of time.

*Grade 4 – Fair* – Loans graded 4 are those which exhibit some weakness or downward trend in financial condition and although the repayment history is satisfactory, it requires supervision by bank personnel. The borrower may have little experience in their business area or employed only a short amount of time at their current employment. The loan may be secured by good collateral; however, it may require close supervision as to value and/or quality and may not have sufficient liquidation value to completely cover the loan.

*Grade 5a – Watch* – Loans graded 5a contain a discernible weakness; however, the weakness is not sufficiently pronounced so as to cause concern for the possible loss of interest or principal. Loans in this category may exhibit outward signs of stress, such as slowness in financial disclosures or recent payments. However, such signs are not of long duration or of sufficient severity that default appears imminent. Loans in this category are not so deficient as to cause alarm, but do require close monitoring for further deterioration and possible downgrade.

*Grade 5b – Other Assets Especially Mentioned (OAEM)* – Loans graded 5b may otherwise be classified more severely except that the loan is well secured by properly margined collateral, it is generally performing in accordance with the original contract or modification thereof and such performance has seasoned for a period of 90 days, or the ultimate collection of all principal and interest is reasonably expected. Loans in this grade are unsupported by sufficient evidence of the borrower's sound net worth or repayment capacity or may be subject to third party action that would cause concern for future prompt repayment.

*Grade 6 – Substandard* – Loans graded 6 contain clearly pronounced credit weaknesses that are below acceptable credit standards for the Corporation. Such weaknesses may be due to either collateral deficiencies or inherent financial weakness of the borrower, but in either case represents less than acceptable credit risk. Loans in this grade are unsupported by sufficient evidence of the borrower's sound net worth, repayment capacity or acceptable collateral.

*Grade 7 – Doubtful* – Loans graded 7 have such a pronounced credit weaknesses that the Corporation is clearly exposed to a significant degree of potential loss of principal or interest. These loan generally have a defined weakness which jeopardizes the ultimate repayment of the debt.

*Grade 8 – Loss* – Loans graded 8 are of such deteriorated credit quality that repayment of principal and interest can no longer be considered. These loans are of such little value that their continuance as an active bank asset is not warranted. As of December 31, 2016, all Grade 8 loans have been charged-off.

The following tables present internal loan grading by class of loans at December 31, 2016 and 2015:

<u>December 31, 2016</u>	Commercial, Financial, and <u>Agricultural</u>	Construction <u>Real Estate</u>	Commercial <u>Real Estate</u>	Residential <u>Real Estate</u>	Agricultural <u>Real Estate</u>	Consumer and Other	<u>Total</u>
Rating:							
Grade 1- Exceptional	\$ 615,535	\$ 0	\$ 0	\$ 24,963	\$ 0	\$ 395,765	\$ 1,036,263
Grade 2- Above Avg.	0	0	0	7,172	289,561	10,195	306,928
Grade 3- Acceptable	28,049,484	7,456,101	24,383,326	29,654,781	8,899,344	1,343,547	99,786,583
Grade 4- Fair	40,358,471	18,402,769	62,023,892	48,747,687	6,306,754	2,182,145	178,021,718
Grade 5a- Watch	111,488	0	1,071,667	832,624	22,642	16,002	2,054,423
Grade 5b- OAEM	1,561,359	14,210	2,883,133	1,260,719	0	3,247	5,722,668
Grade 6- Substandard	214,862	126,215	1,370,794	2,743,037	1,061,825	9,591	5,526,324
Grade 7- Doubtful	88,224	0	0	0	0	0	88,224
Total loans	<u>\$70,999,423</u>	<u>\$25,999,295</u>	<u>\$91,732,812</u>	<u>\$83,270,983</u>	<u>\$16,580,126</u>	<u>\$3,960,492</u>	<u>\$292,543,131</u>

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, continued**

December 31, 2015	Commercial, Financial, and Agricultural	Construction Real Estate	Commercial Real Estate	Residential Real Estate	Agricultural Real Estate	Consumer and Other	Total
Rating:							
Grade 1- Exceptional	\$ 731,270	\$ 0	\$ 0	\$ 25,988	\$ 0	\$ 416,250	\$ 1,173,508
Grade 2- Above Avg.	0	0	0	10,011	329,069	0	339,080
Grade 3- Acceptable	30,581,968	7,569,566	26,285,799	31,303,029	9,648,983	1,756,139	107,145,484
Grade 4- Fair	26,075,703	11,022,826	53,296,973	30,946,390	3,930,746	1,230,515	126,503,153
Grade 5a- Watch	217,295	1,097,222	4,791,317	1,263,077	638,402	5,999	8,013,312
Grade 5b- OAEM	560,678	0	523,596	1,233,611	0	13,802	2,331,687
Grade 6- Substandard	6,273	141,456	879,674	3,155,625	1,073,066	11,675	5,267,769
Grade 7- Doubtful	0	0	0	31,388	0	0	31,388
Total loans	<u>\$58,173,187</u>	<u>\$19,831,070</u>	<u>\$85,777,359</u>	<u>\$67,969,119</u>	<u>\$15,620,266</u>	<u>\$3,434,380</u>	<u>\$250,805,381</u>

Allowance for Loan Losses Methodology

The allowance for loan losses (ALL) is determined by a calculation based on segmenting the loans into the following categories: (1) impaired loans and nonaccrual loans, (2) loans with a credit risk rating of 5b, 6, 7 or 8, (3) other outstanding loans, and (4) other commitments to lend. In addition, unallocated general reserves are estimated based on migration and economic analysis of the loan portfolio.

The ALL is calculated by the addition of the estimated loss derived from each of the above categories. The impaired loans and nonaccrual loans are analyzed on an individual basis to determine if the future collateral value is sufficient to support the outstanding debt of the loan. If an estimated loss is calculated, it is included in the estimated ALL until it is charged to the loan loss reserve. The calculation for loan risk graded 5b, 6, 7 or 8, other outstanding loans and other commitments to lend is based on assigning an estimated loss factor based on a twelve quarter rolling historical weighted average net loss rate. The estimated requirement for unallocated general reserves from migration and economic analysis is determined by considering (1) trends in asset quality, (2) level and trends in charge-off experience, (3) macroeconomic trends and conditions, (4) microeconomic trends and conditions and (5) risk profile of lending activities. Within each of these categories, a high risk factor percentage and a low risk factor percentage from a rating of excessive, high, moderate or low will be determined by management and applied to the loan portfolio. This results in a high and low range of the estimated reserves required. By adding the estimated high and low value from the migration and economic analysis to the estimated reserve from the loan portfolio, a high and low range of total estimated loss reserves is obtained. This amount is then compared to the actual amount in the loan loss reserve.

The calculation of ALL is performed on a monthly basis and is presented to the Loan Committee and the Board of Directors.

Changes in the allowance for loan losses are as follows:

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Balance, January 1	\$ 3,032,242	\$ 3,114,151	\$ 3,077,561
Provision charged to operations	160,000	141,300	330,000
Loans charged off	( 116,006)	( 319,200)	( 341,377)
Recoveries	<u>48,375</u>	<u>95,991</u>	<u>47,967</u>
Balance, December 31	<u>\$ 3,124,611</u>	<u>\$ 3,032,242</u>	<u>\$ 3,114,151</u>

The following tables detail activity in the ALL by class of loans for the years ended December 31, 2016 and 2015. Allocation of a portion of the allowance to one category of loans does not preclude its availability to absorb losses in other categories.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, continued

	Commercial, Financial, and Agricultural	Construction Real Estate	Commercial Real Estate	Residential Real Estate	Agricultural Real Estate	Consumer and Other	Total
<u>December 31, 2016</u>							
<u>Allowance for loan losses:</u>							
Beginning balance, December 31, 2015	\$ 144,781	\$ 1,043,083	\$ 1,192,098	\$ 381,891	\$ 86,656	\$ 183,733	\$ 3,032,242
Charge-offs	103,387	0	0	3,394	0	9,225	116,006
Recoveries	<u>28,303</u>	<u>0</u>	<u>0</u>	<u>16,994</u>	<u>0</u>	<u>3,078</u>	<u>48,375</u>
Net charge-offs	75,084	0	0	(13,600)	0	6,147	67,631
Provisions charged to operations	<u>121,570</u>	<u>0</u>	<u>0</u>	<u>24,698</u>	<u>0</u>	<u>13,732</u>	<u>160,000</u>
Balance at end of period, December 31, 2016	<u>\$ 191,267</u>	<u>\$ 1,043,083</u>	<u>\$ 1,192,098</u>	<u>\$ 420,189</u>	<u>\$ 86,656</u>	<u>\$ 191,318</u>	<u>\$ 3,124,611</u>
Ending balance - Individually evaluated for impairment	\$ 12,021	\$ 0	\$ 245,472	\$ 291,936	\$ 0	\$ 0	\$ 549,429
Collectively evaluated for impairment	<u>179,246</u>	<u>1,043,083</u>	<u>946,626</u>	<u>128,253</u>	<u>86,656</u>	<u>191,318</u>	<u>2,575,182</u>
Balance at end of period	<u>\$ 191,267</u>	<u>\$ 1,043,083</u>	<u>\$ 1,192,098</u>	<u>\$ 420,189</u>	<u>\$ 86,656</u>	<u>\$ 191,318</u>	<u>\$ 3,124,611</u>
<u>Loans :</u>							
Ending balance - Individually evaluated for impairment	\$ 102,086	\$ 126,215	\$ 4,496,700	\$ 2,281,439	\$ 1,061,826	\$ 3,246	\$ 8,071,512
Collectively evaluated for impairment	<u>70,897,337</u>	<u>25,873,080</u>	<u>87,236,112</u>	<u>80,989,544</u>	<u>15,518,300</u>	<u>3,957,246</u>	<u>284,471,619</u>
Balance at end of period	<u>\$70,999,423</u>	<u>\$25,999,295</u>	<u>\$91,732,812</u>	<u>\$83,270,983</u>	<u>\$16,580,126</u>	<u>\$3,960,492</u>	<u>\$292,543,131</u>
<u>December 31, 2015</u>							
<u>Allowance for loan losses:</u>							
Beginning balance, December 31, 2014	\$ 299,850	\$ 1,043,083	\$ 1,192,098	\$ 312,822	\$ 86,656	\$ 179,642	\$ 3,114,151
Charge-offs	263,809	0	0	33,238	0	22,153	319,200
Recoveries	<u>42,253</u>	<u>0</u>	<u>0</u>	<u>22,047</u>	<u>0</u>	<u>31,691</u>	<u>95,991</u>
Net charge-offs	221,556	0	0	11,191	0	(9,538)	223,209
Provisions charged to operations	<u>66,487</u>	<u>0</u>	<u>0</u>	<u>80,260</u>	<u>0</u>	<u>(5,447)</u>	<u>141,300</u>
Balance at end of period, December 31, 2015	<u>\$ 144,781</u>	<u>\$ 1,043,083</u>	<u>\$ 1,192,098</u>	<u>\$ 381,891</u>	<u>\$ 86,656</u>	<u>\$ 183,733</u>	<u>\$ 3,032,242</u>
Ending balance - Individually evaluated for impairment	\$ 0	\$ 0	\$ 212,283	\$ 91,831	\$ 0	\$ 0	\$ 304,114
Collectively evaluated for impairment	<u>144,781</u>	<u>1,043,083</u>	<u>979,815</u>	<u>290,060</u>	<u>86,656</u>	<u>183,733</u>	<u>2,728,128</u>
Balance at end of period	<u>\$ 144,781</u>	<u>\$ 1,043,083</u>	<u>\$ 1,192,098</u>	<u>\$ 381,891</u>	<u>\$ 86,656</u>	<u>\$ 183,733</u>	<u>\$ 3,032,242</u>
<u>Loans :</u>							
Ending balance - Individually evaluated for impairment	\$ 0	\$ 1,012,831	\$ 5,414,491	\$ 2,896,953	\$ 1,682,207	\$ 4,569	\$ 11,011,051
Collectively evaluated for impairment	<u>58,173,187</u>	<u>18,818,239</u>	<u>80,362,868</u>	<u>65,072,166</u>	<u>13,938,059</u>	<u>3,429,811</u>	<u>239,794,330</u>
Balance at end of period	<u>\$58,173,187</u>	<u>\$19,831,070</u>	<u>\$85,777,359</u>	<u>\$67,969,119</u>	<u>\$15,620,266</u>	<u>\$3,434,380</u>	<u>\$250,805,381</u>

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, continued

The following table is a summary of amounts included in the ALL for the impaired loans with specific reserves and the recorded balance of the related loans.

	Year Ended December 31,		
	<u>2016</u>	<u>2015</u>	<u>2014</u>
Allowance for loss on impaired loans	\$ 549,429	\$ 304,114	\$ 478,814
Recorded balance of impaired loans	\$ 3,560,901	\$ 5,558,615	\$ 4,126,957

### 4. PREMISES AND EQUIPMENT

The amounts reported as bank premises and equipment at December 31, 2016 and 2015, are as follows:

	<u>2016</u>	<u>2015</u>
Land	\$ 3,866,891	\$ 3,089,352
Building	12,512,392	13,396,340
Furniture and equipment	8,846,887	9,006,056
Construction in process	<u>162,231</u>	<u>0</u>
	25,388,401	25,491,748
Less accumulated depreciation	<u>(14,179,116)</u>	<u>(14,334,304)</u>
Total	\$ <u>11,209,285</u>	\$ <u>11,157,444</u>

Depreciation of premises and equipment was \$923,578, \$961,964, and \$890,812 in 2016, 2015, and 2014, respectively. The Corporation depreciates its long-lived assets on various methods over their estimated productive lives, as more fully described in Note 1, Summary of Significant Accounting Policies.

A building is being leased for a loan production office opened in Tifton, Georgia, in January 2016. Land has been purchased for a full-service banking center in Tifton, Georgia, and construction is expected to begin by second quarter 2017.

### 5. INTANGIBLE ASSETS

The following table lists the Corporation's account relationship intangible assets at December 31, 2016 and 2015. These assets have less than three years of remaining amortization.

	<u>2016</u>	<u>2015</u>
Amortizing intangible assets		
Account relationships	\$ <u>35,156</u>	\$ <u>50,781</u>
Total intangible assets	\$ <u>35,156</u>	\$ <u>50,781</u>

The intangible assets' carrying amount, accumulated amortization and amortization expense for December 31, 2016, and the three succeeding fiscal years are as follows:

	<u>2016</u>	<u>2017</u>	<u>2018</u>	<u>2019</u>
Amortizing intangible assets				
Account relationships				
Gross carrying amount	\$ 125,000	\$ 125,000	\$ 125,000	\$ 125,000
Accumulated amortization	<u>89,844</u>	<u>105,469</u>	<u>121,094</u>	<u>125,000</u>
Net carrying amount	\$ 35,156	\$ 19,531	\$ 3,906	\$ 0
Amortization expense	\$ 15,625	\$ 15,625	\$ 15,625	\$ 3,906

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, continued**

**6. DEPOSITS**

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

	<u>Amount</u>
2017	\$69,571,788
2018	11,512,646
2019	1,348,802
2020	301,975
2021 and thereafter	<u>23,789</u>
Total	<u>\$82,759,000</u>

The amount of overdraft deposits reclassified as loans were \$55,586 and \$62,216 for the years ended December 31, 2016 and 2015, respectively. There are 32 certificates of deposit totaling \$11,581,144 that are above the FDIC insurance limit of \$250,000.

**7. SHORT-TERM BORROWED FUNDS**

Federal funds purchased generally mature within one to four days. On December 31, 2016, the Corporation did not have any federal funds purchased. The Corporation had approximately \$95,000,000 in unused federal funds accommodations at year-end 2016. Other short-term borrowed funds consist of FHLB advances of \$8,447,619 with interest at 1.28% as of December 31, 2016, and \$7,590,476 with interest at 1.22% as of December 31, 2015. The Corporation maintains a line of credit with the Federal Reserve Bank's Discount Window. The maximum amount that can be borrowed is dependent upon the amount of unpledged securities held by the Corporation as the amount of borrowings must be fully secured.

Information concerning federal funds purchased and FHLB short-term advances are summarized as follows:

	<u>2016</u>	<u>2015</u>
Average balance during the year	\$ 8,119,161	\$ 7,028,679
Average interest rate during the year	1.28%	0.96%
Maximum month-end balance during the year	\$10,590,476	\$10,133,333

**8. LONG-TERM DEBT**

Long-term debt at December 31, 2016 and 2015, consisted of the following:

	<u>2016</u>	<u>2015</u>
Advance from FHLB with a 3.39% fixed rate of interest maturing August 20, 2018 (convertible to a variable rate at quarterly options of FHLB – no conversion option has been made).	\$ 5,000,000	\$ 5,000,000
Advance from FHLB with a 2.78% fixed rate of interest maturing September 10, 2018 (convertible to a variable rate at quarterly options of FHLB – no conversion option has been made).	5,000,000	5,000,000
Advance from FHLB with 1.43% fixed rate of interest with annual installment payments maturing September 4, 2018.	1,800,000	3,600,000
Advance from FHLB with 0.89% fixed rate of interest with annual installment payments maturing July 24, 2017.	0	3,333,333
Advance from FHLB with 1.25% fixed rate of interest with annual installment payments maturing September 30, 2020.	4,800,000	6,400,000
Advance from FHLB with 1.94% fixed rate of interest with annual installment payments maturing December 16, 2022.	4,285,714	5,142,857
Advance from FHLB with 1.42% fixed rate of interest with annual installment payments maturing August 30, 2023.	<u>5,142,857</u>	<u>0</u>
Total long-term debt	<u>\$26,028,571</u>	<u>\$28,476,190</u>

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, continued

The advances from FHLB are collateralized by the pledging of a combination of 1-4 family residential mortgages, multifamily loans, and investment securities. At December 31, 2016, 1-4 family residential mortgage loans and multifamily loans with a lendable collateral value of \$57,611,388 were pledged to secure these advances. In 2015, the advances were secured by 1-4 family residential mortgage loans and multifamily loans with a lendable collateral value of \$44,138,262. The amount of FHLB Stock held is based on membership and level of FHLB advances. At year end 2016 and 2015, the amount of stock held that is based on membership was \$372,500 and \$336,300, respectively, and the amount of stock held that is based on the level of FHLB advances was \$1,501,700 and \$1,532,900, respectively. At December 31, 2016, the Corporation had approximately \$77,500,000 of unused lines of credit with the FHLB.

The following are maturities of long-term debt for the next five years. At December 31, 2016, there was no floating rate long-term debt; however, two of these advances have convertible call features. Two advances totaling \$10,000,000 have convertible options by the issuer to convert the rates to a 3-month LIBOR. The Bank intends to pay off these advances at the conversion dates. The Bank has the ability to hold this debt until conversion and the means of repayment.

<u>Due in:</u>	<u>Fixed Rate Amount</u>
2017	\$ 0
2018*	15,114,286
2019	3,314,286
2020	3,314,286
2021	1,714,285
Later years	<u>2,571,428</u>
Total long-term debt	<u>\$26,028,571</u>

\*Fixed rate advances with convertible options of \$10,000,000.

### 9. EMPLOYEE BENEFITS AND RETIREMENT PLANS

#### Pension Plan

The Corporation has a noncontributory defined benefit pension plan which covers most employees who have attained the age of 21 years and completed one year of continuous service. The Corporation is providing for the cost of this plan as benefits are accrued based upon actuarial determinations employing the aggregate funding method.

The table of actuarially computed benefit obligations and net assets and the related changes of the Plan at December 31, 2016, 2015, and 2014, is presented below.

	<u>2016</u>	<u>2015</u>	<u>2014</u>
<u>Change in Benefit Obligation</u>			
Benefit obligation at beginning of year	\$13,885,378	\$13,322,751	\$13,308,069
Service cost	0	0	0
Interest cost	764,323	714,604	727,305
Amendments	0	0	0
Settlement	(841,941)	0	0
Benefits paid	(1,131,148)	(1,079,912)	(1,020,747)
Other – net	<u>472,947</u>	<u>927,935</u>	<u>308,124</u>
Benefit obligation at end of year	<u>\$13,149,559</u>	<u>\$13,885,378</u>	<u>\$13,322,751</u>
<u>Change in Plan Assets</u>			
Fair value of plan assets at beginning of year	\$11,420,270	\$11,889,678	\$11,819,296
Actual return on plan assets	576,964	110,504	485,129
Employer contribution	550,000	500,000	606,000
Benefits paid	<u>(1,973,089)</u>	<u>(1,079,912)</u>	<u>(1,020,747)</u>
Fair value of plan assets at end of year	<u>\$10,574,145</u>	<u>\$11,420,270</u>	<u>\$11,889,678</u>
	<u>2016</u>	<u>2015</u>	<u>2014</u>
Funded status	\$(2,575,414)	\$(2,465,108)	\$(1,433,073)
Unrecognized net actuarial (gain)/loss	0	0	0
Unrecognized prior service cost	0	0	0
Pension liability included in other liabilities	<u>\$(2,575,414)</u>	<u>\$(2,465,108)</u>	<u>\$(1,433,073)</u>
Accumulated benefit obligation	<u>\$13,149,559</u>	<u>\$13,885,378</u>	<u>\$13,322,751</u>

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, continued**

Amount recognized in consolidated balance sheet consist of the following:	<u>2016</u>	<u>2015</u>	<u>2014</u>
Accrued Pension	\$ <u>2,575,414</u>	\$ <u>2,465,108</u>	\$ <u>1,433,073</u>
Deferred tax assets	\$ 875,641	\$ 838,137	\$ 487,245
Accumulated other comprehensive income	<u>1,699,773</u>	<u>1,626,971</u>	<u>945,828</u>
Total	<u>\$2,575,414</u>	<u>\$2,465,108</u>	<u>\$1,433,073</u>

Components of Pension Cost	<u>2016</u>	<u>2015</u>	<u>2014</u>
Service cost	\$ 0	\$ 0	\$ 0
Interest cost on benefit obligation	764,323	714,604	727,305
Expected return on plan assets	(775,423)	(928,160)	(932,417)
Other - net	<u>657,260</u>	<u>448,707</u>	<u>471,185</u>
Net periodic pension cost	646,160	235,151	266,073
Partial recognition of loss due to settlement	<u>426,599</u>	<u>0</u>	<u>0</u>
Total	<u>\$1,072,759</u>	<u>\$ 235,151</u>	<u>\$ 266,073</u>

Other changes in plan assets and benefit obligations recognized in comprehensive income:

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Net loss (gain)	\$ 110,306	\$ 1,032,035	\$ (55,700)
Prior service costs	<u>0</u>	<u>0</u>	<u>0</u>
Total recognized in other comprehensive income (loss)	110,306	1,032,035	(55,700)
Net periodic pension cost	646,160	235,151	266,073
Partial recognition of loss due to settlement	<u>426,599</u>	<u>0</u>	<u>0</u>
Total recognized in net periodic pension cost and other comprehensive income	<u>\$ 1,183,065</u>	<u>\$ 1,267,186</u>	<u>\$ 210,373</u>

After adopting ASC Topic 960, Employer's Accounting for Deferred Benefit Pension Plan and Other Postretirement Plans, and freezing its pension retirement plan, the Corporation increased the accrued liability by \$110,306 in 2016 and \$1,032,035 in 2015. Also, changes were made to other comprehensive income (loss) of \$(72,802) for 2016 and \$(681,143) for 2015 on a pre-tax basis. During 2016, the fair value of the plan assets decreased \$846,125.

At December 31, 2016, the plan assets included cash and cash equivalents, certificates of deposits with banks, U.S. government agency securities, corporate notes, and equity securities.

Assumptions used to determine the benefit obligation as of December 31, 2016 and 2015 respectively were:

Weighted-Average Assumptions as of December 31	<u>2016</u>	<u>2015</u>
Discount rate	5.70%	5.75%
Rate of compensation increase	N/A	N/A

For the years ended December 31, 2016, 2015, and 2014, the assumptions used to determine net periodic pension costs are as follows:

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Discount rate	5.75%	5.60%	5.70%
Expected return on plan assets	7.00%	8.00%	8.00%
Rate of compensation increase	N/A	N/A	N/A

The expected rate of return represents the average rate of return to be earned on plan assets over the period the benefits included in the benefit obligation are to be paid. In determining the expected rate of return, the Corporation considers long-term compound annualized returns of historical market data as well as actual returns on the Corporation's plan assets, and applies adjustments that reflect more recent capital market experience.

The Corporation's pension plan investment objective is both security and long-term stability, with moderate growth. The investment strategies and policies employed provide for investments, other than "fixed-dollar" investments, to prevent erosion by inflation. Sufficient funds are held in a liquid nature (money market, short-term securities) to allow for the payment of plan benefits and expenses, without subjecting the funds to loss upon liquidation. In an effort to provide a higher return with lower risk, the fund assets are allocated



## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, continued

between stocks, fixed income securities, and cash equivalents. All plan investments and transactions are in compliance with ERISA and any other law applicable to employee benefit plans. The targeted investment portfolio is allocated up to 33% in equities, 50% to 90% in fixed-income investments, and up to 20% in cash equivalent investments. All the Corporation's equity investments are in mutual funds with a Morningstar rating of 3 or higher, have at least \$300 million in investments, and have been in existence 5 years or more. Fixed income securities include issues of the U.S. government and its agencies and corporate notes. Any corporate note purchased has a rating (by Standard & Poor's or Moody's) of "A" or better. The average maturity of the fixed income portion of the portfolio does not exceed 10 years.

### Pension Asset Allocation and Fair Value Measurement as of December 31

	2016			2015		
	<u>Fair Value</u>	<u>Level 1</u>	<u>%</u>	<u>Fair Value</u>	<u>Level 1</u>	<u>%</u>
Investment at fair value as determined by quoted market price:						
Equity	\$ 3,955,631	\$ 3,955,631	38%	\$ 3,236,166	\$ 3,236,166	28%
Fixed income	<u>2,670,663</u>	<u>2,670,663</u>	<u>25%</u>	<u>4,268,825</u>	<u>4,268,825</u>	<u>37%</u>
Total	\$ 6,626,294	\$ 6,626,294	63%	\$ 7,504,991	\$ 7,504,991	65%
Investment as estimated fair value:						
Certificates of deposit	\$ 3,514,182	\$ 3,514,182	33%	\$ 3,257,418	\$ 3,257,418	29%
Cash and cash equivalent	<u>433,669</u>	<u>433,669</u>	<u>4%</u>	<u>657,861</u>	<u>657,861</u>	<u>6%</u>
Total	\$ 3,947,851	\$ 3,947,851	37%	\$ 3,915,279	\$ 3,915,279	35%
Total	<u>\$10,574,145</u>	<u>\$10,574,145</u>	<u>100%</u>	<u>\$11,420,270</u>	<u>\$11,420,270</u>	<u>100%</u>

All of the pension plan's investments were reported as Level 1 assets and received Level 1 fair value measurement.

ASC Topic 820, Fair Value Measurements and Disclosures, establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy consists of three broad levels: Level 1 inputs consist of unadjusted quoted prices in active markets for identical assets and have the highest priority, and Level 3 inputs have the lowest priority. These levels are:

Level 1 - The fair values of mutual funds, preferred stock, corporate notes, and U.S. government agency securities were based on quoted market prices. Money market funds and certificates of deposit were reported at fair value.

Level 2 - Valuation is based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that were not active, and model-based valuation techniques for which all significant assumptions were observable in the market.

Level 3 - Valuation is generated from model-based techniques that use at least one significant assumption not observable in the market. These unobservable assumptions reflect estimates of assumptions that market participants would use in pricing the asset or liability. Valuation techniques include use of option pricing models, discounted cash flow models and similar techniques.

### Estimated Contributions

The Corporation expects to contribute \$500,000 to its pension plan in 2017.

### Estimated Future Benefit Payments

The following benefit payments, which reflect expected future service and decrements as appropriate, are expected to be paid for fiscal years beginning:

2017	\$ 1,186,000
2018	1,163,000
2019	1,137,000
2020	1,108,000
2021	1,081,000
Years 2022 – 2026	5,157,000

The estimated amortization amount for 2017 is a net loss of \$521,477, no prior service cost or credit, and no net transition asset or obligation.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, continued

### Southwest Georgia Bank 401(K) Plan

In place of the Corporation's frozen defined pension retirement plan, the Corporation offers its employees a 401(K) Plan. This 401(K) plan is a qualified defined contribution plan as provided for under Section 401(K) of the Internal Revenue Code. This plan is a "safe-harbor" plan meaning that the Corporation will match contributions dollar for dollar for the first four percent of salary participants defer into the plan. The plan does allow for discretionary match in excess of the four percent and that the participants are allowed to defer the maximum amount of salary. The Corporation matched the employee participants for the first four percent of salary contributing to the plan \$186,253, \$188,338, and \$202,233 for the years ended December 31, 2016, 2015, and 2014, respectively.

### Employee Stock Ownership Plan

The Corporation has a nondiscriminatory Employee Stock Ownership Plan and Trust (the "ESOP") administered by a trustee. The plan was established to purchase and hold Southwest Georgia Financial Corporation stock for all eligible employees. Contributions to the plan are made solely by the Corporation and are at the discretion of the Board of Directors. The annual amount of the contribution is determined by taking into consideration the financial conditions, profitability, and fiscal requirements of the Corporation. There were contributions of \$400,000, \$294,642, and \$321,000 for the years ended December 31, 2016, 2015, and 2014, respectively. Contributions to eligible participants are based on percentage of annual compensation. As of December 31, 2016, the ESOP holds 262,104 shares of the Corporation's outstanding common stock. All 249,991 released shares are allocated to the participants. The 12,113 unreleased shares are pledged as collateral for an \$185,000 long-term debt incurred from repurchasing participants' shares. Dividends paid by the Corporation on ESOP shares are allocated to the participants based on shares held. ESOP shares are included in the Corporation's outstanding shares and earnings per share computation.

### Directors Deferred Compensation Plan

The Corporation has a voluntary deferred compensation plan for the Board of Directors administered by an insurance company. The plan stipulates that if a director participates in the Plan for four years, the Corporation will pay the director future monthly income for ten years beginning at normal retirement age, and the Corporation will make specified monthly payments to the director's beneficiaries in the event of his or her death prior to the completion of such payments. The plan is funded by life insurance policies with the Corporation as the named beneficiary. This plan is closed to new director enrollment and participation.

### Directors and Executive Officers Stock Purchase Plan

The Corporation has adopted a stock purchase plan for the executive officers and directors of Southwest Georgia Financial Corporation. Under the plan, participants may elect to contribute up to \$900 monthly of salary or directors' fees and receive corporate common stock with an aggregate value of two times their contribution. The expense incurred during 2016, 2015, and 2014 on the part of the Corporation totaled \$290,573, \$282,600, and \$287,150, respectively.

### Stock Option Plan

Effective March 19, 1997, the Corporation established a Key Individual Stock Option Plan (the "Option Plan") which provides for the issuance of options to key employees and directors of the Corporation. In April 1997, the Option Plan was approved by the Corporation's stockholders, and was effective for the duration of ten years. Under the Option Plan, the exercise price of each option equals the market price of the Corporation's stock on the grant date for a term of ten years. All of these stock options are fully vested. The fair value of each stock option grant is estimated on the grant date using an option-pricing model using weighted-average assumptions. The fair value of each option was expensed over its vesting period. A maximum of 196,680 shares of common stock were authorized for issuance with respect to options granted under the Option Plan. The Option Plan provided for the grant of incentive stock options and nonqualified stock options to key employees of the Corporation. The Option Plan is administered by the Personnel Committee of the Board of Directors.

The following table sets forth the number of stock options granted, the average fair value of options granted, and the weighted-average assumptions used to determine the fair value of the stock options granted.

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Number of stock options granted	0	0	0
Average fair value of stock options granted	0	0	0
Number of option shares exercisable	0	1,000	2,500
Average price of stock options exercisable	\$ 0.00	\$ 19.95	\$ 21.21

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, continued

A summary of the status of the Corporation's Option Plan as of December 31, 2016, 2015 and 2014, and the changes in stock options during the years are presented below:

	No. of Shares	Average Price
Outstanding at December 31, 2013	10,900	\$ 20.19
Granted	0	0
Expired	(8,400)	19.89
Exercised	0	0
Outstanding at December 31, 2014	2,500	\$ 21.21
Granted	0	0
Expired	(1,500)	22.05
Exercised	0	0
Outstanding at December 31, 2015	1,000	\$ 19.95
Granted	0	0
Expired	(1,000)	19.95
Exercised	0	0
Outstanding at December 31, 2016	0	\$ 0.00

As of December 31, 2016, all stock options had expired.

### Dividend Reinvestment and Share Purchase Plan

The Corporation maintains a dividend reinvestment and share purchase plan. The purpose of the plan is to provide stockholders of record of the Corporation's common stock, who elect to participate in the plan, with a simple and convenient method of investing cash dividends and voluntary cash contributions in shares of the common stock without payment of any brokerage commissions or other charges. Eligible participants may purchase common stock through automatic reinvestment of common stock dividends on all or partial shares and make additional voluntary cash payments of not less than \$5 nor more than \$5,000 per month. The participant's price of common stock purchased with dividends or voluntary cash payments will be the average price of all shares purchased in the open market, or if issued from unissued shares or treasury stock the price will be the average of the high and low sales prices of the stock on the NYSE MKT LLC on the dividend payable date or other purchase date. During the years ended December 31, 2016, 2015, and 2014, shares issued through the plan were 6,955, 6,702, and 6,503, respectively, at an average price of \$15.92, \$14.73, and \$13.70, per share, respectively. These numbers of shares and average price per share are not adjusted by stock dividends.

### Equity Incentive Award

The Corporation has a 2013 Omnibus Incentive Plan (the "Incentive Plan") that was approved by our shareholders at the Corporation's 2014 Annual Meeting. The Incentive Plan was established to attract, retain and motivate the Corporation's employees, consultants, advisors and directors, to promote the success of our business by linking their personal interests to those of our shareholders and to encourage stock ownership on the part of management. Under the Incentive Plan, the Corporation may issue a maximum aggregate amount of 125,000 shares of common stock pursuant to (i) stock options, which includes incentive stock options and non-qualified stock options, (ii) stock appreciation rights, (iii) restricted stock awards, (iv) restricted stock units, (v) incentive awards, (vi) other stock-based awards and (vii) dividend equivalents. The Corporation may also grant cash-based awards under the Incentive Plan. The Corporation did not grant any equity incentive awards during 2016 or 2015.

## 10. INCOME TAXES

Components of income tax expense for 2016, 2015, and 2014 are as follows:

	2016	2015	2014
Current expense (benefit)	\$ 1,163,230	\$ 900,543	\$ 435,943
Deferred taxes (benefit)	<u>(10,754)</u>	<u>(73,379)</u>	<u>303,614</u>
Total income taxes	<u>\$ 1,152,476</u>	<u>\$ 827,164</u>	<u>\$ 739,557</u>

The reasons for the difference between the federal income taxes in the consolidated statements of income and the amount and percentage computed by the applying the combine statutory federal and state income tax rate to income taxes are as follows:

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, continued**

	2016		2015		2014	
	Amount	%	Amount	%	Amount	%
Taxes at statutory income tax rate	\$ 1,763,394	34.0	\$ 1,428,272	34.0	\$ 1,238,752	34.0
Reductions in taxes resulting from exempt income	(547,556)	(10.6)	(540,861)	(12.9)	(454,779)	(12.5)
Other timing differences	(63,362)	(1.2)	(60,247)	(1.4)	(44,416)	(1.2)
Total income taxes	<u>\$ 1,152,476</u>	<u>22.2</u>	<u>\$ 827,164</u>	<u>19.7</u>	<u>\$ 739,557</u>	<u>20.3</u>

The sources of timing differences for tax reporting purposes and the related deferred taxes recognized in 2016, 2015, and 2014 are summarized as follows:

	2016	2015	2014
Nonqualified retirement plan	\$ 0	\$ (7,229)	\$ 0
Deferred gain on covered transaction	498	(24,154)	0
Nonaccrual loan interest	32,157	(34,104)	0
Foreclosed assets expenses	(3,413)	(4,577)	74,130
Bad debt expense in excess of tax	(31,405)	27,850	(12,441)
Realized impairment gain on equity securities	0	13,233	163,625
Accretion of discounted bonds	33,187	26,370	20,058
Gain on disposition of discounted bonds	(23,059)	(3,503)	(2,470)
Book and tax depreciation difference	(18,719)	(67,265)	60,712
Total deferred taxes	<u>\$ (10,754)</u>	<u>\$ (73,379)</u>	<u>\$ 303,614</u>

	December 31	
	2016	2015
Deferred tax assets:		
Nonaccrual loan interest	\$ 1,947	\$ 34,104
Deferred gain on covered transaction	23,657	24,154
Alternative minimum tax	434,920	564,920
Foreclosed assets expenses	9,618	6,205
Intangible asset amortization	298,699	298,699
Bad debt expense in excess of tax	1,062,364	1,030,959
Realized loss on other-than-temporarily impaired equity securities	214,353	214,353
Nonqualified retirement plan	0	0
Pension plan	875,641	838,137
Total deferred tax assets	<u>2,921,199</u>	<u>3,011,531</u>
Deferred tax liabilities:		
Accretion on bonds and gain on discounted bonds	69,133	59,005
Book and tax depreciation difference	243,593	262,312
Unrealized gain (loss) on securities available for sale	(44,416)	243,979
Total deferred tax liabilities	<u>268,310</u>	<u>565,296</u>
Net deferred tax assets	<u>\$ 2,652,889</u>	<u>\$ 2,446,235</u>

**11. RELATED PARTY TRANSACTIONS**

The ESOP held 262,104 shares of the Corporation's stock as of December 31, 2016, of which 12,113 shares have been pledged. In the normal course of business, the Bank has made loans at prevailing interest rates and terms to directors and executive officers of the Corporation and its subsidiaries, and to their affiliates. The aggregate indebtedness to the Bank of these related parties approximated \$1,431,000 and \$1,209,000 at December 31, 2016 and 2015, respectively. During 2016, approximately \$2,311,000 of such loans were made, and repayments totaled approximately \$2,217,000. None of these above mentioned loans were restructured, nor were any related party loans charged off during 2016 or 2015. Also, during 2016 and 2015, directors and executive officers had approximately \$2,941,000 and \$2,586,000, respectively, in deposits with the Bank.

**12. COMMITMENTS, CONTINGENT LIABILITIES, AND FINANCIAL INSTRUMENTS WITH OFF-BALANCE SHEET RISK**

In the normal course of business, various claims and lawsuits may arise against the Corporation. Management, after reviewing with counsel all actions and proceedings, considers that the aggregate liability or loss, if any, will not be material.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, continued

The Corporation is a party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers and to reduce its own risk exposure to fluctuations in interest rates. These financial instruments include commitments to extend credit in the form of loans or through letters of credit. The instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amounts recognized in the Consolidated Balance Sheets. The contract or notional amounts of the instruments reflect the extent of involvement the Corporation has in particular classes of financial instruments.

Commitments to extend credit are contractual obligations to lend to a customer as long as all established contractual conditions are satisfied. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee by a customer.

Standby letters of credit and financial guarantees are conditional commitments issued by the Corporation to guarantee the performance of a customer to a third party. Standby letters of credit and financial guarantees are generally terminated through the performance of a specified condition or through the lapse of time.

The Corporation's exposure to credit loss in the event of nonperformance by the other party to commitments to extend credit and standby letters of credit is represented by the contractual or notional amounts of these instruments. As these off-balance sheet financial instruments have essentially the same credit risk involved in extending loans, the Corporation generally uses the same credit and collateral policies in making these commitments and conditional obligations as it does for on-balance sheet instruments. Since many of the commitments to extend credit and standby letters of credit are expected to expire without being drawn upon, the contractual or notional amounts do not represent future cash requirements.

The contractual or notional amounts of financial instruments having credit risk in excess of that reported in the Consolidated Balance Sheets are as follows:

	<u>Dec. 31, 2016</u>	<u>Dec. 31, 2015</u>
Financial instruments whose contract amounts represent credit risk:		
Commitments to extend credit	\$ <u>34,031,164</u>	\$ <u>24,780,028</u>
Standby letters of credit and financial guarantees	\$ <u>2,660,000</u>	\$ <u>960,000</u>

The Corporation's operating leases are comprised of purchase obligations for data processing services and a rental agreement for our loan production office in Tifton, Georgia. We have no capital lease obligations. The following table shows scheduled future cash payments under those obligations as of December 31, 2016.

	<u>Payments Due by Period</u>				
	<u>Total</u>	Less than 1 <u>Year</u>	1-3 <u>Years</u>	4-5 <u>Years</u>	After 5 <u>Years</u>
Operating leases	\$36,192	\$20,748	\$10,296	\$5,148	\$ 0

Rental expenses were \$15,600, \$1,300, and \$0 for the years ended December 31, 2016, 2015, and 2014, respectively.

### 13. FAIR VALUE MEASUREMENTS AND DISCLOSURES

Effective January 1, 2008, the Corporation adopted ASC Topic 820, Fair Value Measurements and Disclosures, which provides a framework for measuring fair value under GAAP. ASC Topic 820 applies to all financial statement elements that are being measured and reported on a fair value basis.

The Corporation utilizes fair value measurements to record fair value adjustments to certain assets and liabilities and to determine fair value disclosures. Securities available for sale are recorded at fair value on a recurring basis. From time to time, the Corporation may be required to record at fair value other assets on a nonrecurring basis, such as impaired loans and foreclosed real estate. Additionally, the Corporation is required to disclose, but not record, the fair value of other financial instruments.

#### Fair Value Hierarchy:

Under ASC Topic 820, the Corporation groups assets and liabilities at fair value in three levels, based on the markets in which the assets and liabilities are traded and the reliability of the assumptions used to determine fair value. These levels are:

Level 1 – Valuation is based upon quoted prices for identical instruments traded in active markets.

Level 2 – Valuation is based upon quoted prices for similar instruments in active markets, quoted prices for identical or

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, continued

similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market.

Level 3 – Valuation is generated from model-based techniques that use at least one significant assumption not observable in the market. These unobservable assumptions reflect estimates of assumptions that market participants would use in pricing the asset or liability. Valuation techniques include use of option pricing models, discounted cash flow models and similar techniques.

Following is a description of valuation methodologies used for assets and liabilities which are either recorded or disclosed at fair value.

### Cash and Cash Equivalents:

For disclosure purposes for cash, due from banks, federal funds sold and certificates of deposit in other banks, the carrying amount is a reasonable estimate of fair value.

### Investment Securities Available for Sale:

Investment securities available for sale are recorded at fair value on a recurring basis. Fair value measurement is based upon quoted prices, if available. If quoted prices are not available, fair values are measured using independent pricing models or other model-based valuation techniques such as the present value of future cash flows, adjusted for the security's credit rating, prepayment assumptions and other factors such as credit loss assumptions. Level 1 securities include those traded on an active exchange, such as the New York Stock Exchange and U.S. Treasury securities that are traded by dealers or brokers in active over-the-counter market funds. Level 2 securities include mortgage-backed securities issued by government sponsored enterprises and state, county and municipal bonds. Securities classified as Level 3 include asset-backed securities in less liquid markets.

### Investment Securities Held to Maturity:

Investment securities held to maturity are not recorded at fair value on a recurring basis. For disclosure purposes, fair value measurement is based upon quoted prices, if available.

### Federal Home Loan Bank Stock:

For disclosure purposes, the carrying value of other investments approximate fair value.

### Loans:

The Corporation does not record loans at fair value on a recurring basis. However, from time to time, a loan is considered impaired and a specific allocation is established within the allowance for loan losses. Loans for which it is probable that payment of interest and principal will not be made in accordance with the contractual terms of the loan agreement are considered impaired. Once a loan is identified as individually impaired, management measures impairment in accordance with ASC Topic 310, *Accounting by Creditors for Impairment of a Loan*. The fair value of impaired loans is estimated using one of three methods, including collateral value, market value of similar debt, and discounted cash flows. Those impaired loans not requiring an allowance represent loans for which the fair value of the expected repayments or collateral exceed the recorded investments in such loans. In accordance with ASC Topic 820, impaired loans where an allowance is established based on the fair value of collateral require classification in the fair value hierarchy. When the fair value of the collateral is based on an observable market price or a current appraised value, the Corporation records the impaired loan as nonrecurring Level 2. When an appraised value is not available or management determines the fair value of the collateral is further impaired below the appraised value and there is no observable market price, the Corporation records the impaired loan as nonrecurring Level 3.

For disclosure purposes, the fair value of fixed rate loans which are not considered impaired, 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 unimpaired variable rate loans, the carrying amount is a reasonable estimate of fair value for disclosure purposes.

### Foreclosed Assets:

Other real estate properties are adjusted to fair value upon transfer of the loans to other real estate. Subsequently, other real estate assets are carried at the lower of carrying value or fair value. Fair value is based upon independent market prices, appraised values of the collateral or management's estimation of the value of the collateral. When the fair value of the collateral is based on an observable market price or a current appraised value, the Corporation records the other real estate as nonrecurring Level 2. When an appraised value is not available or management determines the fair value of the collateral is further impaired below the appraised value and there is no observable market price, the Corporation records the other real estate asset as nonrecurring Level 3.

### Deposits:

For disclosure purposes, the fair value of demand deposits, savings accounts, NOW accounts and money market deposits is the amount payable on demand at the reporting date, while the fair value of fixed maturity certificates of deposit is estimated by discounting the future cash flows using current rates at which comparable certificates would be issued.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, continued

### Federal Funds Purchased:

For disclosure purposes, the carrying amount for Federal funds purchased is a reasonable estimate of fair value due to the short-term nature of these financial instruments.

### FHLB Advances:

For disclosure purposes, the fair value of the FHLB fixed rate borrowing is estimated using discounted cash flows, based on the current incremental borrowing rates for similar types of borrowing arrangements.

### Commitments to Extend Credit and Standby Letters of Credit:

Because commitments to extend credit and standby letters of credit are made using variable rates and have short maturities, the carrying value and the fair value are immaterial for disclosure.

### Assets Recorded at Fair Value on a Recurring Basis:

The table below presents the recorded amount of assets measured at fair value on a recurring basis as of December 31, 2016 and 2015.

<u>December 31, 2016</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
Investment securities available for sale:				
U.S. government treasury securities	\$ 0	\$ 962,150	\$ 0	\$ 962,150
U.S. government agency securities	0	40,984,897	0	40,984,897
State and municipal securities	0	6,452,597	0	6,452,597
Residential mortgage-backed securities	0	2,529,314	0	2,529,314
Corporate notes	0	2,524,165	0	2,524,165
Equity securities	0	112,380	0	112,380
Total	<u>\$ 0</u>	<u>\$ 53,565,503</u>	<u>\$ 0</u>	<u>\$ 53,565,503</u>

<u>December 31, 2015</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
Investment securities available for sale:				
U.S. government agency securities	\$ 0	\$ 42,642,322	\$ 0	\$ 42,642,322
State and municipal securities	0	2,607,684	0	2,607,684
Residential mortgage-backed securities	0	3,741,445	0	3,741,445
Corporate notes	0	2,472,960	0	2,472,960
Equity securities	0	12,000	0	12,000
Total	<u>\$ 0</u>	<u>\$ 51,476,411</u>	<u>\$ 0</u>	<u>\$ 51,476,411</u>

### Assets Recorded at Fair Value on a Nonrecurring Basis:

The Corporation may be required, from time to time, to measure certain assets at fair value on a nonrecurring basis in accordance with GAAP. These include assets that are measured at the lower of cost or market that were recognized at fair value below cost at the end of the period. Assets measured at fair value on a nonrecurring basis are included in the table below as of December 31, 2016 and 2015.

<u>December 31, 2016</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
Foreclosed assets	\$ 0	\$ 0	\$ 126,713	\$ 126,713
Impaired loans	0	0	3,011,472	3,011,472
Total assets at fair value	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 3,138,185</u>	<u>\$ 3,138,185</u>

<u>December 31, 2015</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
Foreclosed assets	\$ 0	\$ 0	\$ 81,750	\$ 81,750
Impaired loans	0	0	5,254,501	5,254,501
Total assets at fair value	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 5,336,251</u>	<u>\$ 5,336,251</u>

Foreclosed properties that are included above as measured at fair value on a nonrecurring basis are those properties that resulted from a loan that had been foreclosed and charged down or have been written down subsequent to foreclosure. Foreclosed properties are generally recorded at the appraised value less estimated selling costs in the range of 15 – 20%. Loans that are reported above as being measured at fair value on a nonrecurring basis are generally impaired loans that have been either partially charged off or have specific reserves assigned to them. Nonaccrual impaired loans that are collateral dependent are generally written down to a range of 80 – 85% of appraised value which considers the estimated costs to sell. Specific reserves are established for impaired loans based on appraised value of collateral or discounted cash flows.

The carrying amount and estimated fair values of the Corporation's assets and liabilities which are required to be either disclosed or recorded at fair value at December 31, 2016 and 2015, are as follows:

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, continued**

<u>December 31, 2016</u>	Carrying <u>Amount</u>	Estimated Fair Value			
		<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
		(Dollars in thousands)			
Assets:					
Cash and cash equivalents	\$ 26,520	\$ 26,520	\$ 0	\$ 0	\$ 26,520
Certificates of deposit in other banks	0	0	0	0	0
Investment securities available for sale	53,566	0	53,566	0	53,566
Investment securities held to maturity	54,603	0	55,123	0	55,123
Federal Home Loan Bank stock	1,874	0	1,874	0	1,874
Loans, net	289,400	0	286,869	3,011	289,880
Liabilities:					
Deposits	371,493	0	371,793	0	371,793
Federal Home Loan Bank advances	34,476	0	34,337	0	34,337

<u>December 31, 2015</u>	Carrying <u>Amount</u>	Estimated Fair Value			
		<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
		(Dollars in thousands)			
Assets:					
Cash and cash equivalents	\$ 31,080	\$ 31,080	\$ 0	\$ 0	\$ 31,080
Certificates of deposit in other banks	245	245	0	0	245
Investment securities available for sale	51,476	0	51,476	0	51,476
Investment securities held to maturity	60,889	0	62,199	0	62,199
Federal Home Loan Bank stock	1,869	0	1,869	0	1,869
Loans, net	247,754	0	243,460	5,255	248,715
Liabilities:					
Deposits	339,016	0	339,337	0	339,337
Federal Home Loan Bank advances	36,067	0	35,964	0	35,964

Limitations:

Fair value estimates are made at a specific point in time, based on relevant market information and information about the financial statement element. 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 included herein are based on existing on- and off-balance-sheet financial instruments without attempting to estimate the value of anticipated future business and the fair value of assets and liabilities that are not required to be recorded or disclosed at fair value like 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.

14. SUPPLEMENTAL FINANCIAL DATA

Components of other income and other operating expense in excess of one percent of gross revenue for the respective periods are as follows:

	Years Ended December 31		
	<u>2016</u>	<u>2015</u>	<u>2014</u>
Income:			
Bank card interchange fees	\$506,506	\$487,933	\$466,455
Expense:			
Other professional fees	\$202,267	\$230,920	\$232,159
Director & board committee fees	\$328,919	\$336,458	\$349,597
FDIC insurance assessment	\$201,605	\$240,223	\$234,555
Administrative expense – employee benefit plans	\$231,311	\$224,021	\$207,299



**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, continued**

**15. STOCKHOLDERS' EQUITY / REGULATORY MATTERS**

Dividends paid by the Bank subsidiary are the primary source of funds available to the parent company for payment of dividends to its stockholders and other needs. Banking regulations limit the amount of dividends that may be paid without prior approval of the Bank's regulatory agency. At December 31, 2016, approximately \$2,049,022 of the Bank's net assets were available for payment of dividends without prior approval from the regulatory authorities.

The Federal Reserve Board requires that banks maintain reserves based on their average deposits in the form of vault cash and average deposit balances at the Federal Reserve Banks. For the year ended December 31, 2016, the Bank had a total reserve requirement of \$5,367,000.

The Corporation (on a consolidated basis) and the Bank are 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 such agencies that, if undertaken, could have a direct material effect on the Corporation's and Bank's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Corporation and the Bank must meet specific capital guidelines that involve quantitative measures of their assets, liabilities and certain off-balance-sheet items as calculated under regulatory accounting practices. The capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors. Prompt corrective action provisions are not applicable to bank holding companies.

Quantitative measures established by regulation to ensure capital adequacy require the Corporation and the Bank to maintain minimum amounts and ratios (set forth in the following table) of Total, Common Equity Tier I, and Tier I capital (as defined in the regulations) to risk-weighted assets (as defined) and of Tier I capital to average assets (as defined). As of December 31, 2016 and 2015, the Corporation and the Bank meets all capital adequacy requirements to which they are subject.

As of December 31, 2016, the most recent notification from the Federal Deposit Insurance Corporation categorized the Bank as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized, an institution must maintain minimum Total risk-based, Common Equity Tier I risk-based, Tier I risk-based and Tier I leverage ratios as set forth in the following tables. Under the Basel III rules, the Bank must hold a capital conservation buffer above the minimum regulatory risk-based capital ratios. The capital conservation buffer is being phased in from 0.0% for 2015 to 2.50% by 2019. The capital conservation buffer for 2016 is 0.625%. There are no conditions or events since the notification that management believes have changed the Bank's category. The Corporation's and the Bank's actual capital amounts and ratios as of December 31, 2016 and 2015, are also presented in the table.

As a result of regulatory limitations at December 31, 2016, approximately \$34,563,138 of the parent company's investments in net assets of the subsidiary bank of \$36,612,160, as shown in the accompanying condensed balance sheets in Note 16, was restricted from transfer by the subsidiary bank to the parent company in the form of cash dividends.

The Corporation's and the Bank's ratios under the above rules at December 31, 2016 and 2015, are set forth in the following tables. The Corporation's leverage ratio at December 31, 2016, was 8.87%.

<u>As of December 31, 2016</u>	<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>
<u>Southwest Georgia Financial Corporation</u>						
Common equity Tier 1 (to risk-weighted assets)	\$40,187,232	13.03%	\$13,878,302	≥ 5.13%	N/A*	N/A*
Total capital (to risk-weighted assets)	\$43,311,843	14.04%	\$24,672,536	≥ 8.63%	N/A*	N/A*
Tier I capital (to risk-weighted assets)	\$40,187,232	13.03%	\$18,504,402	≥ 6.63%	N/A*	N/A*
Leverage (tier I capital to average assets)	\$40,187,232	8.87%	\$18,113,752	≥ 4.00%	N/A*	N/A*
<u>Southwest Georgia Bank</u>						
Common equity Tier 1 (to risk-weighted assets)	\$38,377,058	12.47%	\$13,848,917	≥ 5.13%	\$20,003,991	≥ 6.50%
Total capital (to risk-weighted assets)	\$41,501,669	13.49%	\$24,620,297	≥ 8.63%	\$30,775,371	≥ 10.00%
Tier I capital (to risk-weighted assets)	\$38,377,058	12.47%	\$18,465,223	≥ 6.63%	\$24,620,297	≥ 8.00%
Leverage (tier I capital to average assets)	\$38,377,058	8.49%	\$18,077,111	≥ 4.00%	\$22,596,389	≥ 5.00%

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, continued**

<u>As of December 31, 2015</u>	<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>
<u>Southwest Georgia Financial Corporation</u>						
Common equity Tier 1 (to risk-weighted assets)	\$37,230,740	14.07%	\$11,907,692	≥ 4.50%	N/A*	N/A*
Total capital (to risk-weighted assets)	\$40,262,982	15.22%	\$21,169,230	≥ 8.00%	N/A*	N/A*
Tier I capital (to risk-weighted assets)	\$37,230,740	14.07%	\$15,876,922	≥ 6.00%	N/A*	N/A*
Leverage (tier I capital to average assets)	\$37,230,740	9.13%	\$16,316,153	≥ 4.00%	N/A*	N/A*
<u>Southwest Georgia Bank</u>						
Common equity Tier 1 (to risk-weighted assets)	\$34,279,795	12.99%	\$11,874,310	≥ 4.50%	\$17,151,781	≥ 6.50%
Total capital (to risk-weighted assets)	\$37,312,037	14.14%	\$21,109,884	≥ 8.00%	\$26,387,355	≥ 10.00%
Tier I capital (to risk-weighted assets)	\$34,279,795	12.99%	\$15,832,413	≥ 6.00%	\$21,109,884	≥ 8.00%
Leverage (tier I capital to average assets)	\$34,279,795	8.43%	\$16,274,473	≥ 4.00%	\$20,343,091	≥ 5.00%

\*N/A - As of December 31, 2016, the Corporation met the definition under the Basel III Capital Rules of a small bank holding company and, therefore, was exempt from consolidated risk-based and leverage capital adequacy guidelines for bank holding companies.

**16. PARENT COMPANY FINANCIAL DATA**

Southwest Georgia Financial Corporation's condensed balance sheets as of December 31, 2016 and 2015, and its related condensed statements of operations and cash flows for the years ended are as follows:

Condensed Balance Sheets  
as of December 31, 2016 and 2015  
(Dollars in thousands)

	<u>2016</u>	<u>2015</u>
<b>ASSETS</b>		
Cash	\$ 940	\$ 1,919
Investment in consolidated wholly-owned bank subsidiary, at equity	36,612	33,147
Loans	185	363
Other assets	<u>685</u>	<u>669</u>
Total assets	\$ <u>38,422</u>	\$ <u>36,098</u>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Total liabilities	\$ <u>0</u>	\$ <u>0</u>
Stockholders' equity:		
Common stock, \$1 par value, 5,000,000 shares authorized, 4,293,835 shares for 2016 and 2015 issued	4,294	4,294
Additional paid-in capital	31,701	31,701
Retained earnings	30,334	27,370
Accumulated other comprehensive loss	(1,786)	(1,153)
Treasury stock, at cost, 1,746,398 for 2016 and 1,745,998 for 2015	(26,121)	(26,114)
Total stockholders' equity	<u>38,422</u>	<u>36,098</u>
Total liabilities and stockholders' equity	\$ <u>38,422</u>	\$ <u>36,098</u>

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, continued**

16. PARENT COMPANY FINANCIAL DATA (continued)

Condensed Statements of Income and Expense  
for the years ended December 31, 2016, 2015, and 2014  
(Dollars in thousands)

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Income:			
Dividend received from bank subsidiary	\$ 0	\$ 2,685	\$ 1,000
Interest income	<u>23</u>	<u>12</u>	<u>10</u>
Total income	<u>23</u>	<u>2,697</u>	<u>1,010</u>
Expenses:			
Other	<u>178</u>	<u>141</u>	<u>166</u>
Income before income taxes and equity in Undistributed income of bank subsidiary	( 155)	2,556	844
Income tax benefit – allocated from consolidated return	( 91)	( 87)	( 88)
Income before equity in undistributed income of subsidiary	( 64)	2,643	932
Equity in undistributed income of subsidiary	<u>4,098</u>	<u>731</u>	<u>1,972</u>
Net income	4,034	3,374	2,904
Retained earnings – beginning of year	27,370	25,015	22,926
Cash dividend declared	( 1,070)	( 1,019)	( 815)
Retained earnings – end of year	\$ <u>30,334</u>	\$ <u>27,370</u>	\$ <u>25,015</u>

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, continued**

16. PARENT COMPANY FINANCIAL DATA (continued)

Condensed Statements of Cash Flows  
for the years ended December 31, 2016, 2015, and 2014  
(Dollars in thousands)

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Cash flow from operating activities:			
Net income	\$ 4,034	\$ 3,374	\$ 2,904
Adjustments to reconcile net income to net cash used by operating activities:			
Equity in undistributed earnings of Subsidiary	(4,098)	(731)	(1,972)
Changes in:			
Other assets	<u>(16)</u>	<u>(34)</u>	<u>(68)</u>
Net cash provided (used) for operating activities	<u>(80)</u>	<u>2,609</u>	<u>864</u>
Cash flow from investing activities:			
Net change in loans	<u>178</u>	<u>(347)</u>	<u>4</u>
Net cash provided (used) for investing activities	<u>178</u>	<u>(347)</u>	<u>4</u>
Cash flow from financing activities:			
Cash dividend paid to stockholders	(1,070)	(1,019)	(815)
Payment to repurchase common stock	<u>(7)</u>	<u>0</u>	<u>0</u>
Net cash used for financing activities	<u>(1,077)</u>	<u>(1,019)</u>	<u>(815)</u>
Increase (decrease) in cash	(979)	1,243	53
Cash – beginning of year	<u>1,919</u>	<u>676</u>	<u>623</u>
Cash – end of year	\$ <u><u>940</u></u>	\$ <u><u>1,919</u></u>	\$ <u><u>676</u></u>

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, continued**

**17. EARNINGS PER SHARE**

Earnings per share are based on the weighted average number of common shares outstanding during the year.

	Year Ended December 31, 2016		
	<u>Income</u>	<u>Weighted Average Shares</u>	<u>Per Share Amount</u>
Basic earnings per share:			
Net income	\$ <u>4,033,977</u>	<u>2,547,778</u>	\$ <u>1.58</u>
Diluted earnings per share:			
Net income	\$ <u>4,033,977</u>	<u>2,547,778</u>	\$ <u>1.58</u>

	Year Ended December 31, 2015		
	<u>Income</u>	<u>Weighted Average Shares</u>	<u>Per Share Amount</u>
Basic earnings per share:			
Net income	\$ <u>3,373,635</u>	<u>2,547,837</u>	\$ <u>1.32</u>
Diluted earnings per share:			
Net income	\$ <u>3,373,635</u>	<u>2,547,837</u>	\$ <u>1.32</u>

	Year Ended December 31, 2014		
	<u>Income</u>	<u>Weighted Average Shares</u>	<u>Per Share Amount</u>
Basic earnings per share:			
Net income	\$ <u>2,903,830</u>	<u>2,547,837</u>	\$ <u>1.14</u>
Diluted earnings per share:			
Net income	\$ <u>2,903,830</u>	<u>2,547,837</u>	\$ <u>1.14</u>

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, continued

18. QUARTERLY DATA

SOUTHWEST GEORGIA FINANCIAL CORPORATION  
 QUARTERLY DATA  
 (UNAUDITED)  
 (Dollars in thousands)

	For the Year 2016			
	Fourth	Third	Second	First
Interest and dividend income	\$ 4,449	\$ 4,408	\$ 4,287	\$ 4,269
Interest expense	431	412	394	375
Net interest income	4,018	3,996	3,893	3,894
Provision for loan losses	45	45	40	30
Net interest income after provision for loan losses	3,973	3,951	3,853	3,864
Noninterest income	1,076	1,060	1,097	1,226
Noninterest expenses	3,767	3,739	3,680	3,728
Income before income taxes	1,282	1,272	1,270	1,362
Provision for income taxes	280	299	259	314
Net income	<u>\$ 1,002</u>	<u>\$ 973</u>	<u>\$ 1,011</u>	<u>\$ 1,048</u>
Earnings per share of common stock:				
Basic	<u>\$ .39</u>	<u>\$ .38</u>	<u>\$ .40</u>	<u>\$ .41</u>
Diluted	<u>\$ .39</u>	<u>\$ .38</u>	<u>\$ .40</u>	<u>\$ .41</u>

	For the Year 2015			
	Fourth	Third	Second	First
Interest and dividend income	\$ 3,946	\$ 3,889	\$ 3,898	\$ 3,695
Interest expense	353	325	324	315
Net interest income	3,593	3,564	3,574	3,380
Provision for loan losses	0	51	45	45
Net interest income after provision for loan losses	3,593	3,513	3,529	3,335
Noninterest income	1,046	1,008	1,045	1,161
Noninterest expenses	3,590	3,459	3,493	3,487
Income before income taxes	1,049	1,062	1,081	1,009
Provision for income taxes	206	205	216	200
Net income	<u>\$ 843</u>	<u>\$ 857</u>	<u>\$ 865</u>	<u>\$ 809</u>
Earnings per share of common stock:				
Basic	<u>\$ .33</u>	<u>\$ .33</u>	<u>\$ .34</u>	<u>\$ .32</u>
Diluted	<u>\$ .33</u>	<u>\$ .33</u>	<u>\$ .34</u>	<u>\$ .32</u>

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, continued

### 19. SEGMENT REPORTING

The Corporation operations are divided into four reportable business segments: The Retail and Commercial Banking Services, Insurance Services, Wealth Strategies Services, and Financial Management Services. These operating segments have been identified primarily based on the Corporation's organizational structure.

The Retail and Commercial Banking Services segment serves consumer and commercial customers by offering a variety of loan and deposit products, and other traditional banking services.

The Insurance Services segment offers clients a full spectrum of commercial and personal lines insurance products including life, health, property, and casualty insurance.

The Wealth Strategies Services segment provides personal trust administration, estate settlement, investment management, employee retirement benefit services, and the Individual Retirement Account (IRA) administration. Also, this segment offers full-service retail brokerage which includes the sale of retail investment products including stocks, bonds, mutual funds, and annuities.

The Financial Management Services segment is responsible for the management of the investment securities portfolio. It also is responsible for managing financial risks, including liquidity and interest rate risk.

The accounting policies of the segments are the same as those described in the summary of significant accounting policies. The Corporation evaluates performance based on profit or loss from operations after income taxes not including nonrecurring gains or losses.

The Corporation's reportable segments are strategic business units that offer different products and services. They are managed separately because each segment appeals to different markets and, accordingly, requires different technology and marketing strategies.

The Corporation allocates capital and funds used or funds provided for each reportable business segment. Also, each segment is credited or charged for the cost of funds provided or used. These credits and charges are reflected as net intersegment interest income (expense) in the table below. The Corporation does allocate income taxes to the segments. Other revenue represents noninterest income, exclusive of the net gain (loss) on disposition of assets and expenses associated with administrative activities which are not allocated to the segments. Those expenses include audit, compliance, investor relations, marketing, personnel, and other executive or parent company expenditures.

The Corporation does not have operating segments other than those reported. Parent Company and the Administrative Offices financial information is included in the "Other" category, and is deemed to represent an overhead function rather than an operating segment. The Administrative Offices include audit, marketing, information technology, personnel, and the executive office.

The Corporation does not have a single external customer from which it derives 10% or more of its revenue and operates in one geographical area.

Information about reportable business segments, and reconciliation of such information to the consolidated financial statements for the years ended December 31, 2016, 2015, and 2014, are as follows:

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, continued**

	Segment Reporting						Totals
	Retail and Commercial Banking	Insurance Services	Wealth Strategies	Financial Management	Inter- segment Elimination	Other	
	(Dollars in thousands)						
Net Interest Income (expense)							
external customers	\$ 13,837	0	0	1,940	0	24	\$ 15,801
Net intersegment interest income (expense)	1,671	11	(6)	(1,676)	0	0	0
Net Interest Income	15,508	11	(6)	264	0	24	15,801
Provision for Loan Losses	160	0	0	0	0	0	160
Noninterest Income (expense)							
external customers	2,316	1,477	584	80	0	2	4,459
Intersegment noninterest income (expense)	(11)	11	32	0	(32)	0	0
Total Noninterest Income	2,305	1,488	616	80	(32)	2	4,459
Noninterest Expenses:							
Depreciation	738	30	23	57	0	76	924
Amortization of intangibles	0	16	0	0	0	0	16
Other Noninterest expenses	9,260	1,184	585	737	0	2,208	13,974
Total Noninterest expenses	9,998	1,230	608	794	0	2,284	14,914
Pre-tax Income	7,655	269	2	(450)	(32)	(2,258)	5,186
Provision for Income Taxes	1,794	61	(7)	(107)	0	(589)	1,152
Net Income	\$ 5,861	208	9	(343)	(32)	(1,669)	\$ 4,034
Assets	\$ 507,538	1,414	199	148,099	(209,619)	870	\$ 448,501
Expenditures for Fixed Assets	\$ 1,409	15	11	20	0	0	\$ 1,455

Amounts included in the "Other" column are as follows:

	Other
Net interest Income:	
Parent Company	\$ 24
Noninterest Income:	
Executive office miscellaneous income	2
Noninterest Expenses:	
Parent Company corporate expenses	178
Executive office expenses not allocated to segments	2,106
Provision for Income taxes:	
Parent Company income taxes (benefit)	(91)
Executive office income taxes not allocated to segments	(498)
Net Income:	\$ (1,669)

Segment assets:

Parent Company assets, after intercompany elimination	\$ 870
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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, continued

	Segment Reporting						Totals
	Retail and Commercial Banking	Insurance Services	Wealth Strategies	Financial Management	Inter- segment Elimination	Other	
	(Dollars in thousands)						
Net Interest Income (expense)							
external customers	\$ 11,888	0	0	2,212	0	12	\$ 14,112
Net intersegment interest income (expense)	1,901	6	(5)	(1,902)	0	0	0
Net Interest Income	13,789	6	(5)	310	0	12	14,112
Provision for Loan Losses	141	0	0	0	0	0	141
Noninterest Income (expense)							
external customers	2,110	1,371	700	78	0	1	4,260
Intersegment noninterest income (expense)	(6)	6	35	0	(35)	0	0
Total Noninterest Income	2,104	1,377	735	78	(35)	1	4,260
Noninterest Expenses:							
Depreciation	767	31	23	66	0	75	962
Amortization of intangibles	0	16	0	0	0	0	16
Other Noninterest expenses	8,492	1,203	717	687	0	1,953	13,052
Total Noninterest expenses	9,259	1,250	740	753	0	2,028	14,030
Pre-tax Income	6,493	133	(10)	(365)	(35)	(2,015)	4,201
Provision for Income Taxes	1,390	28	(10)	(81)	0	(500)	827
Net Income	\$ 5,103	105	0	(284)	(35)	(1,515)	\$ 3,374
Assets	\$ 453,406	1,287	175	149,830	(190,875)	1,032	\$ 414,855
Expenditures for Fixed Assets	\$ 353	14	0	4	0	0	\$ 371

Amounts included in the "Other" column are as follows:

	Other
Net interest Income:	
Parent Company	\$ 12
Noninterest Income:	
Executive office miscellaneous income	1
Noninterest Expenses:	
Parent Company corporate expenses	141
Executive office expenses not allocated to segments	1,887
Provision for Income taxes:	
Parent Company income taxes (benefit)	(87)
Executive office income taxes not allocated to segments	(413)
Net Income:	\$ (1,515)
Segment assets:	
Parent Company assets, after intercompany elimination	\$ 1,032

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, continued**

	Segment Reporting						
	For the year ended December 31, 2014						
	Retail and Commercial Banking	Insurance Services	Wealth Strategies	Financial Management	Inter- segment Elimination	Other	Totals
	(Dollars in thousands)						
Net Interest Income (expense)							
external customers	\$ 11,376	0	0	1,972	0	9	\$ 13,357
Net intersegment interest income (expense)	1,662	4	(5)	(1,661)	0	0	0
Net Interest Income	13,038	4	(5)	311	0	9	13,357
Provision for Loan Losses	330	0	0	0	0	0	330
Noninterest Income (expense)							
external customers	2,782	1,316	651	234	0	3	4,986
Intersegment noninterest income (expense)	(4)	4	35	0	(35)	0	0
Total Noninterest Income	2,778	1,320	686	234	(35)	3	4,986
Noninterest Expenses:							
Depreciation	698	31	21	66	0	75	891
Amortization of intangibles	28	16	1	0	0	0	45
Other Noninterest expenses	8,854	1,231	666	656	0	2,027	13,434
Total Noninterest expenses	9,580	1,278	688	722	0	2,102	14,370
Pre-tax Income	5,906	46	(7)	(177)	(35)	(2,090)	3,643
Provision for Income Taxes	1,304	10	(10)	(40)	0	(525)	739
Net Income	\$ 4,602	36	3	(137)	(35)	(1,565)	\$ 2,904
Assets	\$ 404,679	1,411	219	139,175	(171,855)	651	\$ 374,280
Expenditures for Fixed Assets	\$ 2,162	28	1	121	0	0	\$ 2,312

Amounts included in the "Other" column are as follows:

	Other
Net interest Income:	
Parent Company	\$ 9
Noninterest Income:	
Executive office miscellaneous income	3
Noninterest Expenses:	
Parent Company corporate expenses	166
Executive office expenses not allocated to segments	1,936
Provision for Income taxes:	
Parent Company income taxes (benefit)	(88)
Executive office income taxes not allocated to segments	(437)
Net Income:	\$ (1,565)

Segment assets:

Parent Company assets, after intercompany elimination	\$ 651
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## **NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, continued**

### **20. SUBSEQUENT EVENTS**

The Corporation performed an evaluation of subsequent events through March 31, 2017, the date upon which the Corporation's financial statements were available for issue. The Corporation has not evaluated subsequent events after this date.

### **ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE**

The Corporation did not change accountants nor have any disagreements with its accountants on any matters of accounting practices or principles or financial statement disclosure.

### **ITEM 9A. CONTROLS AND PROCEDURES**

#### **Disclosure Controls and Procedures**

The Corporation's management, including the Chief Executive Officer and Chief Financial Officer, supervised and participated in an evaluation of the effectiveness of the Corporation's disclosure controls and procedures (as defined in federal securities rules) as of December 31, 2016. Based on, and as of the date of, that evaluation, the Corporation's Chief Executive Officer and Chief Financial Officer have concluded that the Corporation's disclosure controls and procedures were effective in accumulating and communicating information to management, including the Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosures of that information under the SEC's rules and forms and that the Corporation's disclosure controls and procedures are designed to ensure that the information required to be disclosed in reports that are filed or submitted by the Corporation under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms.

#### **Management's Annual Report on Internal Control over Financial Reporting**

The Corporation's management is responsible for establishing and maintaining adequate internal control over financial reporting. Management's assessment of the effectiveness of the Corporation's internal control over financial reporting as of December 31, 2016, is included in Item 8 of this Annual Report on Form 10-K under the heading "Management's Report on Internal Controls Over Financial Reporting."

#### **Changes in Internal Control Over Financial Reporting**

No changes were made to the Corporation's internal control over financial reporting during the last fiscal quarter that materially affected or could reasonably likely to materially affect the Corporation's internal controls over financial reporting.

### **ITEM 9B. OTHER INFORMATION**

None.

## **PART III**

### **ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE**

The information contained under the heading "Information About Nominees For Director" and "Compliance with Section 16(a) of the Exchange Act" in the definitive Proxy Statement to be used in connection with the solicitation of proxies for the Corporation's annual meeting of shareholders to be held on May 23, 2017, to be filed with the SEC, is incorporated herein by reference.

### **ITEM 11. EXECUTIVE COMPENSATION**

The information contained under the heading "Executive Compensation" in the definitive Proxy Statement to be used in connection with the solicitation of proxies for the Corporation's annual meeting of shareholders to be held on May 23, 2017, to be filed with the SEC, is incorporated herein by reference.

### **ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS**

The information contained under the heading "Voting Securities and Principal Holders" in the definitive Proxy Statement to be used in connection with the solicitation of proxies for the Corporation's annual meeting of shareholders to be held on May 23, 2017, to be filed with the SEC, and the information contained in Item 5 hereof under the heading "Securities Authorized for Issuance Under Equity Compensation Plans," is incorporated herein by reference.

### ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE

The information contained under the heading “Certain Relationships and Related Party Transactions” in the definitive Proxy Statement to be used in connection with the solicitation of proxies for the Corporation’s annual meeting of shareholders to be held on May 23, 2017, to be filed with the SEC, is incorporated herein by reference.

### ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES

The information contained under the heading “Information Concerning the Corporation’s Accountants” in the definitive Proxy Statement to be used in connection with the solicitation of proxies for the Corporation’s annual meeting of shareholders to be held on May 23, 2017, to be filed with the SEC, is incorporated herein by reference.

## PART IV

### ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

(a) Financial Statements

The following consolidated financial statements and supplementary information for the fiscal years ended December 31, 2016, 2015, and 2014 are included in Part II, Item 8 herein:

- (i) Report of Independent Auditors
- (ii) Consolidated Balance Sheets – December 31, 2016 and 2015
- (iii) Consolidated Statements of Income – Years ended December 31, 2016, 2015, and 2014
- (iv) Consolidated Statements of Comprehensive Income – Years ended December 31, 2016, 2015, and 2014
- (v) Consolidated Statements of Changes in Stockholders’ Equity – Years ended December 31, 2016, 2015, and 2014
- (vi) Consolidated Statements of Cash Flows – Years ended December 31, 2016, 2015, and 2014
- (vii) Notes to Consolidated Financial Statements – December 31, 2016

(b) Financial Statement Schedules

All applicable financial statement schedules required have been included in the Notes to the Consolidated Financial Statements.

(c) Exhibits:

The exhibits filed as part of this registration statement are as follows:

<u>Exhibit Number</u>	<u>Description Of Exhibit</u>
3.1	Articles of Incorporation of Southwest Georgia Financial Corporation, as amended and restated (included as Exhibit 3.1 to the Corporation’s Form 10-KSB dated December 31, 1996, previously filed with the SEC and incorporated herein by reference).
3.2	Bylaws of the Corporation, as amended (included as Exhibit 3.2 to the Corporation’s Form 10-KSB dated December 31, 1995, previously filed with the SEC and incorporated herein by reference).
10.1	Form of Directors’ Deferred Compensation Plan of the Corporation (included as Exhibit 10.3 to the Corporation’s Form S-18 dated January 23, 1990, previously filed with the SEC and incorporated herein by reference).*

- 10.2 Directors and Executive Officers Stock Purchase Plan of the Corporation dated August 22, 2012 (included as Exhibit 4 to the Corporation's Form S-8 dated October 11, 2012, previously filed with the SEC and incorporated herein by reference).\*
- 10.3 Amendment No. 1 to Directors and Executive Officers Stock Purchase Plan of the Corporation dated March 23, 2016.\*
- 10.4 Supplemental Retirement Plan of the Corporation dated December 21, 1994 (included as Exhibit 10.11 to the Corporation's Form 10-KSB dated December 31, 1994, previously filed with the SEC and incorporated herein by reference).\*
- 10.5 Trust under the Corporation's Supplemental Retirement Plan, as amended (included as Exhibit 10.6b to the Corporation's Form 10-K dated December 31, 1997, previously filed with the SEC and incorporated herein by reference).\*
- 10.6 Dividend Reinvestment and Share Purchases Plan of the Corporation, as amended and restated by Amendment No. 1 (included as Exhibit 99 to the Corporation's Form S-3DPOS dated September 30, 1998, previously filed with the SEC and incorporated herein by reference).
- 10.7 Key Individual Stock Option Plan of the Corporation dated March 19, 1997 (included as Exhibit 10.9 to the Corporation's Form 10-K dated December 31, 1997, previously filed with the SEC and incorporated herein by reference).\*
- 10.8 Employment Agreement of DeWitt Drew (included as Exhibit 10.11 to the Corporation's Form S-4 dated January 6, 2004, previously filed with the SEC and incorporated herein by reference).\*
- 10.9 2013 Omnibus Incentive Plan of the Corporation dated December 18, 2013 (included as Appendix I to the Corporation's Proxy Statement dated April 17, 2014, previously filed with the SEC and incorporated herein by reference).\*
- 10.10 Employee Stock Ownership Plan and Trust of the Corporation, as restated effective as of January 1, 2014.\*
- 10.11 Southwest Georgia Bank 401(k) Plan, as restated effective as of January 1, 2015.\*
- 10.12 Pension Retirement Plan of the Corporation, as amended and restated effective as of January 1, 2015; amended effective as of December 1, 2016.\*
- 14 Code of Ethical Conduct dated February 27, 2008 (included as Exhibit 14 to the Corporation's Form 8-K dated February 27, 2008, previously filed with the SEC and incorporated herein by reference).
- 21 Subsidiaries of the Corporation (included as Exhibit 21 to the Corporation's Form 10-K dated December 31, 2002, previously filed with the SEC, incorporated herein by reference).
- 23.1 Consent of TJS Deemer Dana, LLP
- 31.1 Section 302 Certification of Periodic Financial Report by Chief Executive Officer.
- 31.2 Section 302 Certification of Periodic Financial Report by Chief Financial Officer.
- 32.1 Section 906 Certification of Periodic Financial Report by Chief Executive Officer.
- 32.2 Section 906 Certification of Periodic Financial Report by Chief Financial Officer.

101.INS XBRL Instance Document  
 101.SCH XBRL Taxonomy Extension Schema Document  
 101.CAL XBRL Taxonomy Extension Calculation Linkbase Document  
 101.DEF XBRL Taxonomy Extension Definition Linkbase Document  
 101.LAB XBRL Taxonomy Extension Label Linkbase Document  
 101.PRE XBRL Taxonomy Extension Presentation Linkbase Document

\* Management contract or compensatory plan or arrangement required to be filed as an exhibit to this form.

**ITEM 16. FORM 10-K SUMMARY**

None.

**SIGNATURES**

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Corporation has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Southwest Georgia Financial Corporation  
 (Corporation)

Date: March 31, 2017

By: /s/ DeWitt Drew  
 DEWITT DREW  
 President and Chief Executive Officer

Date: March 31, 2017

/s/ George R. Kirkland  
 GEORGE R. KIRKLAND  
 Executive Vice President, Chief  
 Financial Officer and Treasurer

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the Corporation and in the capacities and on the dates indicated.

/s/ Michael J. McLean  
 MICHAEL J. MCLEAN  
 Chairman

Date: March 31, 2017

/s/ Richard L. Moss  
 RICHARD L. MOSS  
 Vice Chairman

Date: March 31, 2017

/s/ Cecil H. Barber  
 CECIL H. BARBER  
 Director

Date: March 31, 2017

/s/ John J. Cole, Jr.  
 JOHN J. COLE, JR.  
 Director

Date: March 31, 2017

/s/ Roy Reeves  
 ROY REEVES  
 Director

Date: March 31, 2017

/s/ Johnny R. Slocumb  
 JOHNNY R. SLOCUMB  
 Director

Date: March 31, 2017

/s/ M. Lane Wear  
M. LANE WEAR  
Director

Date: March 31, 2017

/s/ Marcus R. Wells  
MARCUS R. WELLS  
Director

Date: March 31, 2017

Exhibit Index

<u>Exhibit Number</u>	<u>Description of Exhibit</u>
10.3	Amendment No. 1 to Directors and Executive Officers Stock Purchase Plan of the Corporation dated March 23, 2016.
10.10	Employee Stock Ownership Plan and Trust of the Corporation, as restated effective as of January 1, 2014.
10.11	Southwest Georgia Bank 401(k) Plan, as restated effective as of January 1, 2015.
10.12	Pension Retirement Plan of the Corporation, as amended and restated effective as of January 1, 2015; amended effective as of December 1, 2016.
23.1	Consent of TJS Deemer Dana, LLP
31.1	Section 302 Certification of Periodic Financial Report by Chief Executive Officer.
31.2	Section 302 Certification of Periodic Financial Report by Chief Financial Officer.
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## Board of Directors

(TOP ROW L-R)

**Michael McLean**<sup>2,3</sup> *Chairman and Owner, McLean Engineering Company, Inc.*  
**Marcus Wells**<sup>2,4</sup> *Physical Therapist and Director of Business Development, Colquitt Regional Medical Center*

**Cecil H. Barber**<sup>1,3</sup> *Vice President, Barber Contracting Company*  
**DeWitt Drew**<sup>2,4</sup> *President and Chief Executive Officer, Southwest Georgia Financial Corporation and Southwest Georgia Bank*

(BOTTOM ROW L-R)

**Roy H. Reeves**<sup>2,4</sup> *Owner, Reeves Properties, LP*  
**John J. Cole Jr.**<sup>2,4</sup> *Executive Vice President and Chief Operating Officer, Southwest Georgia Financial Corporation and Southwest Georgia Bank*

**Richard L. Moss**<sup>1,3</sup> *Vice Chairman and President, Moss Farms, Inc.*  
**M. Lane Wear**<sup>1,3</sup> *CPA and Partner, Vines, Wear & Mangum, LLP*  
**Johnny R. Slocumb**<sup>1,4</sup> *Owner, Slocumb Company*

## Senior Management

(TOP ROW L-R)

**Jeffrey Judson Moritz** *Senior Vice President and Valdosta Region President*  
**Gregory P. Costin** *Senior Vice President*  
**David L. Shiver** *Senior Vice President and Sylvester Region President*  
**Chad J. Carpenter** *Senior Vice President and Tifton Region President*  
**John J. Cole, Jr.** *Executive Vice President and Chief Operating Officer*  
**Danny E. Singley** *Executive Vice President and Chief Credit Officer*  
**Jeffery E. Hanson** *Executive Vice President and Chief Banking Officer*

(BOTTOM ROW L-R)

**Pamela J. Yeager** *Senior Vice President*  
**Ross K. Dekle** *Senior Vice President and Moultrie Region President*  
**Donna S. Lott** *Senior Vice President and Cashier*  
**George R. Kirkland** *Executive Vice President, Chief Financial Officer and Treasurer*  
**Karen T. Boyd** *Senior Vice President and Controller*

## Sylvester Advisory Board

**David L. Shiver** *Senior Vice President*  
**Johnny T. Cochran** *Farmer*  
**William J. Yearta** *Owner, Fletcher-Yearta Jewelers*  
**Morris I. Bryant** *Retired Banker*

1. Audit Committee
2. Loan Committee
3. Personnel Committee
4. Wealth Strategies Committee

## Shareholder Information

### CORPORATE HEADQUARTERS

Southwest Georgia Financial Corporation  
201 First Street, Southeast  
Moultrie, GA 31768  
Phone: 229.985.1120  
Fax: 229.985.0251

### ANNUAL MEETING

Tuesday, May 23, 2017 at 4:30 p.m.  
Southwest Georgia Bank  
Administrative Services Building  
205 Second Street, Southeast  
Moultrie, GA 31768

### STOCK SYMBOL

Southwest Georgia Financial Corporation common stock is traded on the NYSE MKT under the symbol SGB.

### SGB QUARTERLY COMMON STOCK PRICES AND DIVIDENDS

Quarter Ended	High	Market Price Low	Close	Dividends Paid
<b>2016</b>				
December 31	\$19.99	\$15.33	\$19.99	\$0.11
September 30	\$17.00	\$14.51	\$16.25	\$0.11
June 30	\$15.25	\$14.00	\$14.62	\$0.10
March 31	\$15.95	\$13.27	\$14.01	\$0.10
<b>2015</b>				
December 31	\$15.95	\$14.24	\$15.95	\$0.10
September 30	\$15.95	\$13.02	\$15.50	\$0.10
June 30	\$16.40	\$13.21	\$14.13	\$0.10
March 31	\$15.85	\$12.83	\$13.60	\$0.10

### SHAREHOLDERS OF RECORD

Southwest Georgia Financial Corporation had 416 shareholders of record as of December 31, 2016. There are approximately 485 additional shareholders holding shares through trust and brokerage firms.

### SHAREHOLDER SERVICES

Shareholder inquiries to change name, address, or stock ownership, to report lost certificates, or to consolidate accounts should be directed to the Transfer Agent:

American Stock Transfer & Trust Company  
6201 15th Avenue  
Brooklyn, NY 11219  
Phone: 800.937.5449  
Fax: 718.921.8124  
Web: [www.amstock.com](http://www.amstock.com)

### DIVIDEND REINVESTMENT PLAN

The Dividend Reinvestment Plan offers a convenient, low-cost method for shareholders to purchase additional shares of Southwest Georgia Financial Corporation. For more information or to participate in this plan, contact:

American Stock Transfer & Trust Company  
6201 15th Avenue  
Brooklyn, NY 11219  
Phone: 800.937.5449  
Fax: 718.921.8124  
Web: [www.amstock.com](http://www.amstock.com)

### INDEPENDENT ACCOUNTANTS

TJS Deemer Dana LLP  
1004 Hillcrest Parkway  
Dublin, GA 31021

### INVESTOR RELATIONS

To obtain further information on Southwest Georgia Financial Corporation, contact:

George R. Kirkland  
*Executive Vice President, Chief Financial Officer  
and Treasurer*  
Southwest Georgia Financial Corporation  
P.O. Box 3488  
Moultrie, GA 31776-3488  
Phone: 229.873.3830  
Fax: 229.890.2211  
Email: [investorinfo@sgfc.com](mailto:investorinfo@sgfc.com)



*Southwest Georgia Financial Corporation*

# Southwest Georgia Financial Corporation

April 20, 2017

Dear Shareholder:

The Annual Meeting of the Shareholders of Southwest Georgia Financial Corporation will be held on Tuesday, May 23, 2017, in the Southwest Georgia Bank Administrative Services Building, 205 Second Street S.E., Moultrie, Georgia, at 4:30 P.M. for the purposes set forth in the accompanying Notice of Annual Meeting of Shareholders and Proxy Statement.

This year we will have a special drawing for shareholders who attend the meeting. We will give away two \$500.00 cash prizes--you must be present to win and you must be a shareholder of Southwest Georgia Financial Corporation. (\*Directors, advisory board members, officers, and staff of Southwest Georgia Bank and Southwest Georgia Financial Corporation and their immediate families are not eligible to participate in the drawing).

In order to ensure that your shares are voted at the meeting, please complete, date, sign, and return the Proxy in the enclosed postage-paid envelope at your earliest convenience or if you have internet access, you may vote your shares by following the "Vote by Internet" instructions on the enclosed proxy card. Every shareholder's vote is important, no matter how many shares you own.

We encourage you to attend this annual meeting of the shareholders and join us in the lobby immediately following the meeting for hors d'oeuvres and refreshments. We look forward to your attendance and continued support.

Very truly yours,



DeWitt Drew  
President and Chief Executive Officer

\* Immediate family is considered to be husband, wife, and children living at home.

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**SOUTHWEST GEORGIA FINANCIAL CORPORATION**  
**P.O. Box 3488**  
**201 First Street, S.E.**  
**Moultrie, Georgia 31768**

**NOTICE OF ANNUAL MEETING OF SHAREHOLDERS**  
**To Be Held on May 23, 2017**

The annual meeting of shareholders of Southwest Georgia Financial Corporation (“the Corporation”) will be held on Tuesday, May 23, 2017, at 4:30 p.m. at the Southwest Georgia Bank Administrative Services Building, located at 205 Second Street, S.E., Moultrie, Georgia, for the purposes of considering and voting upon:

1. The election of eight directors to constitute the Board of Directors to serve until the next annual meeting and until their successors are elected and qualified;
2. The approval of an advisory “say on pay” resolution supporting the compensation plan for executive officers;
3. The ratification of the appointment of TJS Deemer Dana LLP as our independent auditors for the fiscal year 2017; and
4. Such other matters as may properly come before the meeting or any adjournment thereof.

Only shareholders of record at the close of business on April 10, 2017, will be entitled to notice of and to vote at the annual meeting or any adjournment thereof.

A Proxy Statement and a Proxy solicited by the Board of Directors are enclosed herewith. Also enclosed is the Corporation’s 2016 Annual Report to Shareholders, which contains financial data and other information about the Corporation. Even if you plan to attend the meeting in Moultrie, Georgia, please provide us with voting instructions in one of the following ways as soon as possible:

- Please mark, sign, date, and return the enclosed proxy card promptly using the business reply envelope;
- If you have internet access, you may vote your shares by following the “Vote by Internet” instructions on the enclosed proxy card; or
- If your shares are held in “street-name”, that is held for your account by a broker, bank or other nominee, you will receive instructions from your nominee which you must follow in order to have your shares voted.

The Corporation is mailing a full set of its Proxy materials to its shareholders. The Corporation’s Proxy Statement, Proxy Card, and 2016 Annual Report to Shareholders are also available on the Corporation’s website at <https://www.sgfc.com/pdf/2016annualreportandproxy.pdf>.

For directions to the annual meeting, call (229) 985-1120. If you attend the meeting you may, if you wish, withdraw your Proxy and vote in person.

By Order of the Board of Directors,



DeWitt Drew  
President and Chief Executive Officer

April 20, 2017

**WHETHER OR NOT YOU EXPECT TO BE PRESENT AT THE ANNUAL MEETING, PLEASE COMPLETE AND RETURN THE ENCLOSED PROXY CARD PROMPTLY IN THE ENCLOSED BUSINESS REPLY ENVELOPE OR VOTE YOUR SHARES VIA THE INTERNET. IF YOU ARE PRESENT AT THE ANNUAL MEETING, YOU MAY, IF YOU WISH, REVOKE YOUR PROXY AT THAT TIME AND EXERCISE THE RIGHT TO VOTE YOUR SHARES PERSONALLY.**

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**SOUTHWEST GEORGIA FINANCIAL CORPORATION**  
**P.O. Box 3488**  
**201 First Street, S.E.**  
**Moultrie, Georgia 31768**

**PROXY STATEMENT**

**April 20, 2017**

This Proxy Statement is furnished in connection with the solicitation of Proxies by the Board of Directors of Southwest Georgia Financial Corporation (the "Corporation") for use at the Annual Meeting of Shareholders of the Corporation to be held on May 23, 2017 (the "Annual Meeting"), and any postponement and adjournment thereof, for the purposes set forth in the accompanying notice of the meeting. The expenses of this solicitation, including the cost of preparing and mailing this Proxy Statement, will be paid by the Corporation. Copies of solicitation materials may be furnished to banks, brokerage houses, and other custodians, nominees, and fiduciaries for forwarding to beneficial owners of shares of the Corporation's common stock, and normal handling charges may be paid for such forwarding service. In addition to solicitations by mail, directors and regular employees of the Corporation may solicit Proxies in person or by telephone. It is anticipated that this Proxy Statement and the accompanying Proxy will first be mailed to shareholders on April 20, 2017.

**QUESTIONS AND ANSWERS ABOUT THE ANNUAL MEETING**

**What is the purpose of the Annual Meeting?**

At the Annual Meeting, shareholders will act upon the matters set forth in the accompanying notice of meeting, including:

1. The election of eight directors to constitute the Board of Directors to serve until the next annual meeting and until their successors are elected and qualified;
2. The approval of an advisory "say on pay" resolution supporting the compensation plan for executive officers; and
3. The ratification of the appointment of TJS Deemer Dana LLP as our independent auditors for the fiscal year 2017.

**Who is entitled to vote?**

All shareholders of record of the Corporation's common stock at the close of business on April 10, 2017, which is referred to as the record date, are entitled to receive notice of the Annual Meeting and to vote the shares of common stock held by them on the record date. Each outstanding share of common stock entitles its holder to cast one vote for each matter to be voted upon.

**How do I cast my vote?**

You may vote your shares in one of the following ways:

- 1) You may vote your shares by marking, signing, dating and returning the enclosed proxy card in the business reply envelope provided to you;
- 2) You may vote your shares by following the "Vote by Internet" instructions on the enclosed proxy card if you have internet access; or
- 3) You may vote your shares in person at the Annual Meeting.

If your shares of common stock are held in “street name”, that is held for your account by a broker, bank, or other nominee, you will receive instructions from your nominee which you must follow in order to have your shares voted.

If the Proxy is returned but no choice is specified thereon, it will be voted “for” all proposals.

### **What are the quorum and voting requirements?**

A quorum is present when the holders of a majority of the shares outstanding on the record date are present in person or represented by proxy at the Annual Meeting. On the record date, the Corporation had outstanding and entitled to vote 2,547,437 shares of common stock, par value \$1.00 per share.

The required vote for each item of business at the Annual Meeting is as follows:

1. For Proposal 1, the election of directors, those nominees receiving the greatest number of votes at the Annual Meeting shall be deemed elected;
2. For Proposal 2, the approval of the advisory “say on pay” resolution supporting the compensation plan for the executive officers, the affirmative vote of a majority of the shares entitled to vote and present in person or represented by proxy at the Annual Meeting; and
3. For Proposal 3, the ratification of the appointment of TJS Deemer Dana LLP as independent auditors for 2017, the affirmative vote of a majority of the shares entitled to vote and present in person or represented by proxy at the Annual Meeting.

### **How are votes counted?**

Abstentions and broker non-votes will be counted for purposes of establishing a quorum. Abstentions will be counted towards the tabulations of votes cast on a proposal and will have the same effect as negative votes. Broker non-votes are proxies received from brokers or other nominees holding shares on behalf of their clients (in “street name”) who have not been given specific voting instructions from their clients with respect to non-routine matters. Typically, the ratification of auditors is considered a routine matter by brokers and other nominees allowing them to have discretionary voting power to vote shares they hold on behalf of their clients for such matter. Broker non-votes will not be counted for purposes of determining whether a proposal has been approved.

Proposal 1 is the election of directors. Because directors are elected by a plurality of the votes cast, the director nominees who get the most votes will be elected. Directors cannot be voted “against” and votes to “withhold authority” to vote for a certain nominee will have no effect if the nominee receives a plurality of the votes cast. For all other proposals that come before the meeting, you may vote “for” or “against” the proposal.

If you hold your shares of common stock in your own name as a holder of record, and you fail to vote your shares, either in person or by proxy, the votes represented by your shares will be excluded entirely from the vote.

### **Will other matters be voted on at the Annual Meeting?**

The Corporation is not aware of any other matters to be presented at the Annual Meeting other than those described in this Proxy Statement. If any other matters not described in the Proxy Statement are properly presented at the meeting, proxies will be voted in accordance with the best judgment of the proxy holders.

### **Can I revoke my Proxy instructions?**

Any Proxy given pursuant to this solicitation may be revoked by any shareholder who attends the meeting and gives oral notice of his or her election to vote in person, without compliance with any other formalities. In addition, any Proxy given pursuant to this solicitation may be revoked prior to the Annual Meeting by delivering a signed writing revoking it or a duly executed Proxy bearing a later date to the Secretary of the Corporation at Southwest Georgia



Financial Corporation, P.O. Box 3488, Moultrie, Georgia 31776-3488. Any shareholder of record as of the record date attending the Annual Meeting may vote in person by ballot whether or not a Proxy has been previously given, but the presence (without further action) of a shareholder at the Annual Meeting will not constitute revocation of a previously given Proxy.

Any shareholder holding shares in "street name" by a broker or other nominee must contact the broker or nominee to obtain instructions for revoking the Proxy instructions.

**What other information should I review before voting?**

The 2016 Annual Report to Shareholders, including financial statements for the year ended December 31, 2016, is enclosed with this Proxy Statement. The Annual Report on Form 10-K, except for the exhibits, is part of the Proxy materials. The Corporation will furnish, without charge, a copy of its complete Annual Report on Form 10-K filed with the Securities and Exchange Commission (the "SEC") for the fiscal year ended December 31, 2016, including financial statements and footnotes, to any record or any beneficial owner of its common stock as of April 10, 2017, who requests a copy of such report. Any request for the Annual Report on Form 10-K should be in writing addressed to:

Mr. George R. Kirkland  
Southwest Georgia Financial Corporation  
P.O. Box 3488  
Moultrie, Georgia 31776-3488

**If the person requesting the Annual Report on Form 10-K was not a shareholder of record on April 10, 2017, the request must include a representation that the person was a beneficial owner of common stock on that date. Copies of any exhibit to the Annual Report on Form 10-K will be furnished on request and upon receipt of the payment of the Corporation's expense in furnishing the exhibits.**

You may also obtain copies of the Corporation's Annual Report on Form 10-K from the SEC at prescribed rates by writing to the Public Reference Facilities of the SEC, 100 F. Street, N.E., Room 1580, Washington, D.C. 20549. Please call the SEC at (800) SEC-0330 for further information. The Corporation's SEC filings, including its Annual Report on Form 10-K, are publicly available on the SEC's website located at [www.sec.gov](http://www.sec.gov).

**NOTICE REGARDING THE AVAILABILITY OF PROXY MATERIALS**

We have posted materials related to the 2017 Annual Meeting on the internet. The following materials are available on the internet at <https://www.sgfc.com/pdf/2016annualreportandproxy.pdf>:

- This Proxy Statement for the 2017 Annual Meeting, and
- The Corporation's 2016 Annual Report to Shareholders, which includes the Corporation's Annual Report on Form 10-K for the year ended December 31, 2016 as filed with the SEC.

## VOTING SECURITIES AND PRINCIPAL HOLDERS

The following table sets forth, as of March 3, 2017, the beneficial ownership of the Corporation's common stock by each "person" (as that term is defined by the SEC) known by the Corporation to be the beneficial owner of more than 5% of the Corporation's common stock, by each director and named executive officer of the Corporation, and by all directors and named executive officers as a group.

<u>Name of Beneficial Owner</u>	<u>Amount and Nature of Beneficial Ownership (1)</u>	<u>Percent of Class</u>	
The Employee Stock Ownership Plan and Trust of Southwest Georgia Financial Corporation 201 First Street, S.E., Moultrie, Georgia 31768	262,104	10.29%	
Cecil H. Barber	36,321	1.43%	
John J. Cole, Jr.	74,213	2.91%	(2)
DeWitt Drew	28,486	1.12%	(3)
Michael McLean	76,340	3.00%	(4)
Richard L. Moss	34,390	1.35%	
Roy H. Reeves	36,383	1.43%	
Johnny R. Slocumb	60,701	2.38%	
M. Lane Wear	13,169	*	
Marcus R. Wells	12,667	*	
Danny E. Singley	13,383	*	(5)
George R. Kirkland	50,865	2.00%	(6)
Jeffery E. Hanson	9,321	*	(7)
All Directors and Named Executive Officers as a Group (12 persons)	<u>622,655</u>	<u>24.44%</u>	

\* Indicates less than one percent (1%).

- (1) Based on 2,547,437 shares outstanding as of March 3, 2017, which includes shares underlying outstanding stock options exercisable within 60 days of March 3, 2017, which are deemed to be outstanding for purposes of calculating the percentage owned by a holder.
- (2) Includes 52,705 shares allocated to the account of Mr. Cole in the Employee Stock Ownership Plan and Trust, over which shares Mr. Cole exercises voting power.
- (3) Includes 12,004 shares allocated to the account of Mr. Drew in the Employee Stock Ownership Plan and Trust, over which shares Mr. Drew exercises voting power.
- (4) Includes 48,579 shares of which Mr. McLean holds the voting power of attorney for E. J. McLean, Jr.
- (5) Includes 3,393 shares allocated to the account of Mr. Singley in the Employee Stock Ownership Plan and Trust, over which shares Mr. Singley exercises voting power.
- (6) Includes 14,951 shares allocated to the account of Mr. Kirkland in the Employee Stock Ownership Plan and Trust, over which shares Mr. Kirkland exercises voting power.
- (7) Includes 2,635 shares allocated to the account of Mr. Hanson in the Employee Stock Ownership Plan and Trust, over which shares Mr. Hanson exercises voting power.

## **PROPOSAL 1: ELECTION OF DIRECTORS**

The bylaws of the Corporation provide that the Board of Directors shall consist of not less than five nor more than 25 directors. The exact number of directors is currently set at nine by Board resolution. However, the number of directors may be increased or decreased within the foregoing range from time to time by the Board of Directors or by resolution of the shareholders. Because current Chairman and Director, Michael J. McLean, will not run for reelection in 2017, the Board will set the number of directors at eight immediately after the Annual Meeting.

The terms of office for directors continue until the next Annual Meeting and until their successors are elected and qualified or until their earlier resignation, removal from office, or death.

Each Proxy executed and returned by a shareholder will be voted as specified thereon by the shareholder. If no specification is made, the Proxy will be voted for the election of the nominees named below to constitute the entire Board of Directors. In the event that any nominee withdraws or for any reason is not able to serve as a director, the Proxy will be voted for such other person as may be designated by the Board of Directors as substitute nominee. Management of the Corporation has no reason to believe that any nominee will not serve if elected.

### **Vote Required**

Directors are elected by a plurality of the votes cast by the holders of the shares entitled to vote in an election at a meeting at which a quorum is present.

### **Recommendation**

**The Board of Directors unanimously recommends a vote "FOR" each nominee for director.**

## **INFORMATION ABOUT NOMINEES FOR DIRECTOR**

The following information is as of April 10, 2017, and has been furnished by the respective nominees for director. Except as otherwise indicated, each nominee has been or was engaged in his present or last principal employment, in the same or a similar position, for more than five years.

### **Name (Age)**

### **Information about Nominee**

- |                        |  |
|------------------------|--|
| Cecil H. Barber (52)   | A director of Southwest Georgia Bank (the “Bank”) and the Corporation since 1999, Mr. Barber is Vice President of Barber Contracting, a general contracting company. Mr. Barber earned a Bachelor of Science degree in Civil Engineering from Georgia Institute of Technology. Also, he has participated in various internal training workshops for directors. Mr. Barber’s business experience and familiarity with the local community and businesses deems him qualified as a board member.   |
| John J. Cole, Jr. (67) | A director of the Bank and of the Corporation, Mr. Cole became Executive Vice President and Chief Operating Officer of the Bank and the Corporation in 2011. He has been Executive and Senior Vice President of the Bank and Corporation since 1992. He has served in various other positions with the Bank since 1976 and the Corporation since 1981. Mr. Cole earned a Bachelor of Science degree in Business Administration from Valdosta State University. Mr. Cole graduated from the School for Bank Administration at the University of Wisconsin as well as Stonier Graduate School of Banking. Also, he has participated in various internal training workshops for directors. Mr. Cole’s education and vast knowledge of the banking industry and the operation of the Bank are assets to the Board. |
| DeWitt Drew (60)       | Mr. Drew has been President and Chief Executive Officer of the Bank and Corporation since May 2002. Previously, he served as President and Chief Operating Officer during 2000 and 2001 and Executive Vice President during 1999 for the Bank and Corporation. Mr. Drew earned a Bachelor of Science degree in Business Administration with a concentration in Accounting from the University of South Alabama. He is a graduate of The Graduate School of Banking of the South at Louisiana State University. Also, he has participated in various internal training workshops for directors. Mr. Drew’s role in leading the Corporation and the Bank and breadth of banking education and experience are critical to the Board.  |
| Richard L. Moss (65)   | Vice Chairman of the Board of the Corporation and Assistant Presiding Director of the Bank since 2006, Mr. Moss has been a director of the Bank since 1980 and of the Corporation since 1981. Mr. Moss is President of Moss Farms. Mr. Moss earned a Bachelor of Science degree in Agricultural Economics from North Carolina State University. Also, he has participated in various internal training workshops for directors. Mr. Moss’s extensive agricultural knowledge and experience within the agricultural community, which is a big part of the Bank’s customer base, are invaluable to the Board.  |
| Roy H. Reeves (57)     | A director of the Bank and the Corporation since 1991, Mr. Reeves is the owner of Reeves Properties, L.P., a property rental company. Mr. Reeves earned a Bachelor degree in Business Administration from the University of Georgia. He has attended several Georgia Bankers Association sponsored bank director training programs and participated in various other internal training workshops for directors. Mr. Reeves’s professional experience in real estate projects offer a unique insight into the markets in which we operate.  |

**Name (Age)**

**Information about Nominee**

Johnny R. Slocumb (64)	A director of the Bank and the Corporation since 1991, Mr. Slocumb is the owner of Slocumb and Associates, Inc., a company which offers real estate and insurance services. Mr. Slocumb earned a Bachelor of Science degree in Business from Georgia Southwestern College. Also, he has participated in various internal training workshops for directors. Mr. Slocumb's business insight, especially in the real estate and insurance industries, and knowledge of our market are necessary to direct the Corporation.
M. Lane Wear (65)	A director of the Bank and of the Corporation since 2007. Mr. Wear is a Certified Public Accountant and has been a partner with Vines, Wear and Mangum, LLP since 1986. Mr. Wear earned a Bachelor of Business Administration degree from Georgia Southern College. Also, he has participated in various internal training workshops for directors. Mr. Wear's accounting background and financial acumen are imperative to the Board.
Marcus R. Wells (59)	A director of the Bank and of the Corporation since 2007. A licensed physical therapist, Mr. Wells became Director of Business Development and physical therapist at Colquitt Regional Medical Center in June 2013. Previously, he was owner and Chief Executive Officer of Alliance Rehab, Inc., d/b/a Moultrie Physical Therapy & Rehabilitation from January 2004 through May 2013. Previously, he was employed from 1999 to March 2003 and was managing partner from April 2003 to December 2003 by Moultrie Physical Therapy & Rehabilitation. Also, Mr. Wells has been Chief Executive Officer of POINT, Inc., (Prevention of Occupational & Industrial Trauma) since 1998. Mr. Wells earned an Associate in Arts degree from Tallahassee Community College and a Bachelor of Science degree in Physical Therapy from Florida A & M University. He has earned certificates from Community Bankers Association of Georgia and from Terry College of Business at the University of Georgia in bank director and fundamentals training. Also, he has participated in various other internal training workshops for directors. Mr. Wells' broad director training, ties to the local community, and business experience deems him qualified as a board member.

There are no family relationships between any director, executive officer, or nominee for director of the Corporation or any of its subsidiaries.

**Meetings and Composition of the Board of Directors**

The Board of Directors held 12 regular meetings during 2016. All of the directors attended at least 90% of the Board and committee meetings held during 2016 and their tenure as directors. Directors are expected to be present at all Board of Directors meetings of the Corporation. Directors are expected to be present at the Annual Meeting of the Corporation. All of the directors attended the Corporation's 2016 Annual Meeting.

The Board of Directors has determined that seven of the nine members of the Board of Directors are "independent" as defined under applicable federal securities laws and listing standards of the NYSE MKT LLC (the "NYSE MKT"). The "independent" directors are Messrs. Barber, McLean, who is retiring from the Board of Directors this year, Moss, Reeves, Slocumb, Wear, and Wells.

**Board Leadership Structure and Role in Risk Oversight**

The Corporation is led by Mr. DeWitt Drew who serves as the President and Chief Executive Officer. Mr. Drew has been President and Chief Executive Officer since 2002. The Board of Directors is currently led by Michael J. McLean as Chairman, who is retiring from the Board of Directors this year, and is comprised of nine directors total, seven of whom have been determined to be independent directors. Each of the Audit, Personnel and Nominating Committees of the Board of Directors are comprised entirely of independent directors.

The Chief Executive Officer is responsible for oversight of the day-to-day operations and business affairs of the Corporation, including directing the business conducted by the employees, managers and officers of the Corporation. The Chairman is responsible for leading the Board of Directors in its duty to oversee the management of the business and affairs of the Corporation and ensuring that he and the other directors act in the best interest of the Corporation and its shareholders.

Risk oversight of the Corporation is the responsibility of the Board of Directors. It administers this oversight function by evaluating various components of risks to the Corporation at each meeting of the Board of Directors. The current structure of the Board of Directors is appropriate for the Corporation at this time and facilitates careful oversight of risk for the Corporation by the independent directors. The Corporation believes it is important to maintain the separate roles of the Chairman of the Board of Directors and the Chief Executive Officer. This allows the Chairman to be an independent leader for the Board of Directors as well as a liaison between the Board of Directors and management. The independent directors met in executive session without the non-independent directors and management four times in 2016. This executive session of the Board of Directors allowed the Board of Directors to review key decisions and discuss matters in a manner that is independent of senior management and non-independent directors.

### **Committees of the Board of Directors**

The Board of Directors has established three committees, a Personnel Committee, an Audit Committee, and a Nominating Committee.

#### *Personnel Committee*

The Personnel Committee is currently composed of four members, Cecil Barber, Michael J. McLean, who is retiring from the Board of Directors this year, Richard L. Moss, and Marcus R. Wells. The Board of Directors has determined that all of these directors are “independent” under applicable federal securities laws and listing standards of the NYSE MKT. The Personnel Committee held seven meetings during 2016.

The Personnel Committee is responsible for establishing and administering the policies that govern the compensation arrangements for executive officers and other employees. The Personnel Committee is also responsible for oversight and administration of certain executive and employee compensation and benefit plans, including the Corporation’s Pension Retirement Plan (the “Pension Plan”), Supplemental Retirement Plan (the “Supplemental Plan”), Directors and Executive Officers Stock Purchase Plan (the “Stock Purchase Plan”), Key Individual Stock Option Plan (the “Option Plan”) and the 2013 Omnibus Incentive Plan (the “Incentive Plan”), as well as the Bank’s 401(k) Plan effective January 1, 2007 (the “401(k) Plan”). It periodically reviews and makes recommendations to the Board with respect to Director Compensation.

#### *Audit Committee*

The Audit Committee presently consists of four directors, M. Lane Wear, Richard L. Moss, Cecil Barber, and Johnny R. Slocumb. The Audit Committee held 8 meetings during 2016.

The Board of Directors has determined that all of the members of the Audit Committee are “independent” under applicable federal securities laws and listing standards of the NYSE MKT and have sufficient knowledge in financial and accounting matters to serve on the Audit Committee, including the ability to read and understand fundamental financial statements. Mr. Wear, the chairman of the Audit Committee, qualifies as “financially sophisticated” under the listing standards of the NYSE MKT or as an “audit committee financial expert” under the federal securities laws.

The Audit Committee is responsible for recommending the selection of independent auditors; meeting with the independent auditors to review the scope and results of the audit; reviewing with management and the internal auditor the systems of internal control and the internal audit reports; and ascertaining that any and all operational deficiencies are satisfactorily corrected.

#### *Nominating Committee*

The Board of Directors has a standing Nominating Committee that presently consists of seven members, Richard L. Moss, Cecil Barber, Michael J. McLean, who is retiring from the Board of Directors this year, Roy H. Reeves, M. Lane Wear, Johnny R. Slocumb, and Marcus R. Wells. The Nominating Committee held one meeting during 2016. The

Nominating Committee nominates all directors and presents a slate of nominees for the Board of Directors to be approved by a majority of independent directors. The Board of Directors has determined that all of the members of the Nominating Committee are “independent” under applicable federal securities laws and listing standards of the NYSE MKT.

### *Charters*

The Board of Directors has adopted written Personnel, Audit, and Nominating Committee Charters that are annually reviewed and assessed. The charters are all posted on the Corporation’s website located at [www.sgfc.com](http://www.sgfc.com).

### **Director Nominations**

A candidate for the Board of Directors must meet the eligibility requirements set forth in the Corporation’s bylaws and in any applicable Board or committee resolutions. The Nominating Committee considers diversity in qualifications and characteristics that it deems appropriate from time to time when selecting individuals to be nominated for election to the Board of Directors. These qualifications and characteristics may include, without limitation, independence, integrity, business experience, education, accounting and financial expertise, age, reputation, civic and community relationships, and knowledge and experience in matters impacting financial institutions. In addition, prior to nominating an existing director for re-election to the Board of Directors, the Nominating Committee will consider and review an existing director’s Board and committee attendance, performance, and length of Board service.

The Nominating Committee will consider in accordance with the analysis described above all director nominees properly recommended by shareholders. Any shareholder wishing to recommend a candidate for consideration as a possible director nominee for election at an upcoming meeting of shareholders must provide written notice to Mr. George R. Kirkland, Southwest Georgia Financial Corporation, P. O. Box 3488, Moultrie, GA, 31776-3488 pursuant to the deadlines described in “Shareholders Proposals and Director Nominations.”

### **Code of Ethical Conduct**

The Corporation has adopted a Code of Ethics Policies and Procedures designed to promote ethical conduct by all of the Corporation’s directors, officers, and employees. The Code of Ethics Policies and Procedures includes a Code of Ethical Conduct for the Principal Executive Officer and Principal Financial Officers which sets forth standards applicable to all officers, directors, and employees but has provisions specifically applicable to the Corporation’s Chief Executive Officer and Chief Financial Officer. The Code of Ethics Policies and Procedures complies with the federal securities law requirement that issuers have a code of ethics applicable to the principal executive officer and principal financial officer, and the NYSE MKT requirement that listed companies have a code of ethical conduct applicable to all directors, officers, and employees. The Corporation’s Code of Ethical Conduct applicable to the Chief Executive Officer and the Chief Financial Officer is posted on its website, [www.sgfc.com](http://www.sgfc.com). The Corporation has not had any amendment to or waiver of the Code of Ethical Conduct. If there is an amendment or waiver, the Corporation will post such amendment or waiver on its website.

## EXECUTIVE COMPENSATION

### Overview and Administration

The objective of the Corporation's compensation program is to offer a compensation package that will attract, motivate, reward, and retain high-performing and dedicated employees. The package must balance competitive need and individual performance with affordability. The package must also provide financial security for employees and dependents upon retirement, disability, or death. The compensation program is designed to reward performance, longevity, professional growth, initiative, and increased responsibility.

The Personnel Committee of the Corporation reviews, evaluates, and approves compensation and benefits for all executive officers, including the "Named Executive Officers", who are DeWitt Drew, President and Chief Executive Officer of the Corporation and the Bank, John Cole, Jr., Executive Vice President and Chief Operating Officer of the Corporation and the Bank, and Jeffery E. Hanson, Executive Vice President and Chief Banking Officer of the Corporation and the Bank. The Personnel Committee also reviews general policy matters relating to compensation and benefits. The executive officers recommend to the Personnel Committee compensation for other employees based on comparison to compensation data received from banking related compensation and benefits surveys.

In 2016, the Corporation held an advisory "say on pay" vote on the compensation of its executive officers. The Corporation's shareholders approved such compensation, with 98% of the shares entitled to vote and present in person or represented by proxy at the 2016 Annual Meeting supporting the compensation plan for executive officers. As the Personnel Committee evaluated its compensation policies and overall objectives for 2016, it took into consideration this support of the Corporation's shareholders. As a result, the Personnel Committee decided to retain the general approach and structure of the Corporation's compensation plan for its executive officers. While this annual vote is not binding on the Corporation, our Board of Directors or our Personnel Committee, we value the opinions of our shareholders and, to the extent there is any significant vote against the compensation of our executive officers, we will consider our shareholders' concerns and the Personnel Committee will evaluate whether any actions are necessary to address those concerns.

All remuneration paid to the Corporation's officers during the year ended December 31, 2016, was paid by subsidiaries of the Corporation.

### Elements of Compensation

*Annual Base Salary and Cash Bonus.* Executive officer annual base salary and bonus awards are determined by the Personnel Committee with reference to Corporation-wide, divisional, and individual performance for the previous fiscal year based on a wide range of measures, which include comparisons with competitors' performance and internal goals set before the start of each fiscal year and by comparison to the level of executive officers' compensation of other financial institutions of comparable size in comparable markets. No relative weights are assigned for these factors.

The Personnel Committee believes that the most meaningful performance and pay equity comparisons are made against companies of similar size and in comparable markets. In keeping with this belief, the Committee consistently participates in and uses compensation and benefit surveys from the Georgia Bankers Association and the Bank Administration Institute and measures the Corporation's performance with peer comparison from the Federal Financial Institution Examining Council Peer Group Report.

During 2016, the Personnel Committee set annual salary and bonus for the Named Executive Officers in 2016 based primarily on Corporation-wide performance. The Personnel Committee believes that returns on assets ("ROA") and equity ("ROE") are the most appropriate measures for evaluating this performance.

In 2016, the Corporation had net income of \$4.0 million, an increase of \$660 thousand when compared with the previous year's net income, and the ROA of 0.94% and ROE of 10.51% increased 11% and 12%, respectively, from an ROA of 0.85% and ROE of 9.38% in 2015. Net income, ROA and ROE were higher than the 2016 performance goals of \$3.6 million in net income, ROA of 0.86% and ROE of 10.19%. Earnings growth was driven by higher net interest income resulting from loan growth of 17% and an improved asset mix that was funded by low cost core deposits.

In view of corporate performance, all of the Named Executive Officers received raises in their annual base salary of up to 9.6% in 2016 and most received bonuses of 25% of base salary. In 2015, the Named Executive Officers' salary increases were up to 3% and their bonuses were up to 25% of base salary. The Named Executive Officers' base salaries and



annual bonuses for 2016 are listed in “Executive Compensation - Summary Compensation Table”.

*Equity Incentive Awards.* The Corporation’s 2013 Omnibus Incentive Plan, or Incentive Plan, was approved by our shareholders at the Corporation’s 2014 Annual Meeting. The Incentive Plan was established to attract, retain and motivate the Corporation’s employees, consultants, advisors and directors, to promote the success of our business by linking their personal interests to those of our shareholders and to encourage stock ownership on the part of management. Under the Incentive Plan, the Corporation may issue a maximum aggregate amount of 125,000 shares of common stock pursuant to (i) stock options, which includes incentive stock options and non-qualified stock options, (ii) stock appreciation rights, (iii) restricted stock awards, (iv) restricted stock units, (v) incentive awards, (vi) other stock-based awards and (vii) dividend equivalents. The Corporation may also grant cash-based awards under the Plan.

In fiscal year 2016, the Corporation did not grant any equity incentive awards to the Named Executive Officers or any other employee or director under the newly adopted and approved Incentive Plan or any other plan.

### **Retirement and Other Benefits**

The Corporation offers retirement and other benefits that the Personnel Committee believes provides employees with a highly competitive package of benefits. The Corporation believes these forms of compensation enhance the ability to competitively search, hire, and retain a strong and competent executive staff, and that the 401(k) Plan, ESOP and Stock Purchase Plan encourage corporate ownership among employees.

*Pension Plan.* The Corporation’s Pension Plan is a qualified noncontributory defined benefit pension plan and is described in “Executive Compensation – Pension Benefits”. The Corporation froze the Pension Plan in 2006.

*401(k) Plan.* In place of the frozen Pension Plan, the Corporation and Bank adopted the 401(k) Plan for the benefit of almost all of the employees who attain the age of 21 years and complete a year of service. The 401(k) Plan is a qualified defined contribution plan as provided for under Section 401(k) of the Internal Revenue Code of 1986, as amended (the “Code”). This 401(k) Plan will match contributions dollar for dollar for the first 4% of compensation that each participant defers into the 401(k) Plan each payroll period. The 401(k) Plan allows for a discretionary match in excess of 4% and for participants to defer up to 80% of their respective compensation, subject to the maximum deferrals permitted under the Code. In 2016, the Corporation matched up to 4% of qualified compensation for Mr. Drew, Mr. Cole and Mr. Hanson in the amounts of \$10,600, \$8,762 and \$8,761, respectively.

*Employee Stock Ownership Plan.* The Corporation has a qualified, nondiscriminatory Employee Stock Ownership Plan (“ESOP”) administered by an ESOP Committee, and its assets are held and managed by a trustee. This ESOP is designed to motivate and reward employees as corporate owners and to provide to eligible employees additional retirement benefits. The ESOP covers almost all employees who have completed at least two years of service. Contributions to the ESOP are at the discretion of the Board of Directors and are allocated to participants who are actively employed on the last day of the plan year and who have completed a year of service for such year (as defined in the ESOP). The annual amount of the contribution is determined by taking into consideration the prevailing financial conditions and fiscal requirements of the Corporation. The total annual contribution is limited by the amount that the Corporation can deduct for federal income tax purposes. Each eligible participant’s contribution is based on a percentage of annual compensation. This form of compensation plan supports the Corporation’s overall mission statement to attain motivated and dedicated employees. In 2016, the Corporation’s subsidiaries made ESOP contributions to Mr. Drew, Mr. Cole and Mr. Hanson in the amounts of \$15,736, \$13,979 and \$12,724, respectively.

*Supplemental Retirement Plan.* The Corporation’s Supplemental Plan is a non-qualified retirement plan which provides benefits for any excess annual retirement benefits which cannot be paid under the Pension Plan and ESOP, and is described in “Executive Compensation – Pension Benefits”. There was no impact to the ESOP part of this plan as a result of the frozen Pension Plan. Mr. Drew is the only active participant in the Supplemental Retirement Plan and the Bank made a contribution for Mr. Drew in 2016 in the amount of \$5,457.

*Stock Purchase Plan.* Amendment No. 1 to the Corporation’s Stock Purchase Plan was approved by the shareholders at the 2016 Annual Meeting, which authorized up to 450,000 shares to be purchased by the plan. Under the amended Stock Purchase Plan, participants may elect to contribute up to \$900 of salary or directors’ fees each month and receive common stock with an aggregate value of two times the contribution, with the maximum level of monthly

contribution set by the Board of Directors. In 2016, the Corporation contributed \$10,800 to each of the Stock Purchase Plan accounts of Mr. Drew and Mr. Cole, and \$1,200 to the account of Mr. Hanson.

*Insurance.* The Corporation provides to all employees group term life insurance benefit of two and a half times their annual base salary not to exceed \$350,000. The Corporation's subsidiaries paid premiums of \$2,376, \$4,572, and \$828 for Mr. Drew, Mr. Cole, and Mr. Hanson, respectively, during 2016. The excess premium paid over \$50,000 of life insurance benefit is non-cash compensation to the employee. Mr. Drew was the only management officer with bank owned life insurance compensation of \$1,310 during 2016.

### **Employment Contracts and Change in Control Arrangements**

*DeWitt Drew.* On October 1, 2003, the Corporation and the Bank entered into an employment agreement with DeWitt Drew. Under the employment agreement, Mr. Drew serves as the President and Chief Executive Officer of the Corporation and the Bank and is entitled to receive an annual base salary (currently \$293,000) which is subject to normal annual increases as shall be determined by the Board of Directors of the Corporation from time to time. The employment agreement commenced on October 1, 2003, and is for a rolling five-year term that is extended for an additional day each day of his employment. In addition to the base salary, Mr. Drew is eligible to earn incentive or bonus compensation in accordance with such bonus plan as may be established by the Board of Directors of the Corporation for the fiscal year. Mr. Drew receives benefits of the kind customarily granted to other executives of the Bank and the Corporation, including participation in the Corporation's benefit plans. The Bank also pays the premiums on a \$1 million split dollar life insurance policy for Mr. Drew. If Mr. Drew's employment terminates for any reason, he agrees not to provide banking services or solicit certain bank customers within certain geographical limits for a period of two years after such termination.

If Mr. Drew's employment is terminated for Cause (as defined in the employment agreement) or if he voluntarily terminates his employment, the Bank and the Corporation will have no further financial obligation to him. The stock options that are vested as of the termination date will be exercisable for 90 days and then terminate. If Mr. Drew's employment is terminated without cause or by Mr. Drew for Good Reason (as defined) after a Change in Control (as defined), he is entitled to the salary and medical benefits provided to him under the employment agreement for the remainder of the then current term, subject to the terms and conditions of the employment agreement. Any options he has been granted as of the termination date will immediately vest and expire upon their normal expiration date in the case of a Change in Control or one year in case of another termination without cause. If Mr. Drew's employment is terminated due to a disability, he shall continue to receive his salary for the remainder of the then current term and receive medical benefits until the earlier of the end of the then current term or he is entitled to disability coverage. If Mr. Drew's employment terminates because of death or disability, his options will vest and will expire upon their normal expiration date. In the event of any such termination, except as set forth below, Mr. Drew would be entitled to approximately \$1,501,371, which is the sum of his present salary and medical benefits for the five-year term.

Mr. Drew's employment agreement provides that the compensation and benefits provided for under the agreement shall be reduced or modified so as to insure that the payments thereunder do not constitute an "excess parachute payment" as defined under Section 280G of the Internal Revenue Code (an "Excess Severance Payment"). The agreement does not provide for the payment of any taxes or a gross-up of payments to pay any taxes in the event any of the compensation or benefits were considered to be an Excess Severance Payment.

*Jeffery E. Hanson.* As of May 10, 2012, the Bank entered into an employment agreement with Jeffery E. Hanson. Under the employment agreement, Mr. Hanson, who now serves as Executive Vice President and Chief Banking Officer of the Bank, is entitled to receive an annual base salary (currently \$185,000) subject to normal annual increases as determined by the Board of Directors from time to time. The employment agreement commenced on May 10, 2012, for a three-year term and automatically renewed for an additional three-year term. In addition to the base salary, Mr. Hanson is eligible to earn incentive or bonus compensation in accordance with such bonus plan as may be established by the Board of Directors of the Corporation for the fiscal year. Mr. Hanson receives benefits of the kind customarily granted to other executives of the Bank and the Corporation, including participation in the 401(k) plan, disability insurance, medical insurance, and life insurance pursuant to the employment agreement. If Mr. Hanson's employment terminates for any reason other than without Cause (as defined in the employment agreement) or for Good Reason (as defined), he agrees not to provide banking services or solicit certain bank customers within certain geographical limits for a period of one year after such termination.

If Mr. Hanson's employment is terminated for Cause or if he voluntarily terminates his employment, the Bank and

the Corporation will have no further financial obligation to him. The stock options that are vested as of the termination date will be exercisable for 90 days and then terminate. If Mr. Hanson's employment is terminated without Cause or by Mr. Hanson for Good Reason, he is entitled to the salary and medical benefits provided to him under the employment agreement for one year, subject to the terms and conditions of the employment agreement. Any options he has been granted as of the termination date will immediately vest and be exercisable for one year and then terminate. If Mr. Hanson's employment is terminated due to a disability, he shall continue to receive his salary for one year and receive medical benefits until the earlier of one year or he is entitled to disability coverage. If Mr. Hanson's employment terminates because of death or disability, his options if any will vest and will expire upon their normal expiration date. In the event of any such termination, Mr. Hanson would be entitled to approximately \$185,000, which is the sum of his present salary for one year.

### Summary Compensation Table

The following table provides information about the compensation paid or accrued with respect to the Named Executive Officers for each of the past two fiscal years. No other executive officers of the Corporation are required to be included in this table and/or were paid \$100,000 or more in total compensation during 2016.

<b>Name and Principal Position During 2016</b>	<b>Year</b>	<b>Salary</b>	<b>Bonus</b>	<b>All Other Compensation<sup>(1)</sup></b>	<b>Total</b>
DeWitt Drew President and CEO of the Corporation and the Bank	2016	\$265,000	\$75,000	\$57,079 <sup>(2)</sup>	\$397,079
	2015	\$260,000	\$60,000	\$54,001	\$374,001
John J. Cole, Jr. Executive Vice President and COO of the Corporation and the Bank	2016	\$175,000	\$43,750	\$48,913 <sup>(3)</sup>	\$267,663
	2015	\$170,000	\$42,500	\$49,184	\$261,684
Jeffery E Hanson Executive Vice President and CBO of the Corporation and the Bank	2016	\$175,000	\$43,750	\$23,513	\$242,263
	2015	\$170,000	\$42,500	\$22,729	\$235,229

(1) Amounts shown include stock purchase plan contributions, 401(k) match, ESOP contributions, group term life insurance, and bank owned life insurance benefits.

(2) Includes director's fees for 2016 of \$10,800.

(3) Includes director's fees for 2016 of \$10,800.

### Equity-Based Compensation

The Corporation established the Option Plan to provide for the grant of stock options to officers of the Corporation. Although the Option Plan is administered by the Personnel Committee of the Board of Directors, no new stock options or other awards have been granted under the Option Plan since 2007. As of December 31, 2016, there were no outstanding equity awards under the Option Plan.

As previously described, the Corporation's Incentive Plan was approved by our shareholders at the Corporation's 2014 Annual Meeting and was established to attract, retain and motivate the Corporation's employees, consultants, advisors and directors, to promote the success of our business by linking their personal interests to those of our shareholders and to encourage stock ownership on the part of management. Under the Incentive Plan, the Corporation may issue a maximum aggregate amount of 125,000 shares of common stock. As of December 31, 2016, no grants of equity incentive awards had been made under the Incentive Plan.

### Pension Benefits

The Corporation maintains the Pension Plan which was frozen effective December 31, 2006 as a result of the increasing costs to keep it funded. The cost of the Pension Plan which represents the current and future benefits of current and retired employees has been funded by the Corporation's subsidiaries. These benefits accrue based upon actuarial

determinations employing the aggregate funding method. The compensation covered by the Pension Plan has included total annual compensation including bonuses and overtime pay. The employee benefits earned through December 31, 2006, are preserved and the funds will be maintained in a trust account to pay future benefits through retirement, but new benefits will not accrue under the Pension Plan. The portion of compensation which is considered covered compensation under the Pension Plan equals the annual salary and bonus amounts indicated in “Executive Compensation - Summary Compensation Table”.

All executive officers who exceed the maximum covered compensation limited by federal law of \$265,000 are covered under the Corporation’s Supplemental Retirement Plan. Any excess annual retirement benefit which could not be paid under the Pension Plan and ESOP because of the above federal limitation will be payable under the Supplemental Retirement Plan. During 2016, only DeWitt Drew, the Chief Executive Officer qualified for the Supplemental Retirement Plan.

Generally, when a participant retires, both the Pension Plan and the Supplemental Plan will pay to the participant benefits in the form of equal monthly installments for such participant’s life unless the participant elects to have his retirement benefits payable under one of several optional forms of payment. The benefits are based on compensation and years of service and are taxable to the participant. The normal retirement age defined in the plan is 65.

### **Director Compensation**

All of the members of the Board of Directors of the Corporation also serve on the Bank’s Board of Directors. Each Board member is compensated for his board services by the Bank. The annual director fees for the Chairman, Vice Chairman, and each director are \$12,000, \$8,400, and \$6,000, respectively. In addition, directors are paid \$400 for each Board meeting attended and \$200 for each committee meeting attended (committee meeting attendance fees are paid only to outside directors). Directors could contribute their directors’ fees to the Corporation’s stock purchase plan described in “Retirement and Other Benefits - Stock Purchase Plan” and receive common stock of the Corporation with an aggregate value of two times their contribution.

The Corporation has a voluntary deferred compensation plan (the “Deferred Compensation Plan”) for the Board of Directors administered by an insurance company. The Deferred Compensation Plan stipulates that if a director participates in the Deferred Compensation Plan for four years, the Corporation will pay the director future monthly income for ten years beginning at normal retirement age, and the Corporation will make specified monthly payments to the director’s beneficiaries in the event of his or her death prior to the completion of such ten-year payments. The Deferred Compensation Plan is funded by life insurance policies, with the Corporation as the named beneficiary. This Deferred Compensation Plan is closed to new director enrollment and participation. The only current participant is Richard L. Moss.

The following table summarizes 2016 non-employee director compensation. There were no option or stock awards granted to directors for 2016, and directors do not participate in the Pension Plan or receive any non-qualified deferred compensation. Mr. Drew and Mr. Cole were the only employees on the Board of Directors for 2016 and their compensation for that service is described in “Executive Compensation – Summary Compensation Table”. The Corporation believes that the total level of compensation for directors is reasonably comparable with other small publicly traded community bank holding companies.

### **Director Compensation Table**

<b><u>Name</u></b>	<b><u>Fees Earned or Paid in Cash</u></b>	<b><u>All Other Compensation</u></b>	<b><u>Total</u></b>
Cecil H. Barber	\$16,300	\$10,800	\$27,100
Michael J. McLean	\$26,900	\$10,800	\$37,700
Richard L. Moss	\$10,700	\$10,800	\$21,500
Roy H. Reeves	\$22,300	\$10,800	\$33,100
Johnny R. Slocumb	\$15,300	\$10,800	\$26,100
M. Lane Wear	\$23,700	\$10,800	\$34,500
Marcus R. Wells	\$20,900	\$10,800	\$31,700

## **CERTAIN RELATIONSHIPS AND RELATED PARTY TRANSACTIONS**

The Corporation has a written related person transaction policy that governs the review, approval and ratification of any transaction that would be required to be disclosed by the Corporation pursuant to Item 404 of Regulation S-K under the Securities Act of 1933. The Board of Directors or the Audit Committee must approve all such transactions under the policy.

The Bank from time to time has had, and expects to have in the future, banking transactions in the ordinary course of business with officers and directors of the Corporation and other related persons, on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with unaffiliated third parties. Such transactions have not involved more than the normal risk of collectability or presented other unfavorable features. At December 31, 2016, loans to officers, directors, and principal shareholders of the Corporation and the Bank and to other related persons amounted to \$1.4 million. Also, during 2016, directors and executive officers had approximately \$2.9 million in deposits with the Bank.

## REPORT OF THE AUDIT COMMITTEE

The Audit Committee operates pursuant to an Audit Committee Charter (“the Charter”) that was adopted by the Board of Directors on May 24, 2000, and revised on July 23, 2003. The Corporation’s management is responsible for its internal accounting controls and the financial reporting process. The Corporation’s independent accountants, TJS Deemer Dana LLP (“TJS DD”), are responsible for performing an audit of the Corporation’s consolidated financial statements in accordance with auditing standards of the Public Company Accounting Oversight Board and for expressing an opinion as to their conformity with generally accepted accounting principles. The Audit Committee’s responsibility is to monitor and oversee these processes.

The Audit Committee was involved with the selection process and the approval of TJS DD as the Corporation’s principal independent auditors. Also, the Audit Committee has approved TJS DD to provide non-audit services such as various compliance procedure reviews, employee benefit plan review audits and an information technology review audit.

In keeping with its responsibilities, the Audit Committee has reviewed and discussed the Corporation’s audited consolidated financial statements with management and the independent accountants. The Audit Committee has discussed with the Corporation’s independent accountants the matters required to be discussed by Statement on Auditing Standards No. 61, “Communications with Audit Committee,” as currently in effect. In addition, the Audit Committee has received the written disclosures from the independent accountants required by Independence Standards Board Standard No.1, “Independence Discussions with Audit Committees,” and has discussed with the independent accountants their independence. The Audit Committee has considered whether the provision of non-audit services by the independent auditors is compatible with maintaining their independence.

The Audit Committee also discussed with management and the auditors the quality and adequacy of the Corporation’s internal controls over financial reporting and the internal audit function’s organization, responsibilities, budget, and staffing.

Members of the Audit Committee rely without independent verification on the information provided to them and on the representations made by management and the independent auditors. Accordingly, the Audit Committee’s oversight does not provide an independent basis to determine that management has maintained appropriate accounting and financial reporting principles or appropriate internal controls and procedures designed to assure compliance with accounting standards and applicable laws and regulations. Furthermore, the Audit Committee’s considerations and discussions referred to above do not assure that the audit of the Corporation’s financial statements has been carried out in accordance with standards of the Public Company Accounting Oversight Board, that the financial statements are presented in accordance with generally accepted accounting principles or that the Corporation’s auditors are in fact “independent”.

Based on the reports and discussions described in this report, and subject to the limitations on the role and responsibilities of the Audit Committee referred to above and in the Audit Committee Charter, the Audit Committee recommended to the Board of Directors that the audited consolidated financial statements of the Corporation be included in the Annual Report on Form 10-K for the year ending December 31, 2016, for filing with the SEC.

This report is respectfully submitted by the Audit Committee of the Board of Directors.

M. Lane Wear  
Johnny R. Slocumb

Richard L. Moss  
Cecil Barber

## **PROPOSAL 2: APPROVAL OF ADVISORY RESOLUTION SUPPORTING THE COMPENSATION PLAN FOR EXECUTIVE OFFICERS**

### **General**

Pursuant to Section 14A of the Securities Exchange Act of 1934, the Corporation is asking its shareholders to vote, on an advisory basis, on the compensation of its Named Executive Officers as described in this Proxy Statement. This proposal, commonly known as a “say on pay” proposal, gives the Corporation’s shareholders the opportunity to express their views on the compensation of the Corporation’s Named Executive Officers.

### **Compensation Program and Philosophy**

Our executive compensation program is designed to attract, reward and retain key employees, including our Named Executive Officers, who are critical to the Corporation’s long-term success. Shareholders are urged to read the “Executive Compensation” section of this Proxy Statement for greater detail about the Corporation’s executive compensation programs, including information about the fiscal year 2016 compensation of the Named Executive Officers.

The Corporation is asking the shareholders to indicate their support for the compensation of the Corporation’s Named Executive Officers as described in this Proxy Statement by voting in favor of the following resolution:

“RESOLVED, that the shareholders approve the compensation of the Named Executive Officers, as described in the “Executive Compensation” section of this Proxy Statement, pursuant to the compensation disclosure rules of the Securities and Exchange Commission, including the compensation tables, notes and narratives.”

Even though this say on pay vote is advisory and therefore will not be binding on the Corporation, the Personnel Committee and the Board of Directors value the opinions of the Corporation’s shareholders. Accordingly, to the extent there is a significant vote against the compensation of the Named Executive Officers, the Board of Directors will consider the shareholders’ concerns and the Personnel Committee will evaluate what actions may be necessary or appropriate to address those concerns.

### **Vote Required**

The affirmative vote of a majority of the shares entitled to vote and present in person or represented by proxy at the Annual Meeting is required to approve, on an advisory basis, the “say on pay” resolution supporting the compensation plan for the executive officers.

### **Recommendation**

**The Board of Directors unanimously recommends a vote “FOR” Proposal 2.**

**PROPOSAL 3: RATIFICATION OF TJS DEEMER DANA LLP  
AS INDEPENDENT AUDITORS FOR 2017**

TJS DD was the principal independent public accountant for the Corporation during the years ended December 31, 2016 and 2015. Representatives of TJS DD are expected to be present at the Annual Meeting and will have the opportunity to make a statement if they desire to do so and to respond to appropriate questions. Subject to the vote of the shareholders, the Corporation anticipates that TJS DD will be the Corporation's accountants for the current fiscal year.

**Recommendation**

**The Board of Directors unanimously recommends that you vote "FOR" the ratification of TJS DD as independent auditors for 2017.**



## **INFORMATION CONCERNING THE CORPORATION'S ACCOUNTANTS**

### **Audit Fees**

The aggregate fees billed for professional services by TJS DD for the audit of the Corporation and reviews of the Corporation's quarterly financial statements for 2016 and 2015 were \$64,488 and \$62,101, respectfully.

### **Audit-Related Fees**

The aggregate fees billed for professional services by TJS DD for an agreed upon procedural review of the wealth strategies division and of the Bank's loan portfolio for 2016 and 2015 were \$6,250 and \$6,150, respectively. Other professional services billed for by TJS DD were for a Bank Secrecy Act procedures review of \$5,025 in 2016 and \$4,600 in 2015, and Asset and Liability Management procedures review of \$2,100 in 2016 and \$2,050 in 2015.

### **Tax Fees**

The aggregate fees billed for professional services by TJS DD for tax compliance for 2016 and 2015 were \$2,700 and \$2,600, respectively.

### **All Other Fees**

The aggregate fees billed for professional services by TJS DD for the Corporation in 2016 were the Pension Plan audit of \$5,650, 401(k) Plan audit of \$5,650, Employee Stock Ownership Plan audit of \$15,000, information technology audit of \$4,600 and a compliance audit of \$4,850. In 2015, the services performed and fees billed for audits of the Pension Plan, 401(k) Plan, Employee Stock Ownership Plan, and information technology were \$5,500, \$5,500, \$15,000 and \$4,550, respectively.

The Audit Committee approves all audit and non-audit services performed by the Corporation's independent public accountant.

## **SECTION 16(a) BENEFICIAL OWNERSHIP REPORTING COMPLIANCE**

Pursuant to Section 16(a) of the Securities Exchange Act of 1934, each executive officer, director and beneficial owner of 10% or more of the Corporation's common stock is required to file certain forms with the SEC. Based solely on its review of the copies of such reports received by the Corporation, or written representations from certain reporting persons, the Corporation believes that during the last fiscal year all Section 16 filing requirements applicable to its reporting persons were fulfilled.

## **SHAREHOLDER PROPOSALS AND DIRECTOR NOMINATIONS**

Any proposals of shareholders or recommendations for director nominees intended to be presented at the Corporation's 2018 Annual Meeting must be received by December 20, 2017, in order to be eligible for inclusion in the Corporation's Proxy Statement and Proxy for that meeting. The Corporation must be notified of any other matter intended to be presented by a shareholder at the 2018 Annual Meeting no later than March 5, 2018.

## **SHAREHOLDER COMMUNICATIONS**

The Board of Directors maintains a process for shareholders to communicate with the Board of Directors. Shareholders wishing to communicate with the Board of Directors should send any communication in writing to Mr. George R. Kirkland, Southwest Georgia Financial Corporation, P. O. Box 3488, Moultrie, GA 31776-3488. Any such communication should state the number of shares beneficially owned by the shareholder making the communication. The communication will be forwarded to the full Board of Directors or to any individual director or directors to whom the communication is directed unless the communication is illegal or otherwise inappropriate.

**OTHER MATTERS THAT MAY COME BEFORE THE MEETING**

Management of the Corporation knows of no matters other than those stated above that are to be brought before the Annual Meeting. If any other matters should be presented for consideration and voting, however, it is the intention of the persons named as proxies in the enclosed Proxy to vote in accordance with their judgment as to what is in the best interest of the Corporation.

By order of the Board of Directors,



DeWitt Drew  
President and  
Chief Executive Officer

April 20, 2017

ANNUAL MEETING OF SHAREHOLDERS OF  
**SOUTHWEST GEORGIA FINANCIAL CORPORATION**

May 23, 2017

**NOTICE OF INTERNET AVAILABILITY OF PROXY MATERIAL:**  
The Notice of Meeting, proxy statement and proxy card  
are available at <https://www.sgfc.com/pdf/2016annualreportandproxy.pdf>

Please sign, date and mail  
your proxy card in the  
envelope provided as soon  
as possible.

↓ Please detach along perforated line and mail in the envelope provided. ↓

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THE BOARD OF DIRECTORS RECOMMENDS A VOTE "FOR" THE ELECTION OF DIRECTORS AND ALL PROPOSALS.  
PLEASE SIGN, DATE AND RETURN PROMPTLY IN THE ENCLOSED ENVELOPE. PLEASE MARK YOUR VOTE IN BLUE OR BLACK INK AS SHOWN HERE

1. Election of Directors:

FOR ALL NOMINEES

WITHHOLD AUTHORITY  
FOR ALL NOMINEES

FOR ALL EXCEPT  
(See instructions below)

**NOMINEES:**

- Cecil H. Barber
- John J. Cole, Jr.
- DeWitt Drew
- Richard L. Moss
- Roy H. Reeves
- Johnny R. Slocumb
- M. Lane Wear
- Marcus R. Wells

**INSTRUCTIONS:** To withhold authority to vote for any individual nominee(s), mark "FOR ALL EXCEPT"  
and fill in the circle next to each nominee you wish to withhold, as shown here: ●

- 2. To approve the advisory "say on pay" resolution supporting the compensation plan for the executive officers.  FOR  AGAINST  ABSTAIN
- 3. To ratify the appointment of TJS Deemer Dana, LLP as our independent auditors for the fiscal year 2017.  FOR  AGAINST  ABSTAIN
- 4. Other Matters to Come Before the Meeting

THE BOARD OF DIRECTORS FAVORS A VOTE "FOR" THE ELECTION AS DIRECTORS OF THE PERSONS NAMED IN THE PROXY AND ACCOMPANYING PROXY STATEMENT AND, UNLESS THE VOTE OF THE SHAREHOLDER INDICATES OTHERWISE, THIS PROXY WILL BE SO VOTED.

To change the address on your account, please check the box at right and indicate your new address in the address space above. Please note that changes to the registered name(s) on the account may not be submitted via this method.

Signature of Shareholder

Date:

Signature of Shareholder

Date:

**Note:** Please sign exactly as your name or names appear on this Proxy. When shares are held jointly, each holder should sign. When signing as executor, administrator, attorney, trustee or guardian, please give full title as such. If the signer is a corporation, please sign full corporate name by duly authorized officer, giving full title as such. If signer is a partnership, please sign in partnership name by authorized person.

□



**COMMON STOCK  
OF  
SOUTHWEST GEORGIA FINANCIAL CORPORATION**

**THIS PROXY IS SOLICITED BY THE BOARD OF DIRECTORS FOR  
THE 2017 ANNUAL MEETING OF SHAREHOLDERS**

The undersigned hereby appoint(s) John J. Cole, Jr. and George R. Kirkland, or either of them with power of substitution to each, as Proxies of the undersigned to vote the Common Stock of the undersigned at the Annual Meeting of Shareholders of SOUTHWEST GEORGIA FINANCIAL CORPORATION (the "Corporation") to be held on May 23, 2017, and any adjournment thereof.

**SEE REVERSE SIDE**